JOURNAL OF CONTEMPORARY MANAGEMENT
VOLUME 11

# A new approach to the interpretation of contracts and the management of strategic corporate relationships

**D DONNELLY** (University of KwaZulu-Natal)

**Abstract**
The paper sets out the most recent legal theory on the approach to be taken by courts to the interpretation of contracts, and examines how this approach has been applied in two recent decisions of the South African Supreme Court of Appeal and the United Kingdom Supreme Court. The new iterative approach to contractual interpretation emphasises reading language in context, as a means to achieve the contractual purpose, despite unclear contractual wording, giving preference to a business-like result.
However, legal theory of contractual interpretation disallows any reference the contracting parties' actual intentions and remains bound by the language used. Courts cannot rewrite what may turn out, in the light of changed (or unanticipated) circumstances, to be a bad bargain.
The paper examines inter-disciplinary connections between this legal theory and management studies on the substitutability/compatibility of formal contracts and relational contracts in the management of strategic relationships. Formal contracts are viewed as an inadequate, or even destructive, means to secure post-contractual cooperation between parties when adapting to changing environments. However, a recent empirical study has suggested that formal contracts can enhance post-contract cooperation when used to balance risk allocation and create trust and perceptions of fairness in strategic alliances.

***Key phrases***
*interpretation of contracts, iterative approach to interpretation, relational contract theory, risk and trust in strategic interorganisational relationships*

## 1. INTRODUCTION

In 2012, an important legal decision was handed down by the Supreme Court of Appeal, which will have ramifications for the interpretation of commercial contracts. The decision, NJMPF v Endumeni (2012), set out comprehensively for the first time in South African law, a new approach to interpretation that has been called an 'iterative' or 'unitary' approach to the construction of legal documents.

There remains debate about whether the new approach to interpretation represents "a fundamental change" (Lord Hoffmann in ICS v West Bromich Building Society 1998:114), or

merely "a change of emphasis" (Bingham 2008:374; Lewison 2011:3). Nevertheless, it has brought about a greater flexibility in the court's treatment of the actual words used in the contract. It is this flexibility which suggests possible connections to management studies on the substitutability/compatibility of formal contracts and relational contracts in the management of long-term strategic relationships between independent corporate organisations.

This paper will first consider the theoretical framework of relational contract theory. It will then set out the legal theory of 'iterative interpretation' of legal documents, as outlined and applied in South Africa's Supreme Court of Appeal and, in the most recent case, in the United Kingdom's Supreme Court. Finally, conclusions will be drawn about whether this new approach to interpretation of contracts addresses any of the shortcomings of formal contracts as a management device for long-term strategic corporate relationships.

## 2. RELATIONAL CONTRACT THEORY AND THE MANAGEMENT OF LONG-TERM STRATEGIC RELATIONSHIPS

Long-term strategic relationships between corporate organisations, such as joint ventures, entail high levels of risk and require high levels of trust (Ring & Van de Ven 1992:492). The large number of unknowns involved at the commencement of such relationships creates particularly difficult problems for the drafting, interpretation and enforcement of the formal contracts framing such relationships.

Early transaction cost economics (TCE) analysis raised questions about the efficacy of contractual governance models in cooperative relationships (Ring & Van de Ven 1992:485). Rejecting the assumptions of TCE, Ring & Van de Ven (1992:485) outlined a role for 'relational contracts' as a governance structure for strategic relationships, such as those employed for joint research and product development goals, without the high investment costs of mergers and the need for hierarchical management structures.

However, whilst once-off market-based contracts (e.g. sale and purchase) and even repetitive contractual relationships, are well-regulated by existing contract law and legal enforcement measures (Ring & Van de Ven 1992:485,492), 'relational contracts' on the other hand, rely upon internal dispute resolution mechanisms rather than legal enforcement as the means to preserving the long-term relationship, in the interests of realising long-term equity and efficiency outcomes (Ring & Van de Ven 1992:487).

