

# **PROPERTY CASE LAW KALEIDOSCOPE – RECENT DEVELOPMENTS**

## **LECTURE OUTLINE**

### **Introduction**

There is, in theory, no limit to this lecture. Even within a particular area or within particular areas of law there are any number of significant recent cases which deserve attention.

In an attempt to address this problem I have limited this lecture in three ways.

First, I have confined myself to only a few cases in the field of property law, and in particular landlord and tenant law.

Second, and as you will know, areas of law come and go. Litigation tracks the economy. As the economic tide goes out, problems that were obscured by a rising property market come into view. As those problems come into view they generate litigation very different to the sort of litigation we have seen over the past ten years. With this in mind I have paid particular attention to those areas where we can expect to see and/or are already seeing an upturn in legal work driven by the current economic climate.

Third, I have tried to concentrate on areas which are particularly relevant to property contracts, both in terms of negotiating such contracts, and in terms of dealing with such contracts when things go wrong.

This lecture is not therefore exhaustive. Within the above two parameters I have tried to pick out those cases which have, in my view, dealt with some of the issues which we, concerned with property dealings, are most likely to meet from day to day.

### **Proprietary estoppel – An uneasy relationship with Section 2 of the Law of Property (Miscellaneous Provisions) Act 1989**

Cobbe v Yeoman's Row Management Ltd [2008] UKHL 55

Thorne v Major [2009] UKHL 16

This first of these cases provides a salutary warning on the perils of taking the law to be settled by a first instance or Court of Appeal decision. Nearly two years ago I gave a lecture on recent case law, in which I dealt with the decision of the Court of Appeal in this case. I explained that the decision of the Court of Appeal continued to offer hope to those seeking to escape from the toils of Section 2 of the Law of Property (Miscellaneous Provisions) Act 1989. The facts were as follows. The claimant, an experienced property developer, orally agreed with the third defendant to purchase a property from the first defendant, a company of which the third defendant was the sole director. The property was to be converted into six town houses by the claimant, who would then retain the profit from the development, subject to an overage provision whereby the parties would share the profit above an agreed level. In the belief that the property would be sold to him at the agreed price the developer spent 18 months and considerable sums of money progressing the development project. Once planning permission had been obtained the defendants reneged on the oral agreement and demanded a larger sum for the development property. The judge at first instance allowed the claimant's claims in proprietary estoppel and constructive trust and awarded to the claimant a lien on the freehold of the property as to one half of the increased value produced by the grant of planning permission. The Court of Appeal upheld this decision. Section 2 of the 1989 Act was held to be irrelevant to a claim to enforce a cause of action for proprietary estoppel.

This triumph over Section 2 proved to be short lived. The House of Lords allowed the appeal of the first defendant and dismissed the claimant's claims based on proprietary estoppel and constructive trust. The House of Lords decided that the claimant was entitled to no more than a quantum meruit in respect of the money and services which he had provided in progressing the development project. Some commentators have greeted the decision of the House of Lords as heralding some kind of death of proprietary estoppel. A reading of the speeches in the House of Lords, given by Lord Scott and Lord Walker, does however show that the decision was not this far reaching. In the view of both Lord Scott and Lord Walker the critical point in the case was that both parties to the development had dealt with each other in the knowledge that they did not have a binding legal agreement for the development and sale of the property. The parties expected to enter into a binding legal agreement, but the full terms of that agreement remained to be settled. All that the claimant had was an expectation of an interest in the relevant land, which depended upon a successful negotiation of the outstanding terms of the contract for the sale of the land to the claimant. This was insufficient to found either a claim in proprietary estoppel or a claim in constructive trust. Lord Scott also expressed the view that if the relevant agreement between the parties had been a complete agreement but had failed to comply with the formalities required by Section 2, the agreement could

not have been rendered enforceable by proprietary estoppel. Proprietary estoppel cannot be used as a means as avoiding the requirements of Section 2.

The message from the decision in House of Lords in Cobbe is very clear, at least for those involved in commercial property dealings. Put all the terms of your agreement in writing, in one document, signed by all the parties. The days of entering into a lucrative development on the strength of handshake are well and truly over.

