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Summary

Michaelmas Term
[2015] UKSC 72
On appeal from: [2014] EWCA Civ 603

JUDGMENT

Marks and Spencer plc (Appellant) *v* BNP Paribas Securities Services Trust Company (Jersey) Limited and another (Respondents)

before

Lord Neuberger, President
Lord Clarke
Lord Sumption
Lord Carnwath
Lord Hodge

JUDGMENT GIVEN ON

2 December 2015

Heard on 7 October 2015

Appellant	*Respondents*
Guy Fetherstonhaugh QC	Nicholas Dowding QC

Kester Lees (Instructed by King & Wood Mallesons LLP)	Mark Sefton (Instructed by Allen & Overy)

LORD NEUBERGER: (with whom Lord Sumption and Lord Hodge agree)

Introductory

1. This appeal concerns a tenant's break clause in a lease. The lease had been granted for a term expiring on 2 February 2018, and, in the normal way, the rent was payable in advance on the usual quarter days. The tenant exercised its right under the break clause to determine the lease on 24 January 2012, after it had paid the full quarter's rent due on 25 December 2011. The issue is whether it can recover from the landlords the apportioned rent in respect of the period from 24 January to 24 March 2012. The resolution of that issue turns on the interpretation of the lease, and it requires the court to consider the principles by reference to which a term is to be implied into a contract.

The Contractual documentation

2. The defendants were the landlords and the claimant was the tenant under four sub-underleases of different floors in a building known as The Point ("the Building") in Paddington Basin, London W2. Each sub-underlease was set out in a Schedule to a deed made on 15 January 2010, which varied or "restated" the provisions of a previous sub-underlease which had been granted to the claimant in 2006. The origin of most of the provisions of each of the four sub-underleases granted in 2010 is to be found in the four sub-underleases granted in 2006. In this judgment, it is only necessary to refer to one of the four deeds ("the Deed"), the sub-underlease it granted ("the Lease") and the sub-underlease ("the earlier Lease") it replaced, as any differences between the four Deeds, the four 2010 sub-underleases and the four 2006 sub-underleases are irrelevant for present purposes.

3. The Lease demised the third floor of the Building ("the Premises") together with the use of two car parking spaces to the claimant "for a term of years starting on 25 January 2006 and ending on 2 February 2018". The reddendum reserved a rent consisting of (a) "the Basic Rent" and (b) "the Car

Park Licence Fee". The Basic Rent was "£919,800 plus VAT per annum", which was to be "reviewed in accordance with Schedule 4", which provided for reviews on certain specified "review dates". The Basic Rent was to be "paid yearly and proportionately for any part of a year by equal quarterly instalments in advance on the [usual] quarter days". As at 25 December 2011, the Basic Rent was £1,236,689 per annum plus VAT. The Car Park Licence Fee was £6,000 per annum, which was to "be paid by equal quarterly instalments in advance on the [usual] quarter days". The Lease was validly excluded from the ambit of sections 24-28 of the Landlord and Tenant Act 1954, which meant that, if not determined before 2 February 2018, the Lease would end on that date.

4. Clause 8.1 of the Lease entitled the claimant (so long as it remained the tenant) to determine the Lease, by giving the landlords six months' prior written notice (a "break notice") to take effect on the "first break date", namely 24 January 2012, and clause 8.2 provided for a "second break date" of 24 January 2016. Clause 8.3 stipulated that a break notice would only have effect "if on the break date there are no arrears of Basic Rent or VAT on Basic Rent". Clause 8.4 provided that a break notice would only take effect on the first break date "if on or prior to the first break date the tenant pays to the landlord the sum of £919,800 plus VAT". Clause 8.5 was concerned with consequential conveyancing machinery. Clause 8.6 entitled the landlords to "waive compliance with all or any of the conditions ... set out in clause 8.3". Clause 8.7 stated that if "the provisions of this clause are complied with" the Lease should end on the break date "without prejudice to the rights of either party in respect of any previous breach by the other". A very similar clause to clause 8 was contained in the earlier Lease: hence the choice of break dates, which were on anniversaries of the date of grant of the earlier Lease.

5. Schedule 5 to the Lease dealt with insurance. In brief, the landlords covenanted to insure the Building against specified risks, and the tenant was obliged to "pay to the landlord ... a fair proportion [assessed by reference to the ratio of the floor area of the Premises to that of the Building] of every premium payable by the landlord ... for insuring the Building ...". These payments were "reserved as rent".

6. Schedule 7 to the Lease was concerned with the services which the landlord covenanted to provide to the occupiers of the Building, and the service charge which the tenant was to pay in return. The service charge, which was reserved as rent, was to be "a fair proportion" (assessed in a similar way to the insurance rent) of the cost to the landlords of providing the services. This was initially to be based on an annual estimate, which was to be paid "on account" in advance by equal instalments on the usual quarter days. Paragraph 4.5 of the Schedule provided for payment by the tenant of a balancing sum in ten working days if the actual expenditure was greater than the payment on account, and

paragraph 4.6 entitled the tenant to be credited with any "overpayment ... against the next ... payment on account", if the expenditure was less than the payment on account.

7. As is almost invariably the case with modern commercial leases, the Lease was a very full and detailed document. It ran to some 70 pages, including 15 pages of tenant's covenants and nine pages of landlords' covenants, and it included, in clause 5, a right for the landlords to forfeit the Lease for non-payment of rent or other breach of covenant by the tenant. The provisions for review of the Basic Rent in Schedule 4 ran to four pages, and required a periodic review of the rent to the then-current market rental value of the Premises as at certain specified "review dates". Paragraph 8 of Schedule 4 stated that if the reviewed rent was not determined by a review date, rent at the preceding rate is to be payable and, once the reviewed rent is determined, a balancing figure is payable by the tenant to the landlords.

8. It is not necessary to say much about the Deed, save that clause 4 provided that, if the tenant did not exercise its right to break the Lease (and the other three sub-underleases) on 24 January 2012, the landlords would pay the tenant £150,000 by crediting it against the tenant's liability for the rent due on the following quarter day, 25 March 2012.

The factual background

9. On 7 July 2011, pursuant to clause 8.1, the claimant tenant served a break notice on the defendant landlords to determine the Lease on 24 January 2012. On 19 July 2011, the defendants invoiced the claimant for its share of the insurance rent premium under Schedule 5 ("the insurance rent") in respect of the year from 1 July 2011, in the sum of £14,972.85 plus VAT, which the claimant paid two weeks later.

10. Shortly before 25 December 2011, the claimant paid the defendants the rent due on that date in respect of the quarter from that date up to and including 24 March 2012, the day before the next quarter day, thereby ensuring that clause 8.3 of the Lease was satisfied. This rent consisted of the Basic Rent (as reviewed) of £309,172.25 plus VAT, and the Car Park Licence Fee of £1,500. On or about 18 January 2012, the claimant paid the defendants £919,800 plus VAT, pursuant to clause 8.4 of the Lease. As a result of these payments, the break notice served on 7 July 2011 was effective, and the Lease determined on 24 January 2012.

