IN THE SUPREME COURT OF NEW ZEALAND

SC 53/2005
[2007] NZSC 37

	BETWEEN	WHOLESALE DISTRIBUTORS LIMITED Appellant
	AND	GIBBONS HOLDINGS LIMITED Respondent

Hearing: 7 March 2006

Court: Elias CJ, Blanchard, Tipping, Anderson and Thomas JJ

Counsel: G P Curry and B F Peachey for Appellant
W M Wilson QC and M J Radich for Respondent

Judgment: 30 May 2007

JUDGMENT OF THE COURT

A. The appeal is dismissed.

B. The appellant is to pay the respondent costs of $15,000 together with its reasonable disbursements to be fixed if necessary by the Registrar.

REASONS

ELIAS CJ

[1] By deed of assignment of lease dated 3 April 1997 GUS Properties Limited assigned to Wholesale Distributors Limited (WDL) all its "estate right title and interest in the Premises and the Lease all as set out in the First Schedule". The premises comprised a warehouse and land owned by Port Nelson Limited which were leased under a head lease dated 22 April 1982 to Gibbons Holdings Limited. The head lease, following renewals, determines on 31 October 2023. The First Schedule to the deed of assignment of 3 April 1997 set out the legal description of the premises and identified the lease being assigned as the "Deed of Lease dated 10 July 1991" by which Gibbons had subleased the premises to GUS. Under the deed of sublease between Gibbons and GUS the premises were leased for an initial term determining on 30 October 2002, with the parties expressly obliged to enter into a new lease for a term expiring on 31 October 2010. The terms of the 1991 sublease between Gibbons and GUS made it clear that the transaction was structured as two leases to avoid the sublease (which was intended to cover a period which straddled the renewal of the head lease) operating as an assignment of the head lease on expiry of its then current term. The 1997 deed of assignment of lease between GUS and WDL was in printed form, which was adapted by the parties. Against the printed heading "Expiry Date of Lease" contained in the First Schedule were inserted the words "31 October 2002[1] with a New Lease being granted for a term expiring 31 October 2010". By cl 4 of the Second Schedule WDL covenanted with Gibbons in return for Gibbons's consent to the assignment (required under the terms of the 1991 sublease) that:

> from the Date of Assignment and during the remainder of the term of the lease the Assignee will pay the rent provided for in the Lease and keep and perform all the covenants in the Lease.

[2] Gibbons seeks to enforce the covenant to pay rent against WDL for the term expiring on 31 October 2010. WDL maintains that its covenant to pay rent is limited to the term of the lease in existence at the date of the assignment, which expired on

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[1] In fact, the lease expired on 30 October 2002, as the deed of sublease makes clear.

30 October 2002. WDL was successful in the High Court,[2] but on a basis on which it did not rely in the Court of Appeal. In the Court of Appeal, the appeal by Gibbons was allowed.[3] WDL further appeals to this Court on the basis that its obligation to pay rent under cl 4 of the Second Schedule to the deed of assignment is properly construed as an obligation which ended with expiry of the first lease on 30 October 2002.

[3] I have had the advantage of reading in draft the judgments of the other members of the Court. I adopt with gratitude the full statement of the facts set out in the judgment of Tipping J[4] and the clear explanation contained in the judgment of Blanchard J[5] as to why the obligations between Gibbons and GUS were structured as two leases. I am grateful to Thomas J for the analysis that persuades me that the appeal must be dismissed.

[4] The appeal turns on the actual contract between the parties, not any interests which might exist "as a species of property independently of the contract".[6] The period of the contractual obligation to pay rent under cl 4 of the Second Schedule depends on the meaning of "remainder of the term of the lease". The meaning of the phrase is to be objectively assessed in context. The context includes the terms of the 1991 deed of lease referred to in the assignment and the terms of the 1997 deed of assignment between GUS and WDL construed as a whole.

[5] The 1991 deed of sublease between Gibbons and GUS provided that it could not be assigned unless the assignee could be procured by GUS to covenant to observe all the lessee's covenants and agreements, including the payment of rent, "during the residue of the term of years hereby created". The deed of sublease committed the parties to lease the premises until October 2010. In that context the

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2 *Gibbons Holdings Ltd v Wholesale Distributors Ltd* (High Court, Blenheim, CIV 2003-442-19, 5 May 2004, Ellen France J).

3 [2006] 2 NZLR 27 (McGrath and Glazebrook JJ, Chambers J dissenting).

4 At paras [30] – [40] below.

5 At para [16] below.

6 A distinction made in *City of London Corporation v Fell* [1993] QB 589 at p 604 (CA) per Nourse LJ, in a passage approved by the House of Lords ([1994] 1 AC 458 at p 465 per Lord Templeman).

"residue of the term of years" reads naturally as a reference not to the term of years created by the first lease but the term of years covering the obligations of the sublessee: the full period of 20 years provided for on the face of the deed of lease referred to in the 1997 deed of assignment. That interpretation is consistent with cl (u) of the 1991 deed of sublease, which treated the rental to be set for the first two years of the "new" lease as a review of rental under cl (n). On its face, the assigned sublease therefore set up a contractual regime which lasted until 2010. The division of the property interests created into two leases for technical reasons to avoid assignment of the head lease had no material effect on the substance of the underlying obligations, which continued until 2010.

[6] The 1997 deed of assignment obliged WDL to indemnify GUS for any liability GUS might incur arising from default by WDL. GUS has been struck off the register. If it had not been, or if it was restored to the register for the purpose of enforcing the indemnity, WDL would clearly be liable under its obligation to indemnify. It is difficult to understand why the derivative liability would have been assumed by WDL if it were not also taking on the direct obligation to pay the rental. If the "remainder of the term of the lease" is understood not in a technical sense but as a reference to the 21 year contractual regime, no such implausibility arises. Such interpretation is also supported by the acknowledgement in the First Schedule to the deed of assignment alongside the heading "Expiry Date of Lease" that it continued for a second period, until 2010. Such reference is not easy to reconcile with the obligation to pay rent contained in cl 4 of the Second Schedule ending in 2002. I also agree with Thomas J that an interpretation of cl 4 to limit the obligation to pay rent to the term of the first lease period does not make commercial sense. The assignment was part of the sale of the business undertaking of GUS to Wholesale. As Blanchard J notes,[7] other leased premises too were transferred. That the parties intended only an assignment of the lease until 2002 is highly improbable.

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[7] At para [25].

[7] For these reasons, I agree that the reference to "the remainder of the term of the lease" contained in cl 4 is properly understood as a reference to the expiry date of the intended new lease. I do not think it necessary to have regard to the subsequent conduct of the parties in reaching this conclusion, but I accept that how the parties subsequently treated their contractual obligations may be helpful evidence as to the meaning of the contract. I agree with Thomas J that the meaning I prefer based on the terms of the documents and their commercial context is also consistent with the subsequent conduct of WDL in entering into subsequent assignments of the lease for terms extending beyond October 2002. I do not find convincing the suggestion put in argument that these assignments indicate only that WDL was confident of being able to require Gibbons to grant a new lease (through assignment to it of GUS's right to require the new lease to be entered into). I think it highly improbable that WDL thought it had acquired an option without any equivalent obligation to Gibbons in circumstances where it was undoubtedly liable to indemnify GUS for rental in the period of the new lease. All the objective circumstances point to the "remainder of the term of the lease" being a reference to the period to October 2010.

[8] The Court being unanimous, the appeal is dismissed with costs of $15,000 to the respondent, together with its reasonable disbursements to be fixed if necessary by the Registrar.

BLANCHARD J

[9] The interpretation of the contractual documents governing the relationships between the parties to this appeal and the original lessee, GUS Properties Limited, requires an understanding of the architecture of the complicated rules which govern the holding and assignment of leasehold interests in land. I begin with a sketch of those rules.

[10] If A leases premises to B, the relationship between them is one of both privity of estate (B holds that estate from A) and privity of contract (the lease agreement). If B assigns the lease to C, the leasehold estate passes to C who thereafter holds it from A. There is now privity of estate between A and C and consequently there is

no longer privity of estate between A and B. But B remains contractually liable to A for the performance of the lessee's covenants during the remainder of the term of the lease. C's position vis-à-vis A is different. In the absence of any contract whereby C covenants with A to observe the lessee's covenants under the lease, there is no privity of contract between them. But, because privity of estate exists between A and C, there is an obligation on C, while remaining as current lessee, to observe all of the covenants of the lessee which touch and concern the land. The most burdensome of these are normally the obligations to pay the rent and to keep the property in repair. Unless C has entered into a direct contract with A, once C further assigns the lease to D and thus ceases to be the lessee of the premises, C, unlike B, has no liability to A for future breaches of the lessee's obligations.

[11] In *City of London Corporation v Fell*[8] Lord Templeman, with whom the other Law Lords agreed, gave this helpful explanation:

> The effect of common law and statute on a lease is to create rights and obligations which are independent of the parallel rights and obligations of the original human covenantor who and whose heirs may fail or the parallel rights and obligations of a corporate covenantor which may be dissolved. Common law and statute achieve that effect by annexing those rights and obligations so far as they touch and concern the land to the term and to the reversion. Nourse L.J. neatly summarised the position when he said in an impeccable judgment [1993] Q.B. 589, 604:
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> "The contractual obligations which touch and concern the land having become imprinted on the estate, the tenancy is capable of existence as a species of property independently of the contract."
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> …
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> As between landlord and assignee the landlord cannot enforce a covenant against the assignee because the assignee does not covenant. The landlord enforces against the assignee the provisions of a covenant entered into by the original tenant, being provisions which touch and concern the land, because those provisions are annexed by the lease to the term demised by the lease. The assignee is not liable for a breach of covenant committed after the assignee has himself in turn assigned the lease because once he has assigned over he has ceased to be the owner of the term to which the covenants are annexed.
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> Covenants are introduced on the creation of a lease but are not necessary to sustain a lease. Upon an assignment of a lease, the provisions of the covenants by the original tenant continue to attach to the term because those provisions touch and concern the land and not because there continues to

[8] [1994] 1 AC 458 at pp 465 – 466.

> exist an original tenant who has ceased to own any interest in the demised land but remains liable in contract to fulfil the promises he made under covenant. Mr. Arden's submission confuses contract with status, a distinction fundamental to the English system of leasehold tenure of land.

[12] Two matters were not entirely clear until quite recently. The first concerned B's liability to A if an assignee from B (either C or D in the previous example) were without reference to B to agree with A on a variation of the terms of the lease which placed an additional burden on the lessee. Some English cases contained suggestions that B might be liable for the increase in the lessee's burden despite never having agreed to it.[9] In *Friends' Provident Life Office v British Railways Board*[10] the English Court of Appeal put this notion to rest. If what is done amounts to more than a variation and so has to be regarded as a surrender of the lease and a new grant to the current lessee, then B is released from all obligation to A. B is not liable for performance of an assignee under any lease other than the one B signed. But the Court identified only two situations where this surrender and re-grant would occur, namely where the term of the lease was extended beyond the original expiry date and where the boundaries of the premises were extended and more land brought within the lease. In other than these exceptional cases, a variation of the lease covenants between, say, A and D does not altogether release B (or an intermediate assignee, C, who has covenanted with the lessor to observe them), but the variation cannot throw upon B or C any greater burden. So in *Friends' Provident* where there was no rent review provision but an assignee had, in exchange for certain concessions by the lessor, reached agreement with the lessor for an increase in the rent from £12,000 per annum to £35,000 per annum for the rest of the term, the original lessee remained liable for the £12,000 per annum but was not liable for the increase of £23,000 per annum. On the other hand, if the rent had been reduced by variation to, say, £6,000 per annum, that was all the original lessee would have henceforth been liable for in the event of default by the current lessee.

[13] The position is different if the lease provides for a review of rent. Where an increased rent is fixed in accordance with a review provision there is no variation of

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9 See for example *Centrovincial Estates plc v Bulk Storage Ltd* (1983) 46 P & CR 393 at p 396 per Harman J.

10 [1996] 1 All ER 336.

the lease covenants. The original lessee is therefore liable as it would have been if it were still the lessee and had itself faced the rent review provided for in the lease.

[14] The decision of the New Zealand Court of Appeal in *Sina Holdings Ltd v Westpac Banking Corporation*[11] resolved the second doubtful matter. It is entirely consistent with the law as described in *Friends' Provident*. The Court held that where an assignee exercises a right of renewal provided for in the lease, the original lessee (or an intermediate assignee who has covenanted with the lessor) is not liable for the payment of rent or the performance of covenants under the renewed lease. This is because the renewal of a lease, like the two exceptional circumstances described in *Friends' Provident*, constitutes a new grant.