The imperative in framing long-term strategic contracts is to permit adaptation whilst fostering co-operation (Beuve & Saussier 2012:1-2). Scepticism exists about the ability of

formal contracts to achieve such outcomes, and a body of literature has reiterated the proposition that such relationships rely on 'self-enforcement' (Beuve & Saussier 2012:2) and that formal contracts may ultimately erode cooperation and trust (Beuve & Saussier 2012:4).

Relational governance and formal contracts have thus been seen as substitutive rather than as complementary (Beuve & Saussier 2012:18). Traditional analysis restricted the role of the formal contract to relationships without an existing trust relationship, where a formal contract may be utilised to enhance investment incentives and restrain adaptability in order to manage the risk of opportunistic behaviour by contracting parties (Beuve & Saussier 2012:4). Beuve and Saussier's study (2012:3), however, illustrated that the position in the case of highly strategic relationships is more complex, and that formal contracts and relational governance need to be assessed conjointly.

A contract is almost always signed, although co-operation can be achieved without an 'ex-ante' attempt to frame the relationship in terms of a formal contract (Beuve & Saussier 2012:3). Formal contracts are intended to discourage opportunistic behaviour between contracting parties and build trust, and Beuve and Saussier (2012:3) found no evidence that they had the opposite effect.

Formal contracts are in themselves not adaptable. Other commentators have asserted that governance structures which emphasise close monitoring and detailed contractual conditions discourage exploration and adaptation to changing environments (Sorenson & Sorensen 2001:716) and promote certainty over flexibility (Puig 2012:326).

Beuve & Saussier (2012:4) found that, in fact "formal contracting increases the probability of ex-post cooperation between the contracting parties when hazards become severe" and when the relationship is a strategic one. In such circumstances, the parties would be encouraged to seek relational solutions, overcoming the adaptive limits of the formal contract. The formal contract "secures an agreement, increases transparency in the partnership, facilitates learning processes about each partner's conduct, and helps to promote cooperation." (Beuve & Saussier 2012:20).

Thus, they found that in highly strategic relationships there was a positive correlation between the existence of a formal contract and levels of cooperation and trust (Beuve & Saussier 2012:21). The question that arises in these circumstances is how commercial contracts should be drafted and interpreted to ensure that the purposes of the strategic relationship are achieved.

Two considerations appear to be particularly important. Firstly, continued cooperation relies upon "both parties' sense of fairness in their on-going relationship" (Beuve & Saussier 2012:4). When conflict arises and the contract is perceived to operate unfairly, parties are more likely to resile from the agreement, although Beuve & Saussier's findings, concerning the importance of reputation as a factor in maintaining co-operation, might operate in such circumstances as a check on opportunistic behaviour (Beuve & Saussier 2012:6).

Secondly, "the contract is pushed to the background in the daily relationship between firms and is considered only as a reference point in case of conflict" (Beuve & Saussier 2012:5). At such times, the contract should provide a mechanism for balancing the risks borne by the parties, or what is referred to as "hazard equilibrium" (ibid.)

# 3. THE NEW APPROACH TO THE INTERPRETATION OF CONTRACTS

## 3.1 The flexibility of language and elusiveness of a single meaning

A characteristic of long-term strategic relationships, that makes them particularly difficult to regulate by means of formal contracts, is the fact that there are significant 'gaps' in knowledge when the contract is formulated, and that it is impossible to design a contract to cover every eventuality that may arise in the course of the relationship between the contracting parties (Beuve & Saussier 2012:2). Furthermore, language is now recognised by our courts as being inherently flexible and capable of multiple meanings, depending on the context in which it is used (NJMPF v Endumeni 2012).

Thus inevitably, no matter how detailed the contract, conflict may arise when an unexpected event occurs and the parties realise that the formal agreement is capable of a construction that was not anticipated by either of them in the drafting process. Even if the parties had anticipated the event, it is possible that under new or altered circumstances they now perceive it to operate unfairly, and put forward an interpretation of the contract that was not contemplated when it was entered into, but which appears as one of the available (possible) interpretations of the words used.