11. On 3 September 2012, more than eight months after the expiry of the Lease, the defendants served on the claimant a service charge certificate in respect of the services provided in the calendar year 2011. This showed that the cost of the services had been less than the estimate, and the defendants credited the claimant with its excess payment.

12. Although there were similar issues about the Car Park Licence Fee, the insurance rent and the service charge, the principal issue between the parties at trial was whether the claimant was entitled to be refunded a sum equal to the apportioned Basic Rent in respect of the period 24 January 2012 (when the Lease expired) and 25 March 2012, given that the claimant had paid the Basic Rent (in the sum of £309,172.25 plus VAT) on 25 December 2011 in respect of that period even though the Lease had expired on 24 January 2012. In a carefully reasoned judgment, Morgan J held that the claimant was so entitled - [2013] EWHC 1279 (Ch). For reasons given by Arden LJ (with whom Jackson and Fulford LJJ agreed), the Court of Appeal allowed the defendants' appeal - [2014] EWCA Civ 603.

13. The claimant now appeals to this court, contending, as it did in the courts below, that there should be implied into the Lease a term that, if the tenant exercises the right to break under clause 8 and the Lease consequently determines on 24 January, the landlords ought to pay back a proportion of the Basic Rent paid by the tenant due on the immediately preceding 25 December ("the apportioned sum"), being apportioned in respect of the period 24 January up to and including the ensuing 24 March 2012. A similar issue arises in relation to the Car Park Licence Fee and the insurance rent, which I shall deal with at the end of this judgment.

Implied terms in contracts

14. It is rightly accepted on behalf of the claimant that there is no provision in the Lease which expressly obliges the landlords to pay the apportioned sum to the tenant. Accordingly, it follows that in order to succeed the claimant has to establish that such an obligation must be implied into the Lease.

15. As Lady Hale pointed out in *Geys v Société Générale* [2013] 1 AC 523, para 55, there are two types of contractual implied term. The first, with which this case is concerned, is a term which is implied into a particular contract, in the light of the express terms, commercial common sense, and the facts known to both parties at the time the contract was made. The second type of implied terms arises because, unless such a term is expressly excluded, the law (sometimes by

statute, sometimes through the common law) effectively imposes certain terms into certain classes of relationship.

16. There have, of course, been many judicial observations as to the nature of the requirements which have to be satisfied before a term can be implied into a detailed commercial contract. They include three classic statements, which have been frequently quoted in law books and judgments. In *The Moorcock* (1889) 14 PD 64, 68, Bowen LJ observed that in all the cases where a term had been implied, "it will be found that ... the law is raising an implication from the presumed intention of the parties with the object of giving the transaction such efficacy as both parties must have intended that at all events it should have". In *Reigate v Union Manufacturing Co (Ramsbottom) Ltd* [1918] 1 KB 592, 605, Scrutton LJ said that "[a] term can only be implied if it is necessary in the business sense to give efficacy to the contract". He added that a term would only be implied if "it is such a term that it can confidently be said that if at the time the contract was being negotiated" the parties had been asked what would happen in a certain event, they would both have replied "'Of course, so and so will happen; we did not trouble to say that; it is too clear'". And in *Shirlaw v Southern Foundries (1926) Ltd* [1939] 2 KB 206, 227, MacKinnon LJ observed that, "[p]rima facie that which in any contract is left to be implied and need not be expressed is something so obvious that it goes without saying". Reflecting what Scrutton LJ had said 20 years earlier, MacKinnon LJ also famously added that a term would only be implied "if, while the parties were making their bargain, an officious bystander were to suggest some express provision for it in their agreement, they would testily suppress him with a common 'Oh, of course!'".

17. Support for the notion that a term will only be implied if it satisfies the test of business necessity is to be found in a number of observations made in the House of Lords. Notable examples included Lord Pearson (with whom Lord Guest and Lord Diplock agreed) in *Trollope & Colls Ltd v North West Metropolitan Regional Hospital Board* [1973] 1 WLR 601, 609, and Lord Wilberforce, Lord Cross, Lord Salmon and Lord Edmund-Davies in *Liverpool City Council v Irwin* [1977] AC 239, 254, 258, 262 and 266 respectively. More recently, the test of "necessary to give business efficacy" to the contract in issue was mentioned by Lady Hale in *Geys* at para 55 and by Lord Carnwath in *Arnold v Britton* [2015] 2 WLR 1593, para 112.

18. In the Privy Council case of *BP Refinery (Westernport) Pty Ltd v President, Councillors and Ratepayers of the Shire of Hastings* (1977) 52 ALJR 20, [1977] UKPC 13, 26, Lord Simon (speaking for the majority, which included Viscount Dilhorne and Lord Keith) said that:

> "[F]or a term to be implied, the following conditions (which may overlap) must be satisfied: (1) it must be reasonable and equitable; (2) it must be necessary to give business efficacy to the contract, so that no term will be implied if the contract is effective without it; (3) it must be so obvious that 'it goes without saying'; (4) it must be capable of clear expression; (5) it must not contradict any express term of the contract."

19. In *Philips Electronique Grand Public SA v British Sky Broadcasting Ltd* [1995] EMLR 472, 481, Sir Thomas Bingham MR set out Lord Simon's formulation, and described it as a summary which "distil[led] the essence of much learning on implied terms" but whose "simplicity could be almost misleading". Sir Thomas then explained that it was "difficult to infer with confidence what the parties must have intended when they have entered into a lengthy and carefully-drafted contract but have omitted to make provision for the matter in issue", because "it may well be doubtful whether the omission was the result of the parties' oversight or of their deliberate decision", or indeed the parties might suspect that "they are unlikely to agree on what is to happen in a certain ... eventuality" and "may well choose to leave the matter uncovered in their contract in the hope that the eventuality will not occur". Sir Thomas went on to say this at p 482:

> "The question of whether a term should be implied, and if so what, almost inevitably arises after a crisis has been reached in the performance of the contract. So the court comes to the task of implication with the benefit of hindsight, and it is tempting for the court then to fashion a term which will reflect the merits of the situation as they then appear. Tempting, but wrong. [He then quoted the observations of Scrutton LJ in *Reigate*, and continued] [I]t is not enough to show that had the parties foreseen the eventuality which in fact occurred they would have wished to make provision for it, unless it can also be shown either that there was only one contractual solution or that one of several possible solutions would without doubt have been preferred ..."

20. Sir Thomas's approach in *Philips* was consistent with his reasoning, as Bingham LJ in the earlier case *The APJ Priti* [1987] 2 Lloyd's Rep 37, 42, where he rejected the argument that a warranty, to the effect that the port declared was prospectively safe, could be implied into a voyage charter-party. His reasons for rejecting the implication were "because the omission of an express warranty may well have been deliberate, because such an implied term is not necessary for the

business efficacy of the charter and because such an implied term would at best lie uneasily beside the express terms of the charter".

