SHERIFFDOM OF TAYSIDE, CENTRAL AND FIFE AT DUNDEE

[2023] SC DUN 25

PER-CA21-22

JUDGMENT OF SHERIFF JILLIAN MARTIN-BROWN

in the cause

INVERLOCHY CASTLE MANAGEMENT INTERNATIONAL LIMITED

Pursuer

against

(FIRST) ARCHIE MacDONALD; and (SECOND) ANNE MacDONALD

Defenders

Pursuer: Manson, Adv; BTO Solicitors LLP
Defenders: J Brown, Adv; Levy and McRae Solicitors LLP

DUNDEE, 26 May 2023

Introduction

[1] This dispute concerns the relevancy and specification of averments about: (i) implied terms in a contract; (ii) fiduciary duties; (iii) breach of contract; (iv) loss of profit; and (v) a proposed order for count, reckoning and payment arising from a contract between the parties relating to the operation of a hotel owned by the defenders.

Background Facts and Circumstances

[2] The pursuer avers that it manages luxury hotels on behalf of their owners. The defenders are the owners of a boutique hotel at the Old Manse of Blair in Blair Atholl. The pursuer and the defenders entered into a contract dated 20 July 2021 ("the Management Agreement") whereby the pursuer agreed to manage the hotel for and on behalf of the

defenders in return for monthly and annual management fees. The pursuer averred that invoices from November 2021 until March 2022 were outstanding in the sum of £33,682.77.

[3] The defenders aver in the principal action that: (i) by virtue of the pursuer's refusal to discharge its obligation to provide access to the books and records maintained by it for the operation of the business, the defenders had been unable to verify purported travel expenses charges which were *prima facie* grossly excessive; and (ii) by virtue of multiple breaches of contract, the pursuer was disentitled from enforcing any obligation on the part of the defenders to pay management fees.

[4] The defenders also crave in the counterclaim for: (i) an order for count, reckoning and payment in relation to the pursuer's intromissions as agent of the defenders; and (ii) damages for breach of contract and breach of fiduciary duty.

Authorities

[5] Parties lodged a lengthy joint list of authorities as follows:

- *Arnold* v *Britton* [2015] A.C. 1619;
- *Bristol and West Building Society* v *Mothew* [1998] Ch. 1;
- *Green* v *Moran* [2002] S.C. 575;
- *GWR Property Co Limited* v *Forest Outdoor Media Limited* [2022] S.C.L.R. 57;
- *Hilton* v *Barker Booth & Eastwood* [2005] 1 W.L.R. 567;
- *Kelly* v *Cooper* [1993] A.C, 205;
- *MacDonald* v *Glasgow Western Hospitals* [1954] S.C. 453;
- *Marks and Spencer PLC* v *BNP Paribas Securities Services Trust Company (Jersey) Limited* [2016] A.C. 742;
- *Marine & Offshore (Scotland) Limited* v *Jack* [2018] S.C.L.R. 606;

- *Midlothian Council* v *Bracewell Stirling Architects* [2018] S.C.L.R. 606;
- *Rossetti Marketing Limited* v *Diamond Sofa Company Limited* [2013] Bus. L.R .543;
- *Royal Bank of Scotland* v *Holmes* [1999] S.L.T. 563;
- *Scanmudring AS* v *James Fisher MFE Limited* [2019] S.L.T. 295;
- *Soofi* v *Dykes* [2017] CSIH 40; 2017 W.W.D. 21-232;
- *Wood* v *Capita Insurance Services Limited* [2017] A.C. 1173;
- *Court of Session Practice*, para. 2052;
- Bowstead and Reynolds, *Agency* (19th edn), para. 6-039.
- Getzler, *Inconsistent Fiduciary Duties and Implied Consent* LQR 2006, 122 (Jan) 1-8
- Macphail, *Sheriff Court Practice* (4th edn), para. 21.02;
- McBryde, *The Law of Contract in Scotland* (3rd edn), para. 14-12; and
- McGregor, *The Law of Agency in Scotland*, Ch. 6.

Pursuer's Submissions

Implied Terms

[6] The pursuer submitted that there was no proper basis for the purported implied term in Answer to Condescendence 6 that the pursuer would take all reasonable measures to operate the business in accordance with the terms of its licence, in a manner likely to encourage its customers to return, and in a manner calculated to maximise the efficiency and profitability of the business.

[7] The pursuer submitted that it was not necessary to imply such a term to give business efficacy to the agreement. It was not so obvious that it went without saying. It

innovated on and contradicted the express terms. The agreement would not lack commercial or practical coherence without the term. Accordingly, the averment setting out the purported implied term was irrelevant.

