**IN THE SUPREME COURT OF NEW ZEALAND**

**SC 65/2008**
**[2010] NZSC 5**

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| | BETWEEN | VECTOR GAS LIMITED<br>Appellant |
| | AND | BAY OF PLENTY ENERGY LIMITED<br>Respondent |

Hearing: 23 June 2009

Court: Blanchard, Tipping, McGrath, Wilson and Gault JJ

Counsel: J E Hodder SC and K E Cornége for Appellant
H N McIntosh and K F M Wevers for Respondent

Judgment: 10 February 2010

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## JUDGMENT OF THE COURT

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**A The appeal is allowed.**

**B The respondent is to pay to the appellant costs of $15,000 together with reasonable disbursements as fixed by the Registrar.**

**C Costs in the lower Courts are to be fixed by those Courts in the light of this Court's judgment.**

## REASONS

**BLANCHARD J**

[1] This appeal requires the Court to interpret a gas supply contract entered into in somewhat unusual circumstances.

[2] On 8 October 2004 Chapman Tripp, the lawyers for the appellant, then known as National Gas Corporation (NGC), wrote a short letter to Russell McVeagh, the lawyers for Bay of Plenty Energy Ltd (BoPE). After acknowledging an earlier letter from the other firm, Chapman Tripp said:

> 2 Without prejudice to its position, NGC is prepared to agree to continue to supply gas based on the terms of the Agreement for Supply of Gas dated 10 October 1995 (the "Agreement") pending determination of BoPE's proceeding, or 30 June 2006, whichever is the earlier, provided that BoPE undertakes to:
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> 2.1 file that proceeding on or before 31 October 2004: and
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> 2.2 in the event that BoPE is unsuccessful in, or withdraws, that proceeding, pay NGC on demand, for each GJ supplied, the difference between the price set out in the Agreement and $6.50 per GJ, plus interest at the Interest Rate set out in the Agreement.

That offer was accepted by BoPE on the same day.

[3] BoPE was subsequently unsuccessful in its proceeding. The present issue between the parties is whether the payment BoPE must consequentially make to NGC for gas supplied to it in the meantime does or does not include the cost of transmission of that gas to the point at which it was taken by BoPE. If the price of $6.50 per gigajoule does include transmission costs BoPE will have to pay approximately $1.4 m more. If it does not include transmission costs, the additional amounts due by BoPE will be approximately $4.6 m. That difference of over $3m is substantial even when put against the payment of a little over $10m already made by BoPE at the rate under the agreement of 10 October 1995.

[4] I begin the task of interpretation by looking at ordinary meaning. "$6.50 per GJ" by itself, with reference to a gas supply, "for each GJ supplied", is perhaps more likely to be a price inclusive of supply but not necessarily so. It could be taken to be

for gas alone. There is therefore an ambiguity, although it is not essential to find an ambiguity before proceeding to look at the background to a contract to assist in interpreting the language which has been used.[1]

[5] NGC's obligation is to "continue to supply gas based on the terms" of the 1995 Agreement. It is therefore necessary, in order to start resolving the doubt about the meaning of "$6.50 per GJ," or more accurately what it includes and therefore the scope of the agreement recorded in the letter, to go to the Agreement for Supply of Gas of 10 October 1995 (the 1995 Agreement) to which the letter refers. When one does so, one finds that the price fixed under the 1995 Agreement did include the cost of transmission. That might, at first sight, appear to resolve the point in favour of BoPE. But, to correctly understand words in a contract they must be placed in their full context (famously called by Lord Wilberforce the "factual matrix"[2]) and here, as appears from the letter, that context is an interim settlement of an aspect of a larger dispute about supply under the 1995 Agreement. The letter says that what has been agreed to is without prejudice to the position of NGC in that dispute. The supply of gas pursuant to the letter is to be made "pending determination of BoPE's proceeding or 30 June 2006 whichever is the earlier".

[6] So, in order to fully understand the letter, the interpreter must refer to the 1995 Agreement and must comprehend that the larger dispute was over whether NGC had any obligation at all to continue making supply (whether the 1995 Agreement had already come to an end as a result of a notice given by NGC). The genesis of the agreement made on 8 October 2004 was the desire of the parties to decide what was to happen about gas supply pending resolution of the larger dispute. BoPE had been contending that it had a right to continued supply and had threatened to issue a proceeding to enforce that right. This is the proceeding referred to in the letter. The letter says that BoPE will file its proceeding. If it is successful in that litigation the supply is to be paid for on the terms of the 1995 Agreement. It is implicit that in the interim BoPE will pay for the gas at the rate provided for in the

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1 *Investors Compensation Scheme Ltd v West Bromwich Building Society* [1998] 1 WLR 896 (HL) at pp 912 – 913; *Chartbrook Ltd v Persimmon Homes Ltd* [2009] 1 AC 110 (HL) at para [37]; *Ansley v Prospectus Nominees Unlimited* [2004] 2 NZLR 590 (CA) at para [36] and *Franklins Pty Ltd v Metcash Trading Ltd* [2009] NSWCA 407 at [14] – [18]; [63] and [239] – [305].

2 *Reardon Smith Line Ltd v Hansen-Tangen* [1976] 1 WLR 989 (HL) at p 997.

1995 Agreement. The crux of the letter is the adjustment to be made if BoPE's proceeding on the larger dispute is unsuccessful. In that event, BoPE agrees to pay NGC the difference between "$6.50 per GJ" and the lower rate of payment under the 1995 Agreement.

[7] The words "$6.50 per GJ" also have as an important part of their context or background what both parties must have been anticipating would happen if an interim agreement were not reached. Putting oneself in the position of the parties in that circumstance, it is very easy to see that BoPE was not likely to have tolerated a situation in which supply of gas was simply withdrawn by NGC pending resolution of the dispute. Absent an interim agreement, BoPE, like any other purchaser in a similar position, would certainly have sought to have the High Court order NGC to continue to supply it on the terms of the 1995 Agreement until the Court could give judgment on the larger dispute. But, equally obviously, the Court would not make such an interim order unless BoPE gave an undertaking to meet any loss which NGC might suffer if it were ultimately found that BoPE was not entitled to a continued supply at the rate provided for under the 1995 Agreement. The negotiating parties both would also readily have perceived that the loss to NGC, and therefore what BoPE would have to pay under its undertaking, would almost certainly be measured by comparing what NGC was likely to receive on the basis of current market rates, if it sold the gas to someone else, with the price fixed under the 1995 Agreement. As Wilson J points out in his judgment,[3] in or around October 2004 NGC was managing to obtain contracts at an average price of $6.68 per GJ *plus* transmission costs. In contrast, an *inclusive* price of $6.50 per GJ was the equivalent of a gas only price of $4.64 per GJ.

[8] When this background to the agreement of 8 October 2004 is appreciated it can at once be seen that, on BoPE's contended interpretation, NGC has astoundingly elected to enter into a settlement agreement which placed it at a considerable monetary disadvantage if and when it were ultimately successful in the larger dispute, as compared with what both parties must, very realistically, have foreseen that NGC was most likely to receive in that circumstance from the undertaking

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[3] At para [111].

which would be required before BoPE could obtain injunctive relief, and thereby continued supply. BoPE's suggested interpretation of the interim agreement, which was in effect a proxy or substitute for an interim order of the Court, is thus exposed as commercially absurd. There is no reason why NGC would have elected to enter into an interim agreement on such an extremely unfavourable basis when allowing the matter to go to court would have produced a much more favourable outcome for it. The suggestion that it might perhaps have done so in order to preserve its reputation is fanciful, as Wilson J concludes.[4]

[9] Therefore, unless there has been a mistake (but none has been pleaded and rectification has seemingly been sought only as a precaution and far too late, after the hearing in this Court), the only commercially sensible conclusion is that the interim agreement, and therefore the price of $6.50 per GJ, was not intended to cover anything other than the price of the gas itself, with transmission costs to be met separately. That explanation is far more probable than the one suggested by BoPE, even giving due weight to Lord Hoffmann's observation in *Chartbrook Ltd v Persimmon Homes Ltd*[5] that the fact that a contract may appear to be unduly favourable to one of the parties is not a sufficient reason for supposing that it does not mean what it says.

[10] As I have said, the interim agreement was plainly a proxy for what the Court would almost inevitably require from BoPE if it were to grant an interim injunction restraining NGC from terminating supply. The difference between the terms of the projected undertaking and the terms of the interim agreement, if the latter were to be given BoPE's interpretation, cannot be regarded as merely the product of a bad deal from NGC's point of view. No party in its position, acting rationally, would ever in these circumstances have agreed to give up recovery from BoPE of the transmission costs or, putting it another way, would have agreed to discount the current market price by the equivalent of the transmission costs.

[11] Lord Hoffmann remarked in the fifth principle of his statement of interpretation in *Investors Compensation Scheme Ltd v West Bromwich Building*

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4 At para [138].
5 [2009] 1 AC 110 at para [20].

*Society*, that if one would conclude from the background that something must have gone wrong with the language, the law does not require judges to attribute to parties an intention which they plainly could not have had.[6] The same is true where the language is per se apt and the issue is what it encompasses. In this case the business commonsense of the matter leads to the conclusion that "$6.50 per GJ" was not intended to cover anything other than the price of the gas itself.

[12] If the material before the Court consisted only of what has already been described, I would therefore already conclude that "$6.50 per GJ" was the price of the gas alone and that transmission costs were additional and were to be fixed on a quantum meruit, in the absence of an agreement relating to them. There is also evidence that NGC had posted prices for transmission costs. The parties accepted those prices for the purpose of BoPE making a payment to NGC after the High Court judgment was delivered finding in favour of NGC. In the circumstances there is no need to explore further that question of quantum.

[13] The conclusion to which I have already come about the meaning of "$6.50 per GJ" is merely reinforced if reference is made to the negotiations between the parties which led to the letter of 15 October 2004. The traditional view has been that it is impermissible to have regard to negotiations when interpreting a contract. The House of Lords has recently confirmed that view in *Chartbrook* and it continues to hold sway in Australia.[7] It is not, however, an absolute rule of exception. It has no application when the negotiations are considered "not in order to provide a gloss on the terms of the contract, but rather to establish the parties' knowledge of the circumstances with reference to which they use the words in the contract".[8] Those circumstances include, just as much as "the genesis of the transaction, the background, the context, the market in which the parties are operating",[9] the subject

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6 At p 913, citing *Antaios Compania Naviera SA v Salen Rederiera AB* [1985] AC 191 at p 201 per Lord Diplock. See also *Commissioner of Inland Revenue v Renouf Corporation Ltd* (1998) 18 NZTC 13,914 (CA) at p 13,918.

7 *Codelfa Construction Pty Ltd v State Rail Authority of New South Wales* (1982) 149 CLR 337.

8 *Bank of Scotland v Dunedin Property Investment Co Ltd* 1998 SC 657 at p 665 per Lord President (Rodger).

9 *Reardon Smith* at pp 995 – 996 per Lord Wilberforce.

matter of the intended contract as Mason J made clear in *Codelfa Construction Pty Ltd v State Rail Authority of New South Wales*:[10]

> Obviously the prior negotiations will tend to establish objective background facts which were known to both parties and the subject matter of the contract. To the extent to which they have this tendency they are admissible.

[14] The scope of the subject matter in part defines "the commercial or business object of the transaction objectively ascertained", which Lord Wilberforce himself in *Prenn v Simmonds*[11] considered to be a surrounding fact to which reference could be made. Differing in this respect from the view McGrath J takes as to the extent of what he calls the "subject matter exception",[12] I see no reason why it can be called in aid, if necessary, for the purpose of ascertaining that the contract was concerned with a gas supply but not to learn that it dealt with gas only. If there is, as I think, a subject matter exception, there cannot sensibly be degrees of subject matter. There is of course an important qualification that any material which is simply declarative of the subjective intentions of one party must be disregarded. But there is no reason in principle why the Court should not have regard to communications between the parties for the light they may throw upon the objective commercial purpose and, in particular, what ground the contract was to cover. The question of how much further the courts of this country should go towards admitting evidence of negotiations for the light they may shed on the objective intention of the parties can be left for another day.

[15] In this case, a reading of the critical letters of 28 September 2004 from NGC to BoPE and Russell McVeagh's reply of 5 October 2004 on behalf of BoPE leaves me in no doubt that thereafter the parties had put the question of transmission costs to one side and were focused on terms for the gas alone, should BoPE's foreshadowed legal proceeding be unsuccessful. Despite Mr McIntosh's efforts to the contrary, in which he was distinctly hampered by having been a party to the letters in question, I am unpersuaded that on an objective reading of the reply of 5 October 2004 it can fairly be taken as bringing the transmission costs back within the scope of the interim contract which was being negotiated. I agree with the

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10 At p 352.
11 [1971] 1 WLR 1381 (HL).
12 At para [83].

analysis of that reply made by Tipping J at paras [44] – [46] of his reasons and by Wilson J at para [143] of his reasons.

[16] I would allow the appeal and restore the judgment of Harrison J on NGC's counterclaim. I would award the appellant costs of $15,000 in this Court together with its reasonable disbursements as fixed by the Registrar, with costs in the lower Courts to be fixed by those Courts in the light of this Court's judgment.

**TIPPING J**

**Introduction**

[17] This case concerns the interpretation of a contract for the supply of gas. The question is whether the expression "$6.50 per gigajoule" means that the respondent purchaser (BoPE) must pay the appellant supplier (NGC) $6.50 plus transmission charges of approximately $1.86 per gigajoule, for each gigajoule of gas supplied, or simply $6.50 per gigajoule on the basis that NGC is responsible for supplying the gas at its expense to BoPE's premises within that price. The High Court held[13] that it was the former, that is $6.50 plus transmission costs. The Court of Appeal allowed an appeal by BoPE,[14] accepting its submission that it was the latter. NGC appeals to this Court seeking the reinstatement of the High Court's determination.