21. In my judgment, the judicial observations so far considered represent a clear, consistent and principled approach. It could be dangerous to reformulate the principles, but I would add six comments on the summary given by Lord Simon in *BP Refinery* as extended by Sir Thomas Bingham in *Philips* and exemplified in *The APJ Priti*. First, in *Equitable Life Assurance Society v Hyman* [2002] 1 AC 408, 459, Lord Steyn rightly observed that the implication of a term was "not critically dependent on proof of an actual intention of the parties" when negotiating the contract. If one approaches the question by reference to what the parties would have agreed, one is not strictly concerned with the hypothetical answer of the actual parties, but with that of notional reasonable people in the position of the parties at the time at which they were contracting. Secondly, a term should not be implied into a detailed commercial contract merely because it appears fair or merely because one considers that the parties would have agreed it if it had been suggested to them. Those are necessary but not sufficient grounds for including a term. However, and thirdly, it is questionable whether Lord Simon's first requirement, reasonableness and equitableness, will usually, if ever, add anything: if a term satisfies the other requirements, it is hard to think that it would not be reasonable and equitable. Fourthly, as Lord Hoffmann I think suggested in *Attorney General of Belize v Belize Telecom Ltd* [2009] 1 WLR 1988, para 27, although Lord Simon's requirements are otherwise cumulative, I would accept that business necessity and obviousness, his second and third requirements, can be alternatives in the sense that only one of them needs to be satisfied, although I suspect that in practice it would be a rare case where only one of those two requirements would be satisfied. Fifthly, if one approaches the issue by reference to the officious bystander, it is "vital to formulate the question to be posed by [him] with the utmost care", to quote from Lewison, *The Interpretation of Contracts* 5th ed (2011), para 6.09. Sixthly, necessity for business efficacy involves a value judgment. It is rightly common ground on this appeal that the test is not one of "absolute necessity", not least because the necessity is judged by reference to business efficacy. It may well be that a more helpful way of putting Lord Simon's second requirement is, as suggested by Lord Sumption in argument, that a term can only be implied if, without the term, the contract would lack commercial or practical coherence.

22. Before leaving this issue of general principle, it is appropriate to refer a little further to *Belize Telecom*, where Lord Hoffmann suggested that the process of implying terms into a contract was part of the exercise of the construction, or interpretation, of the contract. In summary, he said at para 21 that "[t]here is only one question: is that what the instrument, read as a whole against the relevant background, would reasonably be understood to mean?". There are two points to be made about that observation.

23. First, the notion that a term will be implied if a reasonable reader of the contract, knowing all its provisions and the surrounding circumstances, would understand it to be implied is quite acceptable, provided that (i) the reasonable reader is treated as reading the contract at the time it was made and (ii) he would consider the term to be so obvious as to go without saying or to be necessary for business efficacy. (The difference between what the reasonable reader would understand and what the parties, acting reasonably, would agree, appears to me to be a notional distinction without a practical difference.) The first proviso emphasises that the question whether a term is implied is to be judged at the date the contract is made. The second proviso is important because otherwise Lord Hoffmann's formulation may be interpreted as suggesting that reasonableness is a sufficient ground for implying a term. (For the same reason, it would be wrong to treat Lord Steyn's statement in *Equitable Life Assurance Society v Hyman* [2002] 1 AC 408, 459 that a term will be implied if it is "essential to give effect to the reasonable expectations of the parties" as diluting the test of necessity. That is clear from what Lord Steyn said earlier on the same page, namely that " [t]he legal test for the implication of ... a term is ... strict necessity", which he described as a "stringent test".)

24. It is necessary to emphasise that there has been no dilution of the requirements which have to be satisfied before a term will be implied, because it is apparent that *Belize Telecom* has been interpreted by both academic lawyers and judges as having changed the law. Examples of academic articles include C Peters *The implication of terms in fact* [2009] CLJ 513, P Davies, *Recent developments in the Law of Implied Terms* [2010] LMCLQ 140, J McCaughran *Implied terms: the journey of the man on the Clapham Omnibus* [2011] CLJ 607, and JW Carter and W Courtney, *Belize Telecom: a reply to Professor McLauchlan* [2015] LMCLQ 245). And in *Foo Jong Peng v Phua Kiah Mai* [2012] 4 SLR 1267, paras 34-36, the Singapore Court of Appeal refused to follow the reasoning in *Belize* at least in so far as "it suggest[ed] that the traditional 'business efficacy' and 'officious bystander' tests are not central to the implication of terms" (reasoning which was followed in *Sembcorp Marine Ltd v PPL Holdings Pte Ltd* [2013] SGCA 43). The Singapore Court of Appeal were in my view right to hold that the law governing the circumstances in which a term will be implied into a contract remains unchanged following *Belize Telecom.*

25. The second point to be made about what was said in *Belize Telecom* concerns the suggestion that the process of implying a term is part of the exercise of interpretation. Although some support may arguably be found for such a view in *Trollope* at p 609, the first clear expression of that view to which we were referred was in *Banque Bruxelles Lambert SA v Eagle Star Insurance Co Ltd* [1997] AC 191, 212, where Lord Hoffmann suggested that the issue of whether to imply a term into a contract was "one of construction of the agreement as a whole in its commercial setting". Lord Steyn quoted this passage

with approval in *Equitable Life* at p 459, and, as just mentioned, Lord Hoffmann took this proposition further in *Belize Telecom*, paras 17-27. Thus, at para 18, he said that "the implication of the term is not an addition to the instrument. It only spells out what the instrument means"; and at para 23, he referred to "The danger ... in detaching the phrase 'necessary to give business efficacy' from the basic process of construction". Whether or not one agrees with that approach as a matter of principle must depend on what precisely one understands by the word "construction".

26. I accept that both (i) construing the words which the parties have used in their contract and (ii) implying terms into the contract, involve determining the scope and meaning of the contract. However, Lord Hoffmann's analysis in *Belize Telecom* could obscure the fact that construing the words used and implying additional words are different processes governed by different rules.

27. Of course, it is fair to say that the factors to be taken into account on an issue of construction, namely the words used in the contract, the surrounding circumstances known to both parties at the time of the contract, commercial common sense, and the reasonable reader or reasonable parties, are also taken into account on an issue of implication. However, that does not mean that the exercise of implication should be properly classified as part of the exercise of interpretation, let alone that it should be carried out at the same time as interpretation. When one is implying a term or a phrase, one is not construing words, as the words to be implied are *ex hypothesi* not there to be construed; and to speak of construing the contract as a whole, including the implied terms, is not helpful, not least because it begs the question as to what construction actually means in this context.

28. In most, possibly all, disputes about whether a term should be implied into a contract, it is only after the process of construing the express words is complete that the issue of an implied term falls to be considered. Until one has decided what the parties have expressly agreed, it is difficult to see how one can set about deciding whether a term should be implied and if so what term. This appeal is just such a case. Further, given that it is a cardinal rule that no term can be implied into a contract if it contradicts an express term, it would seem logically to follow that, until the express terms of a contract have been construed, it is, at least normally, not sensibly possible to decide whether a further term should be implied. Having said that, I accept Lord Carnwath's point in para 71 to the extent that in some cases it could conceivably be appropriate to reconsider the interpretation of the express terms of a contract once one has decided whether to imply a term, but, even if that is right, it does not alter the fact that the express terms of a contract must be interpreted before one can consider any question of implication.