Fiduciary Duties

[8] The pursuer submitted that the express terms of the agreement disclosed that it was jointly understood that the pursuer would be providing services to other businesses whilst engaged by the defender. Accordingly, the defenders' reliance upon fiduciary duties of undivided loyalty and conflicting interests and their application to the complaints made in answer six were irrelevant.

Breach of Contract

[9] The pursuer submitted that the defenders' averments failed to set up any relevant basis to contend that the pursuer acted beyond the scope of the wide discretion afforded to it under the express terms of the agreement. Instead, the defenders' averments represented a series of subjective complaints based upon the defenders' jaded perception of the pursuer. The defenders did not aver the facts and circumstances that saw the pursuer move outwith the bounds of a reasonable exercise of discretion and were bound to fail. The allegations made were so general and vague that no sensible inquiry could take place. Ambush was plainly impermissible. The defenders required to be held to a greater standard of specification standing their allegations of bad faith and wilful misconduct and their pleadings fell shorter still when that standard was applied.

Loss of Profit

[10] The pursuer submitted that parties agreed in clause 16.3 of the agreement that the pursuer was to have no liability for indirect or consequential loss or for any loss of any profits, even if the pursuer had been negligent. A limited exception was agreed in relation to "wilful default". However, the defenders had no relevant averments based on wilful default and accordingly, no relevant basis upon which to seek damages from the pursuer in the counterclaim. The court had a duty to enforce the contractual arrangements agreed upon by the parties. The court should not displace the natural and ordinary meaning of the words used simply because a term appeared to be have been imprudently agreed upon by one of the parties.

Count, Reckoning and Payment

[11] Finally, in the counterclaim the defenders sought an order for count, reckoning and payment, failing which an estimated liability of £250,000. They also sought £500,000 in damages. Those remedies could not proceed properly in tandem. By adopting a damages claim, the defenders could not properly plead ignorance as to their entitlement because that served to undermine the basis of the accounting remedy. A party was not entitled to an accounting remedy simply because it had not seen all that it would like to see.

[12] The defenders had made their election to sue for payment of damages, based on the same facts and circumstances which went towards the payment claim under the accounting. By doing so, the defenders had assumed the burden of making relevant and specific averments and giving fair notice of the valuation of their claim. The defenders could not, at the same time, seek to shift that burden on to the pursuer.

[13] The defenders had seen fit to quantify damages in the sum of £500,000 but the basis had not been pled and was therefore irrelevant.

Defenders' Submissions

Implied Terms

[14] The defenders submitted that the implied term contended for was of a general type that was commonplace. Contracts for professional services typically included implied terms that the services would be rendered to the standard of the ordinarily competent member of the relevant profession. It would have been understood by both parties that the pursuer would manage it with a view to profit. The implied term contended for in the present case met all the relevant tests.

[15] Clause 30.2 required the parties to co-operate in good faith with each other and with third parties when required to further the purposes of this agreement. It was evident that the fundamental purpose was the management of the business. Perhaps it was possible to construe the contract to import some objective check on the pursuer's discretion. In that event no implication was necessary. But if not, the implication did become necessary.

Fiduciary Duties

[16] The defenders submitted that it was beyond doubt that as a general proposition, agents owed fiduciary duties to their principals. There was nothing in the present case to take the pursuer outside that general rule. The ability of the pursuer to act for parties with competing interests was dependent on informed consent. There was no inherent or inevitable conflict in the pursuer managing other hotels but there may be particular

circumstances in which an actual direct conflict of interests arose. It was a fact dependent issue upon which some form of inquiry was likely to be required.

Breach of Contract

[17] The defenders submitted that the context of managing a five star hotel was relevant. No reasonable person looking at the agreement would conclude that the pursuer as manager could do whatever they liked, such as cancelling bookings, shutting the hotel or being rude to guests. The discretion was not without limit, whether by implication or construction of the agreement. There was no ambush. Instead, there was a series of examples.

Loss of Profit

[18] The defenders submitted that multiple breaches of fiduciary and non-fiduciary duties had made the business loss making and diminished its capital value. It was a straightforward claim for damages. The sum claimed for could only be a broad estimate because the books were not available and any calculation of the value of the business depended on the accounts.

[19] The idea that this commercial action should go back in time to the 1950s and require detailed pleadings ignored the wide ranging flexible procedural provisions available in commercial cases. This case should not go to proof before an accounting was offered. Once that progressed and information was available, a valuation could be carried out by an expert.