## 3.2 An objective approach

The legal rule regarding interpretation of contracts in South Africa, which is sometimes surprising to non-lawyers, is that the subjective intention of the parties at the time of contracting, leaving aside the remedies of rectification and estoppel, is irrelevant to the

court's determination of the meaning of the contract (Wallis 2010:679). In short, the words chosen must speak for themselves.

According to Lewison (2011:para 2.05) the intention of the parties has no existence independent of the meaning of the words of the contract. Increasingly, this intention is being regarded as a troublesome fiction rather than a helpful aphorism. This is not a universal position. The subjective approach is favoured in Europe (Lewison 2011:24), where studies such as the one in France by Beuve & Saussier (2012) were conducted.

### 3.3 Primacy of the words used in the contract

A necessary corollary of the objective approach to contractual interpretation is that the words used remain the first source of reference. The principles of interpretation of contracts, developed in the nineteenth century, were marked by a slavish devotion to language (text) at the expense of context. The approach was highly formalistic, relying on established canons of constructions (namely, rules by which the interpretative task was to be undertaken). The first or 'golden' rule was that words were to be given their 'ordinary grammatical meaning'. Only in cases of ambiguity was reference permitted to 'context' in the sense of the terms of the contract as a whole, and the background to and purpose of the contract.

Emphasis on the words used by the parties can run counter to business sense, with some of the more outlandish results of literalism prompting the question: "Surely we have a right to expect some modicum of intelligence from the judiciary?" (Spigelman 2005:internet). Against this background, it is therefore unsurprising to note that writers in the field of management studies have regarded formal contracts as eroding rather than promoting cooperation and trust in relationships between contracting partners.

## 4. THE APPLICATION OF THE NEW APPROACH TO INTERPRETATION IN NJMPF V ENDUMENI (2012)

Over the last century, literalism has slowly fallen out of favour and, more recently, a new approach to interpretation has emerged. The new approach is referred to as an 'iterative process', having first been described as such by the United Kingdom Court of Appeal in Re Sigma Finance Corp (2008).

This new approach was fully outlined and applied for the first time in South Africa in the case of NJMPF v Endumeni (2012).

## 4.1 The facts of NJMPF v Endumeni (2012)

The case required the court to interpret regulations governing the relationship between the Natal Joint Municipal Pension Fund and its members. It arose when a retiring member, who was a senior employee in the Endumeni Municipality, utilised the ability to switch between funds to enhance his retirement benefit in such a way that, although he was only 43 years old, his retirement package would be calculated on a notional 45 years of service. He did so by contributing to the provident fund on the basis of a pensionable emolument of R5000 per month (well below his actual earnings) and switching to the Superannuation Fund ('the Fund') twelve months before retiring, and paying a contribution to the Fund up to his retirement twelve months later, based on a pensionable emolument of R34000 per month. As a result, he received a withdrawal benefit of R2,7 million, which was only partially funded.

From a legal perspective, this result was "not only possible but entirely legitimate" (NJMPF v Endumeni 2012:para 2). Thus, although to the layperson there may appear to be something unethical in the employee's actions (moreover, since after receiving his retirement benefit he was immediately re-hired as a consultant) there was nevertheless no legal question about his entitlement to the benefit.

What gave rise to the litigation was the Fund's response to this unanticipated event. It sought to recover the shortfall in funding by claiming an adjusted contribution from the Endumeni Municipality under the proviso to the definition of 'pensionable emoluments' in reg 1(xxi)*(h)* of the regulations governing the operations of the Fund. Without such recovery it would have been underfunded and left with no alternative but to draw on the Fund's surplus (thus reducing member benefits) or raise a surcharge against all municipalities participating in the Fund.

