Chapter 13

'I accept that both (i) construing the words which the parties have used in their contract and (ii) implying terms into the contract, involve determining the scope and meaning of the contract. However, Lord Hoffmann's analysis in *Belize Telecom* could obscure the fact that construing the words used and implying additional words are different processes governed by different rules.' (Lord Neuberger in *Marks and Spencer plc v BNP Paribas Securities Services Trust Company (Jersey) Ltd*).

What is the basis for the implication of terms in contract law?

Lord Hoffmann's analysis in *Belize* blurred the distinction between contractual interpretation and the implication of terms. While Lord Neuberger accepts that there are similarities between the two, in particular noting that both involve giving meaning to contracts, his Lordship maintains that they are fundamentally different exercises, drawing upon two important points. First, interpretation involves resolving ambiguities and attributing meaning to the language of the contract, whereas implication is concerned with matters for which the parties have made no provision. Second, since no term can be implied into a contract if it contradicts an express term, it follows that interpretation of the contract terms is a distinct stage that comes prior to any question of implication. In establishing that the two are separate exercises, Lord Neuberger reinforces the traditional requirements which have to be satisfied before a term will be implied, and the idea that the touchstone of implication is necessity, not reasonableness. This essay seeks to establish that interpretation and implication serve different purposes and are regulated by different tests, and that Lord Neuberger was right to distinguish between them in this recent Supreme Court decision. The scope of this essay will be confined to terms implied by the courts and will not discuss implication by statute, which is of practical importance but is relatively uncontroversial, given the democratic legitimacy of Parliament.

Kramer (in *Implication in Fact as an Instance of Contractual Interpretation* [2004] CLJ 384), like Lord Hoffmann, sees implication in fact as being different in degree, but not in kind, from interpretation; the same argument could apply to terms implied by law, since they are recognised as 'shades on a continuous spectrum' (Lord Wilberforce in *Liverpool CC v Irwin*). There is perhaps some truth in what Kramer and Lord Hoffmann have to say, as both interpretation and implication seek to give meaning to the contract by looking at its commercial purpose the context in which it was made. In *Investors Compensation Scheme*, Lord Hoffmann introduced a contextual/purposive approach to interpretation, by asking what a *reasonable* person, having all the background knowledge which would reasonably have been available to the parties in the situation in which they were at the time of contract, would have understood the words in the contract to mean. Subsequently in *Belize*, Lord Hoffmann commented that the traditional 'business efficacy' (*The Moorcock*) and 'officious bystander' (*Shirlaw v Southern Foundries*) tests for implying terms in fact are not independent tests, but a collection of different ways in which judges have expressed the 'central' question: is that what the instrument, read as a whole against the relevant background, would reasonably be understood to mean? The similarities between the two formulations are striking, but his Lordship's introduction of 'reasonableness' into implication is unsatisfactory.

Comment [A1]: But of course there may not be any ambiguity at all.

Comment [A2]: This should read as: 'no express provision'.

Comment [A3]: Should these requirements be highlighted here?

Comment [A4]: But surely *Belize* does not extend to terms implied at law – which rest upon a different basis.

Comment [A5]: Is this purposive approach universally accepted?

Comment [A6]: Although on a different reading *Belize* does not drift from necessity to reasonableness – see also *The Reborn*.

Lord Neuberger himself acknowledged that 'it is fair to say that the factors to be taken into account on an issue of construction, namely the words used in the contract, the surrounding circumstances known to both parties at the time of contract, commercial common sense, and the reasonable reader or reasonable parties, are also taken into account on an issue of implication' (at [27], *Marks & Spencer*). However, interpretation and implication are fundamentally different exercises. At its most basic, interpretation is concerned with a lack of specificity in the *language* of the contract, and implication with an *omission* altogether.

Comment [A7]: But as Lord Neuberger also says, perhaps both can be seen as determining the scope of the obligations owed.

The basis of implication is controversial. Parties may fail to include certain terms into their contracts for various reasons: they may have lacked the foresight, time and resources to draft an exhaustive contract. Thus, implied terms play a significant role as '[g]ap-filling is quite simply essential for contracting to work' (Low and Loi, *"The Many Tests" for Terms Implied in Fact: Welcome Clarity*(2009) 125 LQR 561). At the same time, it 'acts to supplement [the contract] with terms additional to those expressly chosen by the parties' (Davies, *Recent Developments in the Law of Implied Terms*(2010) LMCLQ 140); namely, it operates where the contract is silent. As Birmingham MR explained in *Philips Electronique*, the implication of contract terms involves a 'more ambitious undertaking' and is 'so potentially intrusive' upon the parties' freedom to contract that the law 'imposes strict constraints on the exercise of this extraordinary power'. For this reason, the courts have time and again stressed that the touchstone for implied terms is necessity, not reasonableness (*Mediterranean Salvage*), making it clear that 'construing the words used and implying additional words are different processes governed by different rules' (*Marks & Spencer*).

Comment [A8]: Can you interpret silence?

Necessity is present in the traditional tests of implication, which the Supreme Court has reinforced, in two senses: it serves to restrict the operation of contractual implication to instances where an implied term is necessary for the contract to work, and it ensures that the term (and obligation) implied into the contract is only as onerous as necessary to secure efficacy. The most famous test for implying a term in fact is the 'officious bystander' test, which allows the courts to imply terms which are so obvious for the contract to have effect that they need not be expressed (*Shirlaw*). In *The Moorcock*, Bowen LJ formulated the well-known 'business efficacy' test for implying terms in fact. The essence of the test, which can operate alongside or overlap with the test in *Shirlaw*, is similarly that, without the implied term, the contract will not work: the shipowner 'would be simply buying an opportunity of danger'. The Court of Appeal in this case, found it necessary to imply a duty, but declined to impose an absolute obligation on the wharf owner, only requiring that they take 'reasonable care to see whether the berth, which is the essential part of the use of the jetty, is safe', and if it is not, and they have not taken reasonable care, 'to warn the people with whom they have dealings that they have not done so'. Terms implied by law have the same theoretical basis;[they are standardised or general default rules 'necessary to the type of contract or relationship', and only a qualified duty as is necessary to give the contract effect is imposed (*Liverpool CC v Irwin*; although not necessarily to give effect to the *actual intentions* of the parties as wider policy considerations may be taken into account).

Comment [A9]: Perhaps worth exploring the relationship between the two a little more.

Comment [A10]: Compare *The Reborn.*

Comment [A11]: Controversial – not rest upon intention but wider policy considerations – so is this really the same basis? See eg *Peden.*

Lord Neuberger's judgment in *Marks & Spencer* is a welcome clarification of the law, reaffirming the traditional approach to implication, and the distinction between implication and interpretation. His Lordship does not deny that the two exercises are linked, but explains that they are different stages in the contractual enquiry, and have different bases. While interpretation asks what the reasonable

man would take the words of the contract to mean, implication is much more constrained and will only operate where it is necessary for the contract to have effect. It is a helpful, gap-filling device that the courts use with great caution, and rightly so, for it goes beyond the express words of the parties and entails supplementing terms into a contract that is otherwise silent.

Overall essay feedback: Very good – clear, well-structured and well-supported with detailed and careful use of a range of material. Perhaps you could bring out the possibility that interpretation and implication exist with some sort of "superstructure" of construction, and engage a bit more closely with what was said by Lord Hoffmann in *Belize*, as well as Lord Neuberger (and Lord Carnwath) in *Marks & Spencer*. But this is fluent and persuasive, and would probably get a First in the exam.