[18] The case raises issues concerning the proper approach to interpretation questions and the admissibility of extrinsic evidence, particularly evidence concerning prior negotiations when a written contract is being interpreted. Before addressing the facts in more detail, I will examine the legal principles against which the interpretation question must be determined.

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13 *Bay of Plenty Electricity Ltd v Vector Gas Ltd* (High Court, Wellington, CIV-2004-485-002287, 3 August 2007, Harrison J).

14 *Bay of Plenty Electricity Ltd v Vector Gas Ltd* [2008] NZCA 338 (Chambers, Ellen France and Baragwanath JJ).

## Legal principles

[19] The ultimate objective in a contract interpretation dispute is to establish the meaning the parties intended their words to bear. In order to be admissible, extrinsic evidence must be relevant to that question.[15] The language used by the parties, appropriately interpreted, is the only source of their intended meaning. As a matter of policy, our law has always required interpretation issues to be addressed on an objective basis. The necessary inquiry therefore concerns what a reasonable and properly informed third party would consider the parties intended the words of their contract to mean. The court embodies that person. To be properly informed the court must be aware of the commercial or other context in which the contract was made and of all the facts and circumstances known to and likely to be operating on the parties' minds. Evidence is not relevant if it does no more than tend to prove what individual parties subjectively intended or understood their words to mean, or what their negotiating stance was at any particular time.[16]

[20] Although subjective evidence would be relevant if a subjective approach were taken to interpretation issues,[17] the common law has consistently eschewed that approach. The common law focuses strongly on the agreement in its final form as representing the ultimate consensus of the parties. Hence it is regarded as irrelevant how the parties reached that consensus. To inquire into that process would not be consistent with an objective inquiry into the meaning of a document which is

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15 Support for relevance being the basis and criterion for the admissibility of extrinsic evidence comes from *Bank of Credit and Commerce International SA v Ali* [2002] 1 AC 251 at para [39] per Lord Hoffmann, explaining his reference to "absolutely anything" in *Investors Compensation Scheme Ltd v West Bromwich Building Society* [1998] 1 WLR 896 at p 913.

16 When Lord Wilberforce said in *Prenn v Simmonds* [1971] 1 WLR 1381 (HL) at p 1384 that the reason for excluding evidence of prior negotiations was "simply that such evidence is unhelpful", he must have been reflecting the underlying point that the evidence was unhelpful because it was irrelevant. Compare Lord Hoffmann's statement in *Chartbrook Ltd v Persimmon Homes Ltd* [2009] 1 AC 1101 at para [32] and his statement at para [34] that "as Lord Wilberforce said, inadmissibility is normally based in irrelevance". He added more controversially that inadmissibility can sometimes only be justified on pragmatic grounds.

17 Such as is taken in French law which treats what the parties intended as a question of subjective fact unaffected by any constructional rules. The French approach was heavily influential in the drafting of the *Unidroit Principles of International Commercial Contracts* (1994 and 2004 revision) which allow reference to prior negotiations (art 4.3). But that is not the common law way.

generally designed to be the sole record of the final agreement.[18] A party cannot be heard to say – never mind what I signed, this is what I really meant.

[21] The objective approach is regarded as having two principal advantages. These are greater certainty and the saving of time and cost: greater certainty, because the subjective approach is apt to undermine the security of the written words by means of which the parties recorded their consensus; and saving time and cost, because a subjective approach is generally thought to require a fuller search for and examination of extrinsic evidence. A lesser, but still significant, perceived advantage is avoiding the effect a subjective approach might have on third parties who may have relied on what the words of the document appeared objectively to mean. But, despite its eschewing a subjective approach, the common law does not require the court, through the objective method, to ascribe to the parties an intention that a properly informed and reasonable person would not ascribe to them when aware of all the circumstances in which the contract was made.

[22] Nor does the objective approach require there to be an embargo[19] on going outside the terms of the written instrument when the words in issue appear to have a plain and unambiguous meaning.[20] This is because a meaning that may appear to the court to be plain and unambiguous, devoid of external context, may not ultimately, in context, be what a reasonable person aware of all the relevant circumstances would consider the parties intended their words to mean.[21] An example of that situation is when plain words, read contextually, lead to a result which does not

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[18] The position is, of course, different if the contract is said to have been partly oral and partly written. It is not, however, different just because the ultimate consensus is recorded in an exchange of letters as opposed to a formal document executed by each party.

[19] The so-called plain meaning rule: see for example *Benjamin Developments Ltd v Robt Jones (Pacific) Ltd* [1994] 3 NZLR 189 (CA); *Melanesian Mission Trust Board v Australian Mutual Provident Society* [1997] 1 NZLR 391 (PC) at pp 394 – 395; and the discussion in Burrows, Finn and Todd, *Law of Contract in New Zealand* (3 ed, 2007), para [6.2.2(b)].

[20] See *Investors Compensation Scheme Ltd* at pp 912 – 913 and *Chartbrook* at para [37] which represent a clear retreat from the earlier plain meaning rule, and *Ansley v Prospectus Nominees Unlimited* [2004] 2 NZLR 590 (CA) at para [36] per Gault P.

[21] See Burrows, Finn and Todd, para [6.2.2(c)].

make sense, whether commercially or otherwise: a meaning that flouts business commonsense must yield to one that accords with business commonsense.[22] The appropriate contextual meaning, if disputed, will, almost invariably, involve consideration of facts and circumstances not apparent solely from the written contract. While displacement of an apparently plain and unambiguous meaning may well be difficult as a matter of proof, an absolute rule precluding any attempt would not be consistent either with principle or with modern authority.

[23] The proposition that a party may not refer to extrinsic evidence "to create an ambiguity"[23] is at least potentially misleading. It does not mean context is irrelevant unless there is a patent ambiguity. Context is always a necessary ingredient in ascertaining meaning. You cannot claim to have identified the intended meaning without reference to context. Hence it is always permissible to go outside the written words for the purpose of identifying the context in which the contract was made and its objective purpose. While there are no necessary preconditions which must be satisfied before going outside the words of the contract,[24] the exercise is and remains one of interpretation. Subject to the private dictionary and estoppel exceptions to be mentioned below, it is fundamental that words can never be *construed*[25] as having a meaning they cannot reasonably bear. This is an important control on the raising of implausible interpretation arguments. Furthermore, the plainer the words, the more improbable it is that the parties intended them to be understood in any sense other than what they plainly say.

[24] In some recent cases it has been suggested that contractual context should be

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22 See *Antaios Compania Naviera SA v Salen Rederierna AB, The Antaios* [1985] AC 191 at p 201 per Lord Diplock. There is now a developing literature about interpretation issues. See, for example, Steyn, "The Intractable Problem of the Interpretation of Legal Texts" (2003) 25 Sydney L Rev 5, p 6 and the cases there cited; Hoffmann, "The Intolerable Wrestle with Words and Meanings" (1997) 114 S Afr LJ 656; Kirby, "Towards a Grand Theory of Interpretation: The Case of Statutes and Contracts" (2002) 24(2) Stat LR 95; Nicholls, "My Kingdom for a Horse: The Meaning of Words" (2005) 121 LQR 577.

23 See *Potter v Potter* [2003] 3 NZLR 145 (CA) at para [34] per Fisher J.

24 For an early articulation of this proposition see the statement of Lord Justice-Clerk Moncreiff in *Inglis v John Buttery & Co* (1877) 4th Series, vol 5, R 58 at p 64 (approved by Lord Blackburn in the same case (1878) 3 App Cas 552 at p 577) that the Court was entitled to be placed in the position in which the parties stood before they signed whether their words "be clear and distinct or the reverse".

25 As opposed to the contract being rectified so as to achieve the intended meaning or outcome.

referred to as a "cross-check".[26] In practical terms this is likely to be what happens in most cases. Anyone reading a contractual document will naturally form at least a provisional view of what its words mean, simply by reading them. That view is, in a sense, then checked against the contractual context. This description of the process is valid, provided the initial view is provisional only and the reader is prepared to accept that the provisional meaning may be altered once context has been brought to account. The concept of cross-check is helpful in affirming the point made earlier that a meaning which appears plain and unambiguous on its face is always susceptible to being altered by context, albeit that outcome will usually be difficult of achievement. Those attempting the exercise unsuccessfully may well have to pay for the additional costs caused by their attempt.

[25] A private dictionary meaning is a meaning the words linguistically cannot reasonably bear. It is, nevertheless, open to a party to show that, despite that fact, the parties intended their words to have that special meaning for the purposes of their contract. This represents a consensual parallel with cases in which words have a special meaning by trade custom.[27] It can also be regarded as a linguistic example of estoppel by convention.[28] The estoppel prevents the accepted special meaning from later being disavowed. Estoppels can also arise in interpretation cases not involving a special meaning. They are then normally based on a common assumption or representation as to meaning.

[26] If parties wish, they may contract on the basis that black means white; albeit the unlikelihood of their doing so, without expressly saying so, will no doubt be a powerful factor when it comes to questions of proof. Whether the parties have adopted a private dictionary meaning must be determined objectively in the same way as other disputes as to meaning are determined.

[27] Against that background I come to the subject of the admissibility of prior negotiations. Some of the difficulties in this area may derive from the concept of "prior negotiations" being employed in a more or less expansive way. Sometimes

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[26] See *Pyne Gould Guinness Ltd v Montgomery Watson (NZ) Ltd* [2001] NZAR 789 (CA) at para [29] and Burrows, Finn and Todd, para [6.2.2(e)].

[27] For example, the baker's dozen.

[28] *Air New Zealand Ltd v Nippon Credit Bank Ltd* [1997] 1 NZLR 218 (CA).

the concept seems to be used as if it encompassed all conduct and circumstances associated with negotiations towards the formation of a contract. It is necessary, however, to distinguish between the subjective content of negotiations; that is, how the parties were thinking, their individual intentions and the stance they were taking at different stages of the negotiating process on the one hand, and, on the other, evidence derived from the negotiations which shows objectively the meaning the parties intended their words to convey. Such evidence includes the circumstances in which the contract was entered into, and any objectively apparent consensus as to meaning operating between the parties.

[28] The vice in admitting subjective evidence of negotiations, is that doing so would be inconsistent with the objective basis on which interpretation issues are resolved. As already seen, evidence of a party's subjective intention is not relevant to an objective resolution of interpretation issues. Although the common law takes the view that it is only the final written contract which records the ultimate consensus of the parties, the way that consensus is expressed may be based on an agreement as to meaning reached during negotiations.

[29] There is no problem with objective evidence directed to the context, factual or linguistic, in which the negotiations were taking place. That kind of evidence can properly inform an objective approach to meaning. Whereas evidence of the subjective content of negotiations is inadmissible on account of its irrelevance, evidence of facts, circumstances and conduct attending the negotiations is admissible if it is capable of shedding objective light on meaning.[29] It is often said in contract interpretation cases that evidence of surrounding circumstances is admissible. Circumstances which surround the making of the contract can operate both before and after its formation. In either case irrelevance should be the touchstone for the exclusion of evidence. I do not consider there are any sufficiently persuasive

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[29] This approach is consistent with Lord Hoffmann's statement in *Chartbrook* at para [33] that evidence of prior negotiations is admissible "as part of the background which may throw light upon what [the parties] meant by the language they used". This statement was in the context of this approach to admissibility not being inconsistent with the English objective theory of contractual interpretation. Hence, when speaking of background, Lord Hoffmann was clearly focusing on objective matters of fact as part of that background.

pragmatic grounds on which to exclude evidence that is relevant.[30] Indeed to do so would require reconciliation with s 7 of the Evidence Act 2006.[31]

[30] In *Gibbons Holdings Ltd v Wholesale Distributors Ltd*[32] I expressed the view that evidence of subsequent conduct should be admissible, if capable of providing objective guidance as to intended meaning.[33] I suggested that, in order to be admissible, post-contract conduct should be shared or mutual.[34] I saw that as a way of emphasising the need to exclude evidence which demonstrated only a party's subjective intention or understanding as to meaning. I now consider that the approach I am taking in these present reasons is a simpler and clearer articulation of the appropriate principle, but one which still preserves the essential line between subjectivity and objectivity of approach.

[31] There is no logical reason why the same approach should not be taken to both post-contract and pre-contract evidence. The key point is that extrinsic evidence is admissible if it tends to establish a fact or circumstance capable of demonstrating objectively what meaning both or all parties intended their words to bear. Extrinsic evidence is also admissible if it tends to establish an estoppel or an agreement as to meaning. Such an agreement can demonstrate a special (private dictionary) meaning or an accepted meaning of words which would otherwise be ambiguous. I should expand a little on the latter proposition.

[32] If the parties have reached agreement on what meaning an otherwise ambiguous word or phrase should have for their purposes, that definitional agreement is itself an objectively determinable fact. When the issue is which of two possible meanings is objectively the more probable, the existence of a definitional

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30 To the extent that Lord Hoffmann appears to suggest that relevant evidence should be excluded on pragmatic grounds at para [34] of his speech in *Chartbrook* I respectfully disagree. I am not, however, entirely clear whether his Lordship was at this point speaking of evidence of previous negotiations that demonstrate only subjective intentions or, rather, was suggesting that some evidence demonstrating a matter of objective context should be excluded for pragmatic reasons. If it was the former, the evidence would, in any event, be inadmissible for irrelevancy and no pragmatic grounds would need to be invoked.