29. In any event, the process of implication involves a rather different exercise from that of construction. As Sir Thomas Bingham trenchantly explained in *Philips* at p 481:

> "The courts' usual role in contractual interpretation is, by resolving ambiguities or reconciling apparent inconsistencies, to attribute the true meaning to the language in which the parties themselves have expressed their contract. The implication of contract terms involves a different and altogether more ambitious undertaking: the interpolation of terms to deal with matters for which, *ex hypothesi*, the parties themselves have made no provision. It is because the implication of terms is so potentially intrusive that the law imposes strict constraints on the exercise of this extraordinary power."

30. It is of some interest to see how implication was dealt with in the recent case in this court of *Aberdeen City Council v Stewart Milne Group Ltd* 2012 SLT 205. At para 20, Lord Hope described the implication of a term into the contract in that case as "the product of the way I would interpret this contract". And at para 33, Lord Clarke said that the point at issue should be resolved "by holding that such a term should be implied rather than by a process of interpretation". He added that "[t]he result is of course the same".

31. It is true that *Belize Telecom* was a unanimous decision of the Judicial Committee of the Privy Council and that the judgment was given by Lord Hoffmann, whose contributions in so many areas of law have been outstanding. However, it is apparent that Lord Hoffmann's observations in *Belize Telecom*, paras 17-27 are open to more than one interpretation on the two points identified in paras 23-24 and 25-30 above, and that some of those interpretations are wrong in law. In those circumstances, the right course for us to take is to say that those observations should henceforth be treated as a characteristically inspired discussion rather than authoritative guidance on the law of implied terms.

32. Having made those general remarks about implied terms, I turn to consider the specific issue on this appeal, namely the claimant's contention that it is entitled to claim the apportioned sum from the defendants by virtue of an implied term to that effect in the Lease. I shall start by focussing on the terms of the Lease and the Deed, and then turn to the broader picture.

The arguments based on the provisions of the Lease and the Deed

33. Each quarter's rent paid in advance under a modern commercial lease, such as the Lease in this case, can fairly be said to be referable to the tenant's use and enjoyment of the demised premises for the forthcoming quarter. Accordingly, the sum of £309,172.25 plus VAT due on 25 December 2011, and paid shortly before that date, can fairly be said, at least in general terms, to have been envisaged as being the tenant's *quid pro quo* for being able to occupy and enjoy the Premises up to 25 March 2012. There is therefore real force in the contention that, if the defendants can retain the apportioned sum, it would be unfairly prejudicial to the claimant and a pure windfall for the defendants. A provision that the defendant landlords should reimburse the claimant tenant the apportioned sum would thus seem to be reasonable and equitable.

34. The claimant's case is reinforced by the fact that, as explained in para 4 above, the two break dates of 24 January 2012 and 2016 owe their origin to the date of grant of the earlier Lease, and that date was dependent on the date on which the head-landlord gave its consent to the grant of the earlier Lease. Thus, it can fairly be said that the parties had agreed the terms of the break clause, not knowing whether the break dates would be shortly after, shortly before or even on, a quarter day. This supports the notion that they are unlikely to have intended that the apportioned rent was intended to be retained by the landlords as part of the compensation for the tenant's operation of the break clause. This point is mildly weakened by the fact that the parties could have varied the break dates, or the terms of clause 8, when they came to renegotiate in 2010 the terms originally agreed in the 2006 Lease, but it still has force.

35. A further point on which the claimant relies arises from the fact that the Basic Rent is stipulated in the Lease to be "paid yearly *and proportionately for any part of a year* by equal quarterly instalments in advance" (emphasis added). It is common ground that the effect of the italicised words is that, if the Lease had run its full course to 2 February 2018, the tenant would only have had to pay an apportioned part of the Basic Rent due on 25 December 2017, because, as at that date, the parties would have known that the Lease would expire before the next quarter day, 25 March 2018. In the present case, it is common ground that, because the claimant had not paid the sum of £919,800 plus VAT due under clause 8.4 before 25 December 2011, it would not have been known as at that date whether the Lease would come to an end before 25 March 2012, and the tenant therefore had to pay the quarter's rent in full: it only became clear that the Lease would determine on 24 January 2012 when the claimant paid the £919,800 plus VAT on 18 January. However, if the claimant had paid the £919,800 plus VAT before 25 December 2011, the claimant argues (rightly in my view) that it would have been clear on 25 December 2011 that the Lease would end on 24 January 2012, so that the claimant would only have had to pay an

appropriate proportion of the Basic Rent on 25 December 2011. The claimant accordingly contends that commercial common sense mandates that it should be in the same financial position whether it pays the £919,800 plus VAT before 25 December 2011 or chooses to wait, as it is entitled to, until after 25 December 2011 to pay that sum. (I might add that this point is somewhat reinforced when one considers what would have happened if the tenant had waited till the second break date to determine the Lease: because clause 8.4 only applies to the first break date, the tenant would have been entitled to pay only an apportioned part of the quarter's Basic Rent on 25 December 2015.)

36. The claimant raised other points which, to my mind, had less force. Thus, the fact that the Basic Rent was payable "yearly *and proportionately for any part of a year*" was said of itself to support the implied term for which the claimant contends. Given that the italicised words did not justify the claimant paying only an apportioned part of the rent due on 25 December 2011 on the facts of this case, those words appear if anything to undermine the claimant's case: the fact that the Lease expressly provided that only part of a quarter's rent was to be paid in some circumstances could fairly be said to undermine the notion that one should imply a term which has a similar effect in other circumstances.

37. There is considerable force in the points discussed in paras 33-35 above, and between them they help make out a powerful case for contending that it is necessary for business efficacy that the term contended for by the claimant should be implied into the Lease. However, it is necessary to consider the countervailing arguments.

38. The defendants rely on the fact that the Lease is a very detailed document, which had been entered into between two substantial and experienced parties, and had been negotiated and drafted by expert solicitors. In particular, the Lease makes provision for a large number of contingencies. Accordingly, it is said, with obvious justification, that the observations of Sir Thomas Bingham in *Philips Electronique* quoted in para 19 above are particularly in point.

39. More specifically, the defendants refer to the express provisions relating to the payment of money in connection with clause 8. First, there is the payment of £919,800 plus VAT under clause 8.4. It is said that, while it involves no logical inconsistency, it is somewhat peculiar to imply into the Lease a term requiring the landlords to pay the tenant around £200,000 plus VAT on 25 January 2012, when the Lease has an express term requiring the tenant to pay the landlords around £900,000 plus VAT by 24 January 2012: the implied term "lie[s] uneasily" with the express terms to use Bingham LJ's expression in *The APJ Priti*. Secondly, there is the condition in clause 8.3 which required the

tenant to have paid all rent due on 25 March 2012 if it wished to exercise the right to break. Given that the effect of that provision is that the tenant must have paid rent for the whole quarter ending on 25 March 2012, it can again be said to be somewhat peculiar to imply a term requiring the landlord to repay the tenant most of that sum.

40. Clauses 8.3 and 8.4 of the Lease, together with clause 4 of the Deed, which provided that the tenant would be paid £150,000 if it did not exercise its right to break, show how carefully and fully the parties considered and identified their rights against each other in relation to clause 8 of the Lease. There is force in the argument that these three provisions show that the parties had directed their minds to the specific question of what payments were to be made between them in connection with clause 8, and in particular what sums were to be paid if the right to break either was implemented or was not implemented, and that this renders it inappropriate for the court to step in and fill in what is no more than an arguable lacuna.