Like buses however, decisions of the House of Lords on particular areas of law often come all at once. No sooner had Cobbe been decided that the House of Lords had to consider Thorner v Major. This was what might have been described as a more conventional estoppel case. The claimant worked full time, and unpaid, on a farm owned by his father's cousin for a period of some 19 years. The father's cousin, Peter, was a widower with no children. Over the years Peter made various statements which caused the claimant to believe that he would inherit the farm on the death of Peter. Peter ultimately died intestate, having made and destroyed a will in which he left the farm to the claimant. The claimant sought a declaration against Peter's estate that he was entitled to the farm on the basis of a proprietary estoppel. At first instance this claim succeeded, but this result was overturned in the Court of Appeal where it was held that Peter's statements had been too vague to amount to a clear and unequivocal representation upon which Peter would have been entitled to rely. The point was also made by the defendants that the size of the farm had varied over the years, so that there was no certainty as to the property which was the subject of the alleged estoppel.

Following the decision in Cobbe the defendants could have been forgiven for thinking that the claimant's appeal to the House of Lords had little prospect of success. It was, after all, a lack of certainty of terms which had sunk Mr. Cobbe. The House of Lords however unanimously allowed the claimant's appeal. The essential reasoning of the House of Lords was that the question of whether a representation had sufficient clarity to found a proprietary estoppel depended upon the context in which it was made. The facts of the case were unusual in the sense that the claimant and Peter had been taciturn and undemonstrative men, who communicated obliquely but understood each other well. In the context of the case therefore there was sufficient certainty in the representations that Peter had made about the ownership of the farm on his death. The objection that there was no certainty in the extent of the property the subject of the alleged estoppel was also swept aside. In the view of their Lordships references to the farm meant the farm as it stood on Peter's death.

It is not easy to reconcile the reasoning of Cobbe and Thorner. In Thorner the claimant clearly had nothing even approaching a contract which would satisfy Section 2, but this did not matter. Proprietary estoppel would fill the gap. In Cobbe lack of certainty of terms was fatal to the claim in estoppel.

The relationship between Section 2 and proprietary estoppel remains unclear in the light of the Thorner decision. One other conclusion which may be drawn from these two cases is that, in relation to estoppel, context is all important. That which works between two taciturn farming men is much less likely to work between two commercial concerns involved in a commercial property transaction.

### **Landlord and Tenant (Covenants) Act 1995 – Rent reviews and original tenants**

Scottish & Newcastle v Raguz [2008] UKHL 65

The 1995 Act was, as you may recall, the product of the last property recession. A feature of the last property recession was a proliferation of claims made by landlords against original tenants of leases. The usual scenario was the insolvency of the current tenant, and a claim made against the original tenant by the landlord.

In relation to leases granted on or after 1<sup>st</sup> January 1996 the 1995 Act abolished the rule of privity of contract, releasing a tenant from his liabilities under the lease, subject to certain exceptions, on assignment of the lease. In relation to leases granted before 1<sup>st</sup> January 1996 the 1995 Act was not so generous, imposing only a procedure for giving notice where a claim for a fixed charge due under the lease was to be made against a former tenant under a lease.

Subsections (2) and (4) of Section 17 of the 1995 Act provide as follows.

*“(2) The former tenant shall not be liable under....the covenant to pay any amount in respect of any fixed charge payable under the covenant unless, within the period of six months beginning with the date when the charge becomes due, the landlord serves on the former tenant a notice informing him (a) that the charge is now due; and (b) that in respect of the charge the landlord intends to recover from the former tenant such amount as is specified in the notice and (where payable) interest calculated on such basis as is so specified....”*

*“(4) Where the landlord has duly served a notice under subsection (2)...the amount (exclusive of interest) which the former tenant....is liable to pay in respect of the fixed*

*charge in question shall not exceed the amount specified in the notice unless (a) his liability in respect of the charge is subsequently determined to be for a greater amount, (b) the notice informed him of the possibility that that liability would be so determined, and (c) within the period of three months beginning with the date of the determination, the landlord serves on him a further notice informing him that the landlord intends to recover that greater amount from him (plus interest, where payable)...*”

The facts of Scottish & Newcastle were somewhat complicated. In a simplified form they were as follows. The appellant was the assignee of two leases of hotel premises from the respondent original tenant under these leases. After further assignments the leases came into the hands of a company which went into administrative receivership. The leases were then sold by the receivers with the assistance of the respondent original tenant, who paid off the arrears of rent in order to secure the landlord’s consent to the assignments. Prior to paying off these arrears the respondent had received a number of statutory demands for rent, pursuant to Section 17 of the 1995 Act. During this period a rent review was in progress in respect of each lease, which had not been determined.