31 Section 7 provides that all relevant evidence is admissible unless specifically declared inadmissible or excluded in particular circumstances which do not encompass contractual interpretation issues.

32 [2008] 1 NZLR 277 (SC).

33 At paras [52] – [53].

34 At paras [52] – [53].

agreement is obviously relevant, indeed it should be decisive. There is no logic in ascribing a meaning to the parties if it is objectively apparent they have agreed what that meaning should be.

[33] The foregoing analysis recognises that, generally speaking, issues of contractual interpretation arise in three circumstances: mistake; ambiguity; and special meaning. A mistake can represent either a drafting error or a linguistic error. Errors of this kind are primarily the subject of rectification. But a clear drafting or linguistic error, combined with equal clarity as to what was intended, can be remedied by way of interpretation, and in that respect context can and should be taken into account.[35] An ambiguity arises when the language used is capable of more than one meaning, either on its face or in context, and the court must decide which of the possible meanings the parties intended their words to bear. A special meaning exists when the words used, even after the contractual context is brought to account, are linguistically still capable of only one meaning or are wholly obscure; but it is nevertheless evident from the objective context that the parties, by custom, usage or agreement, meant their words to bear a meaning which is linguistically impossible (for example, black means white), or represents a specialised and generally unfamiliar usage.

[34] Although an estoppel will usually arise from the adoption of a special meaning, it is in cases where words are capable of bearing more than one meaning that estoppel is likely to have its primary application. A party may be estopped from denying that one of two possible meanings was the meaning the parties intended their words to bear.[36] This, or an agreement as to meaning, is the best analysis of the controversial decision of Kerr J in the *Karen Oltmann*.[37]

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35 See *East v Pantiles (Plant Hire) Ltd* (1981) 263 EG 61 per Brightman J and in New Zealand *Rattrays Wholesale Ltd v Meredyth-Young & A'Court Ltd* [1997] 2 NZLR 363 (HC) at pp 371 – 372. The later cases of *KPMG LLP v Network Rail Infrastructure Ltd* [2007] Bus LR 1336 at para [50] per Carnwarth LJ; and *Chartbrook* at para [23] per Lord Hoffmann, adopted and refined Brightman J's original formulation.

36 See *Norwegian American Cruises v Paul Mundy Ltd (The Vistafjord)* [1988] 2 Lloyd's Rep 343 (CA).

37 *Partenreederei MS Karen Oltmann v Scarsdale Shipping Co Ltd* [1976] 2 Lloyd's Rep 708. See also Steyn (op cit, note 22) and McLauchlan, "Common Assumptions and Contract Interpretation" (1997) 113 LQR 237.

[35] That case concerned a time charter of a vessel for two years. The issue was whether the words in a break clause "after 12 months trading" meant "on the expiry of 12 months" or "at any time after the expiry of 12 months". Evidence of negotiations (in the form of telexed exchanges) was admitted by Kerr J on the following basis:[38]

> If a contract contains words which, in their context, are fairly capable of bearing more than one meaning, and if it is alleged that the parties have in effect negotiated on an agreed basis that the words bore only one of the two possible meanings, then it is permissible for the Court to examine the extrinsic evidence relied upon to see whether the parties have in fact used the words in question in one sense only, so that they have in effect given their own dictionary meaning to the words as the result of their common intention.

[36] The *Karen Oltmann* is sometimes referred to as a special (private dictionary) meaning case because of Kerr J's reference to the parties' "own dictionary meaning". But I agree with the House of Lords in *Chartbrook*[39] that this is not its true basis. The case was one where the word "after" was, on its face, capable of two meanings. If the parties agreed or represented to each other in the telexes that the word "after" meant "on the expiry of" and the agreement or representation was relied on when they entered into the time charter, the parties were each estopped by that agreement or representation from contending that the word "after" bore the alternative meaning. Indeed, on the basis discussed earlier, they were bound by any such definitional agreement.

[37] Of course, the court must be satisfied that an agreement or representation as to meaning, reached or made during negotiations, was still operating at the time the contract was formed and represented a linguistic premise on which it had been formed. The *Karen Oltmann* was correctly decided; but on the basis of agreement or estoppel as to meaning, not on the basis of special meaning. There was nothing special about the meaning of the word "after". It was, however, capable of two meanings. The parties had consensually resolved which meaning was to apply, or an estoppel had been created, and evidence to that effect was admissible.

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38 At p 712.

39 At para [45] per Lord Hoffmann.

**This case**

[38] Against that legal background, I return to the facts. Wilson J has described the general circumstances in which the interpretation issue has arisen. I will not repeat that exercise beyond what is necessary to explain my views. BoPE disputed NGC's termination of the principal agreement. It was necessary for the parties to resolve issues of supply pending the resolution of that dispute. Had BoPE sought an interim injunction requiring supply to be maintained in the meantime, it would have been obliged to give an undertaking to pay damages should its challenge to NGC's termination fail. Those damages would have been calculated on the basis of the difference between the price payable under the principal contract and the market price for the period in question. Whereas the price under the principal contract was a dollar figure inclusive of supply costs, NGC's pricing at the time the contract was terminated had become a dollar figure plus supply costs.

[39] It is inherently most unlikely that NGC would have been willing to enter into any interim arrangement on a basis which was less favourable to it than an undertaking as to damages would have been. This means that commercially the inherent probabilities were that the interim agreement would be on the basis of a dollar figure plus supply costs. This is because the interim agreement was designed to be a commercial substitute for the undertaking BoPE would have been obliged to give if it obtained an interim injunction requiring supply in the meantime. That is the context in which the exchange of correspondence between the parties which led to the agreement should be interpreted.

[40] Before I address that correspondence, I should make a point about the crucial expression "$6.50 per gigajoule". Although it does not ultimately matter for interpretation purposes, I do not consider it can be said, as BoPE suggested, that the expression had a plain and unambiguous meaning. In itself the expression could have meant either $6.50 per gigajoule of gas supplied to BoPE's premises or $6.50 for a gigajoule of gas with transmission/delivery costs payable in addition. When one views the expression in the context of the key letter of 5 October read as a whole, the ambiguity remains. The reference to the interim supply agreement being "based on the terms of" the principal agreement suggests that the sum of $6.50 included delivery costs.

On the other hand, the earlier reference to $6.50, on the first page of the letter, as I shall explain, clearly suggests that the sum of $6.50 was exclusive of delivery costs. Hence, both in itself and in the context of the key letter, the expression $6.50 per gigajoule was ambiguous. It is only when reference is made to the wider commercial context and the previous correspondence that it becomes clear in what sense the parties should be taken to have been using the disputed expression.

[41] On 28 September 2004 NGC wrote to BoPE offering to settle the dispute overall and, if that were not possible, to supply gas in the interim at $6.50 per gigajoule. In its letter, under the separate heading "transportation and metering", NGC said:

> If the above offer is acceptable to you, we should meet [to] discuss what the transmission and metering arrangements will be. These are likely to take into account historic usage and transmission posted pricing.

[42] BoPE replied to NGC's letter through its solicitors, Russell McVeagh. Their letter of 5 October 2004 contained the following paragraphs:

> 4. The issue therefore arises as to a supply of gas for BoPE pending determination of the litigation. In that regard, we record the parties' positions as follows:
>
> (a) NGC:
>
> (i) Has, by your letter noted above, confirmed, on the record:
>
> (aa) that it has sufficient gas available to supply to BoPE for at least the interim period (and, indeed, for the remainder of the term of the Agreement, and beyond); and
>
> (bb) the sale price of the gas in question (ie $6.50 per GJ), thereby quantifying the loss that NGC perceives either party will suffer, depending on the outcome of the litigation.
>
> (ii) Is probably protected from any claim BoPE brings against it for actual loss suffered by way of increased price, by the limitation of liability clause in the Agreement.
>
> (b) BoPE, on the other hand:
>
> (i) cannot currently source an equivalent alternative supply of gas for the remainder of the term of the

Agreement; and

(ii) would in any event probably be barred from recovery of its loss on such an alternative supply by the limitation clause, such that damages for wrongful breach by NGC would not in this case be an adequate remedy.

5. In those circumstances, it would seem that the best course for the parties, in lieu of Todd having to apply for interim injunctive relief, would be for:

(a) NGC to undertake, without prejudice to its position, to simply continue to supply gas on the basis of the Agreement pending determination of BoPE's proceeding as above.

(b) BoPE to undertake to:

(i) file that proceeding on or before 31 October 2004; and

(ii) in the event that BoPE is unsuccessful on its proceeding or withdraws it:

(aa) pay NGC on demand, for each GJ supplied, the difference between the Agreement price and $6.50 (or the current market price, whichever is the lower), plus interest, or

(bb) at BoPE's election, provide NGC with an equivalent amount of gas as taken by BoPE from 1 November 2004, (if: (i) such gas is available from other gas fields; and (ii) Maui open access allows that gas to be transmitted to market.

[43] Paragraph 4(a)(i)(bb) refers to the sale price of the gas in question as being $6.50 per GJ (gigajoule). That, as a recital of NGC's position, can only have meant $6.50 for the gas itself with transmission costs to be paid in addition. If it did not mean that, it would have misrepresented the position NGC took in its letter of 28 September 2004. The point is reinforced by the subsequent words "thereby quantifying the loss". Unless $6.50 per GJ meant that amount for the gas plus transmission costs, it would not truly have quantified NGC's loss. BoPE did not ultimately dispute that the reference to $6.50 per GJ in paragraph 4(a)(i)(bb) was a reference to $6.50 for the gas itself with transmission costs being payable in addition.

[44] In paragraph 5, which is on the second page of Russell McVeagh's letter of 5 October 2004, there is a further reference in (b)(ii)(aa) to $6.50 for each GJ supplied. BoPE's argument is that, whereas the reference on the first page of the letter in paragraph 4 to $6.50 meant $6.50 plus transmission costs, the same reference to $6.50 on the second page in paragraph 5 meant $6.50 inclusive of transmission costs. This was signalled, so the argument ran, by the words in paragraph 5(a) "on the basis of the Agreement", meaning on the basis of the principal agreement where the dollar figure for gas supplied was expressed on a basis which included transmission costs.

[45] I am of the view that no reasonable reader of Russell McVeagh's letter of 5 October, aware of the commercial context in which the correspondence was taking place, and reading that letter as a whole, would have made the astute distinction which BoPE's argument involves. The first reference to $6.50 per GJ in that letter, reciting NGC's position, is beyond doubt a reference to $6.50 plus transmission costs, because that is what NGC was proposing in its letter of 28 September, and Russell McVeagh's letter of 5 October was, in paragraph 4, purporting to record that position. It is altogether too subtle, indeed some might say too clever, a point to suggest that the second reference to $6.50 for each GJ supplied should have been understood to mean $6.50 inclusive of transmission costs. The words "on the basis of the Agreement" cannot possibly, in context, be regarded as flagging such a fundamental change in meaning. In context they can only be understood to have meant otherwise on the basis of the principal agreement, that is, in all respects other than price. I consider a reasonable and properly informed reader would undoubtedly have understood BoPE to be agreeing to pay $6.50 plus transmission costs for the gas to be supplied in terms of any acceptance of the offer made in Russell McVeagh's letter of 5 October. At this point there was objectively a consensus as to what the expression $6.50 per GJ meant.

[46] That construction is entirely consistent with and supported by the commercial context, the agreement being a substitute for an injunction and undertaking as to damages. The construction proposed by BoPE would be wholly inconsistent with the commercial context. Indeed it would involve a concession by NGC for which

there was no commercial rationale. Like Wilson J, I regard the proposition that there was a valid reputational reason for NGC to make the concession inherent in BoPE's suggested meaning as far fetched and unpersuasive. When agreement was ultimately reached in subsequent correspondence on the terms of the interim agreement with the supply price being expressed as $6.50 per GJ, that expression of the price was clearly intended to carry the same meaning as it did in the crucial letter of 5 October.

[47] The letters to which I have referred were part of a sequence containing negotiations leading up to the final agreement reached by means of a letter from Chapman Tripp, now representing NGC, to Russell McVeagh written on 15 October 2004. It is clearly apparent, on an objective basis, that the parties had reached an agreement during the negotiations as to what meaning the expression $6.50 per GJ should bear for the purposes of the contract they ultimately entered into. That agreement was still operating when the final agreement was reached. At the very least, BoPE, by means of Russell McVeagh's letter of 5 October, read as a whole and in context, represented to NGC that $6.50 per GJ was to be understood as meaning $6.50 exclusive of transmission costs which were to be paid in addition. The parties proceeded to conclude their arrangement on that premise.

[48] If the case is analysed as one of estoppel, I do not consider this estoppel had to be pleaded. There can be no question of surprise. It was inherent in NGC's case that the parties were either agreed on the meaning NGC asserted or that BoPE could not deny NGC's asserted meaning. In any event, BoPE cannot be prejudiced by NGC now being allowed to raise an estoppel. The point is not one which could have been countered by the calling of further evidence. It arises from the terms of the correspondence which passed between the parties.

[49] The conclusion I have reached differs from that reached by the Court of Appeal. The key point of principle on which I respectfully differ from that Court concerns their decision to limit reference to the correspondence which led up to the agreement.[40] The Court excluded reference to the crucial letter of 5 October. The

[40] At para [91].

Court of Appeal took as its starting point the letter of 8 October, which replied to that letter. The Court's reason for this approach was that it saw the letter of 8 October as effectively resuming negotiations after Russell McVeagh, for BoPE, had rejected the proposal made by NGC in its letter of 28 September. That analysis overlooks the fact that NGC's settlement proposal was two-pronged. First, it contained a proposal for an overall settlement which BoPE rejected. But it also contained a proposal for an interim settlement which was the subject of reply in Russell McVeagh's letter of 5 October. The letter of 8 October written by Chapman Tripp, on behalf of NGC, was in response to the letter of 5 October. The effect of the Court of Appeal's approach was to draw a line between what was in effect offer and acceptance. That, with respect, represents a most unusual way of approaching the ambit of correspondence leading up to the formation of a contract.