[15] These basic rules are of course subject to the terms and conditions of a particular lease. Those terms and conditions could, for example, provide that after an assignment the original lessee is in fact to be liable for defaults under a renewed lease if the assignee chooses to exercise the right of renewal.

[16] There are some additional complications in cases like the present, involving a sublease, where the sublessor holds under a renewable head lease and the parties to the sublease wish their relationship to continue for a longer period than the term of the current head lease. A sublease purporting to be for the same term or a longer term than the head lease would in fact operate as an assignment of the head lease because the sublessor would have no reversion upon the sublease. This problem is usually overcome by providing, as was done in the present case, for the sublease term to expire a day prior to the term of the head lease; for the sublessor to exercise its right of renewal under the head lease and then, having obtained the new head lease, to grant a new sublease; and for the sublessor to hold the premises in trust for the sublessee during the interregnum. This involves two separate grants by the sublessor to the sublessee, one being the original sublease and the other the new sublease. Those grants are separated by a period of a day. The second sublease does not exist, and cannot exist, until the estate out of which it is granted (the head lease)

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[11] [1996] 1 NZLR 1.

itself comes into existence. This is not to deny that an equitable interest may exist for the sublessee, contingent upon the grant of the new head lease by the head lessor to the head lessee. The point is that the sublessee does not have a present leasehold interest under the second sublease until that sublease has been validly granted.

[17] It is clear that those who drafted the lease between Gibbons Holdings Limited and GUS understood these difficulties. They made quite elaborate arrangements to deal with them.

[18] The deed of lease was for a term of 12 years less one day from the commencement date of 1 November 1990 meaning that the lease would expire at midnight at the end of 30 October 2002. It fixed an annual rent for the first two years of the term and provided in cl (n) for rent reviews every two years at the option of the lessor. The lease document, although not a printed form, has the appearance of being a law firm precedent adapted, not entirely happily in some respects, to the particular circumstances of the sublease. For instance, it contains a right of renewal clause referring to "a further term of the numbers of years specified in the schedule hereto" but no further term is actually specified in the schedule.

[19] In cl (s) there is an acknowledgement that the lease has been entered into on the basis that the lessor will exercise the rights of renewal in the head lease. In cl (t) it is provided that the lessor will "for the day after the expiration of the term hereof", that is 31 October 2002, hold the premises in trust for the lessee (in exchange for payment of one day's rent). Clause (u) states the "intention of the parties" that two days following the expiry of "the lease hereby granted", "the parties shall enter into a new lease of the premises for a period expiring on the 31st day of October 2010". The rental under that new lease for the first two years "shall be fixed in accordance with cl (n) of this lease as if it was a right of review of rental". This explains what is at first a puzzling feature, namely the inclusion of 1 November 2002 in the "review of renewal [sic]" dates in the schedule. It is clear from cl (u) that this is a review under the new lease, not under the expired lease. In cl (u) the date of 2 November 2002 has been inserted in handwriting but it seems certain that this was an error and that the new lease was intended to run from 1 November. There would otherwise be

a gap of another day during which no rental would be payable. The reference to two days is seemingly to the calendar days: 1 November is two days after 30 October even though separated from 30 October by only 24 hours plus two seconds.

[20] The deed of lease prohibited any assignment without the prior consent of the lessor but that consent was not to be arbitrarily or unreasonably withheld. It was provided in cl 14(a) that in the event of the lessor consenting to an assignment the lessee would procure the proposed assignee to enter into a deed of covenant with the lessor, to be prepared by the lessor's solicitor, that the assignee would:

> pay the rent and perform and observe … the covenants and agreements on the part of the Lessee herein contained or implied *during the residue of the term of years hereby created* … (emphasis added)

It is the phrase that I have emphasised which is at the base of the interpretive problem.

[21] The "term of years hereby created" in cl 14(a) might be thought, like the "lease hereby granted" in cl (u), to mean the term of 12 years less one day expiring on 30 October 2002. There is no reference in cl 14(a) to the "new lease" provided for later in cl (u).[12] It would on this literal approach follow that when GUS and Wholesale Distributors Limited (WDL) sought the consent of Gibbons to the assignment of the sublease from GUS to WDL in 1997, Gibbons was not entitled to seek from WDL any covenant relating to performance required after 30 October 2002.

[22] The distinction which the parties were making between the first sublease and the intended second sublease might on this approach also be thought to be apparent in cl (p) which provided for a review of the term of "this lease" on 30 October 2002 – the last day of the term – so as to incorporate in "this lease" the terms of leases for commercial premises in Nelson at that date. Clause (u) required that the new lease would be on the same terms and conditions contained "in this present lease" with the

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[12] There is mention later in cl 14(a), in dealing with covenants by shareholders in an assignee which is a private company, of renewal or extension of the lease or a renewed lease. However that appears to be simply another consequence of the use of a precedent document which has not been fully modified to circumstances in which there was no renewal right. Plainly there could never be an extension or renewal of this sublease.

logical exception of the clauses dealing with the grant of that new sublease, and that requirement was mirrored in the form of consent given to the sublease by the head lessor, Port Nelson Limited. Read against cl (u), the purpose of cl (p) was obviously to ensure that new terms picking up developments in commercial leasing practices would appear in the new sublease.

[23] The deed of assignment entered into some six years later, to which GUS, WDL (entering the scene for the first time), Gibbons and Port Nelson were parties, was presumably intended to be consistent with the deed of lease. GUS assigned to WDL all its interest in the premises and the lease "as set out in the First Schedule" and WDL covenanted with GUS to pay the rent and observe the covenants conditions and provisions "in the Lease". The covenants in the lease of course include the covenant to take up the new lease. There is also a covenant by WDL with Gibbons that WDL will pay the rent and keep and perform "all the covenants in the Lease". However, this covenant, unlike that between WDL and GUS which appears earlier on the same page of the deed, is expressed to apply only "during the remainder of the term of the lease". In the First Schedule there is a description of the premises and an identification of the lease as "Deed of Lease dated 10 July 1991". There is also in the deed of assignment an acknowledgement by GUS, WDL and Gibbons that the current term under the lease is to expire "on the date set out in the First Schedule". In the Schedule alongside the heading "Expiry Date of Lease" is found "31 October 2002[13] with a New Lease being granted for a term expiring 31 October 2010".

[24] As with the provisions of the deed of lease discussed above, on a literal reading of these provisions of the assignment it might appear that WDL covenanted with GUS to undertake all the burdens of the existing sublease, including the obligation to take up the new sublease, but, in contrast, vis-à-vis Gibbons did not undertake to do more than to observe the covenants in the existing sublease during the time that sublease continued to exist, with no obligation relating to anything after its expiry. I was at first disposed to think that the document must be read in this

[13] This is a misstatement as the expiry date was actually 30 October.

way. But, having had the benefit of considering the draft judgment of Thomas J, I have changed my view.

[25] I am now persuaded that it is entirely unlikely that the parties would have intended such a strange outcome. The term of the lease to which WDL's covenant with Gibbons referred was, I consider, both the residue of the existing term and the new term which was to be created out of the head lease, to expire in 2010. The assignment of GUS's interest to WDL encompassed both the legal interest in the existing lease and the equitable interest contingent on the creation of the new head lease. There is, it seems to me, no answer to the question "Why would WDL accept a liability to indemnify GUS against Gibbons's claim for failure by GUS or its assignee to take up the new sublease but decline to accept direct liability to Gibbons for the failure to do so?"[14] The conclusion that this distinction (which would produce no practical difference in result for WDL) could not have been intended is reinforced by appreciation of the broader transaction with GUS, in the course of which the leases of several buildings, including the one in issue, were being transferred as a parcel.

[26] What it seems to me has occurred is that the parties have simply tripped up in the terminology they have used to address a necessarily complicated legal situation, the "architecture" of which I have earlier endeavoured to explain. They did in fact try to make it clear that they were also referring to the new sublease in the covenants in question by somewhat clumsily describing it in the portion of the Schedule headed "Expiry Date of Lease". The most sensible explanation for the inclusion of the words under that heading "with a New Lease being granted for a term expiring 31 October 2010", in the context of the commercial transaction being undertaken and in the context of the documentation as a whole, is that it was the expiry date of the new lease which was the expiry date to which all obligations were related (contingent of course upon the creation of the new head lease in accordance with the covenants relating to that lease).

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[14] As Lord Diplock observed in *Antaios Cia Naviera SA v Salen Rederierna AB* [1985] AC 191 at p 201, "[i]f detailed semantic and syntactical analysis of words in a commercial contract is going to lead to a conclusion that flouts business commonsense, it must be made to yield to business commonsense".

Subsequent conduct

[27] I reserve my position, as I did in *Attorney-General v Dreux Holdings Ltd*,[15] on the question of whether the subsequent actions of the parties can be taken into account in the interpretation of their contract. I have seen no convincing argument against such use and there is force in the argument in its favour. I do not read Lord Hoffmann's remarks in *Investors Compensation Scheme Ltd v West Bromwich Building Society*[16] as being directed to this point. If His Lordship had intended to rule out use of subsequent conduct it would have been easy for him to say so.

[28] However, in this case, the subsequent actions of WDL in relation to the sub-sublease to TNL Group Limited could be of no assistance in the interpretation of WDL's covenant with Gibbons. WDL could fulfil the obligation it incurred to TNL beyond the expiry date of the current sublease because it was entitled to call for the new sublease by virtue of the assignment from GUS. It is unlikely that the minds of the executives who made the arrangements with TNL were addressed to the question of whether WDL was obliged to Gibbons to take up that new sublease.

Result

[29] For these reasons I would dismiss the appeal with costs to the respondent.

TIPPING J

Introduction

[30] The appellant, Wholesale Distributors Limited (WDL), became, by assignment, the sublessee under a deed of sublease in respect of which the respondent, Gibbons Holdings Limited, was and remains the sublessor/head lessee. This deed, which was entered into between Gibbons and the original sublessee, GUS Properties Limited, was structured so as to create two terms; the first of 12 years less

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15 (1997) 7 TCLR 617 (CA).
16 [1998] 1 WLR 896 at p 912.

one day, and the second of eight years. There was a gap of two days between the two terms on a basis I will mention in a moment. This structure was adopted to avoid the effect a single 20-year term would have had on the head lease. A term of that length, which would have extended beyond the existing term of the head lease, would have operated in law as an assignment of the head lease. The parties wished to avoid that consequence. They therefore structured the sublease so as to create an initial term of 12 years less one day, which expired one day before the expiry of the current term of the head lease. This initial term was to be followed by a second term of eight years. The deed of sublease created the initial term of 12 years less one day, and obliged GUS, as original sublessee, to enter into a further lease for a term of eight years, that term to commence two days after the expiry of the initial term. Consistently with the deed, I will call this further lease "the new lease".

[31] The issue with which the appeal is concerned is whether WDL, as assignee of the sublease, is obliged to pay the rent under the new lease. That will be so if WDL, which took the assignment during the currency of the first term, became liable to enter into the new lease. GUS, as original sublessee, was clearly so liable but the courts below have differed as to whether that liability applied also to WDL as its assignee.

[32] In the High Court,[17] Ellen France J held that the obligation to enter into the new lease was only an option which WDL was not obliged to take up. This construction of the relevant clause in the deed of sublease was contrary to its plain terms. WDL did not seek to uphold it when responding to Gibbons' appeal from Ellen France J's conclusion. In the Court of Appeal WDL presented different arguments in support of its contention that it was not liable to enter into the new lease and thus to pay the rent due thereunder. The Court of Appeal was not unanimous in its conclusion.[18] The majority (McGrath and Glazebrook JJ) held that WDL was liable for the rent due under the new lease. The minority (Chambers J) held that it was not.

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17 *Gibbons Holdings Ltd v Wholesale Distributors Ltd* (High Court, Blenheim, CIV 2003-442-19, 5 May 2004).

18 *Gibbons Holdings Ltd v Wholesale Distributors Ltd* [2006] 2 NZLR 27.

The contractual documents

[33] The deed of sublease is dated 10 July 1991. The parties called it simply a deed of lease and I will do the same. The deed created a term of 12 years less one day from 1 November 1990. The term therefore expired at the end of 30 October 2002. Clause 14(a) gave the lessee a right of assignment, subject to the written consent of the lessor, which was not to be arbitrarily or unreasonably withheld. The clause also provided that, as a condition of the right to assign, the lessee was to procure the proposed assignee to enter into a deed of covenant with the lessor to the effect that the assignee would duly and punctually pay the rent and observe all the lessee's covenants. The required direct covenant was expressly said to cover payment of rent and observance of the lessee's covenants "during the residue of the term of years hereby created or during such lesser term which [the assignee] shall so acquire or should be about to acquire".