41. There is, in my view, less force in the defendants' reliance on paragraph 8 of Schedule 4 to the Lease (discussed in para 7 above). I see the logic of the argument that the fact that the rent review provisions expressly dealt with a similar point is an indication that the parties must have intentionally excluded any reference to such a point in clause 8. However, the rent review provisions were no doubt taken from a previous precedent, and, while careful thought would have been given to their precise terms, a provision such as paragraph 8 of Schedule 4 would have been in any sophisticated modern rent review clause. Having said that, I suppose that it might be said that the defendants could make something of the fact that such a provision is not normally included in a standard break clause, but I think that is too remote from the issue in this case to be of any help, and it is, sensibly, not a point which was developed, or even raised, in argument.

The general law on apportionment of rent payable in advance

42. The arguments discussed so far have focussed on the terms of the Lease (and the Deed) and their commercial effect. However, it is also necessary to consider the established legal background against which the Lease was entered into, and in particular the general attitude of the law to the apportionability of rent payable in advance.

43. It has long been well established that rent, whether payable in arrear or advance, is not apportionable in time in common law. Accordingly, if a lease under which the rent is payable in arrear was forfeited or came to an end

prematurely for some other reason, the landlord loses the right to recover the rent due on the rent day following that determination, at least according to the common law - see eg *William Clun's Case* (1613) 10 Co Rep 127a . Parliament sought to remedy this initially in a limited way through the now repealed section 15 of the Distress for Rent Act 1737 and the Apportionment Act 1834, and then more comprehensively through the Apportionment Act 1870, which is still in force. Section 2 of the 1870 Act prospectively provides that "All rents, annuities, dividends, and other periodical payments in the nature of income" should "like interest on money lent, be considered as accruing from day to day, and shall be apportionable in respect of time accordingly".

44. There is no doubt that section 2 applies to rent payable in arrear, as was held by Malins V-C in *Capron v Capron* (1874) LR 17 Eq 288. In *Ellis v Rowbotham* [1900] 1 QB 740, the Court of Appeal held that the 1870 Act did not apply to rent payable in advance and, ever since then, it has been assumed that this was the law. At the invitation of the court, it was argued on behalf of the claimant that *Ellis* should be overruled. I am satisfied that it should be approved. In their brief reasoned judgments, both AL Smith and Romer LJJ explained that (i) the mischief that the 1870 Act was concerned to correct related solely to rent in arrear, and (ii) rent paid in advance could not be said to be "accruing from day to day", unlike rent in arrear. There is no reason to doubt the first reason. As to the second reason, it has obvious force if one treats the statutory reference to a sum "accruing" as a liability to pay the sum accruing. The conclusion reached in *Ellis* is also supported by the reference to "interest on money lent", because interest has virtually invariably been payable in arrear. In addition, sections 3 and 4 of the 1870 Act, which are consequential provisions expressed to apply to "The apportioned part of *any such* rent, annuity, dividend, or other payment" (emphasis added), can only apply to rent or other payments payable in arrear, and not in advance, as they deal with the date when such rent or other payments are to be treated as having become due after the relevant event (ie, in the case of rent, determination of the lease).

45. Even if we were considering the effect of section 2 in the absence of the longstanding decision in *Ellis*, I would have concluded that the section did not apply to rent paid in advance, essentially for the reasons summarised in para 44 above. However, like Collins LJ who concurred in the conclusion reached in *Ellis*, I would not have regarded the issue as "altogether free from doubt", in the light of the very wide words of the section (" *All* rents, annuities" etc). As it is, the conclusion is reinforced by the fact that *Ellis* has stood for well over 100 years, and has been followed and applied in a number of first instance and Court of Appeal decisions without any expressions of doubt as to its correctness - see eg *Hildebrand v Lewis* [1941] 2 KB 135, where at p 139 the Court of Appeal, citing *Ellis* in support, described it as "well settled that where rent is payable in advance the Apportionment Act does not apply". I find it difficult to accept that this court could properly rule that a statute had a meaning which we thought was

simply wrong, however long that meaning had been assumed to be correct. Nonetheless, I consider that, in a case where we had real doubt as to the correct meaning of a statute, we should favour the meaning which has been generally assumed to be correct for a long period, especially when the basis of that assumption is a judicial decision. In this case, however, it is not necessary to go even that far, because, as just explained, I consider that the conclusion reached by the Court of Appeal 115 years ago in *Ellis* was correct.

46. It follows from this conclusion that neither the common law nor statute apportions rent in advance on a time basis. And this was, correctly, generally understood to be the position when the Deed and the Lease were negotiated and executed. The claimant's argument, by contrast, is that a term should be implied into the Lease that the Basic Rent payable in advance on 25 December 2011 should effectively be apportioned on a time basis. The fact that the Lease was negotiated against the background of a clear, general (and correct) understanding that rent payable in advance was not apportionable in time, raises a real problem for the argument that a term can be implied into the Lease that it should be effectively apportionable if the Lease is prematurely determined in accordance with its terms.

47. The point can be taken a little further. It is a very well established rule that a landlord who forfeits a lease under which the rent is payable in advance is entitled to payment of the whole of the rent which fell due on the quarter day preceding the forfeiture. The rule was well described by Lord Denning MR in *Canas Property Co Ltd v KL Television Services Ltd* [1970] 2 QB 433, 442, where he addressed a case where the rent was payable in advance on the usual quarter days and the landlord forfeited the lease by serving a writ (now a claim form) "for instance on 25 April". He said, citing *Ellis*, that, given that "the rent is payable in advance, the writ should claim for the whole quarter's rent due *in advance* on March 25 ... and mesne profits from June 24 ... to the date of delivery of possession". (It may well be that the mesne profits should run from the date of service of the writ, but nothing hangs on that for present purposes.) Lord Denning contrasted the position where the landlord forfeited a lease under which the rent was payable in arrear, where, he said, the writ should claim "rent at the rate of ... from March 25 ... to the date of service of the writ and mesne profits" thereafter. Lord Denning's approach was followed and applied by the Court of Appeal in *Capital and City Holdings Ltd v Dean Warburg Ltd* (1988) 58 P & CR 346.

48. Thus, it is clear that, where a lease provides for payment of rent in advance on the usual quarter days, and the landlord forfeits the lease during the currency of a quarter, he is entitled to retain the whole of the rent due on the quarter day immediately before the forfeiture if it has been paid, and, if it has not been paid, he is entitled to recover and retain the whole of that rent.