[50] I also consider that the Court of Appeal erred in the weight it placed on so-called "reputational matters" as a reason why NGC might be willing to accept, by way of agreement, an outcome substantially less favourable than what it was likely to have achieved pursuant to an undertaking as to damages.[41] For this reason the Court of Appeal failed to take sufficient account of the commercial context in which the agreement was made.

[51] Before closing these reasons, I wish to associate myself with the remarks made by Wilson J at the end of his reasons. Those who practice as litigators in firms and who have been involved in correspondence between the parties, should not appear as counsel if the correspondence with which they are associated is in issue in the litigation. In this case Mr McIntosh is shown as the lead author of the key letter of 5 October which, on BoPE's stance, could be viewed as setting a trap. That is the letter in which the expression "$6.50 per GJ" was said to have fundamentally changed its meaning from page 1 to page 2. The text of this letter was central to the litigation.

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41 At para [93].

[52] For the reasons I have given, I consider that the Court of Appeal erred in reversing Harrison J's interpretation of the agreement between the parties. I would allow the appeal with costs, and reinstate the determination of the High Court.

**McGRATH J**

**Introduction**

[53] The issue for the Court is whether the agreed price for supply of gas by the appellant Vector Gas Limited, formerly NGC New Zealand Limited, (NGC) covered its transmission to the premises of Bay of Plenty Energy (BoPE) at Edgecumbe, or whether an additional payment must be made on that account by BoPE to NGC. In the High Court Harrison J decided that BoPE was bound to pay an additional sum for transmission of the gas on top of the agreed purchase price of $6.50 per GJ.[42] The Court of Appeal reached the contrary conclusion.[43]

**Background**

[54] I adopt the outline of background facts appearing in the reasons for judgment of Wilson J. The question turns on the meaning of the terms of an agreement reached in an exchange of correspondence on 15 October 2004 between Chapman Tripp on behalf of NGC and Russell McVeagh on behalf of BoPE. The agreement was an interim one which was to apply pending determination by the High Court of a dispute over whether NGC had earlier lawfully terminated a gas supply agreement which had been entered into between the parties in 1995 and was not due to expire until 30 June 2006. The key passage in Chapman Tripp's letter reads:

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42 *Bay of Plenty Electricity Ltd v Vector Gas Ltd* (High Court, Wellington, CIV-2004-485-2287, 3 August 2007, Harrison J).

43 *Bay of Plenty Electricity Ltd v Vector Gas Ltd* [2008] NZCA 338 (Chambers, Ellen France and Baragwanath JJ).

> 2 … For the avoidance of doubt, the terms of the proposal are set out in full below. Please can you confirm BoPE's agreement to the terms of the proposal by return.
>
> 3 Without prejudice to its position, NGC will continue to supply gas based on the terms of the Agreement for Supply of Gas dated 10 October 1995 (the "Agreement") pending determination of BoPE's proceeding, or 30 June 2006, whichever is the earlier, provided that BoPE undertakes to:
>
> 3.1 file that proceeding on or before 31 October 2004; and
>
> 3.2 in the event that BoPE is unsuccessful in, or withdraws, that proceeding, pay NGC on demand, for each GJ supplied, the difference between the price set out in the Agreement (as escalated) and $6.50 per GJ, plus interest at the Interest Rate set out in the Agreement, …

[55] In their reply of the same date, Russell McVeagh accepted these terms on behalf of BoPE.

[56] Under these terms NGC was bound to continue to supply gas to BoPE, pending determination by the High Court of the lawfulness of the termination of the earlier agreement. If, as transpired, BoPE failed to establish that the termination was unlawful, it became required to pay NGC $6.50 per GJ for gas that had been supplied under the interim agreement. That agreement made no specific reference to whether that price covered transmission of gas to Edgecumbe. Supply was, however, expressed to be "based on the terms of" the 1995 agreement. That directs inquiry as to any terms concerning the transmission of gas to the 1995 agreement, which provides that the point of supply is at BoPE's premises at Edgecumbe and that transmission to that point is included in the price for supply. Accordingly, the ordinary meaning of the language of the interim agreement, through its incorporation of the terms of the 1995 agreement, is that BoPE is entitled to have the gas it purchases transmitted to its facility for the agreed price. I agree with the Court of Appeal that the meaning of the letter of 15 October 2004 is plain; there is no ambiguity in this respect.[44]

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[44] At para [92].

**Contextual interpretation of commercial agreements**

[57] The ordinary meaning of the text of a commercial agreement, however, is the result of an abstract analysis of the language, without regard to wider influences on meaning. During the past 40 years the common law has retreated from an earlier prevailing view that construction of commercial agreements turns on plain and ordinary meaning so that extrinsic evidence is superfluous. Courts have come to recognise that an understanding of the meaning of language is enhanced in all situations by the awareness of context. They have moved to make greater use of material which indicates the purpose of the parties in order to determine disputed questions of meaning of the language. It is now seen as necessary, as Lord Wilberforce said in delivering the judgment of the House of Lords in *Prenn v Simmonds* in 1971, to place the contractual language in its context and to:[45]

> inquire beyond the language and see what the circumstances were with reference to which the words were used, and the object, appearing from those circumstances, which the person using them had in view.

[58] In 1976, Lord Wilberforce elaborated on the nature of the surrounding circumstances which provide legitimate contextual assistance in ascertaining the meaning of contractual language, when delivering the judgment of the majority of the House of Lords in *Reardon Smith Line Ltd v Hansen-Tangen*, saying:[46]

> In a commercial contract it is certainly right that the Court should know the commercial purpose of the contract and this in turn presupposes knowledge of the genesis of the transaction, the background, the context, the market in which the parties were operating.

[59] Reliance on the commercial background, including the objective aim of the transaction, to clarify meaning of the words of a contract was not, of course, a new concept of interpretation in 1971. Lord Wilberforce had based his approach in *Prenn v Simmonds* on a judgment which Lord Blackburn had delivered in 1877.[47] In New Zealand, in 1958, F B Adams J had said:[48]

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45 [1971] 1 WLR 1381 at p 1384.

46 [1976] 1 WLR 989 at pp 995 – 996.

47 *River Wear Commissioners v Adamson* (1877) 2 App Cas 743 at p 763.

48 *Blakely and Anderson v de Lambert* [1959] NZLR 356 at p 367 (HC) (original emphasis). The passage was approved by Richmond J in *Eastmond v Bowis* [1962] NZLR 954 at p 959 (HC).

> I think that the rule as to admissibility of surrounding circumstances may be correctly stated by saying that, in order to ascertain the meaning with which ambiguous words have been used, the Court may examine objectively all the surrounding facts with reference to which they were used, thus placing itself in the position of the parties who used the words, and ascertaining what the words meant in light of those surrounding circumstances. I emphasize the objectivity of the inquiry, its purpose being to identify, by reference to the facts, some subject matter, whether corporeal or merely conceptual, to which the words were intended to apply. It is not an inquiry into *intention* but into *meaning* as a guide to intention.

The authority cited in support was Lord Blackburn's judgment in *Inglis v Buttery and Co*.[49]

[60] Similar observations were made in the High Court of Australia following a comprehensive discussion of the principles by Mason J in *Codelfa Construction Pty Ltd v State Rail Authority of NSW*.[50] Mason J adhered to the traditional view that evidence of surrounding circumstances was admissible to assist in the interpretation of a contract only if the language was ambiguous or susceptible of more than one meaning. He also said in respect of prior negotiations that to the extent they established objective background facts known to both parties and the subject matter of the contract they were admissible. However, insofar as prior negotiations consisted of statements or actions which reflected their actual intentions and expectations they were not.[51] Mason J pointed out[52] that the admissibility of material identifying the specific subject matter of a contract had been determined by the Privy Council in *Bank of New Zealand v Simpson*[53] in 1900. In that case the Privy Council cited *Macdonald v Longbottom*,[54] which held that extrinsic evidence was admissible to prove that "your wool" in a contract meant not only wool produced by the plaintiff but also that produced on a neighbouring farm.

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49 (1878) 3 App Cas 552.
50 (1982) 149 CLR 337 at pp 347 – 348.
51 At p 352.
52 At p 349.
53 [1900] AC 182 at pp 187 – 189.
54 (1859) 1 E&E 977; 120 ER 1177.

[61] In 1998, the House of Lords further clarified English law on when it is permissible to refer to extrinsic material in the interpretation of commercial agreements when Lord Hoffmann fashioned five principles of interpretation in his judgment on behalf of the majority in *Investors Compensation Scheme Ltd v West Bromwich Building Society*.[55] In summary, Lord Hoffmann said that interpretation of a commercial agreement is the ascertainment of the meaning it would convey to a reasonable person who has all the background knowledge which would reasonably have been available to the parties in the situation in which they were at the time of contract. The language the parties use is generally given its natural and ordinary meaning, reflecting the proposition that the common law does not easily accept that linguistic mistakes have been made in formal documents. The background, however, may lead to the conclusion that something has gone wrong with the language of an agreement. In that case the law does not require the courts to attribute to the parties an intention which they clearly could not have had. The natural and ordinary meaning should not lead to a conclusion that flouts business common sense.

[62] While the approach to contextual interpretation expounded by Lord Wilberforce and Lord Hoffmann built on recognised principles, these seminal judgments have both clarified and added to the situations in which material extrinsic to the contract may be considered in addition to the language to ascertain meaning of a commercial agreement. Lord Wilberforce's indication in *Reardon Smith Line* that in commercial contracts cases it was "certainly right" that the court should know the commercial purpose of the contract including the genesis and background of the transaction, was not restricted to situations where there was ambiguity in contractual language.[56] This was a departure from the prevailing view of what the common law required. The *Investors Compensation Scheme* principles of interpretation likewise made no reference to any requirement of ambiguity in order to apply contextual interpretation. Indeed, as already indicated, they contemplated departure from ordinary meaning where the background demonstrated "something had gone wrong" with the contractual language.

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55 [1998] 1 WLR 896 at pp 912 – 913.

56 At p 995.

[63] Pre-contractual negotiations were identified by Lord Hoffmann as an exception to admissible background evidence, although he emphasised that the boundaries of this exception were unclear.[57]

[64] Lord Hoffmann's principles were quickly adopted in New Zealand.[58] But doubts remained for some time concerning the appropriateness of interpretation of commercial agreements by reference to commercial purpose, background and context. In 1996, shortly before the *Investors Compensation Scheme* judgment was delivered, the Privy Council, in a New Zealand appeal, had reiterated that use of contextual material in interpretation of contracts was confined to resolving ambiguities, adding that rules that existed to resolve ambiguities could not be invoked to create them.[59] As a result, even after the Court of Appeal adopted the approach in *Investors Compensation Scheme*, there were attempts in New Zealand to reconcile Lord Hoffmann's principles with the more restrictive traditional approach reflected in the earlier Privy Council judgment.[60] The resulting uncertainty over the need for ambiguity in the language before a contextual approach was applied was, however, resolved in New Zealand by the Court of Appeal in *Ansley v Prospectus Nominees Unlimited*:[61]

> We do not accept the proposition that the factual matrix is to be considered only where there is ambiguity in the terms of a contract. We do not understand that to be the view of *Investors' Compensation Scheme Ltd v West Bromwich Building Society* ... on which this Court drew in *Boat Park Ltd v Hutchinson*.

[65] *Investors Compensation Scheme* has also been cited by the High Court of Australia in support of the proposition that the construction of commercial documents is determined by what a reasonable person in the position of the parties would understand them to mean, which requires consideration not only of the text of the documents but also the surrounding circumstances known to the parties and the purpose and object of the transaction.[62]

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57 This proposition reflects the third of Lord Hoffmann's principles of interpretation in *Investors Compensation Scheme* at p 913.

58 *Boat Park Ltd v Hutchinson* [1999] 2 NZLR 74 (CA).

59 *Melanesian Mission Trust Board v AMP Society* [1997] 1 NZLR 391 at pp 394 – 395.

60 In particular in *Potter v Potter* [2003] 3 NZLR 145 (CA) at p 156.

61 [2004] 2 NZLR 590 at para [36] per Gault P.

62 *Pacific Carriers Ltd v BNP Paribas* (2004) 218 CLR 451 at p 462.

[66] Since the Court of Appeal's judgment in the present case, the authority of *Investors Compensation Scheme* in England has been reinforced by the House of Lords in *Chartbrook Ltd v Persimmon Homes Ltd*.[63] The principal judgment is again that of Lord Hoffmann. It acknowledges that giving effect to what a reasonable person would have understood the parties to have meant, when using the language which they did, might sometimes require the use of different language. It emphasises that presents no barrier to applying a contextual interpretation.[64] Plain and unambiguous ordinary meanings can be displaced by context and background although, as is also emphasised in *Chartbrook*, there must be a strong case to persuade the court something has gone wrong with the contractual language.[65]

[67] The House of Lords in *Chartbrook* also reaffirmed the rule that pre-contractual negotiations are inadmissible as evidence of the parties' contractual intentions. The rule excluding evidence of pre-contractual negotiations does not, however, exclude use for the purpose of establishing facts relevant as background which were known to the parties. Nor does it preclude such evidence from supporting a claim for rectification or estoppel.[66] Relevant in the present case is estoppel by convention which is defined in the current edition of a leading text as follows:[67]

> This form of estoppel is founded, not on a representation made by a representor and believed by a representee, but on an agreed statement of facts or law, the truth of which has been assumed, by convention of the parties, as the basis of their relationship. When the parties have so acted in their relationship upon the agreed assumption that the given state of facts or law is to be accepted between them as true, that it would be unfair on one for the other to resile from the agreed assumption, then he will be entitled to relief against the other according to whether the estoppel is as to a matter of fact, or promissory, and/or proprietary.