The proviso in question read:

*'Provided further that, should at any time the pensionable emoluments of a member including a section 57 contract employee, increase in excess of that assumed by the actuary from time to time for valuation purposes in terms of Regulation 13, then the committee on the advice of the actuary, may direct that the local authority employing such member pay an adjusted contribution in terms of Regulation 21 to the Fund; …' [my emphasis].*

## 4.2 Rejection of the traditional approach to interpretation

The stance adopted by Endumeni Municipality was quite simply that its employee's actual pensionable emoluments had remained the same during the entire period of his membership

of the Fund. The proviso referred only to an increase in a member's pensionable emoluments and was thus plainly inapplicable if the words were given their 'ordinary meaning'. At first instance this argument had succeeded, but that approach was wrong.

When the words were interpreted in context from the outset, they took on an entirely different meaning. In performing a statutory valuation of a defined benefit fund, the actuary calculates assets and liabilities on the basis of 'reasonable long-term assumptions' about the whole body of members and not upon the pensionable emoluments of any particular member. The section was concerned primarily with the recovery of an underfunding situation caused within a particular local authority. Whilst an increase in any particular member's pensionable emoluments during his membership of the Fund may be the usual way that such a deficit arises, and was a problem of particular concern to the actuary at the time the proviso was drafted, it was not the only way an underfunding situation could arise.

The court thus had greater latitude to find that the regulation did cover the unforeseen eventuality that arose when members manipulated the ability to switch between funds, as this resulted in an increase from the 'imputed' level of pensionable emoluments applied at the time of the switch (NJMPF v Endumeni 2012:para 35). The Supreme Court of Appeal has thus rejected reference to the 'ordinary meaning' of words (divorced from context) and to the 'intention of the parties'. The new approach is encapsulated in the injunction that "from the outset one considers the context and the language together, with neither predominating over the other" (NJMPF v Endumeni 2012:para18).

This, it is must be said, is not altogether a revolutionary approach, for the Court was in fact citing the words of Schreiner JA half a century earlier in the case of Jaga v Dönges NO (1950: 662-663) and reviewed in Bastian Financial Services v General Hendrik Schoeman Primary School (2008:paras 16-19). However, despite earlier moves away from formalism there was still a reluctance to jettison the formal rules of interpretation altogether, and those rules have, until now, to a greater or lesser extent, been applied in most judgments, despite the inherent 'internal tensions' of that approach (Wallis 2010:675).

### 4.3 The essence of the new approach to interpretation

A new approach to interpretation is now laid down in the judgment which does not rely on the old rules of interpretation:

1. The process of interpretation is objective not subjective. That means that it remains impermissible to consider what either of the contracting parties actually thought the words meant at the time of contracting.

2. The document should be given a sensible, businesslike meaning; one that upholds rather than undermines the apparent purpose of the document.
3. The language used remains "the point of departure" (para [18]). However, there is no place for resort to the 'ordinary' meaning of the words, a purely linguistic resolution of possible ambiguity or resort to the subjective meanings in the minds of either party.
4. The meaning of the language is to be ascertained by paying regard to words used and "the ordinary rules of grammar and syntax", but always "read in context and having regard to the purpose of the provision and the background to the preparation and production of the document." (para [18]).

The approach is iterative in that it requires that language and context be viewed together from the beginning, as part of a unitary interpretative process, and that they be checked and re-checked against one another to determine the true meaning of the words used (Grabiner 2012:41; In Re Sigma Finance Corp 2008:para 98).

## 5. RELEVANCE OF THE NEW APPROACH TO DRAFTING AND INTERPRETATION OF FORMAL CONTRACTS

An understanding that courts will adopt an iterative approach to interpretation of commercial contracts should encourage parties to approach the task of drafting and interpreting their contracts with business sense. It should promote trust, in that unbusinesslike results which do not promote the purpose of the agreement will not be upheld by the Court.

The Supreme Court of Appeal has said of the new approach to interpretation:

*"That is how people use and understand language and it is sensible, more transparent and conduces to greater clarity about the task of interpretation for courts to do the same." (NJMPF v Endumeni 2012: para 22)*

The new approach has not altered the fact that, whilst as a matter of policy the law strives to uphold contractual bargains, it will neither re-write a bad bargain nor give legal effect to an agreement that is too vague to give rise to certain and binding contractual obligations. Thus, in the case of relational contracts, parties will continue to have difficulty enforcing agreements which leave provisions required for implementation up to future negotiation and agreement.