[34] Clause (u) of the mutual covenants between the parties required the lessee to enter into a new lease following the expiry of the term created by the deed. It reads:

> (u) NEW LEASE: The parties hereto acknowledge that the term of the head lease expires on the 31st day of October 2002 and contains a right of renewal for a further period of twenty-one (21) years. It is the intention of the parties that two (2) days following the expiry of the lease hereby granted the parties shall enter into a new lease of the premises for a period expiring on the 31st day of October 2010 but it is not the intention of the parties that the granting of such new lease shall operate as an assignment of the head lease. In pursuance of the foregoing arrangements the Lessor shall grant to the Lessee and the Lessee agrees to take on lease a new lease of the premises for a term commencing on the 2nd day of November 2002 and expiring on the 31st day of October 2010 (hereinafter called "the New Lease"). The rental payable under the New Lease for the period expiring on the 31st day of October 2004 shall be fixed in accordance with clause (n) of this lease as if it was a review of rental with such modifications as may be necessary to give effect thereto. The rental payable for the period of two (2) years commencing 1 November 2004 and the rental payable for the period of two (2) years commencing 1 November 2006 shall be similarly determined in accordance with clause (n) of this lease. The New Lease to be entered into by the parties hereto pursuant to this subclause shall be otherwise on the same terms and conditions contained in this present lease except that clauses (s), (t) and (u) hereof shall be deleted.

[35] Clause (u) constitutes an agreement to lease; it is not itself a lease. The clause contemplates the execution of a formal lease creating a further term of

eight years. The term contemplated is distinct from and is in no way a renewal or extension of the term actually created by the deed. While cl (u) creates a contractual obligation, it does not in itself amount to any grant of a leasehold estate in the land.

[36] I move now to consider the relevant terms of the deed of assignment of the lessee's interest to WDL. There are intermediate parties or changes of name on each side, but they are of no present relevance. It is convenient, therefore, to treat the assignment as being from GUS to WDL. Both Gibbons and the head lessor, Port Nelson Limited, consented to the assignment. The deed of assignment is dated 3 April 1997. Clause 1 constitutes the formal assignment to WDL by GUS of all the lessee's estate, right, title and interest in the premises and the lease as set out in the First Schedule. That Schedule sets out the legal description of the premises and describes the lease as "Deed of Lease dated 10 July 1991". Clause 7 of the assignment states that the landlord (Gibbons) consents to the assignment but "without prejudice to the Landlord's rights powers and remedies under the Lease". This clause simply preserves the landlord's rights, powers and remedies under the lease. It does not expand them or assist in determining what they are. It has no impact on the issue to be resolved.

[37] The First Schedule to the assignment contains a standard heading "Expiry Date of Lease". Inserted beside that heading are the words "31 October 2002 with a New Lease being granted for a term expiring 31 October 2010". These words indicate that the lease with which the assignment was concerned was to expire on 31 October 2002;[19] but clearly the parties envisaged a new lease being granted for the further term mentioned. While the language does not amount to any express covenant or agreement by WDL to enter into the new lease, the reference to the new lease in the deed of assignment must have been for a contractually relevant purpose. I shall return to this point.

[38] The Second Schedule to the assignment contains conventional covenants between the assignor and assignee of the leasehold interest. Clause 1 constitutes a covenant by the assignee in favour of the assignor that it, the assignee, will pay the

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[19] Actually it was 30 October 2002 as stipulated in the deed of lease. This inaccuracy has no relevance to the point at issue.

rent and observe all the lessee's covenants. Clause 2 constitutes a covenant by the assignee indemnifying the assignor from the consequences of any default by the assignee in the payment of rent or in the observance or performance of the covenants, conditions and provisions contained in the lease.

[39] Clause 4 of the Second Schedule is the only covenant as between assignee and lessor (that is, as between WDL and Gibbons). It is upon the terms of cl 4 that the issue between the parties ultimately turns. Clause 4 must of course be read in its full context and other provisions in the two deeds are capable of being relevant to its interpretation. Clause 4 is the direct covenant between assignee and lessor envisaged by cl 14(a) of the deed of lease. It reads:

> The Assignee [WDL] covenants with the Landlord [Gibbons] that from the Date of Assignment and during the remainder of the term of the lease the Assignee will pay the rent provided for in the Lease and keep and perform all the covenants in the Lease.

[40] Mr Wilson QC for Gibbons accepted that the liability his client asserts against WDL can ultimately be found only in cl 4. He contended, however, that the majority in the Court of Appeal was correct in construing the clause as creating the liability asserted. This is therefore a convenient point at which to examine the different approaches taken in the Court of Appeal.

Court of Appeal judgments

[41] McGrath and Glazebrook JJ took the view that the definition of the word "lease" in the First Schedule to the deed of assignment, being "Deed of Lease dated 10 July 1991", meant that the term stipulated in the 1991 deed, in the context of a document providing for obligations enuring for a 20-year period, was a term for the whole 20-year period.[20] This construction was reinforced, in their view, by the reference to the "new lease" in the words defining the expiry date of the lease. Their Honours also regarded WDL's covenant in cl 1 of the Second Schedule to the deed of assignment as supporting their view that WDL was bound to take the new

[20] At para [11].

lease.[21] That covenant, as noted above, was given by WDL in favour of its assignor, GUS, and provided that WDL would pay the rent and observe all the covenants contained in the lease.

[42] McGrath and Glazebrook JJ read this reference to "the lease" as meaning, in its context, all the covenants and agreements in the deed of July 1991. Even if that view is right, it does not necessarily mean that WDL had undertaken the same obligations to Gibbons as it had to GUS. Whether it did so depends on the true construction of the words of the direct covenant between WDL and Gibbons. McGrath and Glazebrook JJ also pointed out that WDL's indemnity to GUS meant that if WDL was not bound to take the new lease, as GUS undoubtedly was, Gibbons could sue GUS, which could pass on the liability to WDL under the indemnity.[22]

[43] Their Honours then made reference to the fact that the deed of assignment was in a standard form and had been amended in an attempt to reflect the nature of the particular transaction, which they saw as being "[i]n substance … in the nature of a lease for a 20 year term which took the form of two leases for fixed periods with a holding on trust for one day interposed".[23]

[44] After recording a submission made for WDL, their Honours concluded:[24]

> That is true, but seen in this context, the changes made to the standard form are entirely consistent with an intention that the obligations assumed by the assignee to the landlord included occupation of the premises for the remainder of the full term of 20 years stipulated in the 1991 deed. The meaning of cl 4 which we favour reflects this reality, as well as the commercial purpose of the provision in the 1991 deed that gave rise to the direct covenant in cl 4. That meaning is in our view clear on the wording of the 1997 deed [the deed of assignment] and it is supported by the context. We adopt it.

[45] Chambers J saw the difficulty in Gibbons' argument as being that under cl 4 WDL's promise to Gibbons was to enure only "during the remainder of the term of the lease". That, in context, could mean only one thing. There was, at the date of the assignment, only one term in existence, namely the term expiring on 30 October

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21 At paras [14] – [15].
22 At para [17].
23 At para [19].
24 At para [19].

2002. The remainder of that term must itself, therefore, have expired on that date. In the Judge's view, GUS had promised to take the new lease but WDL had not. After discussing his essential point in further detail, Chambers J expressed the view that the majority's reasoning failed to deal with the arrangement Gibbons and GUS "actually agreed".[25]

Submissions

[46] The arguments in this Court largely followed the points made in the judgments below. Mr Curry urged us to follow the line taken by Chambers J and Mr Wilson did the same in relation to the reasoning of McGrath and Glazebrook JJ. Mr Wilson raised an additional argument based on subsequent conduct. I will deal with it separately. It is not necessary to traverse, point by point, the submissions made to us both orally and in writing. They are to some extent already foreshadowed and I will address them as necessary in the following discussion.

Discussion

[47] The starting point is cl 4 in the Second Schedule to the deed of assignment. As already noted, it is the only covenant entered into by WDL in favour of Gibbons. It is the only promise upon which Gibbons can sue. It is common ground that the privity of estate which once existed between WDL and Gibbons does not create any liability in WDL helpful to Gibbons on the present issue. By cl 4 WDL promised Gibbons that it would pay the rent provided for in the lease and keep and perform all the covenants in the lease. Crucially this promise was to operate, as Chambers J emphasised, "during the remainder of the term of the lease".

[48] While there is considerable semantic force in the conclusion to which Chambers J came, I do not consider it reflects what the parties were seeking to achieve when they entered into the deed of assignment. That transaction was entered into following the sale by GUS of all its business interests associated with the lease it was assigning. It was obliged to enter into the new lease but cannot logically have

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[25] At para [63].

meant to retain that obligation as the primary obligee. The assignment rather clumsily defined the expiry date of the lease being assigned as "31 October 2002 with a new lease being granted for a term expiring 31 October 2010". The purpose of the reference here to the new lease can only have been to treat it as part of the "lease" being assigned. While the only "term" technically in existence was the term expiring on 30 October 2002, the parties must have regarded the intended term of the new lease as falling within the compass of the expression "remainder of the term of the lease" in cl 4 of the deed of assignment. The commercial context supports this reading and so does the fact that WDL agreed to indemnify GUS for any residual liability resting on it to enter into the new lease. The fact that WDL was prepared to indemnify GUS in this respect makes it highly probable that it was also willing to become directly liable to Gibbons. There is no basis for concluding that for some reason WDL was willing to be liable through its indemnity but not directly to Gibbons.

[49] I regard this case as falling close to the borderline between legitimate interpretation and rectification, which was not sought as an alternative. The literal language of cl 4 of the assignment leads to the conclusion to which Chambers J came. I am, however, satisfied, for the reasons given above, that the expression "remainder of the term of the lease" is capable of bearing the meaning suggested both by the commercial context and by the inclusion of the reference to the new lease in the definition of expiry date in the First Schedule to the deed of assignment. That meaning is distinctly more probable on an objective assessment of the parties' intentions. As the words which the parties have used can bear that meaning, their contract must be interpreted accordingly.

Subsequent conduct (generally)

[50] Two questions arise on this aspect of the case. The first is whether the court should be able to consider the subsequent conduct of the parties as an aid to the interpretation of their contract. The second is whether the subsequent conduct relied on by Gibbons in the present case has any material bearing on the true meaning of cl 4. Although I have already held that the meaning asserted by Gibbons is the

correct one, the issue of subsequent conduct has general importance and the point is not wholly redundant in this case. That is because it is desirable for there to be clarity as to whether subsequent conduct can be examined as an aid to interpretation, if only for confirmatory or supporting purposes.

[51] The point of principle must be addressed first. Much has been written about whether evidence of post-contract conduct should be admissible on an interpretation issue. Traditionally it has been regarded as admissible only for rectification, formation and estoppel purposes, and not to assist interpretation. There is, at the outset, some conceptual difficulty in adopting different evidential rules for those purposes on the one hand as against interpretation purposes on the other.

[52] As a matter of principle, the court should not deprive itself of any material which may be helpful in ascertaining the parties' jointly intended meaning, unless there are sufficiently strong policy reasons for the court to limit itself in that way. I say that on the basis that any form of material extrinsic to the document should be admissible only if capable of shedding light on the meaning intended by both parties. Extrinsic material which bears only on the meaning intended or understood by one party should be excluded. The need for the extrinsic material to shed light on the shared intention of the parties applies to both pre-contract and post-contract evidence. Provided this point is kept firmly in mind, I consider the advantages of admitting evidence of post-contract conduct outweigh the disadvantages. The latter comprise primarily the potential for ex post facto subversion of earlier jointly shared intentions and the lengthening of interpretation disputes by encouraging the parties to produce evidence which is often only tenuously relevant at best.

[53] For good policy reasons the common law has consistently adhered to what is usually called an objective approach to contract interpretation. An objective inference from conduct in which the parties are mutually involved after they have contracted does not significantly depart from the conventional approach. I will call conduct in which both parties are involved, either actively or passively, mutual or shared conduct. Inviting inferences from the conduct of one party, in which the other party is not involved, would make a significant inroad into the need to ascertain objectively the shared intention of the parties as to their meaning. The

words they have used, construed in the light of all the relevant and objective circumstances in which the parties have used them, must prima facie be the best guide to their meaning. But, if some mutual or shared post-contract conduct of the parties is objectively capable of shedding light on the meaning they themselves placed on the words in dispute, I consider more is to be gained than lost by allowing the court to take it into account.