The respondent sought an indemnity from the appellant in respect of the arrears of rent paid by the respondent. The appellant argued that certain sums claimed by way of indemnity had not in fact been due from the respondent to the landlord, because the requisite notices had not been served pursuant to Section 17 of the 1995 Act. The sums of money in question were the excess rents produced on the conclusion of the rent reviews; that is to say the increase in the rent payable for the period between the rent review dates in the leases and completion of the rent reviews. These excess rents fell to be paid retrospectively for the period while the rent reviews were in progress.

At first instance Hart J. found that it did not matter whether these sums were legally due or not. In the circumstances of the case the indemnity claim extended to the excess rents produced upon the conclusion of the rent reviews. The Court of Appeal agreed. The real interest in the case lay however in the finding of Hart J., subsequently upheld by the Court of Appeal, that the excess rents had not in fact been due from the original tenant, because there had been a failure to serve the requisite Section 17 notices upon the original tenant. The conclusion of the Judge, indorsed by the Court of Appeal, was that Section 17(2) notices had to be served on the original tenant within six months of the quarter days on which the excess rent would have fallen due, had the process of rent review not been delayed. The landlord had not done this.

The bizarre result which flowed from this conclusion was as follows. In a case where a rent review is delayed beyond the relevant rent review date, and the rent, once reviewed, is payable retrospectively from the rent review date, it is likely that the rent review will produce a reviewed rent which is higher than the passing rent. Pending the resolution of the rent review the tenant will have been paying the passing rent, so that the difference between the passing rent and the reviewed rent will have to be paid, retrospectively, for the period between the rent review date and the conclusion of the rent review. The decision at first instance and in the Court of Appeal in this case meant that this excess rent fell to be treated as accruing due not when the relevant rent review has been concluded, but on each rent payment day between the review date and the conclusion of the rent review. So far as Section 17 of the 1995 Act was concerned, a landlord looking to preserve his ability to claim this excess rent from an original tenant or guarantor had to serve a Section 17(2) notice not within the period of six months from the point when the excess rent fell to be paid, but within six months of the rental day on which the excess rent would have fallen due, but for the delay in the rent review process. This had to be done even where the passing, pre-review rent was being paid and there were thus no actual arrears of rent. The consequence was that the Section 17(2) notice or notices had to be served within six months of rent days on which there were no arrears of rent in existence. This need to serve what was effectively a nil arrears notice was a substantial trap for the unwary.

The House of Lords have, by a majority, now reversed the decision at first instance and in the Court of Appeal. Three members of the House of Lords managed to find a way of reading the reference to the rent now due in Section 17(2) as meaning, in the case of a delayed rent review, the rent then due as the pre-review rent, not including the unascertained increase in the rent following completion of the rent review. This should come as a relief to landlords dealing with drawn out rent reviews. It should also be noted that the House of Lords also expressed the view, with the exception of Lord Scott, that the Judge and the Court of Appeal had been right to find that the indemnity claim could still be made in relation to the arrears of rent claimed by the respondent, even if the same had not been strictly legally due.

### **Surrender by operation of law – the continuing trap for the unwary landlord**

Artworld Financial Corporation v Safaryan [2009] EWCA Civ 303

Every property recession produces a clutch of cases involving tenants trying to get out of leases, and landlords trying to keep tenants in leases. Usually the dispute turns on the operation of a tenant's break clause. I am seeing such cases at the rate of about one every week at the moment. It

is however possible for a tenant to escape from an unwanted lease by another method, if a landlord does not keep his wits about him.

That method is surrender by operation of law. A surrender by operation of law occurs where the landlord's conduct amounts to an unequivocal acceptance that a lease has come to an end. The foundation of the doctrine of surrender by operation of law is estoppel. It is important to note that surrender by operation of law does not depend upon the intentions of the parties, but upon an objective assessment of their conduct. The classic case of a surrender by operation of law is where a landlord accepts back from his tenant the keys to the demised premises. If this acceptance takes place on an unqualified basis, there is likely to be a surrender by operation of law. Given that it may be agents of the landlord who accept the keys, the dangers for the unwary landlord are obvious.