However, the old rules of interpretation are no longer the 'inviolable principles' by which a Court will determine what the agreement means and whether it is vague (see for example

the approach of the majority in Namibian Minerals Corp v Benguela Concessions 1997:563-564). If that approach is no longer followed, there may be cases in which a court, interpreting the language used in context, is able to give business sense to the document. There may even be cause to reconsider giving effect to expectations of good faith in the negotiation and implementation of contracts.

## 6. LIMITATIONS OF THE NEW APPROACH

The limitations of the new approach must be understood. What was not clarified in the decision of NJMPF v Endumeni (2012), because it did not arise on the particular facts, was the extent to which the Court can substitute the words used in the contract.

### 6.1 The problem of uncertainty

In a series of decisions, commencing with Mannai Investment Co v Eagle Star (1997:749), Lord Hoffman had indicated that the court was not bound by the parties' use of the 'wrong' words, although it was emphasised that language remained primary, as "we do not easily accept that people have made linguistic mistakes" (ICS v West Bromwich Building Society 1998: 114-115). Provided, however, it is clear that "something has gone wrong with the language" and it is clear what "a reasonable person would have understood the parties to have meant" there is "[no] limit on the amount of red ink or verbal rearrangement or correction which the court is allowed" (Chartbrook v Persimmon Homes 2009:para 25).

The negative consequence of permitting the courts greater latitude to move beyond the actual words used by the parties is that this may lead to greater uncertainty for contracting parties about how their contract will be interpreted, which will also impact third parties relying on the contract. Uncertainty is attended by increased risk (Spigelman 2007:internet) which undermines the purpose of concluding a formal contract. Many detractors of the new approach raise the spectre of undue delays and costs to litigation (N.L.A Group v Bowers 1999:109) although this can be kept in check if judges restrict the admissible evidence to what is relevant (BCCI v Ali 2002: 269; Lewison 2011:13).

The problem of uncertainty was not avoided by resort to formal rules of interpretation. Different judges could, and frequently did, take opposing views on the 'ordinary' meaning of the words used (Hoffmann 2007:671; Wallis 2010:680). However, interpreting the meaning of words in context is an 'intricate' and difficult exercise (Richter v Bloemfontein Town Council 1922:69), accounting for 'judicial caution' inherent in the old approach (Wallis 2010:687). It appears that in recent judgments a good measure of such caution has been applied.

## 6.2 Constraints imposed upon judicial freedom of interpretation

The Supreme Court of Appeal has correctly emphasised that there are limitations on the extent of judicial 'interpretation' permitted:

*"Judges must be alert to, and guard against, the temptation to substitute what they regard as reasonable, sensible or businesslike for the words actually used. To do so ... is to make a contract for the parties other than the one they in fact made." (NJMPF v Endumeni 2012: para 18).*

Further, no interpretive approach can ever be truly objective. Instead of purporting to uncover the subjective intention of the parties, the court is required to determine how the contract would be understood by "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 the contract" (Rainy Sky v Kookmin Bank 2011: para 14).

This approach is called objective to distinguish it from a search for the subjective intention present in the 'minds of the parties', but no one ignores the fact that the 'reasonable person' is a fiction. In reality, it is suggested that the task of a Court is simply to do its best to advance an interpretation that the Court considers an ordinary person would regard as reasonable, and to be reasonable it must be sensible and business-like when viewed in the context, ascertained as fully as possible within the constraints of the way the case was presented. It is never going to be possible to escape the fact that interpretations of what is commercially reasonable can and will legitimately differ (Chartbrook v Persimmon Homes 2009: para 15; Goff 1984:391 and Lewison 2011:8).