[54] I do not propose to embark on any detailed review of the substantial literature, both judicial and academic, which exists on this topic. In the end the court must decide, on the overall balance of competing interests, whether, and if so, to what extent, evidence of post-contract conduct is to be admissible in aid of interpreting written contracts. Some of the more influential recent materials are *Montreal Trust Co of Canada v Birmingham Lodge Ltd*;[26] *Attorney-General v Dreux Holdings Ltd*;[27] "The Intractable Problem of The Interpretation of Legal Texts";[28] "My Kingdom for a Horse: The Meaning of Words";[29] and "In Defence of a Role for Subsequent Conduct in Contract Interpretation".[30]

[55] I also point out that art 2-208 of the Uniform Commercial Code and art 202(4) of the Restatement of Contract Law (2nd) in the United States allow consideration to be given to specified subsequent conduct in which both parties are involved. As Blanchard J (writing as well for Richardson P and Keith J) suggested in *Dreux*,[31] taking account of subsequent conduct would also accord with general international trade practice. In the same case, Thomas J concluded that, as a matter of principle, the courts should be able to have regard to the subsequent conduct of the parties for the purpose of elucidating the meaning the parties intended their contract to have at the time they entered into it.[32] In short, as I have already indicated, I find the case in favour of admitting post-contract conduct for that purpose distinctly more persuasive than the case for not doing so.

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26 (1995) 125 DLR (4th) 193 (Ont CA).
27 (1997) 7 TCLR 617 (CA).
28 Lord Steyn, (2003) 25 Syd LR 5 (the John Lehane Memorial Lecture for 2002).
29 Lord Nicholls, (2005) 121 LQR 577 (lecture given to the Chancery Bar Association on 16 March 2005).
30 Professor D W McLachlan, (2006) 12 NZBLQ 30.
31 At p 627.
32 At p 640.

[56] Questions of interpretation concern the objective meaning of the parties' words rather than their subjective intentions. The law generally presumes that the objective meaning of their words reflects those intentions. The parties are not allowed, on an interpretation issue, to tell the court what they intended the words to mean or what they thought the words meant. Interpretation difficulties arise when the parties have used words of uncertain meaning and they assert competing meanings for those words. In this situation the traditional view has been that the court must ascertain what meaning the words bear, taking into account the document as a whole and all relevant circumstances that would have been apparent to the parties at the time they contracted. The traditional phrase "matrix of facts" means all the objectively relevant surrounding circumstances.

[57] The phrase was first used by Lord Wilberforce in *Prenn v Simmonds*, where His Lordship said "[t]he time has long passed when agreements, even those under seal, were isolated from the matrix of facts in which they were set".[33] His Lordship then made reference to "mutually known facts" and to the phrase used by Cardozo J in the New York Court of Appeals in *Utica City National Bank v Gunn*, "the genesis and aim of the transaction".[34] Cardozo J also said that surrounding circumstances might "stamp upon a contract a popular or looser meaning" than what Lord Wilberforce later called the strict legal meaning, an expression which he was equating with purely linguistic literalism. His Lordship emphasised that ultimately the search was for the common intention of the parties as at the time they contracted and as objectively manifested. It does not follow from this classic exposition that objective manifestation cannot properly come from the post-contract conduct of the parties. Surrounding circumstances do not have to precede the contract; indeed the very word "surrounding" implies that the circumstances may fall on the other side of this temporal line.

[58] The surrounding circumstances have conventionally been examined as at the date when the parties entered into their contract. On that basis the post-contract conduct of the parties is obviously not within the scope of the court's inquiry. This is one reason why evidence of post-contract conduct has traditionally been excluded

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33 [1971] 1 WLR 1381 at pp 1383 – 1384.
34 (1918) 118 NE 607 at p 608.

in interpretation disputes. It cannot have been known to the parties when they put pen to paper and hence could not bear on their meaning at that time.

[59] This temporal focus was reinforced by Lord Reid's influential speech in *Whitworth Street Estates (Manchester) Ltd v James Miller & Partners Ltd*.[35] His Lordship said that admitting post-contract evidence "might have the result that a contract meant one thing the day it was signed, but by reason of subsequent events meant something different a month or a year later".[36] The subsequent course of English law was shackled by this rare case of even Homer nodding.[37] Evidence of subsequent conduct does not invite a subsequent meaning. It is directed to the original meaning; that is, the meaning of the contract when it was signed. It is a distraction to suggest that post-contract evidence is capable of changing the contract date meaning, when its sole purpose is to elucidate that meaning.

[60] For these reasons, it is now appropriate to allow the traditional date of assessment to come forward to the date of hearing so as to enable the court to take into account how the parties have behaved in the performance of their contractual obligations and in the administration of their contract generally. The focus must still be on objective conduct rather than expressions of subjective intention or understanding. But if the parties have together conducted themselves in the performance of their contract in a way that is relevant to the meaning of the disputed provision, the court should be able to take that into account.

[61] There are connotations of estoppel involved in this approach, albeit the issue is not one of estoppel in any strict sense. Estoppel by convention or otherwise is a separate issue. It can fairly be said that when the issue is examined as at the date of the court hearing, the shared conduct of the parties in the performance of their contract is a part of the surrounding circumstances. The only difference is that post-contract conduct cannot have informed the meaning of the parties' words at the time they contracted, but it can retrospectively have a legitimate bearing on that meaning. There is insufficient reason in principle to insist on a date of contract

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35 [1970] AC 583.

36 At p 603.

37 See Horace, *Ars Poetica (The Art of Poetry)*, line 359: "et idem indignor, quandoque bonus dormitat Homerus" (I am also disappointed when sometimes even great Homer nods).

focus, albeit the ultimate criterion for ascertaining contractual intention remains the objective meaning of the words of the contract at that date. The horizon has expanded but the subject of the search remains the same.

[62] I conclude this topic with the observation that properly focused and limited evidence of post-contract conduct will often be capable of shedding more light[38] on contractual meaning than a lot of the pre-contractual material which is said to bear on that meaning. Post-contract evidence that logically indicates that at the time they contracted the parties attached a particular meaning to the words in dispute can be good evidence that a later attempt by one party to place a different meaning on those words is unpersuasive.

[63] Even if the meaning suggested by the post-contract conduct is not the most immediately obvious objective meaning, the parties' shared conduct will be helpful in identifying what they themselves intended the words to mean. That, after all, must be the ultimate determinant. If the court can be confident from their subsequent conduct what both parties intended their words to mean, and the words are capable of bearing that meaning, it would be inappropriate to presume that they meant something else.[39]

Subsequent conduct (this case)

[64] Gibbons submits that there are four pieces of admissible extrinsic evidence supporting its contention that WDL is bound to take the new lease and pay the rent thereunder. The first is evidence from Mr Muollo of Gibbons and Mr Cottam of GUS that they each believed WDL was bound until 2010. This evidence amounts to no more than the subjective state of mind of each witness. There is no element of mutuality involved, let alone a mutuality involving WDL. The evidence might have been helpful on a rectification suit between Gibbons and GUS but cannot

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38 Even if that light is simply confirmation of a meaning the court would otherwise be inclined to ascribe to the words in issue, as is often the case.

39 The presumption that the parties mean what they appear to have said will, of course, continue to apply in the many cases where subsequent conduct sheds no light on meaning. The presumptive meaning is, in any event, likely to coincide with the meaning which the parties jointly intended.

legitimately bear on the position of WDL and its obligations under cl 4 of the deed of assignment. It is inadmissible on that point.

[65] The second piece of evidence comprises internal WDL documents, created some three years after the assignment, from which it might be inferred that the authors thought WDL was bound to 2010. These documents do not demonstrate any shared intention as to the meaning of cl 4; nor do they illuminate how the matter was viewed by the different people involved in 1997. They also suggest that their authors had no grasp of the way the transaction had been deliberately framed as involving three distinct stages, and only a fragile grasp of the difference between an obligation and an option. This evidence is not admissible. Even if it were, it does not assist the crucial interpretation issue.

[66] The third piece of evidence, which is admissible but not persuasive, derives from the fact that, with Gibbons' consent, WDL subleased part of the premises to TNL Group Limited by deed dated 7 April 1999. This sublease was for an initial term with two rights of renewal, potentially extending to 1 November 2008. This total potential term exceeded the initial term of the lease between WDL and Gibbons. This fact is said by Gibbons to demonstrate that WDL had bound itself to take the new lease because otherwise it would have had no title to honour its obligations to TNL as sublessee from 30 October 2002 onwards. The sublease between WDL and TNL had an initial term of three years, eight months and 29 days from 1 February 1999. The intended expiry date could not have been more precisely calculated as being 29 October 2002. This was one day before the expiry date of the initial term of the lease between Gibbons and WDL.

[67] This structure was obviously deliberate and showed the parties had full awareness of the structure above them and the reasons for it. The First Schedule to the deed between WDL and TNL notes that the final expiry date of the sublease "if renewed" was 1 November 2008. This, of course, was a reference to the fact that the deed gave TNL two rights of renewal for further terms of three years each. The deed between WDL and TNL incorporated the terms of what that document called the head lease, that is, the lease between Gibbons and WDL, with certain specified exceptions. Those exceptions included mutual covenant (u), which provided for the

new lease. The significance of this is that as between WDL and TNL there was no covenant that WDL would take up the new lease. Indeed, although the exclusion of covenant (u) was understandably designed to avoid any suggestion that TNL was obliged to WDL in respect of any new lease, the parties obviously did not think it appropriate to create any liability in WDL to take up the new lease either. WDL's obligations under cl 4.2 of the sublease were limited in duration to the term of the head lease, raising essentially the same limitation point as applied in cl 4 of the GUS/WDL assignment.

[68] WDL's conduct in entering into the sublease to TNL, albeit with the consent of Gibbons, is not conduct of such mutuality as to be legally capable of elucidating the meaning of cl 4 in the assignment. Even if the lack of mutuality aspect were put aside, there is nothing in WDL's conduct which suggests that WDL considered itself obliged to take the new lease, as opposed to having an option to do so. That view would have been erroneous but clearly tenable in view of the High Court's conclusion.

[69] The fourth and final aspect of the evidence of subsequent conduct relied on by Gibbons is the assignment which WDL made of its interest in the lease to Infogate Nominees Limited. This transaction was recorded in a deed dated 29 November 2000 to which Gibbons consented. I can find nothing helpful to Gibbons in this document, which raises essentially the same interpretation issue as that in the assignment directly in issue. Hence none of the admissible post-contract evidence has any influence on the true meaning of cl 4 of the deed of assignment dated 3 April 1997.

[70] For the reasons given earlier, I would dismiss the appeal. I agree with the orders for costs set out above.

ANDERSON J

[71] I also would dismiss this appeal with costs to the respondent.

[72] Considering the deed of assignment as a whole and in its commercial context I think it plain that the parties intended that WDL would discharge the obligations of the lessee in respect of the assigned estate, right, title and interest, which included the interest under the agreement to lease. The use of standard forms to meet an unusual arrangement led to literal awkwardness but the intended commercial arrangement is clear.

[73] As to whether the courts, for the purposes of interpretation, should have regard to conduct occurring after a contract has been made, I think the issue is of limited practical significance. It does not relate to a situation where rectification is apt; nor where the inquiry is whether a contract exists and if so, what its terms are; nor whether the language used has technical or dialectical meanings. A party seeking to rely on post-contract conduct would have to show conduct on the part of all the contracting parties in order to demonstrate a shared and not merely an individually held meaning. For these reasons I would not expect there to be any significant increase in the amount of litigation about the meanings of contracts. Indeed, the possibility of recourse to such evidence of actual mutual understanding of contractual terms might forestall litigation about seemingly ambiguous terms.