This is just what happened to the landlord in the Artworld case. A large and luxurious house was demised by the landlord to the tenant. There were problems with the house, which caused the tenant to vacate the house before the lease had come to an end, and to hand back the keys to the landlord. The landlord proceeded to obtain what was described as a checkout report and an inventory. The landlord also made some limited use of the property itself while the property was empty. When the landlord then sued for the rent due to the end of the term of the lease, the landlord found itself confronted with the argument that the lease had been surrendered by operation of law. Unfortunately for the landlord this argument succeeded, both at first instance and in the Court of Appeal. The message of case is very clear for landlords. If a tenant vacates a property before the end of a term of a lease, do not, as landlord, accept back the keys or do anything else which may be construed as an acceptance that the lease has come to an end.

### **Forfeiture of deposits and completion of contracts**

Aribasala v St. James' Homes (Grosvenor Dock) Ltd (No. 2) [2008] EWHC 456 (Ch)

North Eastern Properties Ltd v Coleman [2009] EWHC 2174 (Ch)

### **The virtual assignment – does it work?**

Clarence House Ltd v National Westminster Bank plc [2009] EWHC 77

### **Administration pre-packs and insolvency**

John Thomas v Ken Thomas Ltd [2006] EWCA Civ 1504

Seahive Investments Ltd v Osibanjo [2008] EWCA Civ 1282

Innovate Logistics Ltd (in administration) v Sunberry Properties Ltd [2008] EWCA Civ 1455

The first of the above cases, in which I was involved, stretches the concept of a recent case well beyond any reasonable limit. I have not however included the case simply out of personal vanity. The case is likely to have considerably more implications now than at the time when it was decided. My client company went into a company voluntary arrangement. Included in the debts compromised by the CVA were certain sums due by way of rent on the premises occupied by the company pursuant to a lease. Prior to approval of the CVA the landlord had commenced forfeiture proceedings in respect of these arrears of rent. The forfeiture claim was held to have been ineffective by the Court of Appeal because, most unusually, the landlord had managed to waive his right to forfeit for the arrears of rent by accepting rent which had subsequently fallen due. This part of the decision is worth studying simply because it illustrates the dangers of a landlord accepting money from his tenant which is appropriated to a particular debt. If the landlord wishes to avoid the appropriation, the money cannot be accepted. Accepting the money under protest is not sufficient. The Court of Appeal also considered whether the compromise of the arrears of rent in the CVA had compromised the right to forfeit. The Court of Appeal held that it had. Neuberger LJ (as he then was) reviewed the tangle of case law on the nature of a proviso for re-entry and the effect of insolvency upon rights of re-entry, and came to the conclusion there was no right to forfeit in respect of non-payment of a debt compromised in a CVA.

On a similar theme is the more recent decision of the Court of Appeal in Seahive Investments Ltd v Osibanjo [2008] EWCA Civ 1282. In this case the landlord presented a bankruptcy petition against his tenant. Shortly before the hearing of this petition the landlord discovered that the tenant was in breach of covenant. The tenant secured the dismissal of the petition by sending a cheque to the landlord which covered both the sum due on the petition and other arrears of rent. The landlord banked the cheque and returned that element of the payment which represented the other arrears of rent. The tenant sought to argue that the landlord's processing of the cheque constituted a waiver of the right to forfeit for the tenant's breaches of covenant. This argument failed. The presentation of the bankruptcy petition did not constitute a waiver of the breach of covenant, nor did the acceptance of the sum due on the bankruptcy petition. The processing of the cheque by the landlord did not constitute the acceptance of the rent arrears which were not part of the bankruptcy debt.

Finally, I refer you to a more recent decision, Innovate Logistics, for an example of the approach taken by the Courts to applications for leave to take proceedings against companies in pre-pack administrations.