Conclusions

49. If one concentrates on the factors identified in paras 33-35 above, there appears to be a strong case for the implied term for which Mr Fetherstonhaugh QC powerfully argued on behalf of the claimant. The point made in para 33 supports the contention that, not merely would an implied term be fair, but that clause 8 could be said to work rather unfairly without the implied term. The point made in para 35, supported by what is said in para 34, provides real support for the proposition that, without the implied term, clause 8 would operate in a rather capricious way. On the other hand, as Mr Dowding QC rightly said on behalf of the defendants, the factors identified in paras 38-40 above chime with the warnings given by Sir Thomas Bingham in *Philips* and his reasons for rejecting an implied warranty in *APJ Priti*. The Lease is a very full and carefully considered contract, which includes express obligations of the same nature as the proposed implied term, namely financial liabilities in connection with the tenant's right to break, and that term would lie somewhat uneasily with some of those provisions.

50. There is little point in resolving the hypothetical question whether, in the absence of the points discussed in paras 43-49 above, I would have concluded that a term should be implied as the claimant contends. Even if I would have reached that conclusion, I consider that it could not have stood once one faced up to the clear and consistent line of judicial decisions which formed the backcloth against which the terms of the Lease, and in particular the provisions of clause 8, were agreed. Save in a very clear case indeed, it would be wrong to attribute to a landlord and a tenant, particularly when they have entered into a full and professionally drafted lease, an intention that the tenant should receive an apportioned part of the rent payable and paid in advance, when the non-apportionability of such rent has been so long and clearly established. Given that it is so clear that the effect of the case-law is that rent payable and paid in advance can be retained by the landlord, save in very exceptional circumstances (eg where the contract could not work or would lead to an absurdity) express words would be needed before it would be right to imply a term to the contrary.

51. I accept that refusing to accede to the proposed implied term in this case can lead to the operation of clause 8 having the somewhat curious effect discussed in para 35 above. However, while the difference in result between the tenant paying the £919,800 plus VAT before or after 25 December 2011 can fairly be said to be capricious or anomalous, it does not begin to justify a suggestion that the contract is unworkable. Indeed, the result cannot be said to be commercially or otherwise absurd, particularly as it is entirely up to the tenant as to when that sum is paid. Further, the fact that rent payable in advance is not apportionable can always lead to potential unfairness. For instance, a landlord with a right to forfeit on 23 March for a continuing breach of covenant

could wait for three days to re-enter, in order to be able to receive the whole of the rent due in respect of the quarter to 24 June.

52. It is instructive to see how Morgan J, who accepted the claimant's case that there was an implied term, approached the question of apportionment of rent in the event of a forfeiture. At para 38 of his judgment, after referring to *Ellis*, he said that he "consider[ed] that the parties are to be taken to have contracted against the background of the established law", and he would not have been "prepared to imply such a term in a forfeiture". However, he held that such a term could be implied where the Lease determined under clause 8, but not where it determined as a result of a forfeiture, because (i) "at the date of the Lease ..., there was no established law to the contrary in the case of a tenant's break clause", whereas there was in relation to forfeiture, and (ii) "it is significant that the parties agreed that the lessee could only break the Lease if it paid a sum equivalent to one year's rent to compensate the lessor for the fact that it is losing its income stream from the break date".

53. I am unconvinced by either of those reasons. The first reason effectively ignores the point that the reasoning in *Ellis*, *Canas* and *Capital and City* applies equally to a case where a lease determines by forfeiture as it does to a case where it determines by exercise of a right to break. The second distinction appears rather to point the opposite way, as explained in para 39 above. The fact that the tenant has to make a payment of over £900,000 plus VAT by 24 January 2012 in order to exercise the right to break, lies uneasily with the notion that one should imply a term that the tenant should be paid around £200,000 plus VAT the following day, but no such problem exists with implying such a term on a forfeiture. Another reason was advanced before us, namely that forfeiture normally arises because of some failure on the part of the tenant. I agree that it does, but not always; more importantly, I do not see that as a justification for rejecting an implied term in relation to a forfeiture if such a term is to be implied in relation to the exercise of a break clause. Further, given that the exercise of the break clause is in the hands of the tenant, and the exercise of a right to forfeit is in the hands of the landlords, any argument for an implied term based on fairness is stronger in relation to forfeiture than in relation to clause 8.

54. Once one discards the two reasons given by the judge for reaching a different conclusion as to an implied term on the exercise of the break clause from that which would apply on a forfeiture, it seems to me that the logic of the analysis of Morgan J, who has considerable experience in this field, is that the claimant's case should fail in relation to the Basic Rent, as the Court of Appeal concluded.

55. Finally, I turn to the Car Park Licence Fee and the insurance rent. The reasons for rejecting the appellant's argument in relation to the Basic Rent apply equally to the Car Park Licence Fee: indeed, the position is *a fortiori* as the reservation of the Car Park Licence Fee includes no words such as "and proportionately for any part of a year", and the sum involved is very small in relative terms. So far as the insurance rent is concerned, the position is less clear. It is in a sense a payment for a service, and, as Morgan J rightly concluded, the service charge should be apportioned. However, that conclusion is based on the provisions of para 4.6 of Schedule 7 to the Lease, summarised in para 6 above, which enables the service charge to be apportioned, through the medium of a payment to the tenant: the reference to a credit plainly extends to giving effect to the credit, through payment, once the landlord and tenant relationship has come to an end. I do not consider the service charge to be a good analogy, because the service charge is paid for various ongoing services rather than a one-off contribution to a single payment, and because there is no such provision in Schedule 5, summarised in para 5 above, in relation to the insurance rent. The appellant argues that the reference to a "fair proportion" in Schedule 5 coupled with fact that there is no reference to the period for which the landlords should take out the insurance renders it easy to imply the term for which the appellant contends. In my view, however, unless it could be shown to have been unreasonable for the respondents to have insured the Building for the whole of the ensuing year when they did so, the reasons for dismissing this appeal in relation to the Basic Rent and the Car Park Licence Fee apply equally to the insurance rent. After all, the insurance rent is a single annual sum, specifically reserved as rent, with no provision for apportionment, and it became payable in full in July 2011; further, the money involved is, relatively speaking, small. It is almost invariable for a landlord, indeed for any property owner, to insure its property on an annual basis, unless there is a specific reason not to do so, and that was clearly the established practice in the present case. It may be that the landlords could not have recovered the insurance rent for a full year in a case where it would have been unreasonable for them to have expected the tenant to pay for a full year's cover. However, no such argument was advanced in this case, and it was probably too late to do so in any event, as the insurance rent had been paid for the year in question.

56. Accordingly, I would dismiss this appeal.

LORD CARNWATH:

57. I agree that the appeal should be dismissed for the reasons given by Lord Neuberger so far as addressed to the issues between the parties. I add some brief comments only on the issue of implied terms, and in particular Lord Neuberger's comments on the status of the Privy Council judgment in the *Belize* case.

58. Unlike him, I would have been content to take my starting point not in the 19th century cases (such as *The Moorcock*), but in the most modern treatment at the highest level. That is undoubtedly to be found in the judgment of the Privy Council in the *Belize* case (*Attorney General of Belize v Belize Telecom Ltd* [2009] 1 WLR 1988). It is important to remember that this was not an expression of the views of Lord Hoffmann alone, as is implied in some commentaries, but was the considered and unanimous judgment of the Board as a whole (including Lady Hale, and Lord Rodger, Lord Carswell, Lord Brown, none of them known for lack of independent thought). In the leading textbook on the subject (Lewison, *Interpretation of Contracts* 5th ed (2014)), the judgment is realistically taken to "represent the current state of the law of England and Wales" (p 284, para 6.03). The rest of that chapter contains an illuminating discussion of the working out of the principles stated by Lord Hoffmann, as applied by the courts in different contractual contexts and different factual situations. We would need very good reasons for treating the judgment as less than authoritative, and we have not been asked by the parties to do so.