## 6.3 The facts of Rainy Sky v Kookmin Bank (2011)

The difficulties that may be encountered in applying the new approach are illustrated in the recent case of Rainy Sky v Kookmin Bank (2011). The case concerned the interpretation of shipbuilder's refund guarantees issued in respect of six shipbuilding contracts, each between one of the six claimants and Jinse Shipbuilding Co Ltd respectively. Each shipbuilding contract provided for the construction by Jinse and sale to the claimants of a ship, and each contract required the builder to ensure that the buyer was issued with refund guarantees in respect of the price of US$33,300,000.

Those guarantees (termed "Advance Payment Bonds") were issued by the respondent, Kookmin Bank. After payment of the first instalment, Jinse began experiencing financial difficulties and was placed under a 'debt workout procedure' under the Korean Corporate Restructuring Promotion Law 2007. A dispute arose between the claimants and Jinse as to

whether this event triggered a repayment provision in the shipbuilding contracts, and that dispute was referred to arbitration.

While these proceedings were pending, the claimants each demanded repayment under the Bonds of the instalments already paid. Kookmin Bank refused this demand and it is not a stretch to speculate that it was only at that point that either party paid sufficient attention to the wording to note that the Bonds contained an apparent contradiction. The relevant paragraphs of the Bonds read:

*"[2] Pursuant to the terms of the Contract, you are entitled, upon your rejection of the Vessel in accordance with the terms of the Contract, your termination, cancellation or rescission of the Contract or upon a Total Loss of the Vessel, to repayment of the pre-delivery instalments ...[my emphasis]*

*[3] In consideration of your agreement to make the pre-delivery instalments under the Contract ...we... undertake to pay to you... on your first written demand, all such sums due to you under the Contract ..." [my emphasis]*

The wording of paragraph 3 (principally the words "all such sums due to you under the Contract") were the subject of two competing interpretations.

The claimants argued that the purpose of the Bonds was to guarantee the repayment of any instalments paid prior to delivery of the ships and that accordingly, "all such sums" meant the "pre- delivery instalments" referred to in the first line of paragraph 3. It thus covered pre-delivery instalments that were repayable under the contracts in the event of insolvency.

Kookmin Bank argued that the wording of paragraph 2 of the Bonds restricted the scope of the Bonds to repayment consequent upon termination of the contract or a total loss of the vessel.

## 6.4 Outcome of the decision in Rainy Sky v Kookmin Bank (2011)

The bank's argument was rejected by the judge at first instance, but upheld on appeal, only to be rejected again by the Supreme Court, in an apparent judicial to-ing and fro-ing explained, in part, by the fact that the three courts had approached the interpretative task in very different ways.

At first instance, the Judge emphasised that, in relation to each transaction, the Bonds and the shipbuilding contract were separate agreements. Thus it regarded the task as being, first and foremost, the interpretation of the Bonds and the Bonds alone. Had it not reached

the conclusion that the wording of the Bonds was ambiguous, it might have forgone further enquiry into the background or context. This is at odds with the new approach to interpretation, as resort to the wider context is no longer constrained by the existence of ambiguity within the text.

In the Court of Appeal, emphasis was placed upon the well-accepted doctrine that the court's task is not to ascertain the subjective intention of the parties. Allied to this, the court's task is not to 'rewrite' a poor commercial bargain. If contract terms appear unfair but are clear, they will be enforced. The rationale behind such a policy is that the court is not privy to the negotiations and the myriad commercial reasons which may have prompted the parties to frame their agreement in those terms. These principles are not in question (Rainy Sky v Kookmin Bank 2011:para 20).

However, the Court of Appeal went on to hold that "[u]nless the most natural meaning of the words produces a result which is so extreme as to suggest that it was unintended, the Court has no alternative but to give effect to its terms." That approach is wrong according to the Supreme Court (Rainy Sky v Kookmin Bank 2011:para 20). In the new approach, words do not need to be ambiguous, much less give rise to absurdity, before context is considered.