[68] The essence of estoppel by convention and its distinguishing characteristic is that there is mutual assent or a common assumption as to the relevant fact:[68]

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63 [2009] 1 AC 1101.

64 At paras [21] and [25].

65 At paras [14] and [15].

66 At para [42] per Lord Hoffmann.

67 Feltham, Hochberg, and Leech, *Spencer Bower: Estoppel by Representation* (4th ed, 2004), p 180.

68 *National Westminster Finance New Zealand Ltd v National Bank of New Zealand Ltd* (Court of Appeal, CA 159/92, 30 March 1993) at p 24 per Tipping J for the Court, partially reported as [1996] 1 NZLR 548.

> … both parties are thinking the same; they both know that the other is thinking the same and each expressly or implicitly agrees that the basis of their thinking shall be the basis of the contract.

[69] The effect of the estoppel is to prevent a party from going back on the mutual assumption if it would be unjust to allow him to do so.[69]

**Pre-Contractual Negotiations**

[70] Until recently, the main reason usually given for why the common law excluded evidence of pre-contractual negotiations was that, insofar as they went beyond background facts known to both parties, they were no more than evidence of statements of intentions of what terms they hoped to achieve. As such they did not shed light on the meaning of the terms later agreed on and tended to be destructive of objectivity in determining the meaning of the contractual language. To the extent, however, that objective facts existing when the contract was made could be proved by pre-contractual negotiations, the evidence was admissible, that being consistent with the objective approach to interpretation.

[71] Other arguments supporting a firm rule of exclusion of evidence of pre-contractual negotiations to ascertain contractual meaning have included the delay, expense and increased degree of uncertainty that would result. Additional work would become necessary to undertake contractual interpretation as a result of the time-consuming examination of extrinsic material. This would usually be with little return. The inconvenience and risk to third parties who subsequently acquire interests of contracting parties, without ready access to the content of prior negotiations, has been another concern.

[72] In recent years, however, academic and extra-judicial writing has challenged the traditional rationalisation of why pre-contractual material is treated as irrelevant. Professor McLauchlan, in particular, points out that evidence of what people said or wrote to each other while they were negotiating *can be* direct evidence of their actual

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[69] *Republic of India Ltd v India Steamship Co Ltd (No 2)* [1998] 1 AC 878 at p 913 per Lord Steyn.

intentions at the time they became bound.[70] Professor McLauchlan argues that if evidence of exchanges between the parties prior to contract establishes their intention that words bear a particular meaning, evidence of their shared meaning should be admissible and prevail.[71] An underlying theme is that admitting evidence of negotiations of this nature is not inconsistent with an objective approach to interpretation.

[73] The force of these criticisms of a general exclusionary rule is, however, lessened by the recent confirmation by the House of Lords that the rule does not exclude evidence of relevant background facts known to the parties. Nor does it exclude evidence that supports a claim for rectification or estoppel. Rectification and estoppels are seen as "legitimate safety devices" which mitigate against effects of rigid application of the rule and, in most cases, prevent it from causing injustice.[72] Such evidence is not directed at proving terms additional to or differing from those in the written agreement. It is directed at proving that it would be unconscionable in the circumstances to allow a party to rely on those terms. The distinction remains valid even if, as in the present case, the agreement provides that the terms are set out "in full".[73]

[74] Estoppel by convention, which is a form of promissory estoppel, is of particular importance, because it prevents unfair departures from common understandings between the parties, on which they have acted. Allowing evidence of pre-contractual negotiations to support a claim to this form of estoppel is a principled supplementary approach in contractual interpretation that will cover many situations previously addressed by the "dictionary exception rule".[74]

[75] In *Chartbrook*, the House of Lords accepted that in some cases, which it thought would be exceptional, the general rule would apply to exclude evidence of negotiations even though they might throw light on what the parties meant by the

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70 McLauchlan, "Contract Interpretation: What is it about?" (2009) 31 Sydney LR 1, pp 12 – 13, and 29.

71 At p 13.

72 *Chartbrook* at para [47] per Lord Hoffmann.

73 *MacDonald v Shinko Australia Pty Ltd* [1999] 2 Qd R 152 (CA).

74 That rule had its origins in *Partenreederei MS Karen Oltmann v Scarsdale Shipping Co Ltd* [1976] 2 Lloyds' Rep 708.

language they adopted in their agreement. The House of Lords considered that in such cases the application of the rule was justified, on pragmatic grounds.[75] Allowing evidence of pre-contractual negotiations to be admitted, whenever that would provide a reliable guide to the parties' intended meaning, would have significant detrimental consequences for efficiency and economy in contractual interpretation, in particular where third parties had acquired contractual interests.

[76] At present in contractual interpretation "'intention' plays no real part; the emphasis is on the meaning conveyed to a reasonable person with the relevant background".[76] The nearest *Investors Compensation Scheme* principles get to relying on intention as a concept in interpretation is to make clear that where the background establishes a linguistic mistake, that does not require a Court to attribute to the parties an intention they plainly did not have.[77] The change in approach proposed by Professor McLauchlan, to my mind, will bring the intentions of the parties into prominence at the risk of significantly altering the longstanding objective theory of contractual interpretation which seeks to ascertain meaning by examining overt contextual indicators rather than inner intentions of the parties.

[77] Over the past 40 years the common law has increasingly come to recognise that the meaning of a contractual text is clarified by the circumstances in which it was written and what they indicate about its purpose. As Lord Bingham has observed, "construction is a composite exercise, neither uncompromisingly literal nor unswervingly purposive".[78] The appropriate combination of these elements in interpretation involves considerations of legal policy. The ordinary or plain meaning of the contractual text is always a principal, and usually the primary, consideration. Extrinsic contextual material, however, often throws important light on the true meaning. Nevertheless, in policy terms I am satisfied of the continuing validity in the policy consideration which Mason J identified in *Codelfa Construction*:[79]

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75 At para [34] per Lord Hoffmann.

76 K J Keith, "Interpreting Treaties Statutes and Contracts", Occasional Paper No 19, New Zealand Centre for Public Law, Wellington 2009, p 18.

77 At p 913 (fifth principle).

78 "A New Thing Under the Sun? The Interpretation of Contract and the *ICS* Decision" (2008) 12 Edin LR 374, p 376.

79 At p 352.

> We do not take into account the actual intentions of the parties and for the very good reason that an investigation of those matters would not only be time consuming but it would also be unrewarding as it would tend to give too much weight to these factors at the expense of the actual language of the written contract.

[78] I am satisfied that the House of Lords judgments in *Investors Compensation Scheme* and *Chartbrook* set sound limits for the common law principles concerning admission of extrinsic material so that considerations of purpose will bear to an appropriate degree in deciding the meaning of a commercial agreement. The current English position is the outcome of decades of close consideration of the conflicting arguments reflected in the views of judges, legal academics and practising lawyers. It has recently been reaffirmed by the House of Lords. It also appears to reflect the current position of the High Court of Australia. I see no point in New Zealand courts at this stage attempting to put a gloss on the general approach so recently stated by the House of Lords. It is better that the common law of New Zealand in this important field of commerce march in step with settled approaches overseas unless and until very good reasons for departure emerge.

[79] Accordingly, I proceed on the basis that the approach to interpretation of contracts which I have summarised in this judgment is that to be followed in New Zealand. This means that I take a rather different approach in my analysis of the contractual language than that of the Court of Appeal.

**Factual background**

[80] I first consider the background circumstances and whether what they indicate about the parties' contractual purpose throws light on the meaning of the 15 October interim agreement. I do so bearing in mind that on the point in issue, I have concluded that the language is not ambiguous and that the Court should not readily accept there is any error in the contractual text. The key background fact is that, when they entered into the interim agreement, the parties were about to enter litigation over whether the 1995 agreement had been lawfully terminated. They were seeking to agree on terms for continuing supply of gas pending the Court's determination of their dispute. They wished to avoid the need for an application for

interim relief. Both would, however, have known that if BoPE did apply for an interim injunction, requiring NGC to continue to supply, it would probably have been successful. But the order would be subject to BoPE undertaking to meet NGC's losses if NGC was successful in the action. Accordingly the object of the parties negotiating in the interim agreement was to agree on terms for interim supply that would reflect the market price NGC could have obtained for the gas at the time the interim agreement was entered into.

[81] The evidence in the High Court indicated that the market price for gas in mid-October 2004 was around $6.50 per gigajoule, plus the cost of transmission to customers. If, under the interim agreement, the price of $6.50 per gigajoule included at cost, the evidence was that NGC would receive $4.64 per gigajoule for its gas.[80] That would be well below the current market price and, accordingly well below what a court would have conditionally ordered that BoPE pay on its undertaking had the matter been the subject of an application for an interim injunction. This would be the effect of giving the contractual language its ordinary meaning.

[82] Such a differential cannot be explained on the basis that BoPE out-negotiated NGC or otherwise secured a better deal in the ordinary course of business, or for reasons of need to safeguard BoPE's reputation. For NGC to have agreed to those terms would be so extraordinary that it would flout business commonsense. The background circumstances known to the parties and the purpose of the interim agreement together give a strong indication that something went wrong with the language used in the 15 October letter.

[83] Both the Court of Appeal and the High Court judgments discuss the correspondence between the parties leading up to the offer and acceptance on 15 October. For reasons already canvassed, I regard this pre-contractual material to be inadmissible evidence unless it is used for a purpose that is not covered by the exclusionary rule. Insofar as it bears on price, this material is not part of the factual background that might throw light on what the parties meant when they agreed on

[80] As Wilson J demonstrates in his judgment at para [111].

terms expressed in Chapman Tripp's letter of 15 October. Nor is it evidence going to the subject matter of the contract. The subject matter was the supply of gas which does not need more precise identification. What is in issue is the price payable under the agreement. The subject matter exception does not permit the admission of pre-contractual material to clarify such a term.

**An estoppel?**

[84] Pre-contractual material is however admissible on questions of rectification and estoppel by convention. Neither were pleaded by NGC. Rectification involves an assertion that there is a defect in the recording of the agreement, so that it has been expressed in terms that neither party intended. NGC's case has not been run on that basis and it would be unfair to permit it to introduce at this stage a new cause of action on which BoPE may well have wished to call evidence.

[85] While estoppel by convention should also be pleaded in such litigation I see no unfairness in this Court addressing that issue. In substance it was before the lower Courts in the form of NGC's contention that the parties had agreed on their own dictionary meaning for the phrase "$6.50 per GJ". Accordingly I am prepared to address the preliminary material to determine its relevance to the estoppel question.

[86] On 28 September 2004 NGC made an offer to supply gas under what would be a new contract during the period after its termination of the 1995 agreement had taken effect. The offer proposed alternative terms, one proposal being to supply gas at $6.50 per gigajoule for a period expiring on 30 June 2006. The alternative proposal for supply over an extended term need not be further considered. The terms were expressed to be "with transportation and metering passed through at cost". The letter added:

> ... we have not included transportation and metering rates in this proposal. Appropriate transmission capacity levels and the provision of metering equipment would need to be agreed at the same time as the new gas supply agreement. If the above offer is acceptable to you, we should meet [to]

> discuss what the transmission and metering arrangements will be. These are likely to take into account historic use and transmission posted pricing.

[87] Russell McVeagh replied on behalf of BoPE on 5 October rejecting what they called the "purported termination". The letter also refused the offers of new terms for supply "because of the severity of the price discrepancy ...". BoPE said it would issue proceedings for specific performance and went on to discuss a basis for supply pending determination of the litigation. The letter proposed that NGC undertake on a without prejudice basis to continue to supply gas on the basis of the 1995 BoPE agreement pending determination of the proceeding. BoPE would undertake to file its proceeding by the end of the month and, in the event that it was unsuccessful in its proceeding would:

> pay NGC on demand, for each GJ supplied, the difference between the [1995] Agreement price and $6.50 (or the current market price, whichever is the lower), plus interest; ...

[88] On 8 October Chapman Tripp replied indicating NGC's agreement, provided that BoPE undertook that if it were unsuccessful in its proceeding it would "pay NGC on demand, for each GJ supplied, the difference between the price set out in the Agreement and $6.50 per GJ ...".

[89] On 15 October Russell McVeagh responded with a counter-proposal with two amendments that are not in point. The same day Chapman Tripp responded in the terms set out earlier in this judgment which were accepted the same day. Later that month it emerged that the parties differed on whether the agreed price under the interim agreement was inclusive of transportation and metering costs.

[90] In his evidence in the High Court the general counsel of BoPE's parent company, Mr Hall, accepted that at the time that the parties reached agreement, the industry drew a distinction between "gas energy" and "delivered" gas price contracts. In the former transmission costs were additional and charged separately. In the latter both elements were included in the delivered price.

[91] NGC's letter of 28 September proposing terms for a new contract explicitly said that costs of transportation of gas to Edgecumbe and metering would be additional to the price of $6.50 per gigajoule. In the language of the industry this

was a "gas energy" price. BoPE rejected that offer, on 5 October, saying that the price was too high. Its counter-offer was for supply to continue under the terms of the 1995 agreement pending the Court's ruling on the validity of NGC's termination. If the Court upheld NGC's position BoPE would pay the lesser of $6.50 and the current market price "for each GJ supplied". It was implicit that this contingent agreement would operate from 31 October 2004, the date the termination of the 1995 agreement was to take effect, until the date the Court delivered judgment in favour of NGC.