59. In the present case, there has been no dispute as to the authority of the *Belize* judgment, only as to its interpretation. The appellants seek to interpret it as supporting a more liberal approach than the traditional "necessity" test (in the words of their printed case):

> "those courts which purport to follow *Belize*, but in so doing apply the tests of business efficacy, absolute necessity and the officious bystander, are departing from the test decided by the Privy Council. The issue, therefore, is whether the type of necessity that is required for the implication of a term is what may be termed (a) absolute necessity (ie the contract simply will not operate without the term); or (b) reasonable necessity (ie the contract will not operate as it must reasonably have been intended by the parties to operate)." (para 59)

The respondents by contrast submit that, properly understood, the judgment should not be read as involving any watering down of the traditional tests.

60. To my mind there is no doubt that the respondents' interpretation is correct. This is so, whether one looks to the words of Lord Hoffmann alone, or to subsequent authority in the higher courts of this country. The appellants have sought to support their submission by a commendably thorough review of the many cases in which *Belize* has been cited, in this country and in other common law jurisdictions. In my view, with the possible exception of the Singapore case referred to by Lord Neuberger to which I will come, such support is lacking.

61. Very soon after it was given, the *Belize* judgment was subject to detailed consideration by Lord Clarke MR in the Court of Appeal in *Mediterranean Salvage & Towage Ltd v Seamar Trading & Commerce Inc* [2009] EWCA Civ 531 (10 June 2009); [2010] 1 All ER (Comm) 1. The judgment was "adopted" also by Rix LJ (para 48). As the third member of the court, I was more cautious at that early stage, deciding the appeal on the narrow basis that the implied term had not been shown by the owners to be "necessary", and their case was not improved by substituting "any of the other formulations of the test discussed in the cases" (para 63).

62. Lord Clarke began by predicting (accurately as it has turned out) that Lord Hoffmann's analysis "will soon be as much referred to as his approach to the construction of contracts in *Investors Compensation Scheme* [1998] 1 WLR 896, 912-913" (para 8). He observed that "the implication of a term is an exercise in the construction of the contract as a whole" (para 9, citing the two House of Lords authorities referred to by Lord Hoffmann). He then quoted extensively from the judgment, including its citation of Lord Simon's summary of the tests for implication of a term (see Lord Neuberger para 18). He did not see the judgment as involving a loosening of the traditional tests:

> "It is thus clear that the various formulations of the test identified by Lord Simon are to be treated as different ways of saying much the same thing. Moreover, as I read Lord Hoffmann's analysis, although he is emphasising that the process of implication is part of the process of construction of the contract, he is not in any way resiling from the often stated proposition that it must be necessary to imply the proposed term. It is never sufficient that it should be reasonable." (para 15)

In support he cited also the speech of Lord Wilberforce in *Liverpool City Council v Irwin* [1977] AC 239, 253-254, rejecting the more flexible approach proposed in the Court of Appeal by Lord Denning MR. Lord Clarke also noted (para 17) the contrast drawn by Sir Thomas Bingham MR in *Philips Electronique* (a passage cited by Lord Neuberger at para 29) between the court's "usual role" in contractual interpretation of finding the "true meaning" of the words actually used by the parties, and the "more ambitious undertaking" involved in "the interpolation of terms to deal with matters for which ... [they] have made no provision". Lord Clarke concluded this passage by noting the "stress" laid by the authorities on "the importance of the test of necessity. Is the proposed implied term necessary to make the contract work?" (para 18).

63. The appellants cite a number of later cases in the Court of Appeal in which the *Belize* judgment has been discussed in some detail (notably *Crema v Cenkos Securities plc* [2011] 1 WLR 2066, para 42ff per Aikens LJ; *Stena Line Ltd v Merchant Navy Ratings Pension Fund Trustees Ltd* [2011] Pens LR 223, para 36ff per Arden LJ; *Jackson v Dear* [2014] 1 BCLC 186, para 15ff per McCombe LJ, adopting the summary of the cases by Briggs J at first instance). None of these involves any material departure from Lord Clarke's analysis. More significantly it gains direct support from the succinct observation by Lady Hale (herself a party to the *Belize* judgment) in *Geys v Société Générale* [2013] 1 AC 523, para 55 (paraphrased by Lord Neuberger at para 15), where she referred to:

> "those terms which are implied into a particular contract because, on its proper construction, the parties must have intended to include them: see *Attorney General of Belize v Belize Telecom Ltd* [2009] 1 WLR 1988. Such terms are only implied where it is necessary to give business efficacy to the particular contract in question."

64. The appellants refer also to the treatment of the *Belize* judgment in other common law countries, including Canada, Australia, New Zealand and Hong Kong. None of these citations raises any doubt as to the authority of the *Belize* judgment, nor any reason to question Lord Clarke's interpretation of it. The one exception appears to be the Singapore Court of Appeal, in which (as Lord Neuberger points out: para 24) the judgment has been subject to detailed and critical analysis in *Foo Jong Peng v Phua Kiah Mai* [2012] 4 SLR 1267 (followed in *Sembcorp Marine Ltd v PPL Holdings Pte Ltd* [2013] SGCA 43). Their analysis draws, *inter alia*, on criticisms made by Paul Davies, *Recent developments in the law of implied terms* [2010] LMCLQ 140. I note that there is no criticism in that article of Lord Clarke's judgment as such. Rather it is cited as a supposed example of the less than "wholly enthusiastic" reception which the *Belize* judgment is thought to have received in later cases.

65. That and other academic articles, as well as the judgment of the Singapore Court of Appeal, have themselves been subject to critical examination in a recent article by Professor Richard Hooley, *Implied terms after Belize Telecom* [2014] CLJ 315, in which he welcomes the "doctrinal coherence to interpretation and implication" brought by the *Belize* judgment. Other academic views, before and since, are cited by Lord Neuberger (para 24).