## **Construing Development Contracts – A cautionary tale**

Chartbrook Limited v Persimmon Homes Limited [2009] UKHL 38

On 16 October 2001 Chartbrook Ltd ("Chartbrook") entered into an agreement with Persimmon Homes Ltd ("Persimmon"), the well known house-builder, for the development of a site in Wandsworth which Chartbrook had recently acquired. The structure of the agreement was that Persimmon would obtain planning permission and then, pursuant to a licence from Chartbrook, enter into possession, construct a mixed residential and commercial development (commercial premises below, flats above, parking in the basement) and sell the properties on long leases. Chartbrook would grant the leases at the direction of Persimmon, which would receive the proceeds for its own account and pay Chartbrook an agreed price for the land. Planning permission was duly granted and the development was built. All that remained was for Chartbrook to be paid the agreed price. What could possibly go wrong?

Such contracts, which I refer to in this lecture as development contracts, are commonplace in the property world. It frequently happens that a developer will agree to purchase a development site, or will agree to develop a site and then purchase the site. In such situations the amount of the purchase price, or at least part of the purchase price, will often depend upon the outcome of events in the future. Equally, it is frequently the case that, in such situations, the contract to purchase the relevant land will itself be conditional. In such a case both the obligation to complete the contract and the settling of the purchase price may depend upon the outcome of events in the future.

In theory there should be no problem with such contracts. Take a simple example. A developer agrees to purchase a plot of development land from the owner of the land. A price, to be paid on completion, is agreed. The obligation to complete is however conditional upon satisfactory planning permission being obtained for the development of the plot of land. In theory, all that the draftsman of the contract has to do is to write into the contract a set of provisions which define what is meant by a satisfactory planning permission, and how the completion machinery is to work if a satisfactory planning permission is obtained.

In reality the position is nowhere near as simple as this. In reality the draftsman of the contract is required to set up, in the drafting of the contract, a system of legal obligations which regulates the application for planning permission, the obtaining of planning permission, the definition of what is a satisfactory planning permission, the obligations if a satisfactory planning permission is not

obtained, the termination machinery if a satisfactory planning permission is not obtained, and the completion machinery if a satisfactory planning permission is obtained. This is no easy task and, perhaps more important, it is not a short task.

In a rising property market problems with the drafting of such agreements may not matter too much. If the deal is profitable to all concerned, there is not the incentive to argue about the precise meaning of the agreement. When however the market turns down, the position is very different. In such cases contracts negotiated in good times become much less attractive when hard times arrive. In such cases a purchaser is very likely to look for a way out of the relevant contract, and/or to look for a way to lower the price. It is at that point that the drafting of the contract comes under very close, and unsympathetic scrutiny.

It is no accident that, since this time last year, a series of conditional contracts have crossed my desk, usually involving developers looking for a way out of obligations negotiated in better times. Are there lessons to be learned from these cases?

I believe that there are, and I believe that they are best learned by a close analysis of the case which I have described at the outset of this lecture, the full title of which is Chartbrook Limited v Persimmon Homes Limited [2009] UKHL 38.

### **The facts of Chartbrook**

As I have mentioned above, it was on 16 October 2001 that Chartbrook entered into its agreement with Persimmon for the development of a site in Wandsworth which Chartbrook had recently acquired.

The provisions for determining the agreed price were to be found in Schedule 6 to the agreement. The price was defined as the aggregate of the total land value and the balancing payment. The total land value was made up of three parts: total residential land value, total commercial land value and total residential car parking land value. Total residential land value was to be £76.34 per square foot multiplied by the area for which planning permission for flats was granted. Total commercial land value was £38.80 per square foot multiplied by the area for which planning permission for shops and other commercial uses was granted. Total residential car parking land value was £3,024 multiplied by the number of spaces for which planning permission was granted. The schedule set out the dates upon which the total land value was to be paid. In principle, payment would fall due as each flat, shop or parking space was sold. But there was also a

backstop provision for payment of specified percentages of the total land value (so far as not already paid) by dates commencing about two and a half years after the grant of planning permission and ending about two years later, by which time the whole sum was due, whether the properties had been sold or not.

The provisions about total land value required the insertion of the appropriate figures from the planning permission (which were not in dispute) into the formulae provided. The other element in the price was the balancing payment. Schedule 6 defined the balancing payment as the additional residential payment ("ARP") and then went on to define the latter expression. So ARP meant the balancing payment.

### **The dispute**

What was in dispute in the case, between Chartbrook and Persimmon, was the definition of the ARP.

