THE IMPLICATION OF TERMS IN FACT

COURTS have long been asked to imply terms in fact into contracts and other instruments. Over the years, they have determined such requests by applying a test whose general substance is well-known (all law students become familiar with the need for "business efficacy" and for hypothetical consultations with an "officious bystander") but whose precise formulation has remained somewhat uncertain. In *(1) Attorney-General of Belize (2) ECOM Ltd. (3) Belize Telecommunications Ltd.* v. *(1) Belize Telecom Ltd. (2) Innovative Communication Co LLC* [2009] UKPC 11 (the "*Belize* case"), the Privy Council reviewed the historical formulations of the test and provided a simplified restatement that is apparently designed to prevail in future.

The *Belize* case concerned a company, Belize Telecommunications Ltd., whose share capital was divided into a single special rights redeemable preference share (the "special share"), B ordinary shares and C ordinary shares (the "C shares"). The company's articles of association provided that while the holder of the special share also held a specified percentage (37.5 *per cent.*) of the C shares, it was entitled to appoint two directors ("special directors"). Two special directors were duly appointed on this basis by Belize Telecom Ltd., then the holder of the special share and the specified percentage of the C shares.

Belize Telecom Ltd. defaulted on certain of its obligations, as a result of which the number of C shares held by it fell below the specified percentage. The articles confirmed that the only entity empowered to remove special directors was a holder of the special share that also held the specified percentage of the C shares, but no such entity existed following Belize Telecom Ltd.'s default. The appellants (Belize Telecommunications Ltd. and other parties interested in removing the special directors appointed by Belize Telecom Ltd.) sought a finding that the articles contained an implied term providing that the special directors would automatically cease to hold office in such circumstances.

Two formulations of the test for the implication of terms in fact are prominent in the jurisprudence. The first is that any term to be implied must be necessary to give "such business efficacy to the transaction as must have been intended at all events by both parties who are business men": *The Moorcock* (1889) 14 P.D. 64, 68 *per* Bowen L.J. The other is that an implied term must be "… so obvious that it goes without saying; so that, if, while the parties were making their bargain, an officious bystander were to suggest some express provision for it in their agreement, they would testily suppress him with a common 'Oh, of course!'": *Shirlaw* v. *Southern Foundries (1926) Ltd* [1939] 2 K.B. 206, 227 *per* MacKinnon L.J.

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More recent cases have added additional complexity. In *BP Refinery (Westernport) Pty. Ltd.* v. *Shire of Hastings* (1977) 180 C.L.R. 266, 283, Lord Simon of Glaisdale (giving the opinion of the majority of the Privy Council) considered that in order to imply a term, the following (potentially overlapping) requirements needed to be met:

> … (1) it must be reasonable and equitable; (2) it must be necessary to give business efficacy to the contract, so that no term will be implied if the contract is effective without it; (3) it must be so obvious that "it goes without saying"; (4) it must be capable of clear expression; (5) it must not contradict any express term of the contract.

In the *Belize* case, Lord Hoffmann (delivering the advice of the Board) highlighted the "dangers in treating these alternative formulations of the question as if they had a life of their own", at [22]. For example, provided that an instrument operated functionally from a business perspective, the business efficacy test could be construed to prevent the implication of a term that reflected a reasonable person's understanding of the instrument's meaning. Similarly, the requirements for an implied term to go without saying and to be obvious to an officious bystander might introduce an undesirable degree of subjectivity. It should not matter, for instance, if the implication of a term is not immediately apparent to an impartial observer, but instead requires careful consideration.

Mindful of these concerns, the Board took the view that the various tests should not be treated as cumulative tests, but should instead be considered to be "a collection of different ways in which judges have tried to express the central idea …", at [27]. In assessing whether a term should be implied, "[t]here is only one question: is that what the instrument, read as a whole against the relevant background, would reasonably be understood to mean?", at [21]. This formulation simplifies the approach and also appears to represent something of a departure from the traditional focus on necessity (in *Liverpool City Council* v. *Irwin* [1977] A.C. 239, at 266, Lord Edmund-Davies reflected the contemporaneous view in commenting that: "The touchstone is always *necessity* and not merely *reasonableness* …"). The trend towards reasonableness is, however, consistent with the general objective approach to contractual interpretation set out by Lord Hoffmann in *Investors Compensation Scheme Ltd.* v. *West Bromwich Building Society* [1998] 1 W.L.R. 896, 912.

In the *Belize* case, the "relevant background" comprised two key aspects of the company's articles. First, the membership of the board clearly reflected the interests of the participants in the company (shareholders other than the holder of the special share were also entitled to appoint and remove particular numbers of directors). Second,

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the powers available to the holder of the special share at particular times were deliberately graduated in accordance with that entity's economic interest in the company at those times (the holder of the special share was also entitled to appoint two directors solely by virtue of holding the special share). Based principally on these factors, the Board found that the articles would reasonably be understood to contain an implied term providing that the special directors would cease to hold office in the circumstances.

The decision is not binding on courts in England and Wales, but its elucidation of the test will be treated as persuasive and is likely to be followed (although initial indications in this regard have been somewhat equivocal: see, *e.g.*, *Mediterranean Salvage and Towage Ltd.* v. *Seamar Trading and Commerce Inc. (The Reborn)* [2009] EWCA Civ 531). If the reasoning in the *Belize* case is followed that will be a welcome development. First, as noted above, the focus on reasonableness draws the test for the implication of terms in fact more closely into line with general principles of contractual interpretation. If one perceives the implication of terms in fact to be simply an example of interpretation, this is a particularly attractive outcome (see *e.g.* Kramer (2004) 63 C.L.J. 384). Second, the restated test avoids the risk that any particular formulation might expand inappropriately beyond its original scope. Even if courts do continue to refer to the historical formulations, their decisions should ultimately be guided by the objective principle of reasonableness set out by the Board. Although there is a residual concern that the restated test may result in greater flexibility for courts, the more likely outcome is that the formulation's clarity will in fact provide greater certainty in this area.

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AN END TO LIMBO: THE DEATH KNELL OF THE TOLERATED TRESPASSER

TWELVE years after giving its endorsement to the notion of the "tolerated trespasser", the House of Lords in *Knowsley Housing Trust* v. *White* [2008] UKHL 70, [2009] 2 W.L.R. 78 has finally reconsidered that controversial status and, in so doing, has consigned it largely to the history books.

Traditionally, the problem concerns secure tenants of public sector housing, whose security of tenure is regulated by the Housing Act 1985. Under that legislation, a secure tenancy may not be terminated by the landlord except via possession proceedings on a number of listed grounds, chief among which is non-payment of rent (Schedule 2, ground 1). Section 85 of the Act empowers the court, when making a

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