[92] The Court of Appeal decided that this terminology did not warrant an inference that each party was referring to a "gas energy" price, because the reason given by BoPE for rejecting NGC's offer was that the price offered was too high. I have difficulty with that finding. BoPE did reject an offer to settle the termination dispute, because it considered the price it would have to pay under the proposed new contract to be too high. It does not, however, follow that BoPE would consider the same price to be too high under an interim supply agreement. Such an agreement would only have effect if BoPE were unsuccessful in challenging the termination. The reality was that BoPE would have known on 5 October that it would have to give an undertaking to the Court that it would pay a market price for gas supplied after 31 October in the event that the Court found the termination was valid. Otherwise it would not obtain from the Court interim relief requiring NGC to continue to supply. In that context a gas energy price of $6.50 for interim supply would be within the expected range that the Court might fix and an acceptable price for BoPE.

[93] NCG's letter of 28 September made offers to supply gas to BoPE for a two year and longer terms. Russell McVeagh's reply of 5 October rejected those offers and instead proposed terms for an interim agreement. NGC's letter had been explicit in its offers in distinguishing between price components. Its letter said that transportation and metering would be "passed through at cost". That component was accordingly additional to "Gas Energy at $6.50 per gigajoule" under the two year term offer. Russell McVeagh's reply referred to the sale price of the gas stated in NCG's letter as being "$6.50 per GJ". The same letter also spoke of "$6.50 (or current market price, whichever is the lower)" in referring to the mechanism for

determining the price under the interim agreement. Nothing indicates that those two references to a price of $6.50 per gigajoule in the letter of 5 October were to carry other than the same meaning. The first reference is explicitly to the gas energy price component, and so must be the second. It follows that, at this point, the parties shared a common understanding that $6.50 was a component price on the same basis as that stated in NGC's letter of 28 September.

[94] Chapman Tripp's offer of 15 October also referred to price, in part, by reference to "$6.50 per gigajoule," thus continuing to negotiate on the common assumption that the parties were referring to a gas energy price. Neither the move to negotiate an interim agreement, nor the references in letters during October to the terms of the 1995 agreement, would have displaced that assumption.

[95] This strong evidence that the writers had a common understanding that they were referring to a gas energy price is reinforced by the fact that the market price for gas was around $6.50 per gigajoule for gas energy contracts in mid October 2004.

[96] I accept that where lawyers are involved in framing contractual terms strong and unequivocal evidence is required to warrant an inference of a common understanding that is inconsistent with what is expressly recorded in their contract.[81] To my mind that standard is met in this case. The parties conducted themselves at all times on the basis of their common assumption that they were both referring to a gas energy price. At the time that form of price was commonly used in the industry, and by NGC in particular, to price gas supply contracts. NGC relied on the common assumption in entering the agreement.

[97] In those circumstances it would be unconscionable to allow BoPE to depart from the mutual assumption on which the parties based their dealings through to acceptance by Russell McVeagh on 15 October. BoPE is estopped from contending that the price payable under the 15 October agreement is other than a gas energy price. There is evidence that there were posted prices for transmission costs at the time of contract which may be availed of if necessary to determine the sum payable.

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[81] *Air New Zealand Ltd v Nippon Credit Bank Ltd* [1997] 1 NZLR 218 (CA) at p 225 per Gault J.

**Conclusions**

[98] For these reasons I would allow the appeal with the consequences proposed in the judgment of Blanchard J.

[99] Finally I wish to say that I agree with the observations of Wilson J concerning the desirability of practitioners not acting as counsel in litigation where they have been personally involved in the matters in issue.

**WILSON J**

**Introduction**

[100] The Natural Gas Corporation of New Zealand Ltd, now the appellant Vector Gas Ltd, supplied gas to the respondent, now a subsidiary of Todd Energy Ltd, under a Gas Supply Agreement into which they had entered in 1995. The gas was on-sold for use in a co-generation installation at a milk processing plant at Edgecumbe in the Bay of Plenty. For convenience, I will refer to the contracting parties as "NGC" and "BoPE", and to their 1995 agreement as "the Agreement".

[101] NGC gave notice of termination of the Agreement in 2004 because a redetermination of the economically recoverable reserves in the Maui gas field had revealed a substantial reduction in those reserves. BoPE disputed the validity of the termination. Following negotiations, the parties reached an agreement whereby, pending the resolution by the courts of whether the termination was valid, NGC would continue to supply gas to BoPE at a cost of $6.50 per gigajoule.

[102] NGC claims that $6.50 was the cost of the gas energy only, with transmission costs to be added. BoPE contends that $6.50 was the total cost, inclusive of transmission costs. The narrow and single issue in this appeal is which of these positions is correct.

[103] At the hearing, Mr McIntosh for BoPE relied on the judgment of the Court of Appeal of England in *Chartbrook Ltd v Persimmon Homes Ltd*.[82] In doing so, counsel properly advised the Court that an appeal to the House of Lords was pending. The judgment of the House of Lords on that appeal was delivered on 1 July.[83] The Court therefore gave counsel the opportunity to make written submissions on that judgment. Both parties availed themselves of the opportunity to do so.

**The facts**

[104] NGC gave notice of termination on 2 August 2004, with effect from 31 October 2004. There followed extensive discussions between the parties. Without prejudice to their differing positions as to whether NGC's termination of the Agreement was valid, they addressed the possibility of a replacement agreement. By letter dated 28 September, NGC offered to BoPE the options of purchasing gas "at $6.50 per gigajoule" for the balance of the term of the Agreement or "at $6.20 per gigajoule" for that period and "at $6.90 per gigajoule" for a further 15 months. The letter went on to say that, because of timing constraints and issues of volume, "we have not included transportation and metering rates in this proposal", that it would be necessary to meet to discuss "transmission and metering arrangements" and that these would be "likely to take into account historic usage and transmission posted pricing".[84]

[105] On 5 October, BoPE's solicitors Russell McVeagh wrote to NGC replying to their 28 September letter. Russell McVeagh rejected NGC's terms for a new agreement and advised that Court proceedings to enforce ongoing performance of the Agreement were about to be issued. They then went on in the fourth paragraph of their letter to record, for the purposes of reaching an interim agreement for the supply of gas until that proceeding was determined, that NGC had in their 28 September letter confirmed that it had gas available to supply and that the price of that gas would be "$6.50 per GJ". Russell McVeagh then proposed in the fifth

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82 [2008] 2 All ER 387.
83 [2009] 1 AC 1101.
84 A reference to the costs of transmission, as "posted" or publicly notified by NGC.

paragraph of their letter that "in lieu of Todd having to apply for interim injunctive relief" NGC should undertake to supply gas "on the basis of the Agreement", pending resolution of BoPE's proceeding. For its part, BoPE should undertake to file that proceeding by 31 October and, if it was discontinued or was unsuccessful, should pay NGC "for each GJ supplied, the difference between the Agreement price and $6.50 (or the current market price, whichever is the lower), plus interest" or, at the election of BoPE, provide an equivalent amount of gas.

[106] By letter dated 8 October, Chapman Tripp replied on behalf of NGC to Russell McVeagh. They confirmed that, pending determination of BoPE's proceeding or 30 June 2006, whichever was the earlier, NGC would continue to supply gas based on the terms of the Agreement provided that BoPE undertook to file its proceeding on or before 31 October and, if it were unsuccessful in or withdrew its proceeding, to pay to NGC "for each GJ supplied, the difference between the price set out in the Agreement and $6.50 per GJ", plus interest. On 15 October, Russell McVeagh wrote to Chapman Tripp accepting that proposal, subject only to two points they thought would not be contentious.

[107] Later that day, 15 October, Chapman Tripp wrote by facsimile to Russell McVeagh. They began their letter by referring to the facsimile from Russell McVeagh earlier that day and to a subsequent telephone discussion. The letter then confirmed the agreement of NGC to the two points raised by Russell McVeagh. It went on to say that "for the avoidance of doubt, the terms of the proposal are set out in full below" and to seek confirmation by return of the agreement of BoPE to "the terms of the proposal". Among these terms were that NGC would continue to supply, based on the terms of the Agreement, provided that, if BoPE were unsuccessful in its challenge to the termination of the Agreement, it would pay NGC "for each GJ supplied" the difference between the price payable under the Agreement and $6.50 per gigajoule, plus interest. As is immediately apparent, the letter did not specify whether the price of $6.50 was inclusive or exclusive of transmission costs.

[108] BoPE complied promptly with that request for confirmation of acceptance when, again on 15 October, Russell McVeagh wrote by facsimile to Chapman Tripp

thanking them for their letter and saying that "we confirm BoPE's agreement to the interim gas supply terms as set out".

**Interim agreement**

[109] Given the exchange of correspondence which I have summarised, the terms of the contract for the continuing supply of gas, pending the determination by the courts of the validity of the termination of the Agreement, were as recorded in Chapman Tripp's 15 October letter. This is the only tenable construction of their words "for the avoidance of doubt, the terms of the proposal are set out in full below". Russell McVeagh and BoPE were fully entitled to assume, from these words, that the proposal to which confirmation of their acceptance was being sought was that set out in Chapman Tripp's letter. By conveying the agreement of BoPE to the terms "as set out" in the letter, Russell McVeagh confirmed that the contract was on these terms, and only on these terms.

[110] As Russell McVeagh stated in their 5 October letter,[85] the purpose of the interim agreement reached on 15 October was to avoid the need for BoPE to obtain "interim injunctive relief". That relief would in all probability have taken the form of NGC being required to continue to supply gas to BoPE under the terms of the Agreement until the validity of the termination of the Agreement had been judicially determined. In order to obtain interim relief, BoPE would have been required to file in the Court a signed undertaking under Rule 238 of the High Court Rules[86] that it would comply with any order made by the Court to compensate NGC "for any damage sustained through the injunction", in the event that the Court held that the termination was valid.

[111] At trial, NGC gave unchallenged evidence that the cost of delivering gas to Edgecumbe was $1.86 per gigajoule, so that a price of $6.50 inclusive of transmission costs equated to a gas energy price of $4.64. In the last three months of

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85 See para [105] above.
86 Now Rule 7.54.

2004, NGC had negotiated 15 new contracts with a weighted average starting price (excluding transmission) of $6.68 per gigajoule. Under the interim agreement, gas was supplied at the price payable under the Agreement, with BoPE paying a total of $10,084,778. If BoPE were unsuccessful in its challenge to the validity of the termination, it would be required to pay NGC a further $4,682,334 if the $6.50 comparator were a gas energy price only but only $1,418,428 if the $6.50 were inclusive of transmission costs.

[112] Mr Hall, the General Counsel of Todd Energy Ltd, gave evidence for BoPE. In cross-examination, he accepted that NGC's original offer of $6.50 per gigajoule, plus transmission costs, represented a market price in October 2004, and that BoPE would normally pay for the cost of delivering gas to Edgecumbe.

[113] It follows from the evidence I have summarised in the preceding two paragraphs that NGC would have incurred a loss of more than three million dollars (plus interest) if it had agreed to a comparator of $6.50 per gigajoule inclusive rather than exclusive of transmission costs. And, if NGC had elected to rely on BoPE's undertaking rather than enter into the interim agreement and had established the validity of its termination, it could reasonably have expected to recover in full both the gas energy price and the cost of transmission, having previously been deprived by the injunction of the ability to do so, and therefore to recover damages of $4,682,334 plus interest.

**High Court and Court of Appeal**

[114] BoPE filed its proceeding on 29 October, seeking a declaration that NGC's purported termination of the Agreement as of 31 October was invalid and an order for specific performance of the Agreement. By way of counterclaim, NGC sought an order that, in addition to the price payable under the Agreement, BoPE was required to pay for gas supplied after 31 October the difference between that price and the total of a "gas only" price of $6.50 per gigajoule and NGC's "posted" transmission charges. The Courts were therefore required to decide whether the termination of the Agreement was invalid and, if it was not, whether BoPE was

required to pay NGC $6.50 per gigajoule or $6.50 plus transmission charges per gigajoule.

[115] In the High Court, Harrison J found that the termination was valid.[87] He went on to construe the interim agreement, and concluded that it was "inherently unlikely" that NGC would have agreed to an interim arrangement whereby BoPE was better placed than it would have been if it lost its challenge to the validity of NGC's notice. And "an experienced commercial entity" like BoPE "could hardly expect" NGC to supply it with gas at "well below market price".[88] The Judge was accordingly "satisfied that at all relevant times the parties were referring to an unbundled or gas energy price of $6.50 excluding transmission costs".[89]

[116] Harrison J therefore entered judgment against BoPE for the difference between the amount which had been paid under the Agreement and the total of $6.50 per gigajoule as the cost of the gas energy and NGC's "posted" transmission charges. Interest was also payable, calculated on a basis specified in the Agreement.