The proper application of the new approach requires language to be considered together with context from the outset. To that principle may be added that "in the event of doubt, the working assumption will be that a fair construction best matches the reasonable expectations of the parties" (Steyn 1997:441). It has further been held that "the reasonable commercial person can safely be assumed to be unimpressed with technical interpretations and undue emphasis on niceties of language" (Society of Lloyd's v Robinson 1999:551). Adopting such an approach, the Supreme Court upheld the buyer's claim that the Bonds did cover the insolvency event.

## 6.5 Caveats concerning the new approach to interpretation

Three caveats are raised. The first is that, when it came down to it, the difference between the judgments was that the Court of Appeal regarded one construction as reasonable and the Supreme Court preferred another (Davies 2012:26; Rainy Sky v Kookmin Bank 2011:para 34 and Stevens 2010:551).

Secondly, at certain points the Supreme Court lapsed into language reminiscent of the old rules, saying that, if it had to decide the question on language alone, it preferred the buyer's construction of the Bonds (Rainy Sky v Kookmin Bank 2011:para 40), that it disagreed that

the bank's construction was the most "natural and ordinary meaning" of the Bonds (Rainy Sky v Kookmin Bank 2011:para 34]), and that reference to common sense and commercial purpose was permissible because there were two competing interpretations, i.e. ambiguity (Rainy Sky v Kookmin Bank 2011:para 40).

There appears to be a residual tension inherent in the judgment, reflected in a lack of clarity over whether it is only permissible to refer to the 'commercial purpose' of the document and 'common-sense' in cases of ambiguity — an interpretation that will be welcomed by some (Davies 2012:27; Lewison 2011:51 and Spigelman 2007:internet) — and what the precise difference is between the two concepts, particularly when used in the expression "commercial common sense". Appeals to common sense have been questionably employed in the past as a term of last resort, sometimes "a cloak for [judicial] prejudice or lack of thought" (Heydon 2012:30). It is to be hoped that this is not the fate of the new approach to contractual interpretation, if properly understood and applied by the parties, their lawyers and the courts of first instance.

Lastly, it is incorrect to suggest that the new approach has opened the door to the negotiations of the parties (although for a contrary view see Puig 2012:334). This does remain an area of unresolved tension, not least because the rationale behind , the objective approach is that third parties rely on the contract (Lewison 2011:7-9,25). Admitting evidence of context from the outset may invite many of the same difficulties outlined by Wallis (2010:675) as attending upon an enquiry into the minds of the parties. Moreover, the law in other fields, such as crime and delict, is not squeamish about investigating the motives and states of mind of the parties, trusting to the judge's ability to sort fact from fabrication through the time-honoured method of cross-examination of witnesses. Nevertheless sound reasons remain, it is suggested, why formal contracts should be treated differently since they are the embodiment of a legal act (Lewison 2011).

Any perceived tension is considerably reduced by accepting that the facts known to any particular third party are equally irrelevant upon an objective approach, and secondly, that the "background knowledge...reasonably available to the parties" may need to be restricted to that which was objectively ascertainable by an outsider to the transaction (Hoffmann 2007:664).

## 7. CONCLUSION

Neither case considered in this article concerned the kind of highly strategic relationship referred to by Beuve & Saussier (2012). The conduct of the litigation illustrates that the

parties adopted opposing views on the interpretation of the clauses in question. During the course of the litigation, a number of technical points were taken into consideration as well, and both cases went on appeal. This illustrated the breakdown of cooperation and commitment to a continued trust relationship and would seem to suggest the limited role that formal contracts can play in promoting co-operation and trust, once conflict arises.

However, the 'iterative approach' emphasises that neither context and purpose nor form and language is to predominate. Interpretation requires a consideration of language in context from the outset. If contracts are poorly drafted (as in Rainy Sky v Kookmin Bank 2011) or unexpected situations arise (as in NJMPF v Endumeni 2012), this new approach may play a significant role in ensuring that the commercial purpose of the contract is upheld.

In emphasising a businesslike interpretation, the approach may encourage parties to seek cooperative solutions to conflict, without resort to court. Despite its detractors, the new approach is thus more, not less, likely to curtail litigation, although that may only be in the context of the strategic relationships identified by Beuve & Saussier (2012).