In theory the position was simple. The definition of ARP was in the following terms.

*"23.4% of the price achieved for each residential unit in excess of the minimum guaranteed residential unit value less the costs and incentives."*

There were then three more defined concepts.

- (1) Residential unit meant a flat.
- (2) The minimum guaranteed residential unit value ("MGRUV") meant the total residential land value divided by the number of flats.
- (3) Costs and incentives ("C & I") meant the additional expense which Persimmon might have to incur to induce someone to buy a flat; for example, by providing fittings better than specification or paying legal expenses. Such payments were economically equivalent to a reduction in the price achieved.

### **The rival constructions**

#### **(1) Chartbrook**

Chartbrook's case went as follows. You took the price achieved, deducted the MGRUV and the C & I and calculated 23.4% of the result. That gave a figure for an individual flat which, together the figures for similar calculations on all the other flats, made up the ARP or balancing payment. That and the total land value constituted the price. On the agreed figures, that produced a total land value of **£4,683,565** and an ARP of **£4,484,862**, making **£9,168,427** in all.

## **(2) Persimmon**

Persimmon's case went as follows. Persimmon said that the purpose of dividing the price into total land value and ARP was to give Chartbrook a minimum price for its land, calculated on current market assumptions, and to allow for the possibility of an increase if the market rose and the flats sold for more than expected. It was agreed that, at the time of the agreement, the parties expected that a 700 square foot flat would sell for about £200,000 or so, maybe slightly more. The MGRUV at £76.34 a square foot for such a flat was £53,438 or 26.7% of a price of £200,000. If the realised price was £228,000, it would represent 23.4%. The purpose of the ARP was to provide that if the flats sold for more than £228,000, Chartbrook would be entitled to the amount by which 23.4% of the higher price exceeded the £53,438 MGRUV. What the definition therefore meant was as follows.

- (1) It was first necessary to deduct C & I from the realised price to arrive at the net price received by Persimmon.
- (2) It was next necessary to calculate 23.4% of that price.
- (3) The ARP was the excess of that figure over MGRUV.

On this method of calculation, ARP was **£897,051**, compared with Chartbrook's claim for **£4,484,862**. The purchase price was therefore, on Persimmon's construction of the relevant part of the agreement, significantly lower than the result contended for by Chartbrook.

## **The decision**

At first instance Briggs J agreed with Chartbrook. In the Court of Appeal a majority, comprising Tuckey LJ and Rimer LJ also agreed with Chartbrook.

Briggs J put the matter this way, at paragraph 53 of his judgment:

*"ARP means 23.4% of something. To the question '23.4% of what?' the clear answer is the excess of the price achieved for each residential unit over the MGRUV, less the costs and incentives."*

In the Court of Appeal Lawrence Collins LJ, dissenting, held that Persimmon's construction was correct.

All five members of the House of Lords also held that Persimmon's construction was correct, and overturned the decisions of the Judge at first instance and the majority in the Court of Appeal.

### **The reasoning in the House of Lords**

In his judgment in the House of Lords Lord Hoffmann set out the principles on which a contract (or any other instrument or utterance) should be interpreted, as summarised by the House of Lords in Investors Compensation Scheme Ltd v West Bromwich Building Society [1998] 1 WLR 896, 912-913. The question was what a reasonable person having all the background knowledge which would have been available to the parties would have understood them to be using the language in the contract to mean. It was emphasised that Courts "do not easily accept that people have made linguistic mistakes, particularly in formal documents". In some cases the context and background may drive a court to the conclusion that "something must have gone wrong with the language". In such a case, the law does not require a court to attribute to the parties an intention which a reasonable person would not have understood them to have had.

What drove Lord Hoffmann and his colleagues in the House of Lords to this decision was the consideration that interpreting the definition of ARP in accordance with ordinary rules of syntax made no commercial sense. The term "*minimum guaranteed residential unit value*", defined by reference to total residential land value, strongly suggests that this was to be a guaranteed minimum payment for the land value in respect of an individual flat. A guaranteed minimum payment connoted the possibility of a larger payment which, depending upon some contingency, might or might not fall due. Hence the term "*additional residential payment*". The element of contingency was held to be reinforced by paragraph 3.3 of the sixth schedule to the agreement, which spoke of the "*date of payment if any of the balancing payment*".