[74] In respect of documents intended for distribution beyond their authors, it is obviously desirable that they should be interpreted according to the ordinary meanings of the language in which they are expressed. Even in respect of transactions limited to the parties, such as contracts, the assumption that the parties understood their words to mean what others would reasonably understand them to mean is a sensible starting point. But where the inquiry is into the meaning of terms which contracting parties have agreed to, and where the conduct of the parties logically suggests that they had a mutual understanding of the terms which is inconsistent with ordinary linguistic use, the courts should take into account all relevant and cogent evidence of that conduct, including post-contract conduct. To regulate the rights and obligations of the parties by reference to something other than the rights and obligations they in fact mutually settled upon is to pay more regard to linguistic form than substantive rights and obligations. Furthermore, in cases of difficult or doubtful construction, post-contract conduct may provide a cross check or reassurance that the meaning a court is leaning towards was that intended by the

parties. Notwithstanding, I do not find it necessary to have recourse to post-contract evidence in this case, the intention of the parties being ascertainable from the terms of the deed, considered in its commercial and documentary context. Had I been in doubt as to their intention I would not have been assisted by the evidence of post-contract conduct in this particular case.

[75] As a generalisation, I think there should be caution about imputing a common intention different from what would naturally be inferred from the language of reasonably common form conveyancing or commercial documents. That is because of the likelihood of subsequent reliance by later assignees or sublessees, unaware of subjective or contextual indications of a common intention.

[76] Idiosyncratic users of language should themselves be cautious. They might, through negligence or principles of estoppel, find themselves with different rights or obligations between the contracting parties on the one hand and subsequent parties on the other, founded on the same terms of the contract.

THOMAS J

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A question of interpretation

[77] By Deed of Lease dated 10 July 1991, the appellant, Gibbons Holdings Limited, subleased the premises in issue in this case to GUS Properties Limited.

GUS assigned its interest in the Deed of Lease to the respondent, Wholesale Distributors Limited (WDL), in a Deed of Assignment dated 3 April 1997. The question in issue in this appeal is whether, as a matter of interpretation of that Deed, WDL is liable to Gibbons to pay the rent and perform the other covenants in the Deed of Lease until 31 October 2010. As will become apparent, this question depends on whether the interest assigned expired on that date or at the earlier date of 30 October 2002.

[78] The issue is not without difficulty as a "legal" analysis of the leasehold arrangements would suggest an outcome at odds with the apparent common intention of the parties. WDL relies upon this legal analysis. Stressing the imperative of an objective approach to the interpretation of the Deed of Assignment, it argues that the parties' intention can be presumed from this analysis. For its part, Gibbons contends that, irrespective of this analysis, the actual intention of the parties is clear and the Deed must be interpreted accordingly. It is the conflict between these competing approaches which has caused this case to be difficult.

[79] In short, I accept that a contract must be construed objectively having regard to the words the parties have used, the context, and the commercial purpose of the bargain. I would also admit dependable evidence of pre-contractual and post-contractual conduct where that evidence would assist the interpretative process. Within this process the basic objective is to ascertain the common intention of the parties. Consequently, where the actual intention of the parties is ascertainable, I hold firm to the view that the contract must be interpreted to give effect to that intention. At no time is it legitimate for the courts to impose an intention on the parties contrary to their actual intention.[40]

The background facts

[80] The background to this dispute has been dealt with in the reasons of Blanchard and Tipping JJ[41] and need not be elaborated at length. Clearly, GUS and

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[40] A possible exception could exist where the actual intention of the parties is discernible but adhering to that intended meaning would seriously prejudice a third party.

[41] At paras [18] – [23] and [30] – [40] respectively.

Gibbons entered into an elaborate arrangement designed to avoid the rule that a sublease for the same or longer term than the head lease operates as an assignment of the head lease. Standard form agreements were adapted in an attempt to give effect to this arrangement.

[81] The head lease is dated 22 April 1982. Under this lease the Nelson Harbour Board (now Port Nelson Limited) leased certain land to Gibbons for an initial term of 21 years from and including 1 November 1982. The lease provided that Gibbons could hold and maintain a warehouse on the land. It also provided for a right of renewal which Gibbons duly exercised on 15 July 2002. The head lease will not expire until 31 October 2023.

[82] By a Deed of Sublease dated 10 July 1991, Gibbons subleased the premises to GUS. Gibbons claims that the parties intended the term of the sublease to be 20 years; that is, from 1 November 1990 to 31 October 2010. To accommodate this intention, it contends, the parties agreed that the first term of the sublease would begin on 1 November 1990 and end on 30 October 2002. The sublease was to be renewed by Gibbons pursuant to a provision in the lease[42] whereby the parties acknowledged that the lease had been entered into on the basis that the lessee would exercise the rights of renewal contained in the head lease. Thus, Gibbons claims that the new lease would begin on 2 November 2002 and end on 31 October 2010. Clause (u) of the sublease provides, inter alia:[43]

> The Lessor [Gibbons] shall grant to the Lessee [GUS] and the Lessee [GUS] agrees to take on lease a new lease of the premises for a term commencing on the 2nd day of November 2002 and expiring on the 31st day of October 2010 (hereinafter called "the New Lease").

[83] In a Deed of Assignment dated 3 April 1997, GUS (then Southway Properties Limited) assigned its interest in the sublease to WDL (then trading under the name Rattrays Wholesale Limited). Under this Deed of Assignment, GUS covenanted to assign all the assignor's estate, right, title and interest in the premises and the lease as set out in the First Schedule to the Deed. The parties expressly acknowledged that the current term under the lease expired on the date set out in the First Schedule and

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42 Clause (s).

43 The full text of cl (u) is set out in Tipping J's judgment at para [34].

that the current rent was as set out in the First Schedule. The Deed expressly provides that, whenever words or phrases appear in the Deed or in any of the Schedules and also appear in the First Schedule to the Deed, those words or phrases should also "mean and include the details supplied after them in the First Schedule". Port Nelson consented to the assignment and duly executed the Deed.

[84] The First Schedule contains the details of the assignment. The "Lease" is referred to as the "Deed of Lease dated 10 July 1991". Following the heading "Expiry Date of Lease" is this entry: "31 October 2002[44] with a New Lease being granted for a term expiring on 31 October 2010".

[85] The Second Schedule stipulates the common indemnity from the assignee to an assignor. Clause 4 then provides:

> THE Assignee covenants with the Landlord that from the Date of Assignment and during the remainder of the term of the lease the Assignee will pay the rent provided for in the Lease and keep and perform all the covenants in the Lease.

The ultimate question, therefore, is whether the phrase "during the remainder of the term of the lease" means the term expiring on 30 October 2002 or 31 October 2010. WDL denies that the parties intended the term of the sublease to extend beyond 30 October 2002 and it is that denial which gives rise to the present dispute.

[86] On 29 November 2000, WDL assigned its interest in the sublease to Infogate Nominees Limited. Infogate went into receivership on 18 October 2002 and was placed in liquidation on 30 January 2003. The receiver stopped paying the rent at about the time the new lease was expected to commence.

The judgments in the Court of Appeal

[87] Ellen France J in the High Court held that the covenants entered into by WDL in the Deed of Assignment did not bind that company during the term of the

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[44] This is an inaccuracy. As is clear from the Deed of Lease, the expiry date was in fact 30 October 2002.

new lease.[45] She concluded that the obligation to enter into the new lease in the Deed of Lease was an option. As it was an option, WDL was not obliged to exercise it. The majority in the Court of Appeal reversed the learned Judge's decision.[46] As more fully set out in the reasons of Tipping J,[47] McGrath and Glazebrook JJ took the view that the word "lease" in the First Schedule referred to the Deed of Lease and that the obligations assumed by WDL included the occupation of the premises for the remainder of the full term of 20 years stipulated in that Deed. The learned Judges' conclusion was reinforced by their perception of the commercial purpose of the assignment.

[88] Chambers J took a different view. In his dissenting judgment the learned Judge concluded that the phrase "during the remainder of the term of the lease" in cl 4 of the Second Schedule refers to the term of the original lease only. He argued that the second sublease does not exist, and cannot exist, until the estate out of which it is granted (the head lease) itself comes into existence, and that WDL was under no contractual obligation to Gibbons to take up the sublease. Tipping J has summarised this point with admirable clarity.[48] As at the date of the assignment there was only one term in existence; that is, the term expiring on 30 October 2002. The remainder of that term must itself, therefore, have expired on that date. In Chambers J's view, GUS had promised to take the new lease but WDL had not. He preferred to interpret the Deed of Assignment in line with the arrangements Gibbons and GUS had "actually agreed".

[89] It should be said at once, however, that notwithstanding the force of Chambers J's argument, an alternative "legal" analysis is available which is not without substance, and which may well have been the perception of the parties. It is

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45 *Gibbons Holdings Ltd v Wholesale Distributors Ltd* (High Court, Blenheim, CIV 2003-442-19, 5 May 2004).

46 *Gibbons Holdings Ltd v Wholesale Distributors Ltd* [2006] 2 NZLR 27.

47 At paras [41] – [44].

48 See Tipping J's reasons at para [45] above.

common ground that the Deed of Lease contained both a lease and an agreement to lease. An equitable interest in an agreement to lease[49] is capable of being assigned. Consequently, when GUS assigned the Deed of Lease to WDL it assigned both the "legal" interest in the lease and the equitable interest in the agreement to lease. The omission in the Deed of Assignment is not the non-existence of an interest to assign but the omission of an express contractual provision which Gibbons could enforce requiring WDL to enter into a new lease in terms of the agreement to lease. The absence of this express contractual provision does not derogate from the existence of the equitable interest which GUS assigned to WDL. It becomes credible that, when the parties came to refer to the "remainder of the term of the lease", therefore, they were referring to the combined term of the leasehold interest in the original lease and the equitable interest in the agreement to lease.

The correct approach

[90] In approaching the task of interpreting the Deed of Assignment two approaches confronted the Court: it could either discern the meaning of the Deed of Assignment and presume that the meaning arrived at represented the intention of the parties or it could interpret the Deed so as to give effect to the parties' actual intention, but accept that the document as drawn may be ineffective to achieve their objective. The first approach focuses heavily on the legal analysis of the terms of the Deed of Lease and the Deed of Assignment and the literal meaning of the words used by the parties in the Deed of Assignment. It is an approach which can easily lapse into legalism. The second approach gives primacy to the intention of the parties but runs the risk of seeming to be at odds with accepted principles of land law.

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[49] Such an interest arises provided that specific performance is available as a matter of jurisdiction; that is, where the agreement to lease is evidenced in writing and is for valuable consideration. The existence of the equitable interest does not depend on whether, as a matter of discretion, a court would be likely to enforce the interest by specific performance or by injunction. See McMorland, *Sale of Land* (2nd ed, 2000), para [10.02].

[91] I favour the second approach simply because it is more realistic. I will therefore seek to interpret the Deed of Assignment to give effect to the common intention of the parties. It is not an analysis of the complicated rules which govern the holding and assignment of leasehold interests in land but the actual intention of the parties which must prevail. This is not to say that the analysis is not relevant but simply that it must give way to the parties' intention. I conclude that the parties intended that WDL would be liable for the rent until the expiry of the new lease on 31 October 2010. In seeking to give legal effect to this intention they may have been under a misunderstanding as to the law or their draftsmanship may have been incomplete.

[92] I do not propose to enter upon the question of what would have happened if Gibbons had sought to require WDL to enter into the new lease. I suspect issues relating to, inter alia, equitable interests, implied terms, promissory or equitable estoppel, specific performance and novation could arise. But the Court is obviously not in a position to address any of those issues in this appeal. The task before the Court is solely one of interpretation.

[93] It is clearly not beyond the bounds of possibility that the parties, or their legal advisers, could have been under a misunderstanding as to the law or simply failed to cover all bases when drafting the Deed of Assignment. In order to avoid the legal consequences of granting a lease for a term extending beyond the term of the head lease, the original parties entered into a complicated arrangement utilising standard form documents and adding or inserting clauses in those documents in an effort to give effect to that arrangement. Blanchard J observes in passing that the lease document had the appearance of a "law firm precedent adapted, not entirely happily in some respects".[50] He provides a notable example, inter alia, of a missing term in the Schedule to the Deed of Lease. One only has to look at the Deed of Assignment itself to know that it, too, was adapted, heavily so, and again not entirely happily.

[94] I would reiterate that, in arguing that when the parties used the phrase "remainder of the term of the lease" in cl 4 of the Second Schedule to the Deed of

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[50] At para [18].

Assignment they were referring to the combined term of the lease which expired on 30 October 2002 and the term of the new lease which expires on 31 October 2010, I will not depart from the cardinal presumption of contractual interpretation that the words the parties have used must be construed objectively without recourse to evidence or speculation as to their subjective intentions. Equally important, however, is the principle, enshrined in ancient authority, that the objective is to discover from the written agreement the intention of the parties. See, for example, *Marquis of Cholmondeley* v *Clinton*.[51] But, first, a pertinent word about "presumed intent" and "actual intention".