**REFERENCES**

**BEUVE J & SAUSSIER S.** 2012. Interfirm cooperation in strategic relationships: the role of formal contract. *Industrial and Corporate Change* 21(4):811-836.

**BINGHAM TH.** 2008. A new thing under the sun: the interpretation of contract and the ICS decision. *Edinburgh Law Review* 12:374.

**DAVIES SP.** 2012. Interpreting commercial contracts: a case of ambiguity? *Lloyd's Maritime & Commercial Law Quarterly*:26-29.

**GOFF R.** 1984. Commercial contracts and the commercial court. *Lloyd's Maritime & Commercial Law Quarterly:382.*

**GRABINER AS.** 2012. The iterative process of contractual interpretation*. Law Quarterly Review 128:41.*

**HEYDON JD.** 2012. How the courts develop commercial law by looking outside the trial record into the external world. *Lloyd's Maritime & Commercial Law Quarterly 30 -64.*

**HOFFMAN L**. 1997. The intolerable wrestle with words and meanings. *South African Law Journal* 114:656-674.

**LEWISON K.** 2011. The Interpretation of contracts. 5th ed. London: Sweet & Maxwell.

**PUIG BV.** 2012. The misalignment of commercial law and commercial practice. *Lloyds' Maritime & Commercial Law Quarterly:317.*

**RING P & VAN DE VEN A.** 1992. Structuring cooperative relationships between organisations. *Strategic Management Journal* 13 (7):483–498, Oct.

**SORENSON O & SORENSON JB.** 2001. Finding the right mix: franchising, organizational learning, and chain performance. *Strategic Management Journal* 22 (6): 713-724.

**SPIGELMAN JJ.** 2005. The principle of legality and the clear statement principle. Opening address to the New South Wales Bar Association Conference 'Working with Statutes' Sydney, 18 March 2005 [Internet: www.lawlink.nsw.gov.au; downloaded on 2013-09-15].

**SPIGELMAN JJ.** 2007. From text to context: contemporary contractual interpretation. Address by the Hon. JJ Spigelman AC Chief Justice of New South Wales to the Risky Business Conference, Sydney, 21 March 2007 [Internet: www.lawlink.nsw.gov.au ; downloaded on 2013-10-15].

**STEVENS A.** 2010. Protecting the life-blood of international commerce: parties beware. *Lloyd's Maritime & Commercial Law Quarterly*:548.

**STEYN J.** 1997. Contract law: fulfilling the reasonable expectations of honest men. *Law Quarterly Review* 116:433-442.

**WALLIS M.** 2010. What's in a word? Interpretation through the eyes of ordinary readers. *The South African Law Journal* 127(4):673–693.

**South African case law:**

Bastian Financial Services (Pty) Ltd v General Hendrik Schoeman Primary School 2008 (5) SA 1 (SCA)

Jaga v Dönges NO and Another; Bhana v Dönges NO and Another 1950 (4) SA 653 (A)

Richter v Bloemfontein Town Council 1922 AD 57

Namibian Minerals Corporation Ltd v Benguela Concessions Ltd 1997 (2) SA 528 (A)

Natal Joint Municipal Pension Fund v Endumeni Muncipality 2012 (4) SA 593 (SCA)

**Foreign case law:**

BCCI v Ali [2002] 1 A.C. 251

Chartbrook Ltd v Persimmon Homes Ltd [2009] 1 AC 1101.

Investors Compensation Scheme Ltd v West Bromwich Building Society [1998] 1 WLR 896

Mannai Investment Co Ltd v Eagle Star Life Assurance Co Ltd [1997] AC 749

N.L.A Group v Bowers [1999] 1 Lloyd's Rep. 109

Rainy Sky SA and Others v Kookmin Bank [2011] UKSC 50 ([2012] Lloyds Rep 34 (SC)

Re Sigma Finance Corp [2008] EWCA Civ 1303 (CA)

Society of Lloyd's v Robinson [1999] 1 All ER (Comm) 545 , 551