On Chartbrook's construction, there was virtually no element of contingency at all. ARP was payable in every case in which a flat sold for more than £53,438. Chartbrook's argument was that this was still a contingency, on the basis that the market for flats in Wandsworth might collapse. Lord Hoffmann was not impressed. He was not prepared to accept that any rational party who wished to make provision for such a catastrophic fall in the housing market would have adopted so precise a sum as £53,438 to represent an estimate of what might happen. That figure could not have been meant to play the part in the calculation which Chartbrook's construction assigned to it. It must have been intended to function as a minimum land value, not a minimum sale price. To compare it with the realised sale price would not have been comparing like with like.

As Lord Hoffmann pointed out, when the language used in an instrument gives rise to difficulties of

construction, the process of interpretation does not require one to formulate some alternative form of words which approximates as closely as possible to that of the parties. The task is to decide what a reasonable person would have understood the parties to have meant by using the language which they did. The fact that the court might have to express that meaning in language quite different from that used by the parties ("12 January" instead of "13 January" in Mannai Investment Co Ltd v Eagle Star Life Assurance Co Ltd [1997] AC 749; "any claim sounding in rescission (whether for undue influence or otherwise)" instead of "any claim (whether sounding in rescission for undue influence or otherwise)" in Investors Compensation Scheme Ltd v West Bromwich Building Society [1998] 1 WLR 896) was no reason for not giving effect to what they appear to have meant.

Lord Hoffmann accepted the following statement of the conditions to be satisfied in order to correct mistakes of construction. In East v Pantiles (Plant Hire) Ltd (1981) 263 EG 61 Brightman LJ stated the conditions for what he called "correction of mistakes by construction" in the following terms:

*"Two conditions must be satisfied: first, there must be a clear mistake on the face of the instrument; secondly, it must be clear what correction ought to be made in order to cure the mistake. If those conditions are satisfied, then the correction is made as a matter of construction."*

### **Two other points**

Two other features of the decision of the House of Lords in this case call for particular mention, before turning to the lessons to be learnt from this decision.

First, Persimmon argued that the House of Lords should take into account the evidence of pre-contractual negotiations, which in the opinion of Lawrence Collins LJ in the Court of Appeal, confirmed Persimmon's argument on construction. The general rule is that evidence of pre-contractual negotiations is inadmissible in construing contracts; see the decision of the House of Lords in Prenn v Simmonds [1971] 1 WLR 1381, 1384 where Lord Wilberforce said that earlier authorities "*contain little to encourage, and much to discourage, evidence of negotiation or of the parties' subjective intentions*".

Although several members of the House of Lords, and in particular Baroness Hale were clearly tempted to overturn the rule excluding evidence of pre-contractual negotiations in the construction of a contract, the House decided to affirm, rather than overturn this rule. Essentially their reasoning, as articulated by Lord Hoffmann, was that to allow evidence of pre-contractual negotiations to be used in aid of construction would require the departure from a long and

consistent line of authority, the binding force of which has frequently been acknowledged. It was felt that there was no clearly established case for departing from the exclusionary rule. The exclusionary rule was justified in the more general interest of economy and predictability in construction of contracts.

Second, Persimmon ran an alternative argument that, if it was wrong in its case on construction, it was entitled to rectification of the agreement in order to get to its desired result.

The requirements for rectification were summarized by Peter Gibson LJ in Swainland Builders Ltd v Freehold Properties Ltd [2002] 2 EGLR 71, 74, at paragraph 33 in the following terms.

*"The party seeking rectification must show that: (1) the parties had a common continuing intention, whether or not amounting to an agreement, in respect of a particular matter in the instrument to be rectified; (2) there was an outward expression of accord; (3) the intention continued at the time of the execution of the instrument sought to be rectified; (4) by mistake, the instrument did not reflect that common intention."*

Although this was unnecessary to the decision in the case, because Persimmon won on construction, it was held that Persimmon could have succeeded in a rectification claim, had the same been required. Lord Hoffmann summarised the pre-contract evidence, and made the point that the common continuing intention, whether or not an actual agreement, fell to be ascertained as a matter of objective fact. It did not depend upon the actual subjective belief of the parties, but upon what, objectively, their continuing common intention could be said to have been. There was in the case the necessary prior consensus in the form of a pre-agreement letter, the terms of which were accepted by Chartbrook and were not subsequently departed from. It therefore followed that (on the assumption that the judge was right in his construction of the ARP definition) both parties were mistaken in thinking that it reflected their prior consensus and Persimmon was entitled to rectification. Persimmon's appeal was not however allowed on that ground, because Persimmon succeeded in its primary argument on construction.