Presumed intent and actual intention

[95] The great Wigmore said:[52]

> The history of the law of interpretation is the history of a progress from a stiff and superstitious formalism to a flexible rationalism.

But I sounded a note of caution in my judgment in *Attorney-General v Dreux Holdings Ltd*.[53] I first acknowledged that under the rubric of formalism much that is artificial has crept into the interpretative function so that the basic object of giving effect to the parties' intention is at times in danger of being befogged. But while "stiff and superstitious" formalism is to be rejected, care must be taken not to destroy the utility of the law relating to the interpretation of contracts. Much of that utility stems from the readiness of judges at times to accept a fiction, that is, that the parties have addressed the situation which has arisen and formed an intention in respect of it. More often than not the parties have not contemplated the circumstances which have developed. In such cases the courts construe a contract in such a way as to arrive at the presumed intent of the parties.

[96] The notion of presumed intent has been popular ever since Viscount Simon, referring to the fact parties to a contract are often faced with a turn of events which they did not anticipate, expressly enunciated the doctrine in *British Movietonews v*

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51 (1820) 2 Jac & W 1 at p 91.
52 *Wigmore on Evidence* (Chadbourne rev 1981), vol 9, para [2461].
53 (1997) 7 TCLR 617 at p 632 (CA).

London and District Cinemas.[54] The doctrine has necessarily had an impact on the way judges and lawyers approach contractual interpretation in general. Aware that in many, if not most, cases the parties did not, because of unforeseen events, have an actual intention in respect of the particular clause in issue, the doctrine permits judges and lawyers to arrive at an interpretation without compromising the basic premise that the contract must not be interpreted subjectively. The presumed intent is imputed to the parties. Inevitably, and understandably, judges and lawyers come to impute an intention to the parties without questioning the process. The imputation becomes a habit of thought or attitude of mind.

[97] But that is **not** this case. In the present case the parties had an actual intention. They either intended the term to expire on 30 October 2002 or to expire on 31 October 2010. They could not have failed to address that question. It does not represent a change of circumstances or turn of events which they did not anticipate. The doctrine of presumed intent, and the habit of thought or attitude of mind which goes with it, can have no application in this case. There can be no presumption that the parties' intention accords with the court's "legal" analysis of the documents in issue. Rather, as I urge, the proper task of the court is to construe the contract objectively with the aim of discerning the actual intention of the parties. When the courts approach a fork in the road, and one road leads to a presumed intent based on the meaning of words and the other road leads to the meaning actually intended, the courts must take that road which leads to the parties' actual intention.

[98] Emphasising the task of the courts in these terms does not require the introduction of a novel principle. It is a truism that parties may not have turned their minds to certain matters that later become relevant. Judges are constantly faced with the task of deciding the rights of parties who have expressed themselves unclearly or incompletely. In interpreting contracts, courts should seek to recognise this reality and to develop and apply the law to recognise that reality. Thus, the courts have recognised that the intention of the parties must prevail even though they may have been under a misunderstanding as to the law. Kim Lewison QC in *The Interpretation of Contracts* (2004) points out that questions of construction often arise against the background of substantive law. Answering the question of

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[54] [1952] AC 166 at pp 185 – 186.

construction one way will produce a different result from answering it another way. "In theory at least", the author continues, "the court should be uninfluenced in construing a contract by what the legal result will be".[55] While accepting that the substantive law may form part of the surrounding circumstances and may be taken into account in construing a contract, Lewison refers only to situations where the legal position may justify attaching a particular meaning or particular weight to a term of the contract whose purpose is not otherwise apparent or where it is necessary to supply the meaning of a term of art.

[99] Continental legal systems appear to be more receptive to the objective of ascertaining the actual intention of the parties. The French Code civil, art 1156, for example, provides that one should seek out the common intention of the parties rather than adhere to the meaning of their words. The importance of ascertaining their real intention is stressed by commentators. The provisions of the civil code in Germany are not so forthright in confronting the conflict between the doctrine of intention and the external phenomenon of expression. Nevertheless, art 1362 of the Codice civile provides that the aim of construction is "to discern the real intention" of the parties.[56]

The actual intention of the parties

[100] I believe that the actual intention of the parties is readily discernible from the wording of the contract, the context, and the commercial purpose of the assignment. The intention is confirmed by the subsequent conduct of the parties, which I will deal with separately.

[101] As already pointed out, the phrase "during the remainder of the term of the lease" in cl 4 of the Second Schedule to the Deed of Assignment is the core provision. Read literally, it could mean the original lease. Read in the context of the assignment as a whole, however, it becomes relatively clear that the parties intended

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55 At para [4.03].

56 Zweigert and Kötz, *An Introduction to Comparative Law* (3rd ed, 1998), pp 402 – 403. See also Zimmerman, *The Law of Obligations: Roman Foundations of the Civilian Tradition* (1990).

the term of the lease to embrace both the term of the original lease and the term of the new lease.

[102] The Deed of Assignment assigns all the assignor's "estate right title and interest in the Premises and the Lease all as set out in the First Schedule". The First Schedule describes the lease as the "Deed of Lease dated 10 July 1991". That Deed of Lease includes both the original lease and the agreement to lease. If the use of the word "lease" in cl 4 is to have the meaning ascribed to it in the First Schedule, that is, the "Deed of Lease dated 10 July 1991", the assignor is assigning both the lease and agreement to lease. At the very least, no attempt is made to stipulate that part only of the Deed of Lease is being assigned.

[103] The significance of this point should not be downplayed. All the assignor's "interest" includes the assignor's equitable interest in the agreement to lease. All the assignor's "right" includes the contractual rights GUS possessed in relation to the agreement to lease. It makes no sense to read this key phrase to mean that the assignor, GUS, assigned all its right and interest in the Deed of Lease to WDL except for the equitable interest arising from the agreement to lease or to suggest that the parties intended to exempt that equitable interest from the assignment of the Deed of Lease. Furthermore, as the use of the word "Lease" in this context clearly includes both the "legal" interest in the original lease and the equitable interest in the agreement to lease, there is no evident reason why the word "lease" in cl 4 of the Second Schedule should be given a different and more restricted meaning.

[104] This apparent meaning is confirmed by the description following the heading "Expiry Date of Lease" in the First Schedule. The expiry date, it will be recalled, reads: "31 October 2002 with a New Lease being granted for a term expiring 31 October 2010". If the intention is that the expiry date is to be 31 October 2002,[57] it is difficult to give any sensible reason for the additional reference to the new lease. It would seem to be otiose unless it is construed as a means of indicating that the expiry date is 31 October 2010 made up of, as the Deed of Lease provides, a lease and an agreement to lease.

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[57] In fact, as noted above, 30 October 2002.

[105] Counsel for WDL, Mr Curry, sought to explain the inclusion of these words by suggesting that one or more of the parties must have wished it to be recorded that the Deed of Lease envisaged a new lease being granted for the further term mentioned. I find this explanation unsatisfactory. What reason, either legal or commercial, would exist for wishing reference to the new lease to be recorded if it were not to have some legal effect? I suspect that, for this explanation to have any plausibility, it is necessary to work backwards from the conclusion that the assignment is intended to apply to the lease only. With that conclusion firmly in mind, it is then necessary to proffer some rationalisation for these inconvenient words. In such circumstances, no doubt, a guess is as good as a mile.

[106] Regard is to be had to the structure of the Deed of Lease. Separation of the term of approximately 20 years into the term of the lease and the term of the new lease existed solely to avoid the legal consequences of granting a term in excess of that provided in the head lease. It was a legal device. Indeed, cl (u) in the Deed of Lease appears to provide for continuity in the review of rent beyond October 2002. WDL was fully aware of this structure at the time it entered into the assignment. The structure was constructed around the roll-over of the head lease, and WDL obtained Gibbons' consent to the assignment. Gibbons became a party to the Deed. If it had been intended to depart from this structure, something more could have been expected in the Deed of Assignment.

[107] Consideration was given for the assignment. Clause 1 of the Deed of Assignment refers to the "Purchase Price", and the purchase price is stated in the First Schedule to be the consideration agreed to in an "Agreement dated 1996 between Progressive Enterprises Limited [WDL's parent company] and Southway Properties Limited [GUS]". The amount of the consideration relating to this particular assignment was not included in any document before the Court or given in evidence. This omission may be unfortunate for it is possible that it would indicate the intention of the parties. There is a vast difference between taking an assignment of the premises and lease for a period of five years and an assignment for a period of 15 years. I appreciate, of course, that the premises were only one of the premises being taken over by WDL from GUS and that no discrete price may have been allocated to this particular assignment. For present purposes, the most that can be

taken from the fact that a purchase price was paid by WDL to GUS is that both parties would have had a clear idea what the consideration was for and a mutual need to be in agreement on the term of the interest being assigned.

[108] The context and commercial purpose of the assignment points to the parties contemplating a term through to 31 October 2010. At the time of the assignment, WDL was acquiring a number of warehouses or distribution centres owned by GUS. The premises which are the subject of the Deed of Lease was one of those warehouses. The bargain between the parties related primarily to the businesses and the premises that went with the businesses. In a sense, the lease was supplementary to that bargain. As Mr Wilson QC submitted, in this context, it is inherently improbable that WDL would have taken only part of the obligations of GUS in relation to this warehouse so that the right and obligation to lease the premises would revert to GUS some five years later. At that time GUS, if it had not become defunct following the assignment, would have had to resume the premises and the business in respect of that one warehouse. It is when the lease is looked at, not in isolation, but as part of the commercial transaction in which GUS's warehouses and distribution premises were being transferred to WDL, that it becomes difficult to accept that the parties were contemplating the term of the original lease only.

[109] The point can be demonstrated by assuming for the moment that the parties had exchanged correspondence either immediately before or immediately after the assignment in which they unequivocally indicated that they intended WDL to be liable for rent until October 2010. The perceived defect in the assignment would still exist. Indeed, even if the Deed of Assignment itself had said, immediately after the words "during the remainder of the term of the lease", "ie until 31 October 2010", the same perceived defect would exist, that is, the non-existence of an estate, other than the interest in the original lease, to assign and the omission of an express provision requiring WDL to enter into the new lease.

[110] I reject out of hand the suggestion that, as they would have been aware of the complicated rules which govern the holding and assignment of leasehold interests, the parties would have intended the estate or interest being assigned to be limited to the original lease. The assumption that they would have known these complicated

rules would be a brave assumption to make when, first, the lawyers for GUS, TNL and Infogate clearly did not, and secondly, those rules did not figure in the High Court and divided the Judges in the Court of Appeal. Having regard to the complicated nature of the rules and the parties' advisers' use, or misuse, of standard forms, the conclusion that these rules indicate the parties' intention to limit the term to 30 October 2002 would require a feat of juristic legerdemain that I am not tempted to perform.

Subsequent conduct

[111] I do not need to expand on the desirability of the courts having regard to subsequent conduct as an aid to interpretation in appropriate cases. I traversed that topic 11 years ago in the *Dreux Holdings* case.[58] It will suffice to reiterate that mutual assent is the key to the formation of a valid contract and it follows that the interpretive function should be directed at ascertaining the mutual intention of the parties: what did they mean by their contract at the time they entered into it?

[112] The opinion I advanced in the *Dreux Holdings* case may not have been as complete as I would like today, but I am comforted by the fact that what I may not have said then will have been said by Professor McLauchlan of the Law Faculty at Victoria University of Wellington.

[113] I pause to pay, or repay, a tribute to the learned Professor. His work to bring some logic and cohesion into the task of contractual interpretation has been as outstanding as it has been tireless. Indeed, since argument was heard on this appeal, Professor McLauchlan has published another article under the title "Contract Formation, Contractual Interpretation, and Subsequent Conduct".[59] That article exhibits the same impeccable scholarship that has marked Professor McLauchlan's earlier essays. I for one am indebted to him. It will undoubtedly be a matter of some satisfaction to him that four members of this Court have now decided that evidence

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58 At pp 28 – 33.
59 (2006) 25 UQLJ 77.

of subsequent conduct may be admitted in appropriate cases. The fact that two of the four do not consider that the evidence of subsequent conduct in this particular case is of assistance does not derogate from the fact that the principle has now been established.