Count, Reckoning and Payment

[20] The challenge to the crave in the counterclaim seeking an accounting was wholly misconceived. It was plain that the pursuer was required to account to the defenders for its intromissions in the functional or mechanical sense of the term. That was so in every relationship of agency. The pursuer was obliged to set out what funds it received as agent and what expenditure it incurred. The money in question belonged to the defenders, save to the extent that the pursuer had properly expended it in the discharge of its duties or was entitled to payment of it by way of fee. They were entitled to have the sum due to them fixed. The pursuer's obligation to do so was absolute and was unrelated to any other aspect of the dispute. The suggestion that it was necessary for the defenders to elect between seeking an accounting and pursuing a claim for damages was obviously unsound.

[21] The sum sued for in the alternative was to reflect the possibility, presumably remote in the present case, that the pursuer would simply refuse to produce an account if ordered to do so. Once an account was produced, the alternative form of the crave was redundant and the sum due was fixed by the accounting process.

[22] None of this implied any conflict with the logically distinct claim for damages for breach of contract and fiduciary duty. The defenders straightforwardly averred that they had lost profit and suffered a diminution of capital value on account of the multiple breaches they asserted. That claim could perfectly straightforwardly co-exist with the right to have the pursuer account for what it had done with the money.

[23] These were commercial proceedings. The defenders had never contended that the action could simply go to proof on that claim at this stage. The court's case management powers were entirely adequate to the task of managing the separate strands of the dispute. It would be wasteful and inefficient to require the defenders to proceed as though the

damages claim was the only strand of the dispute and to seek commission and diligence for the recovery of the primary material obviously necessary to enable the claim to be accurately quantified when those documents would in any event emerge through the parallel process of the accounting, which was far more suited to the efficient disposal of the issue.

Decision

Implied Terms

[24] In *Marks & Spencer* v *BNP*, Lord Neuberger explained at paragraph 28 that in most disputes about whether a term should be implied into a contract, it is only after the process of construing the express words is complete that the issue of an implied term falls to be considered: "*Until one has decided what the parties have expressly agreed, it is difficult to see how one can set about deciding whether a term should be implied and if so what term.*"

[25] More recently, in *GWR* v *Forrest*, Lord Clark indicated at paragraph 28 that the question of whether a term falls to be implied is considered after reaching a view on the proper construction of the contract. At paragraph 19, Lord Clark also indicated that the relevant principles of contractual construction may be summarised as follows: a contract must be construed objectively, contextually, purposively and in a manner which accords with commercial common sense.

[26] Following that approach, it is necessary to look at the terms of the Management Agreement before considering whether a term ought to be implied into the contract in relation to the operation of the business.

[27] Clause 8 deals with operations. In terms of clause 8.1, the pursuer was engaged to be the exclusive operator of the hotel, with the sole and exclusive right to supervise and direct the refurbishment, subject to prior written approval from the defenders. The pursuer had

exclusive responsibility and complete and full control and discretion in the operation, direction, management and supervision of the hotel, subject only to the limitations expressed in the Management Agreement. Clause 8.3 specifies certain areas of sole and exclusive responsibility, including operating policy and standards of service (clause 8.3.1); business promotion (clause 8.3.2); pricing (clause 8.3.5); marketing (clause 8.3.7); and licences (clause 8.3.12).

[28] Clause 9 deals with budgets. In terms of clause 9.2, the yearly budget is subject to the approval of the defenders. Under clause 9.3, the pursuer agreed to use reasonable endeavours to take into account the defenders' reasonable opinions and recommendations and to incorporate and amend the yearly budget where appropriate.

[29] Clause 14 deals with fees. In terms of clause 14.1, the defenders must pay to the pursuer a fixed monthly management fee and an annual management fee as a percentage of turnover.

[30] Clause 15 deals with bank accounts. In terms of clause 15.2, the defenders were required to establish a bank account on or before the Start Date and deposit £60,000 or such greater sum or credit facility from time to time deemed by the pursuer to be reasonably required for the working capital for the normal operation of the business of the hotel.

[31] Clause 30 deals with confidentiality etc. In terms of clause 30.2, each party will act in good faith with the others at all times throughout the Term and will co-operate with the others when required to further the purposes of the Management Agreement.

[32] Viewed objectively, it is clear that the defenders have gave the pursuer full control and discretion as to the operation of the hotel. While the pursuer did not take issue with an implied term that the pursuer would manage the business in a manner to be expected of a

competent operator of luxury hotels, the pursuer did take issue with the implication of a term that the pursuer would take:

> "*all reasonable measures to operate the business in accordance with the terms of its licence, in a manner likely to encourage its customers to return, and in a manner calculated to maximise the efficiency and profitability of the business*."