66. I see no purpose in reviewing the respective academic contributions in any detail, given the weight of judicial authority for the proposition (with which I understand we all agree) that the judgment is not to be read as involving any

relaxation of the traditional, highly restrictive approach to implication of terms. Once that point is established, then I am not convinced with respect that the other points made by the Singapore court are sufficient to justify undermining the authority of the Board's reasoning. The passage from the court's conclusion quoted by Lord Neuberger (para 24) needs to be read in its full context:

> "In summary, although the process of the implication of terms does involve the concept of interpretation, it entails *a specific form or conception of interpretation which is separate and distinct from the more general process of interpretation* (in particular, interpretation of the express terms of a particular document). Indeed, the process of the implication of terms necessarily involves a situation where it is precisely because the express term(s) are missing that the court is compelled to ascertain the presumed intention of the parties via the 'business efficacy' and the 'officious bystander' tests (both of which are premised on the concept of necessity). In this context, terms will not be implied easily or lightly. Neither does the court imply terms based on its idea of what it thinks ought to be the contractual relationship between the contracting parties. The court is *concerned only with the presumed intention of the contracting parties because it can ascertain the subjective intention of the contracting parties only through the objective evidence* which is available before it in the case concerned. In our view, therefore, although the *Belize* test is helpful in reminding us of the importance of the general concept of interpretation (and its accompanying emphasis on the need for objective evidence), we would respectfully *reject that test in so far as it suggests that the traditional 'business efficacy' and 'officious bystander' tests are not central to the implication of terms*. On the contrary, both these tests (premised as they are on the concept of necessity) are an integral as well as indispensable part of the law relating to implied terms in Singapore. ..." (emphasis added)

67. This summary is useful because it draws together in short form the threads of an elaborate and carefully considered judgment. As I read it the key points come down to three:

> i) Although the implication of terms is one aspect of "the concept of interpretation", it should be treated as "separate and distinct from the more general process of interpretation";

ii) The court is concerned not with "what it thinks ought to be the contractual relationship between the contracting parties", but rather with their "presumed intention" as ascertained through "objective evidence";

iii) The central place of the "business efficacy" and "officious bystander" tests should be affirmed as "an integral as well as indispensable part" of the law of Singapore.

68. The first point is an interesting debating point, but to my mind of little practical significance. It is not a point addressed by the parties before us - understandably, if they regarded it (as I would) as settled, if not by the *Belize* judgment itself, then by the authorities relied on by Lord Hoffmann (noted by Lord Neuberger at para 25). Lord Neuberger (para 28) prefers a sequential approach: first interpretation, then implication. However, as he accepts (para 26) both processes are parts of the exercise of "determining the scope and meaning of the contract".

69. On this point also I see no reason to depart from what was said in *Belize.* While I accept that more stringent rules apply to the process of implication, it can be a useful discipline to remind oneself that the object remains to discover what the parties have agreed or (in Lady Hale's words) "must have intended" to agree. In that respect it remains, and must be justified as, a process internal to the relationship between the parties, rather than one imposed from outside by statute or the common law (see the distinction noted by Lord Neuberger: para 15).

70. Nor do I agree that support for such a division can be found in the judgments referred to by Lord Neuberger: that is, the judgments of the Master of the Rolls in the *Philips* case (already cited), and of this court in *Aberdeen City Council*. The passage from the former is useful as emphasising the narrow constraints on implication. But I do not read the Master of the Rolls as treating it as a notionally separate exercise from that of interpretation. (Nor did Lord Clarke MR when quoting the same passage in *Mediterranean Salvage*: see above.) The contrast rather is between two aspects of the court's task in respect of "contractual interpretation": the "usual role" involving the resolution of ambiguities in the language used by the parties, and the "extraordinary power" involving interpolation of terms that they have not used.

71. In the same way the passages cited from *Aberdeen City Council* do not appear to support a sharp distinction between interpretation and implication, still less for the necessity of a sequential approach. No one thought it necessary to refer to *Belize.* Lord Clarke preferred implication, but acknowledged that the

two processes achieved the same result. There is no indication that he had changed his view since *Mediterranean Salvage.* He seems to have treated them as two sides of the same coin. Lord Hope who gave the lead speech (which also had majority support) clearly saw them as part of a single exercise: the implied term was the "product" of interpretation. The case seems if anything to illustrate an "iterative", rather than sequential, process (see Lord Grabiner, *The iterative process of contractual interpretation* (2012) 128 LQR 41). The results of different interpretative techniques were considered and compared, in the light of the language used and its business context, to achieve a result which best represented the assumed intentions of the parties.

72. On the second point, in so far as there is a difference from the Singapore court, I prefer the approach of Lord Neuberger which seems to me entirely consistent with *Belize.* As he says (para 21), one is concerned not with "the hypothetical answer of the actual parties", but with that of "notional reasonable people in the position of the parties at the time at which they were contracting", or in other words of Lord Hoffmann's "reasonable addressee" (*Belize,* para 18).

73. On the third point, there is no doubt as to the continuing significance of the traditional tests, as summarised by Lord Simon. If however the Singapore court intended thereby to prescribe a more rigid application of those tests, whether individually or cumulatively, I prefer the approach of the Board in *Belize* (para 27):

> "The Board considers that this list is best regarded, not as [a] series of independent tests which must each be surmounted, but rather as a collection of different ways in which judges have tried to express the central idea that the proposed implied term must spell out what the contract actually means, or in which they have explained why they did not think that it did so."

This passage is also cited, albeit with only qualified approval, by Lord Neuberger (para 21).

74. In conclusion, while I accept that Lord Hoffmann's judgment has stimulated more than usual academic controversy, I would not myself regard that as a sufficient reason to question its continuing authority. On the contrary, properly understood, I regard it as a valuable and illuminating synthesis of the factors which should guide the court. Applying that approach to the present case leaves me in no doubt that the appeal should be dismissed.

LORD CLARKE:

75. I agree that the appeal should be dismissed for the reasons given by Lord Neuberger. I only add a few words of my own because of the debate between Lord Neuberger and Lord Carnwath on Lord Hoffmann's view on the relationship between the approach to construction and the approach to the implication of a term which he expressed on behalf of the Judicial Committee of the Privy Council in *Attorney General of Belize v Belize Telecom Ltd* [2009] 1 WLR 1988. I do so in part in order to clarify what I said in the cases referred to by Lord Carnwath, especially *Mediterranean Salvage & Towage Ltd v Seamar Trading & Commerce Inc* [2009] EWCA Civ 531, [2010] 1 All ER (Comm) 1 and *Aberdeen City Council v Stewart Milne Group Ltd* 2012 SLT 205.

76. As Lord Carnwath says at para 62, I did not doubt Lord Hoffmann's observation that "the implication of a term is an exercise in the construction of the contract as a whole". I recognise, however, in the light of Lord Neuberger's judgment, especially at paras 22 to 31, that Lord Hoffmann's view involves giving a wide meaning to "construction" because, as Lord Neuberger says at para 27, when one is implying a word or phrase, one is not construing words in the contract because the words to be implied are *ex hypothesi* and not there to be construed. However, like Lord Neuberger (at para 26) I accept that both (i) construing the words which the parties have used in their contract and (ii) implying terms into the contract, involve determining the scope and meaning of the contract. On that basis it can properly be said that both processes are part of construction of the contract in a broad sense.

77. I agree with Lord Neuberger and Lord Carnwath that the critical point is that in *Belize* the Judicial Committee was not watering down the traditional test of necessity. I adhere to the view I expressed at para 15 of my judgment in the *Mediterranean Salvage & Towage* case (which is quoted by Lord Carnwath at para 62) that in *Belize*, although Lord Hoffmann emphasised that the process of implication was part of the process of construction of the contract, he was not resiling from the often stated proposition that it must be necessary to imply the term and that it is not sufficient that it would be reasonable to do so. Another way of putting the test of necessity is to ask whether it is necessary to do so in order to make the contract work: see the detailed discussion by Lord Wilberforce in *Liverpool City Council v Irwin* [1977] AC 239, 253-254.

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