[114] Much of the judicial reluctance to admit evidence of subsequent conduct has been due to an inability to distinguish between the objective task of giving effect to the mutual intention of the parties and the misguided exercise of seeking to ascertain the subjective intention of the parties. The latter exercise is illegitimate and will remain illegitimate. Evidence of subsequent conduct is admitted, not for the purpose of importing an intention which was not expressed in the contract, but with a view to elucidating the meaning which the parties intended their contract to have when they entered into it. The reasonable expectations of the parties to the contract should not be defeated by attributing a meaning to it which their subsequent conduct demonstrates they did not intend. As an Australian Judge has put it: "[J]ustice requires that the parties should be held to the bargain in the sense to which they have agreed."[60]

[115] The case for the admission of evidence of the actual intention of parties as an aid to interpretation has been given an exponential boost by virtue of the seminal article of Lord Nicholls, "My Kingdom for a Horse: The Meaning of Words".[61] Although the Law Lord's well-reasoned argument is primarily directed at pre-contractual negotiations, he has this to say about post-contractual conduct: [62]

> Even so it is surely time the law recognised what we all recognise in our everyday lives, that the parties' subsequent conduct, that is, their conduct after they had reached agreement, may be a useful guide to the meaning they intended to convey by the words of their contract. Such conduct, for what it may be worth in the particular case, is one of the matters the court should be able to take into account when deciding what, in the events which have happened, is the meaning the words would reasonably convey to a reader. Judges are well able to identify, and disregard, self-serving subsequent conduct.

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60 *Cocks v Maddern* [1939] SASR 321 at p 327 (SASC) per Napier J.

61 (2005) 121 LQR 577. See also Steyn, "The Intractable Problem of The Interpretation of Legal Texts" (2003) 25 Sydney LR 5.

62 At p 589.

[116] One must, however, acknowledge the force of an ensuing case note by a Tel Aviv solicitor, Alan Berg, entitled "Thrashing Through the Undergrowth".[63] In the course of the note, Berg takes Lord Nicholls to task. Berg's main point centers on the practical difficulties a lawyer faces in giving a client advice as to the meaning of a clause in a contract. He correctly states that a client who asks a lawyer to advise on the meaning of a particular clause is asking how a court would be likely to interpret it. This means, he argues, that the lawyer would first need to obtain all the relevant background knowledge which was reasonably available to the parties in the situation in which they were at the time of the contract. Berg allows only that this might be possible where the transaction is a straightforward one, the lawyer was personally involved in the drafting, and the transaction is fairly recent.[64] Otherwise, the author adds, the lawyer would have to trawl through volumes of pre-contractual correspondence and drafts.[65] Particular difficulties could occur with purely oral statements between the original parties which would be unlikely to be recorded on the lawyer's file. The difficulties, he implies, would be exacerbated if the contract requiring interpretation had been assigned to other parties. Anderson J succinctly expresses much the same concern in his reasons.[66]

[117] Berg concludes that the "fiction" that contracts are addressed to the original parties should be abandoned.[67] Most professionally drafted commercial contracts, he argues, are intended to be used by, and are therefore addressed to, people who will know the basic background to the deal, but no more than that. There is, therefore, he argues, no logic in insisting that such a contract must be interpreted in the light of *all* the background knowledge which, historically, was reasonably available to the parties at the time of signing.

[118] Berg's criticism deserves close consideration. The notion that lawyers should have to "trawl" through possibly historical pre-contractual correspondence and drafts in order to advise a client on the meaning of a particular clause is intuitively unacceptable. Further, the prospect of a subsequent party having to carry out some

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63 (2006) 122 LQR 354.
64 At p 358.
65 At p 360.
66 At para [75] above
67 At p 359.

sort of "due diligence", so to speak, on what transpired at the time the original contract was entered into and, possibly, the subsequent conduct of the original parties, is also unacceptable. Courts should, of course, always be alert to practical considerations of this kind.

[119] But Berg overstates his case. Notwithstanding his express denial,[68] his approach would herald a retreat to "literalism". His argument is directly aimed at evidence of the surrounding circumstances which is already admissible and, indeed, regarded as essential. Berg does not seek to evade this point. His primary attack is directed at the first of the principles enunciated by Lord Hoffmann in *Investors Compensation Scheme Ltd v West Bromwich Building Society*,[69] that is, that interpretation is the ascertainment of the meaning which the document would convey to a reasonable person having all the background knowledge which would reasonably have been available to the parties in the situation in which they were in at the time of the contract. Lord Nicholl's article merely served to provoke his attack on that basic principle.

[120] Berg's argument is overstated in another respect. It suggests that a lawyer will face an impossible and endless task advising on the contract generally. But for the most part, a party, or the legal adviser, will ensure that the party's core interests are spelt out and specifically protected in the document. In practice, advice will, more often than not, be called for if and when a dispute arises as to the interpretation of a particular clause. Conscientious lawyers will then, as they do now, amass all relevant and available background knowledge before advancing an opinion or advising on legal action. It is lawyers at present who put the courts in the position of being seized of that knowledge. Pre-contractual and post-contractual information relevant to the interpretative exercise will be embraced in that same conscientious inquiry. Ultimately, as Lord Nicholls argues, this evidence is necessary to enable lawyers to give coherent advice. Nor will courts expect the impossible. They will be alert to ensure that no party is disadvantaged by virtue only of the difficulty of obtaining access to evidence of pre-contractual or post-contractual conduct.

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68 At p 359.

69 [1998] 1 WLR 896 at p 912.

[121] Finally, Berg's suggestion that the accepted wisdom that contracts are addressed to the original parties is a "fiction" is unsupportable.[70] For the most part, parties wish their interests to be advanced and protected, and their legal advisers draft their contracts to advance and protect those interests. While there is the possibility that one or other of the parties may wish to assign their interest in the contract, assuming that they are contractually able to do so, the primary concern will be to secure the bargain the parties have struck. One of the parties will have paid or given good consideration for that advantage. Furthermore, many contracts, such as one-off contracts, by their very nature are unlikely to be addressed to potential third parties. Common examples are contracts for the sale of property. Then, relational or long term contracts will, again for the most part, seek to define the relationship which the parties intend to endure throughout the duration of the contract. Contracts will be and are assigned, but to suggest that it is a "fiction" that they are not for the most part addressed to the original parties is a signal overstatement.

[122] Although given reason to pause by Berg's note, I believe that the case for the admission of evidence of subsequent conduct remains compelling. It is compelling simply because the courts must be serious about the task of interpreting contracts in such a way as to give effect to the common intention of the parties.[71] The notion that an intention can be imposed on the parties contrary to their actual intention is repugnant to any concept of fairness, common sense, and the reasonable expectations of honest men and women. It should be repugnant to the common law. But I am more than prepared to let Tipping J have the last word; the advantages of admitting evidence of post-contract conduct outweigh the disadvantages.[72]

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70 See paras [117] – [118] above.

71 Rectification and estoppel are a different matter. Where the contract itself is capable of being interpreted to give effect to the actual intention of the parties, it is unnecessarily onerous to put a party to the task of satisfying the stringent requirements of rectification, such as the requirement that the mistake must relate to expression.

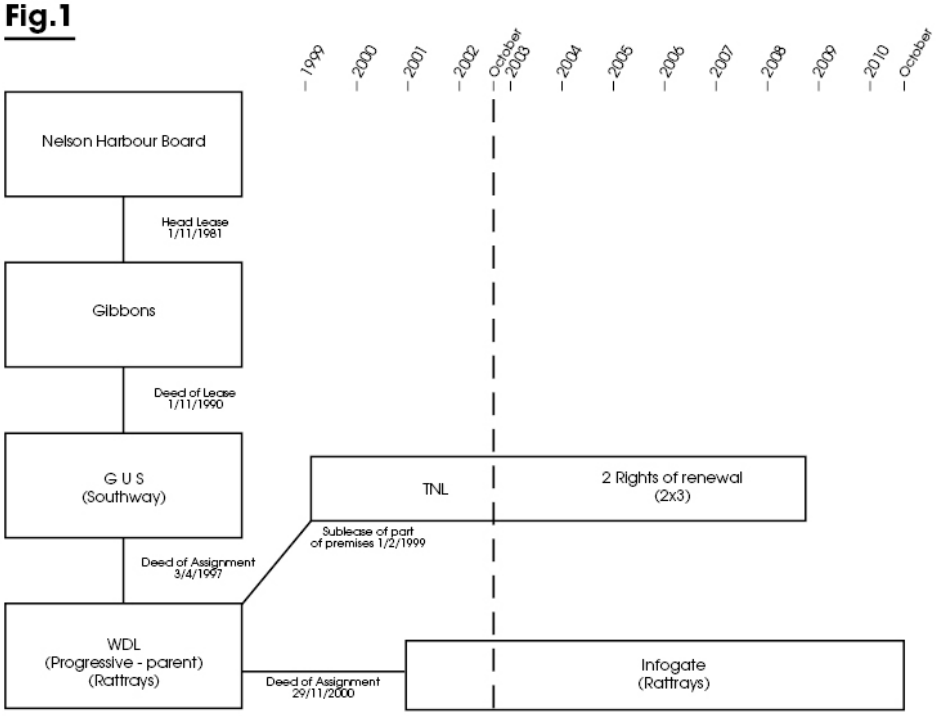
72 Para [52] above.

The subsequent conduct in this case

[123] The evidence of subsequent conduct in this case reliably demonstrates that WDL intended the phrase "during the remainder of the term of the lease" to mean a term lasting until 31 October 2010. It is untenable to suggest otherwise.

[124] On 7 April 1999, WDL subleased part of the premises to TNL Group Limited. It recited in the "Deed of Sub-Sublease" that it had acquired "all the right, title and interest of G.U.S. under the Headlease". The term of the sublease was specified as "Three years, eight months and 29 days" to commence on 1 February 1999. Under the Deed, WDL then granted "Two (2) rights of renewal for further terms of three (3) years each". Following the heading "Final Expiry Date of Sublease if Renewed" is the entry "1 November 2008". Granting TNL two rights of renewal is at odds with WDL's present claim that it had no interest to assign beyond 2002, and that it did not therefore intend to assign an interest beyond that date.

Fig.1



[125] If correct, WDL's present claim would create an implausible situation. It would mean that TNL would enjoy only three years nine months' occupation of the

premises. As the company asked for and received two rights of renewal which would give it the option of occupying the premises until November 2008, it is difficult to accept that WDL believed or intended this outcome. See Figure 1 above.

[126] Documents on WDL's file also confirm that the parties contemplated that the term of the sublease would, if TNL exercised its rights of renewal, extend to 2008. In a letter to TNL, the Property Administrator of Progressive Enterprises Limited, WDL's parent company, advised that the first term would expire on 29 October 2002 and the second period would commence on 2 November 2002 with the premises being held in trust in the interim days, "as per [WDL's] lease". "This", he said, "gives a first term of 4 years plus the option of two further terms of three years each". Again, a memorandum from WDL to Progressive referring to the assignment states that the "Term of Lease" is "3 years 8 months + 2 x 3 [years Right of Renewal]". Clearly, WDL believed that it had an interest beyond October 2002 and intended, if the rights of renewal were exercised, to grant a renewal of the sublease accordingly.

[127] Other relevant evidence of this transaction relates to the negotiations between WDL and TNL. A senior management officer in the latter company claims that it was made clear to WDL that TNL wanted long term security beyond 2002, and that WDL assured it that the company could occupy the premises through to 2008. Hence the unqualified rights of renewal granted to it by WDL. No finding of fact has been made in respect of this evidence, but the probabilities inherent in the circumstances would suggest that TNL would not have accepted the sublease without such an assurance from WDL. Self-evidently, the conduct involved in giving that assurance is inconsistent with the position WDL now adopts.

[128] WDL's conduct in granting the rights of renewal is also inconsistent with its present stance in other respects. Why would it, or any commercial entity, grant a sublease containing two unqualified rights of renewal if it did not believe that it had the legal capacity to execute its promise should TNL elect to renew the sublease? Consider the consequences if, as it now claims, WDL has no estate or interest to assign beyond 30 October 2002. TNL's rights to renew the lease are null and void as from that date. The estate or interest reverts to the defunct GUS. The potential for

litigation is patent. It beggars belief to think that WDL would have committed itself to granting TNL rights of renewal until 2008 if it did not believe that it was, or would be, in a position to grant the renewals.