[33] In *Marks & Spencer*, Lord Neuberger set out at paragraph 21 six observations for implying a term into a contract. Firstly, implication is not critically dependent upon proof of an actual intention of the parties when negotiating the contract. Instead, one is concerned with notional reasonable people in the position of the parties at the time at which they were contracting. Secondly, a term should not be implied into a detailed commercial contract merely because it appears fair or merely because one considers that parties would have agreed it if it had been suggested to them. Thirdly, reasonableness and equitableness will rarely add anything: if a term satisfies the other requirements, it is hard to think that it would not be reasonable and equitable. Fourthly, business necessity and obviousness can be alternatives but it would be a rare case where only one of those two requirements would be satisfied. Fifthly, the question to be posed by the officious bystander should be formulated with the utmost care. Sixthly, necessity for business efficacy involves a value judgement. A term can only be implied if, without the term, the contract would lack commercial or practical coherence.

[34] In *GWR* v *Forrest*, Lord Clark applied the principles set out by Lord Neuberger in *Marks & Spencer* and concluded at paragraph 28 that the missives in that case did not include an implied term of any of the kinds suggested by the defender.

[35] Adopting the same approach and applying the principles set out by Lord Neuberger in *Marks & Spencer* to the Management Agreement in this case, I do not consider that there was an implied term as contended for by the defender. Firstly, it is not necessary to give

business efficacy to the Management Agreement. On the contrary, the parties have agreed a detailed Management Agreement, whereby the defenders have provided the pursuer with exclusive responsibility and control in relation to the operation of the hotel in exchange for access to its expertise and know-how. The Management Agreement is perfectly effective without such an implied term. Secondly, the implied term proposed is not so obvious that it goes without saying. While it is obvious that almost all businesses are carried on with a view to profit in any particular period, it is not obvious that a business seeks to *maximise* profit and efficiency at all times, particularly during a refurbishment period. Thirdly, the purported term innovates on and contradicts the express terms of the Management Agreement. The parties agreed a method of payment via the annual management fee which incentivised increased *turnover* rather than profit. Finally, the Management Agreement does not lack commercial or practical coherence without the implied term. There are limitations on the operational discretion of the pursuer in the form of the yearly budget and the requirement for each party to act in good faith with the others at all times.

[36] Consequently, I am of the view that the defenders' averments in relation to the proposed implied term in Answer to Condescendence 6 are irrelevant and should not be admitted to probation.

Fiduciary Duties

[37] The agent's role as a fiduciary is a central aspect of agency law. The scope of the agent's fiduciary duty is set out in McGregor at paragraphs 6-14 as follows: "*The agent's fiduciary duties are shaped by the nature of the work which the agent is instructed by the principal to perform. This is, essentially, a factual enquiry.*"

[38] In *Bristol & West* v *Mothew*, Millet L.J. indicated at p.18 that:

> "*A fiduciary must act in good faith; he must not make a profit out of his trust; he must not place himself in a position where his duty and his interest may conflict; he may not act for his own benefit or for the benefit of a third person without the informed consent of his principal.*"

[39] Subsequently, in *Rossetti* v *Diamond*, Lord Neuberger indicated at paragraph 22 that an agent can act for two principals with competing interests where both principals agree. In such cases it is for the agent to show that the principal not merely consented, but that the consent was given on a fully informed basis.

[40] Applying those principles to the fiduciary duties of the pursuer in this case, the Management Agreement does not contain an express term that the pursuer must act exclusively for the defenders. On the contrary, in the preamble the parties narrate that the pursuer and its officers and the Executive Staff are engaged in the management and operation of hotels and have acknowledged expertise in this sector of commerce.

[41] However, the issue of whether the pursuer complied with its fiduciary duties when providing services to other businesses while engaged by the defender is dependent upon informed consent. That necessitates a factual enquiry. Consequently, I am of the view that the defenders' averments in relation to fiduciary duties of undivided loyalty and conflicting interests are relevant and should be admitted to probation.

Breach of Contract

[42] Chapter 40 of the Ordinary Cause Rules provides a flexible, efficient and cost-effective means of resolving disputes of a commercial nature. Active case management is designed to focus the minds of the parties on the real issues in dispute. While full and frank disclosure is required of parties, lengthy pleadings are discouraged.

[43] I have already determined that the implied term relating to maximising efficiency and profit is irrelevant and therefore the defenders' averments anent breach of that implied

term are also irrelevant. However, what remains in the principal action are averments anent breaches of fiduciary duties and an implied term that the pursuer would manage the business in the manner to be expected of a competent operator of luxury hotels.