[117] BoPE appealed to the Court of Appeal over both the validity of the termination and the sum payable to NGC if it was unsuccessful on that issue. The Court of Appeal found that the termination was valid but that the price in the interim agreement was $6.50 per gigajoule inclusive of transmission costs.[90] In coming to this view, the Court thought that "the starting point" was Chapman Tripp's 8 October letter, which "effectively resumed negotiations after Russell McVeagh on 5 October had rejected NGC's settlement proposal".[91] Because this was "a wholly new proposal", there was "no occasion to look earlier in the chain of negotiations".[92]

[118] The Court went on to say the terms of Chapman Tripp's 15 October letter were clear because continued supply was on the terms of the Agreement, which was

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87 *Bay of Plenty Electricity Ltd v Vector Gas Ltd* (High Court, Wellington, CIV-2004-485-2287, 3 August 2007).
88 At para [128].
89 At para [130].
90 *Bay of Plenty Electricity Ltd v Vector Gas Ltd* [2008] NZCA 338 at para [91] (Chambers, Ellen France and Baragwanath JJ).
91 At para [91].
92 At para [91].

inclusive of transmission costs.[93] There was "force" in the contention of BoPE that "reputational matters" came "into play" as explaining why NGC may have agreed to an interim arrangement under which BoPE would be better off than it otherwise would have been.[94] NGC's real argument was that there had been a mistake, but mistake was not pleaded and rectification was not sought.[95] BoPE therefore succeeded on the interpretation issue.

**Principles of interpretation**

[119] The general principle is that the words of an enforceable commercial contract should be given their ordinary meaning in the context of the contract in which they appear, because the parties are presumed to have intended the words to be given that meaning. This general principle is however subject to three exceptions, which permit the consideration of evidence extrinsic to the contract to aid in its interpretation, and to the possibility of rectification.

[120] The first exception is that, if there is ambiguity within a contract because the words are not clear or because of internal conflict, resort can and indeed must be had to material outside the contract to resolve the ambiguity. Before this course is followed, however, it must be established to the satisfaction of the Court that there is genuine and relevant ambiguity; assertions by parties of possible different meanings will not suffice. In the words of Professor Steven Burton, written in a North American context but equally applicable in this country:[96]

> It is irrelevant whether the contract language is ambiguous in the abstract. What matters is whether it is ambiguous as between the (usually two) meanings advanced by the parties. One of those meanings may well be outside the array of meanings that the language reasonably bears under the circumstances. When this is the case, a court properly holds that the contract is unambiguous (in the contested respect).

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93 At para [92].
94 At para [93].
95 At para [98].
96 *Elements of Contract Interpretation* (2009), pp 138-139.

[121] Professor Burton also points out, quite correctly, that counsel are always free to make submissions as to the purpose of the contract, as it appears from the contract itself and the pleadings.[97] Extrinsic evidence is not required for such a submission.

[122] If relevant ambiguity is established, the Court may have regard to any extrinsic material which assists in assessing objectively the intention of the contracting parties in using the words they did. Only claims of undeclared intent (what the parties were thinking, in contrast to what they were saying) are excluded because, unlike communications between the parties, they cannot possibly assist in ascertaining objective intent. Prior negotiations may well be relevant; the time has come to remove in this country the barrier imposed by *Prenn v Simmonds*[98] to looking at those negotiations in a situation where they illuminate, in advance of consensus being achieved, what the parties were intending to achieve in their contract. Their conduct subsequent to the contract may also be a helpful guide to what was intended in the contract. Had I been a member of the Court in *Gibbons Holdings Ltd v Wholesale Distributors Ltd*,[99] I would have joined the majority in holding that the evidence of the conduct of Wholesale Distributors Ltd subsequent to the contract was admissible to resolve the ambiguity in the contract. Moreover, I would have held that the fact that some of that conduct was not mutual went to the weight to be accorded the evidence of that conduct and not to its admissibility.[100]

[123] The second exception to the general rule that the words of the contract are to be given their ordinary meaning is that, if that meaning makes no commercial sense, it must yield to an interpretation which is commercially sensible. Evidence may be called to demonstrate the absence of commercial sense in giving the words of the contract their ordinary meaning. As the Court of Appeal said in *Commissioner of Inland Revenue v Renouf Corporation Ltd*, "the Court assumes that the parties were intent on achieving a result which makes commercial sense".[101] *Chartbrook* provides a recent example of the application of this principle. As Lord Hoffmann

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97 Page 225.

98 [1971] 1 WLR 1381 (HL).

99 [2008] 1 NZLR 277 (SC).

100 I acknowledge that this was a submission which I made as counsel for Gibbons Holdings Ltd. This was not however one of the many occasions when, as counsel, I made a submission which, had I been the Judge, I would not have accepted.

101 (1998) 18 NZTC 13,914 (CA) at p 13,919.

said, when delivering the leading judgment, it made "no commercial sense" to interpret the relevant definition "in accordance with ordinary rules of syntax".[102] To like effect, Lord Walker concluded that the consequences of reading the definition in that way were "totally incredible"[103] and a "commercial nonsense".[104] The exception must however be confined to where there is no possible commercial justification for the results of giving the words of the contract their ordinary meaning. It is not the function of the law of contract to protect parties from the consequences of unwise bargains into which they have entered.

[124] The third exception is that a party asserting that the words of the contract should carry their ordinary meaning may be estopped by convention from doing so, if that would be a departure from the parties' common understanding (the "convention") that the words were not to carry their ordinary meaning. This possibility was adverted to by the Court of Appeal in *Air New Zealand Ltd v Nippon Credit Bank Ltd*.[105] As Lord Hoffmann said in *Chartbrook*,[106]

> ... if the parties have negotiated an agreement upon some common assumption, which may include an assumption that certain words will bear a certain meaning, they may be estopped from contending that the words should be given a different meaning.[107]

Estoppel by convention effectively subsumes the "private dictionary" principle, whereby the parties' established use of words in an unusual sense (whether as a matter of trade practice or otherwise) justifies the inference that they were intending those words to carry the unusual meaning when used in their contract. Evidence may be called to establish the estoppel.

[125] As Professor David McLauchlan said in a note on *Air New Zealand*:[108]

> ... there can be no objection in principle to the parties to a written contract being able to choose their own private code or convention as to the meaning of the terms of the contract.

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102 At para [16].
103 At para [88].
104 At para [89].
105 [1997] 1 NZLR 218 (CA), at pp 223-4.
106 At para [47].
107 See also Halsbury's Laws of England (4th ed, re-issue), Easements, Equity, Estoppel (*other than Estoppel by Record)*, 16(2), para [1069] and the authorities there cited.
108 (1997) LQR 237, pp 244 – 245.

and

> ... the position should be no different where, for example, the evidence may establish that one party intended the particular meaning and that party reasonably believed that the other party accepted this meaning.

[126] Rectification of a contract is not of itself a question of interpretation but may obviate a question of interpretation which would otherwise arise. Any party can plead, and seek to establish, that the contract should be rectified because its words did not correctly record the agreement of the parties. Again, *Chartbrook* provides a recent example. Lord Hoffmann, with whom the other members of the House of Lords agreed, held that even if Persimmon had not succeeded on the interpretation issue it would have been entitled to rectification because the written contract did not record the objective consensus which the parties had reached in correspondence and from which they had not departed.[109]

[127] At first sight, it may appear that my formulation of the principles of construction differs considerably from Lord Hoffmann's well-known exposition of those principles in *Investors Compensation Scheme Ltd v West Bromwich Building Society*,[110] adopted by this country's Court of Appeal in *Boat Park Ltd v Hutchinson*,[111] and his recent observations in *Chartbrook*. I think that it is not necessary, whenever construing a contract, to go outside the contract so as to ascertain the meaning which the document would convey to a reasonable person with all the background knowledge available to the parties. To the contrary, the Court should I believe go beyond the contract itself only to resolve a relevant ambiguity or for the purpose of addressing issues of commercial sense or estoppel. To do so in other situations is not only unnecessary but also undesirable because it may, through the introduction of extrinsic material, create uncertainty in the interpretation of a contract which is intrinsically unambiguous.

[128] I think though that, in reality, the difference between Lord Hoffmann's approach and mine is more apparent than real. As Lord Hoffmann himself

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109 In this country, s 6(2)(b) of the Contractual Mistakes Act 1977 prevents relief being sought under that Act against a mistake in the interpretation of the contract in respect of which relief is being sought. The equitable remedy of rectification may however be available.

110 [1998] 1 WLR 896 (HL).

111 [1999] 2 NZLR 74.

emphasised in *Bank of Credit and Commerce International v Ali*, in relation to his formulation in *Investors Compensation*:[112]

> ... the primary source for understanding what the parties meant is their language interpreted in accordance with conventional usage: "we do not easily accept that people have made linguistic mistakes particularly in formal documents". I was certainly not encouraging a trawl through "background" which could not have made a reasonable person think that the parties must have departed from conventional usage.

A departure from "conventional usage" will in all probability come within one or more of the three categories I have identified.[113]

[129] The House of Lords in *Chartbrook* considered but rejected a call to end the rule in *Prenn v Simmonds* and always permit reference to prior negotiations. In order to found rectification in *Chartbrook*, however, the consensus reached some time prior to the contract, as a result of negotiations, must also have existed at the time of the contract. It is difficult to see why pragmatic considerations of difficulty of proof should be seen as a barrier to admitting evidence of negotiations for the purpose of construing the contract but not for the purpose of rectification; whether the test is objective or subjective, assistance can and should where necessary be derived from evidence of the negotiations. While the degree of assistance to be derived from prior negotiations in ascertaining the presumed intention of the parties will vary greatly from one contract to another, courts should not disqualify themselves from obtaining that assistance when it is available. The position of those taking an assignment of or lending on a contract is no reason for excluding reference to prior negotiations; in choosing to involve themselves with the contract those

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112 [2002] 1 AC 251 at p 269.

113 Similarly, the difference between my approach and that of the members of the Court of Appeal of New South Wales in their recent judgments in *Franklins Pty Ltd v Metcash Trading Ltd* [2009] NSWCA 407 is also more apparent than real. Although that Court held that it is not necessary to find an ambiguity in the words of a written contract before the surrounding circumstances can be examined, it also held that evidence of such circumstances is not admissible to contradict the plain meaning of the language of the contract. (I find it difficult to see how it can be said that resort to surrounding circumstances is impermissible if the meaning is plain, but permissible even in the absence of ambiguity). The Court of Appeal also held that there was a "close connection" between the requirement that an interpretation does not flout business commonsense and the principles governing reference to surrounding circumstances, and that the question of whether an estoppel by convention could arise from pre-contractual negotiations was not settled. It held however that subsequent conduct cannot be used to show what the parties intended at the time of contract.

parties must accept that, when interpreting the contract, the courts may have regard to prior negotiations or indeed to the other material outside the contract which, on Lord Hoffmann's approach, they are required to consider. It is I think unsurprising that commentators as eminent as Lord Nicholls (writing extra-judicially)[114] and Professor McLauchlan[115] have argued forcefully that resort to prior negotiations should be permitted. I cannot see any reason for permitting resort to subsequent conduct, but not to prior negotiations, as an aid to interpretation.

[130] Finally, Lord Hoffmann said in *Chartbrook* that, like rectification, estoppel by convention must be "specifically pleaded and clearly established".[116] While agreeing that rectification must be specifically pleaded and that both principles must be clearly established, I question whether estoppel must be pleaded when it is advanced not as a cause of action but in response to the proposition that words in the contract carry their ordinary meaning.

**Rectification**

[131] Applying the relevant principles to the present appeal, it is convenient to address first the question of rectification. If the interim agreement between NGC and BoPE, properly construed, provided for a price of $6.50 per gigajoule delivered, NGC may well have been entitled to rectification to provide that the price was to be $6.50 plus transmission costs.

[132] NGC did not however plead rectification. Indeed, in his written submissions in support of the appeal, Mr Hodder expressly accepted that rectification was not available to NGC. It was only in his subsequent submissions on the judgment of the House of Lords in *Chartbrook*[117] that counsel sought leave to seek rectification if NGC were unsuccessful on the issue of interpretation. It is far too late to do so. NGC must stand or fall on the interpretation question.

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114 "My Kingdom for a Horse: The Meaning of Words" (2005) 121 LQR, pp 577 – 591.
115 "Contract Interpretation: What is it About?" (2009) 31 Sydney L.Rev 5.
116 At para [47].
117 See para [103] above.

**Ambiguity**

[133] As recorded in Chapman Tripp's 15 October letter, BoPE undertook that, if it were unsuccessful in its challenge to the termination of the Agreement, it would pay NGC "for each GJ supplied" the difference between the price payable under the Agreement and $6.50 per gigajoule.

[134] The word "supply" can connote "sale" or "delivery", or both. The point is well-illustrated by the differing approaches of the Judges of the High Court of Australia when considering in *Commonwealth v Sterling Nicholas Duty Free Ltd*[118] whether goods sold to departing international passengers outside an airport but delivered to them after passing through customs were "supplied" within the airport. Barwick CJ considered[119] that the delivery of the goods was not a "supply" of them. Menzies J, with whom McTiernan J agreed,[120] held that because "a supplier is not merely one who sells" but "may be one who delivers", the goods were being supplied at the airport.[121] Windeyer J thought that the goods were not being supplied because, although "supply" is often evidenced by delivery, it was not in this case.[122] Owen J held that "supply" occurred on delivery.[123]

[135] Because "supply" can mean sale, with or without delivery, the reference in the NGC proposal to gas being "supplied" at a cost of $6.50 per gigajoule could, if looked at in isolation, be construed as being either exclusive or inclusive of transmission (delivery) costs. The proposal expressly stated however that NGC would continue to supply gas "based on" the terms of the Agreement, which were thereby imported into the contract for interim supply. Those terms included provisions that NGC was to make the gas available at the "point of sale" and that point was a valve on the premises of the milk processing plant at Edgecumbe. To get the gas to that valve, NGC was required to incur the cost of transmission. On the

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118 (1972) 126 CLR 297.
119 At p 303.
120 At p 307.
121 At p 309.
122 At pp 314 – 315.
123 At p 319.

ordinary and unambiguous meaning of the relevant words in the proposal and the Agreement, the price of $6.50 per gigajoule was therefore inclusive of transmission costs. Accordingly, NGC cannot say that there was an ambiguity in the contract which had to be resolved by referring to matters outside the contract. On this point, I agree with the Court of Appeal.[124]

**Commercial sense**

[136] To recap,[125] if NGC were to supply gas under the Agreement until the validity of its termination were established and if it were to succeed on that issue, there were three possible hypotheses against which NGC's actual charges could be compared in order to quantify its loss –

- a price of $6.50 per gigajoule delivered (BoPE's position), with the result that a further $1,418,428 was payable by BoPE;

- a price of $6.50 per gigajoule exclusive of transmission costs (NGC's position), in which event the additional payment required of BoPE was $4,682,334;

- a market price (on the evidence, $6.50 per gigajoule exclusive of transmission costs) which would, in the absence of agreement, have been the basis of the assessment of BoPE's liability under its undertaking to pay damages and which would therefore have resulted in the same payment as under the second scenario.