[129] The notion that WDL could claim the "benefit" of the assignment from GUS and take up the new lease as provided for in the Deed of Lease falls foul of the same shortcoming. The whole point of Mr Curry's exposition of the complicated rules which govern the holding and assignment of leasehold interests in land is that, as GUS had not entered into the new lease, there was no valid sublease in existence to assign. On this reasoning, WDL got the "benefit" of a non-existent interest. Furthermore, as the benefit/burden distinction is an essential component in his reasoning, the point may be spelt out in other terms. The subject matter of the assignment, the agreement to lease, consists of an obligation on the part of the lessor to grant a lease and an obligation on the part of the lessee to take the lease. If the obligation of the lessee to take the lease is, in effect, cast as an option, the subject matter of the assignment has been transformed in character. This conundrum can only mean that, in logic and law, the agreement to lease is indivisible and the benefit/burden distinction has no application.

[130] The most significant evidence of subsequent conduct confirming the intention of the parties relates to WDL's assignment on 29 November 2000 of all its "estate and interest in the Lease for the remainder of the term of years created by the lease" to Infogate. The reference to the "Lease" in the Deed of Assignment is to the Deed of Lease originally executed by Gibbons and GUS on 10 July 1991. Gibbons consented to the assignment by becoming party to the Deed. The assignment was, again, part of a commercial transaction, in which WDL sold its wholesale grocery business to Infogate. Indeed, Infogate became known as Rattrays Wholesale Limited, the name under which WDL had traded.

[131] It would have been commercial folly for Infogate to acquire a business without the leasehold tenure to operate that business. Yet, at the time of the assignment, the original lease had only one year eleven months to run. See Figure 1 above. Why would Infogate purchase WDL's wholesale grocery business for such a

limited period without long term security? The reality can only be that the parties had a common intention to assign the lease through to 2010.

[132] The assignment from WDL to Infogate may also be read together with various memoranda and notes made by WDL at or about that time. Thus, for example, a note to Progressive refers to the "Assignment of Lease (Nelson) following sale of business to 'Infogate'". After the heading "Term of Lease" appear the categorical words: "Expires 31st October 2010". Another memorandum, from Progressive's Group Finance Manager, lists the expiry dates of six branch leases which are being assigned to Infogate. Included in the list is a reference to the lease in issue: "Nelson 31 October 2010".

[133] Nor do I see why the failure or omission of a party to stipulate a core matter critical to its interests may not, in appropriate circumstances**,** be accepted as evidence of subsequent conduct. As Mahon J said on another occasion referring to an omission in the documents which had been discovered, "[t]hat omission, as I see it, invests the [documents] with a speaking silence which tells its own tale".[73] In the present circumstances, it could be expected that, in its dealings with both TNL and Infogate, WDL would make some reference either in correspondence or internal memoranda that the term or rights being granted did not extend beyond 2002. There is not a word. Other than that WDL was deliberately hoodwinking TNL and Infogate, which I do not suggest, the only sensible conclusion is that WDL believed that it was granting a term and rights beyond that date and that it intended to do so.

[134] Although prepared to accept evidence of subsequent conduct in appropriate cases as an aid to interpreting the meaning of the contract, Tipping J seems to qualify the admissible evidence by requiring it to be shared or mutual to the parties. Thus, the learned Judge states: "Extrinsic material which bears only on the meaning intended or understood by one party should be excluded, save of course for rectification purposes".[74] "Inviting inferences from the conduct of one party, in which the other party is not involved" is disapproved.[75] He also speaks of "some

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73 *Anderton* v *Auckland City Council* [1978] 1 NZLR 657 at pp 697 – 698 (SC).
74 Para [52].
75 Para [53].

mutual or shared post-contract conduct of the parties";[76] "the shared conduct of the parties in the performance of their contract";[77] "[t]here is no element of mutuality involved, let alone a mutuality involving WDL";[78] "[t]hese documents do not demonstrate any shared intention as to the meaning of clause 4";[79] "not conduct of such mutuality";[80] and "the lack of mutuality aspect".[81]

[135] I consider that, as it is expressed, this requirement is misconceived and will undoubtedly cause confusion. There is no reason, certainly in this case, why evidence of subsequent conduct should have to be common to establish a common intention. Conduct which is not, and has not been, "shared" or "mutual" may nevertheless point to a meaning contrary to the meaning later asserted by one of the parties. That party has acted inconsistently with the meaning it seeks to persuade the court to place upon the contract. The value of the evidence stems from the inconsistency. I acknowledge that, notwithstanding the explicit stipulation of "shared" or "mutual" conduct referred to above, Tipping J seems to endorse this view when he observes that there are connotations of estoppel involved in the approach he has outlined, albeit that the issue is not one of estoppel in the strict sense.[82]

[136] It would be unfortunate if the principle that evidence of subsequent conduct is admissible as an aid to interpretation becomes hedged with qualifications which undermine the objective of the principle. Providing that the evidence is relevant to the question of interpretation before the court, it should be sufficient that, following the completion of the contract, the party concerned has acted inconsistently with the meaning it now asserts in court.

[137] I accept, of course, that the courts must be cautious about admitting evidence of subsequent conduct which is equivocal as to the common intention of the

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76 Para [53].
77 Para [61].
78 Para [64].
79 Para [65].
80 Para [68].
81 Para [68].
82 At para [61].

parties.[83] This caution, as Anderson J has been concerned to stress,[84] may be particularly necessary where the contract has been assigned or, in the case of a lease, the land sublet, so that some or all of the parties to the dispute are different from the parties who executed the original contract or lease. On the other hand, exercising caution does not mean that the courts should strain to explain away credible evidence. Difficulties may arise if the courts, as they should, feel constrained to avoid a contract having two meanings: one for the original parties and one for the subsequent parties. But those difficulties do not arise in this case. WDL was a party to the Deed of Assignment in question and each of the matters relied upon relate to conduct which is inconsistent with the meaning it now urges upon the Court.

[138] Thus, the evidence of internal memoranda or notes was not "shared" or "mutual" but the recording of the memoranda or notes is conduct which is inconsistent with the meaning WDL now wishes the Court to adopt. The evidence of the sublease to TNL was not "shared" or "mutual" but is also inconsistent with WDL's present stance. The evidence of the assignment to Infogate was not "shared" or "mutual" but is evidence that WDL acted in a way which is contrary to the meaning it now pursues. At no time did the company, or GUS for that matter, say or infer anything that might indicate that they intended the assignment to be restricted to a term expiring in October 2002.

[139] WDL's response to the evidence of subsequent conduct advanced in this case is highly "legalistic". With respect to the file notes, the deponent says that "as far as [he is] aware none of the documents would have been shown to the Plaintiff [Gibbons] before discovery". With respect to the assignment to Infogate, the deponent states that "it seems we may have calculated the term of the lease incorrectly" and that WDL was "not required to obtain legal advice on this issue before" completing the document. He states that another document was "an internal document" and that it appears that "Mr Thomas [Progressive's Group Finance Manager] has calculated the term incorrectly". With respect to the sublease to TNL, the deponent again makes the point that a memorandum in relation to the sublease is

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[83] Similarly, the courts will need to be alert to the possibility of a party manufacturing internal documents and then alleging those documents to be consistent with its position.

[84] At para [75].

in standard form and "an internal document and would not have been shown to the Plaintiff [Gibbons] before discovery". He concludes: "As far as I am aware, [WDL] would not have intended any of these documents to affect the legal relationship between the Defendant [WDL] and the Plaintiff [Gibbons]". WDL's policy, it is said, has always been that "the legal relationship we have with our lessors and lessees is fully contained in the formal leases and the other formal contractual documents".

[140] Three themes run through these so-called explanations. The first is that the documents were internal documents which were not shown to Gibbons until discovery. It is difficult to see why the fact a document is "internal" means that it cannot be probative evidence of WDL's intention at the time the assignment was completed. Nor would there seem to be any logical reason why, to be admissible evidence of subsequent conduct, a document should have had to be made known to the party relying upon it. Why, for example, should an internal file note which may emphatically record that the party's intention is at variance with its stance in court not be valid evidence of subsequent conduct simply because it is "internal" and was not made known to the other party?

[141] The second theme is that the term of the lease appears to have been calculated incorrectly. This explanation is wafer thin, particularly as there was more than one document in which the term had apparently been "calculated incorrectly".

[142] The third theme is that WDL relies upon the "legal relationship" contained in the formal documents. It now comes to court seeking the Court's assistance to interpret the Deed of Assignment, or more particularly, cl 4 of the Second Schedule to the Deed, literally, and so establish the "legal relationship". But this excursion does not explain away the subsequent conduct which points to the company having had a different intention.

[143] It does not take more than a moment to discern that these explanations are intended to lay the basis for counsel's submission, reflected in the observations of Tipping and Anderson JJ, that the evidence of subsequent conduct in this case should

not be admitted. Marshalling the facts as I have above, however, demonstrates the evasion inherent in these explanations.

Conclusion

[144] Courts today seek to approach contractual interpretation realistically. Just as the intention of the parties prevails over the literal meaning of words, the parties' actual intention will prevail over a presumed intent, and this end is achieved without derogating from the objective approach to contractual interpretation. The importance of seeking to give effect to the intention of the parties is then fully realised. Indeed, the courts are likely to scorn the idea of imposing a "court-divined" intention on the parties which is contrary to their common intention at the time they entered into the contract.

[145] In cases such as the present where one party advances an interpretation at variance with its actual intention and is effectively seeking to deny and resile from the bargain which was struck, the courts may well see its action for what it is – fraudulent. Hope JA's observation in *Air Great Lakes Pty Ltd v K S Easter (Holdings) Pty Ltd*[85] is pertinent. In referring to the conduct of parties in deciding whether they intended to be bound by an agreement, the learned Judge said:[86]

> If the mutual actual intention of the parties who have signed a document is that it should not have contractual operation, it would be *fraudulent* on the part of either of them to seek to enforce it as a contract. Consistently, if the mutual actual intention was that there should be a concluded contract, it would be *fraudulent* to deny that intent …

[146] In the same way, when parties have entered into a contract having a common intention in respect of a particular provision, it is "fraudulent" to seek an interpretation contrary to that intention. Advantage is being taken of rules which were largely devised in an attempt to promote certainty in the law of contract and formulated for the regular occasions where the parties did not contemplate the developments or circumstances which have arisen and take a genuinely different

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85 (1985) 2 NSWLR 309 (NSW CA).

86 At p 319 (emphasis added).

view of the meaning of the contract. No one would deny that in many, if not most, contractual disputes relating to the construction of a clause in a contract, the parties' belief in their cause is unfeigned. It is otherwise when the parties clearly had an intention in respect of the contract or clause in question and one party seeks to deny that intention and so resile from the bargain they have freely entered into.

[147] The courts will not aid and abet this apparent duplicity. Where the disputed interpretation does not arise from a turn of events which was not anticipated but relates to a particular and mutually agreed bargain, the courts are not prepared to allow past rules to become their tyrannical masters. They will seek to reach an interpretation which represents the actual intention of the parties.

[148] It is now ten years since Lord Steyn obtained universal support for his basic proposition that the law of contract should protect the reasonable expectations of honest men and women.[87] The law of contract will not deliver on this exhortation if it is prepared to permit parties to renounce their solemn bargains. A law which accepts this response cannot meet the reasonable expectations of honest men and women. Honest men and women expect to perform the promises they have made and expect the other contracting party to do the same. The law cannot, and should not, appear indifferent to these reasonable expectations.

[149] Notwithstanding its widespread acceptance in most common law and civil jurisdictions in the world and growing judicial support,[88] the courts have not yet incorporated the doctrine of good faith into our law. There is a widespread belief that existing doctrines or judicial devices already encompass a requirement of good faith. It would, it is said, add nothing to the existing tools and principles of the common law, such as estoppel and implied terms.[89] This case serves to demonstrate that this belief is misplaced. It is clearly arguable that WDL have not acted, and are not acting, in good faith. Indeed, if such a doctrine existed in the law, it is doubtful

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87 "Contract Law: Fulfilling the Reasonable Expectations of Honest Men" (1997) 113 LQR 433.

88 See for example the observations of Bingham LJ, as he then was, in *Interfoto Picture Library Ltd v Stiletto Visual Programmes Ltd* [1989] 1 QB 433 at pp 439 and 445 (CA).

89 See for example Bridge, "Doubting Good Faith" (2005) 11 NZBLQ 426, p 428. For a refutation of this point, see Bigwood, "Symposium Introduction: Confessions of a 'Good Faith' Agnostic" (2005) 11 NZBLQ 371, pp 374 – 375.

whether the courts would have been troubled by the company's attempt to achieve an interpretation contrary to its actual intention. I would firmly hold it to that intention.

[150] I would therefore dismiss the appeal.

Solicitors:
Russell McVeagh, Auckland for Appellant
Radich Dwyer, Blenheim for Respondent