[44] The defenders aver at Answer to Condescendence 6 that the pursuer's management of the hotel was grossly inadequate due to collapse in cash flow; poor customer service; and reputational damage. Nineteen occasions of breach of contract are pled. Whether these amount to subjective complaints about the pursuer's wide discretion or whether they amount to breach of contract is a matter for factual enquiry. I do not consider that the defenders are bound to fail.

[45] Nor do I consider that the pursuer is set to be ambushed. The Management Agreement was signed on 20 July 2021 and terminated less than a year later on 13 April 2022. During the course of that relatively short period, the defenders have provided fair notice of nineteen separate occasions of alleged breach of contract.

[46] I am therefore of the view that in general, the defenders' averments anent breaches of contract are relevant and sufficiently specific to be admitted to probation. However, I also require to consider whether the allegations of fraud are lacking in specification.

[47] In *Royal Bank of Scotland* v *Holmes*, Lord Macfadyen indicated at p 569 that:

> "*It is in my view essential for the party alleging fraud clearly and specifically to identify the act or representation founded upon, the occasion on which the act was committed or the representation made, and the circumstances relied on as yielding the inference that that act or representation was fraudulent. It is also, in my view, essential that the person who committed the fraudulent act or made the fraudulent misrepresentation be identified.*"

[48] The defenders aver that the pursuer failed to act in good faith by breaching its fiduciary duty to avoid conflicting interests, save those fully disclosed to the defenders and consented to on an informed basis. That is not an allegation of fraud. The only allegations of fraud are in Answer to Condescendence 6 and subparagraph (xviii) that the pursuer

falsely represented to customers of the hotel that it was owned by the pursuers on registration forms completed by guests. In relation to those limited averments, I do not consider that the defenders have provided clear specification of the act, the occasion, the circumstances and identification of the person committing the fraud. Consequently, I have not admitted those particular averments to probation.

Loss of Profit

[49] Turning to the counterclaim, in statement of fact 5 the defenders aver that they have suffered loss of profit that ought to have been made but for the breaches of a fiduciary obligation of single minded loyalty. They aver that they have suffered a material diminution in the capital value of the hotel business.

[50] However, clause 16.3 of the Management Agreement provides that in no event shall the pursuer be liable for: (i) any indirect or consequential loss; or (ii) any loss of profits whether direct or indirect of the defenders, irrespective of how such indirect or consequential loss or loss of profits was caused, including without limitation as a result of the pursuer's negligence. The clause is stated not to be intended to exclude any liability of the pursuer for wilful default.

[51] The averments of breach of fiduciary duty do not amount to allegations of wilful default. All that is averred is that the pursuer was obliged to act in good faith in the defenders' interests to the exclusion of competing interests, whether its own or those of other hotel proprietors, save to the extent specifically agreed to by the defenders on the basis of full disclosure of all relevant information. There are no averments of a deliberate default, ie that the pursuer knew that it was breaching the contract.

[52] Consequently, I am of the view that the defenders' claim for damages as a result of breach of contract and breach of fiduciary duty in the counterclaim are irrelevant in light of the contractual exclusion of liability for consequential loss and loss of profit and should not be admitted to probation.

Count, Reckoning and Payment

[53] Having excluded the defenders' claim for damages, all that remains in the counterclaim is the action for count, reckoning and payment, failing which payment of a specified sum. Had the claim for damages remained, I would have refused it from probation on the basis that it was lacking in specification. Though quantified at £500,000, no basis is pled for that sum as the measure of damages.

[54] However, I would have rejected the pursuer's contention that a claim for damages cannot co-exist with a claim for count, reckoning and payment. *Macphail i*ndicates at paragraphs 9.93 – 9.94 that:

> "*The pleader may combine any number of craves or state alternative or eventual craves, provided that they may all be disposed of in the same course of procedure and the different grounds of action are distinguished by clear and precise language in the condescendence and pleas-in-law. The craves should be clearly distinguished and consecutively numbered…Alternative craves, for alternative decrees incompatible with each other, are competent…Alternative craves which are irreconcilable, proceeding on alternative averments inconsistent with each other, are competent.*"

[55] Crave 1 in the counterclaim seeks a count, reckoning and payment. Crave 2 is an alternative crave for payment in the event of the pursuer failing to account. Crave 3 is a crave for damages. Each of the craves and corresponding pleas-in-law are clearly distinguished and I would not have rejected the counterclaim as irrelevant as contended for by the pursuer.

Expenses

[56] Parties were agreed that the issue of expenses ought to be resolved at a subsequent case management conference.

Further Procedure

[57] I assigned a case management conference in order to determine further procedure.