[137] At the time it entered into the interim agreement with BoPE, NGC would not have known precisely how much gas it would supply pursuant to that agreement. It would have known however that, if it were to agree to supply gas at a price of $6.50 per gigajoule delivered, it would be incurring a loss, in all probability to the extent of some millions of dollars, by entering the interim agreement rather than relying on the

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[124] See para [118] above.
[125] See para [113] above.

readily available alternative of BoPE's undertaking to pay damages. This was more than a bad bargain for NGC. It would have defied commercial sense for NGC to have contracted on those terms, and BoPE could not reasonably have thought that NGC would be prepared to do so.

[138] The Court of Appeal thought that the willingness of NGC to follow an otherwise commercially irrational path might be explained by "reputational matters".[126] I do not agree. The amount of time which the courts of this country have been required to spend in recent years in hearing and deciding disputes between participants in the gas industry indicates that resort to litigation is not seen as reflecting adversely on those in the industry.[127] And, whether or not BoPE and NGC agreed on terms for interim supply, they would be litigating the validity of the termination.

[139] It follows that, in order to give commercial sense to their contract, the parties must have intended that the price was to be $6.50 per gigajoule, exclusive of transmission costs. Although the importation of the terms of the Agreement indicated that the price was for delivered gas, that made no commercial sense and therefore cannot have been intended.

**Estoppel**

[140] NGC did not plead any form of estoppel. As I have said,[128] I do not see that as a barrier to estoppel by convention being raised in answer to BoPE's argument that the words of the contract carry their ordinary meaning. Of more concern is the fact that NGC did not contend as such for an estoppel until it filed its supplementary submissions following the hearing of this appeal. It did however contend throughout that, in the "private dictionary" of the parties, "$6.50 per gigajoule" meant "$6.50 per gigajoule, exclusive of transmission costs" and thereby raised the same issue,

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126 See para [118] above.

127 As reported examples, see *Bay of Plenty Electricity Ltd v Natural Gas Corporation Energy Ltd* [2002] 1 NZLR 173 (CA); *Electricity Corporation of New Zealand Ltd v Fletcher Challenge Energy Ltd* [2002] 2 NZLR 433 (CA); *NGC New Zealand Ltd v Todd Petroleum Mining Co Ltd* [2004] BCL 1055 (HC); and *Shell (Petroleum Mining) Co Ltd v Todd Petroleum Mining Co Ltd* [2008] 2 NZLR 418.

128 See para [130] above.

albeit under a different legal principle. BoPE is therefore not prejudiced by considering the question as one of possible estoppel by convention.

[141] In considering this question, it is necessary to examine all the relevant correspondence between the parties.[129] There can be no justification for artificially dividing that correspondence, as did the Court of Appeal, between Russell McVeagh's 5 October letter and Chapman Tripp's response three days later. In their letter, Russell McVeagh proposed interim supply, based on the Agreement, and that if BoPE was unsuccessful in its challenge to the termination of the Agreement it would make a payment to NGC on a specified basis or provide replacement gas. In their letter, Chapman Tripp confirmed that NGC would supply in the interim based on the Agreement and that, if BoPE was unsuccessful, a payment would be required. There was therefore a close link between the letters. The chain of correspondence from 28 September to 15 October was unbroken.

[142] In the first of these letters, NGC made clear beyond doubt that its proposed prices were exclusive of transmission costs. In all the references to price in their subsequent correspondence, neither party stated that the price was inclusive of transmission costs. To paraphrase the words of Lord Hoffman in *Chartbrook*,[130] the parties therefore negotiated the interim agreement upon the common assumption that the reference to a price was to that price exclusive of transmission costs.

[143] Mr McIntosh attempted to meet this obvious difficulty for BoPE by submitting that, when Russell McVeagh in the fourth paragraph of their 5 October letter referred to NGC's price as being "$6.50 per GJ", that was to a price exclusive of transmission costs. When however Russell McVeagh proposed in the following paragraph that BoPE if unsuccessful in its challenge to termination should pay "the difference between the Agreement price and $6.50", the latter was a delivered price because the Agreement price was a delivered one. That submission cannot possibly be correct. There was no reason for Chapman Tripp and NGC to think that, when Russell McVeagh referred in successive paragraphs of their letter to a price of $6.50, the first price was exclusive of transmission costs but the second price was inclusive

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129 As summarised at paras [104] to [108] above.
130 See para [124] above.

of them. If Russell McVeagh were intending to refer in the fifth paragraph to a different basis of pricing from that proposed by NGC, as correctly recorded by them in the preceding paragraph, it was incumbent on them to make that clear.

[144] The correspondence between the parties prior to Chapman Tripp's letter of 15 October, viewed objectively, admits of only one construction; all references to price were to a price exclusive of transmission charges. There was no indication that the basis of pricing was intended to change between the previous correspondence and the 15 October letter which set out the terms of the interim agreement. It must follow that, although the wording of that letter when looked at in isolation indicates that the price was inclusive of transmission costs, BoPE is estopped from contending that that was so because to do so would be contrary to the common assumption upon which the contract had been negotiated.

**Result**

[145] Through the importation of the terms of the Agreement, the interim agreement provided that BoPE, if it failed in its challenge to the termination of the Agreement, was liable to pay NGC the difference between the price payable under the Agreement and $6.50 per gigajoule, inclusive of transmission costs. That interpretation cannot however have been intended, because it would make no commercial sense. To make sense, the price must be construed as being exclusive of transmission costs. Alternatively, BoPE is in the light of the previous correspondence between the parties estopped from claiming that the price was for delivered gas. I would therefore allow NGC's appeal and restore the judgment which it obtained in the High Court, with the consequences proposed by Blanchard J.[131]

[131] At para [16] above.

**Comment**

[146] Russell McVeagh's letter dated 5 October and their two letters dated 15 October were written under the name of Mr McIntosh. Chapman Tripp's letters dated 8 and 15 October were written under the name of Mr Hodder.

[147] Whatever the court or tribunal in which they are appearing, it is undesirable for practitioners to appear as counsel in litigation where they have been personally involved in the matters which are being litigated. In that situation, counsel are at risk of acting as witnesses and of losing objectivity.

[148] These dangers have long been recognised. In 1940, Myers CJ stated clearly in *Hutchinson v Davis*[132] that "a practitioner cannot be allowed to act in the dual capacities of counsel and witness". Northcroft and Blair JJ agreed. Correspondence between counsel on other than plainly non-contentious issues after litigation has commenced is best avoided, as the rules for lawyers' conduct make clear,[133] but is of less concern than the involvement of counsel in the matters which gave rise to that litigation.

[149] The present appeal illustrates the risks of counsel losing objectivity and of acting as a witness if they were personally involved in that way. Because he had been involved in negotiating and recording the terms of the interim agreement, it may have been difficult for Mr Hodder to be completely objective as counsel in advising NGC whether to plead rectification from the outset, rather than after the hearing of the appeal to this Court. And, at that hearing, Mr McIntosh sought to explain what he submitted were the differing meanings of "$6.50 per gigajoule" in his letter dated 5 October by asserting that "this was war". When asked whether the recipient of the letter should have appreciated that $6.50 was being used in a materially different sense because of the words "on the basis of the Agreement", Mr McIntosh protested that this was not a "fair question" to put to him. Enough said.

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132 [1940] NZLR 490 (CA), pp 506, 508 and 522.

133 Rule 14.12 of the Lawyers and Conveyances Act (Lawyers: Conduct and Client Care) Rules 2008.

**GAULT J**

[150] The background and facts are fully set out in the judgments of the other members of the Court. They are not in dispute.

[151] I have read and agree with the reasons and conclusion of Blanchard J. I consider also that this case can be approached without any detailed examination of the principles applicable to the interpretation to be given to the words of a formal contractual document. It can be determined simply by ascertaining objectively what the parties must be taken to have agreed to in their correspondence and that of their solicitors. It is not unusual for parties to formulate the terms of an arrangement progressively with a view to accepting contractual obligations when all the terms are agreed, as typically occurs with oral contracts. I regard this as such a case.

[152] It is not possible to comprehend all of the terms of the agreement by looking only at the letter dated 15 October 2004 written by NGC's solicitors to BoPE's solicitors as confirmed by the reply dated the same day. The letter states:

> We advise that NGC is prepared to agree to BoPE's suggested amendments to the terms of its proposal for interim supply set out in our letter of 8 October 2004. For the avoidance of doubt, the terms of the proposal are set out in full below. Please can you confirm BoPE's agreement to the terms of the proposal by return.
>
> 3 Without prejudice to its position, NGC will continue to supply gas based on the terms of the Agreement for Supply of Gas dated 10 October 1995 (the "Agreement") pending determination of BoPE's proceeding, or 30 June 2006, whichever is the earlier, provided that BoPE undertakes to:
>
> 3.1 file that proceeding on or before 31 October 2004; and
>
> 3.2 in the event that BoPE is unsuccessful in, or withdraws, that proceeding, pay NGC on demand, for each GJ [gigajoule] supplied, the difference between the price set out in the Agreement (as escalated) and $6.50 per GJ, plus interest at the Interest Rate set out in the Agreement, provided that such payment will not be triggered by a discontinuance which results from a settlement between the parties (the "interim supply arrangement").
>
> 4 BoPE may terminate the interim supply arrangement at any time on 7 days notice in writing. Such termination will not relieve BoPE of any payment obligation to NGC already incurred under the interim supply arrangement, including the requirement set out in paragraph 3.2 above.

[153] That letter specifies continuance of supply in terms of a prior agreement dated 10 October 1995. It refers to BoPE's proceeding to be filed, and it sets out a payment obligation in the event that the intended proceeding does not succeed. Although the letter purports to set out the terms of the interim arrangement "in full", those terms can be ascertained only with reference to extrinsic matters. It invokes details of the terms of supply of gas in the earlier agreement. It requires reference to prior communications to provide details of the intended proceeding and it is necessary similarly to go outside the letter to ascertain what the parties must have envisaged concerning the point at which gas at the price of $6.50 per GJ would be supplied. That is at source or delivered.

[154] I do not read the 15 October letter as specifying that the point at which the $6.50 price is to apply is to be taken from the 10 October 1995 agreement. While it says that agreement will prescribe the terms of the continuance of supply in the interim and fixes the price against which the $6.50 per GJ is to be compared, the letter does not state that the $6.50 per GJ (expressed in a proviso) is to be applied at the same point as the price set out in the earlier agreement.

[155] The earlier correspondence makes clear that the proceeding referred to would be brought to advance the claim by BoPE that NGC was not entitled to terminate the supply agreement dated 10 October 1995. The interim supply arrangement was reached "in lieu of … interim injunctive relief".

[156] In their letter dated 5 October 2004 the solicitors for BoPE stated that NGC in its letter under reply had confirmed:

> (aa) that it has sufficient gas available to supply BoPE for at least the interim period (and, indeed, for the remainder of the term of the Agreement, and beyond); and

(bb) the sale price of the gas in question (ie $6.50 per GJ), thereby quantifying the loss that NGC perceives either party will suffer, depending on the outcome of the litigation.[134]

[157] These points relate to what was said in the letter dated 28 September 2004 from NGC in which NGC offered (inter alia) to supply gas following termination of the 1995 Agreement at $6.50 per GJ "with transportation and metering passed through at cost". Rather than rejecting NGC's letter of 28 September, as was the Court of Appeal's view, I consider BoPE's letter of 5 October must be read as building upon it.

[158] Plainly when the parties referred to $6.50 GJ they were referring to that price which would quantify NGC's loss from continuing to supply under the 1995 Agreement. Both parties must be taken to have known (in light of current market prices) that it would do that only if it did not include transportation and metering costs. The correspondence thereafter consistently adopted the concept of the difference between the price set out in the Supply Agreement and $6.50 per GJ as appears in the letter of 15 October.

[159] Accordingly I consider that the parties must be taken to have agreed that the price of $6.50 GJ to apply once BoPE's proceeding was unsuccessful would be exclusive of transportation and metering costs.

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[134] That letter from Russell McVeagh dated 5 October 2004 went on to state:

5. In those circumstances, it would seem that the best course for the parties, in lieu of … having to apply for interim injunctive relief, would be for:
   (a) NGC to undertake, without prejudice to its position, to simply to continue to supply gas on the basis of the Agreement pending determination of BoPE's proceeding as above.
   (b) BoPE to undertake to:
      (i) file that proceeding on or before 31 October 2004; and
      (ii) in the event that BoPE is unsuccessful on its proceeding or withdraws it:
         (aa) pay NGC on demand, for each GJ supplied, the difference between the Agreement price and $6.50 (or the current market price, whichever is the lower), plus interest …

[160] I would allow the appeal with costs and restore the High Court judgment.

Solicitors:
Chapman Tripp, Wellington for Appellant
Russell McVeagh, Wellington for Respondent