So it was that Persimmon ultimately won the case. It won the case however after tramping through the Court at first instance, the Court of Appeal and the House of Lords, and after the expenditure of what must have been many thousands of pounds in costs, and a huge amount of lost management time. If there are lessons to be learnt from this case, what are they?

### **Lessons to be learnt from Chartbrook**

I believe that there are two principal lessons to be learnt from Chartbrook. I also believe that those lessons can be learnt equally well by all who have dealings with what I am defining as development contracts, whether lawyers or non-lawyers, and whether dealing with the drafting of a development contract or a dispute over a development contract.

First, a key factor in the reasoning and decision of the House of Lords was the commercial consequences of Chartbrook's construction being right. As Lord Hoffmann put the matter, to interpret the definition of ARP in accordance with the ordinary rules of syntax made no commercial sense. The MGRUV value of £53,438 was the basic payment which Chartbrook was to receive for each of the flats. On Chartbrook's construction Chartbrook was then guaranteed 23.4% of the difference between this figure and the net sale price of each flat. Absent a truly catastrophic crash in Wandsworth flat prices, Chartbrook stood to receive a substantial sum in every case. The commercial sense of the agreement was that it was a percentage of the net sale price of each flat which fell to be compared with the base figure of £53,438. The comparison exercise might or might not produce an excess, as between the percentage figure and the base figure of £53,438. This accorded with the commercial sense of the agreement.

This is a point worth remembering, particularly in a dispute over the meaning of a particular provision in a development contract. If the relevant provision is ambiguous, and one reading of the provision produces a commercially absurd result, a dispute over the construction of the provision is unlikely to be resolved in favour of the commercially absurd result. As a general rule Courts do not like to construe contracts in ways which produce commercially absurd results, unless driven to do so by unambiguous wording. Even unambiguous wording may not survive if it is the result of an obvious mistake, and it is clear what correction needs to be made in order to cure the mistake; see the statement of Brightman J., quoted above, in the East case.

Second, it is worth observing how easily many thousands of pounds worth of litigation might have been avoided. It will be recalled that the formula which was in issue in this case was as follows.

*"23.4% of the price achieved for each residential unit in excess of the minimum guaranteed residential unit value less the costs and incentives."*

Could this formula have been recast into a formula which was not ambiguous and expressed the meaning for which Persimmon contended?. I suggest that it could have been so recast, fairly simply.

*"ARP means the amount, if any, by which 23.4% of the net sale price achieved for each*

*residential unit exceeds the minimum guaranteed residential unit value. The expression “the net sale price” means the price achieved for each residential unit less the costs and incentives.”*

As you will see this recasting of the formula identifies the figure to which the percentage is to be applied, and identifies the figure with which the percentage is to be compared. It is not the only way to deal with the drafting. It is perfectly possible to think of other ways of resolving the ambiguity. In particular it is not necessary to be clever, or to have any particular legal or drafting skill to resolve the ambiguity. There is no harm in taking time to spell out what a particular provision is saying. There are no marks for elegance in drafting. It is better to be long winded, and put matters beyond doubt, than to try to produce something short which leaves space for argument over what was meant.

Hindsight is of course a wonderful thing. I suggest however that hindsight is, to some degree, something which can be learnt. It always pays and it may pay an awful lot, when drafting a development contract, to stand back from contractual machinery and ask two questions.

- (1) Does this contractual machinery work, in the way I want it to work, if I apply it to some specific examples?
- (2) Will this contractual machinery be understood to work, in the way I want it to work, by someone picking up the development contract for the first time?

If the answers to these questions are not both in the affirmative, it is time to go back to the drawing board.

EDWIN JOHNSON QC

Maitland Chambers

Lincoln's Inn

[ejohnson@maitlandchambers.com](mailto:ejohnson@maitlandchambers.com)

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