



FIRST DIVISION, INNER HOUSE, COURT OF SESSION

[2021] CSIH 60
CA159/19

Lord President
Lord Woolman
Lord Pentland

OPINION OF THE COURT

delivered by LORD PENTLAND

in the Reclaiming Motion by

CRIMOND ESTATES LIMITED

Pursuer and Respondent

against

MILE END DEVELOPMENTS LIMITED

Defender and Reclaimer

Pursuer and Respondent: Johnston, QC, G Reid; Lefevres
Defender and Reclaimer: MacColl, QC; Burness Paull LLP

29 October 2021

Introduction

[1] In 2013 the parties entered into a contract in terms of which the pursuer agreed to provide specified project management services to the defender in return for sharing in the net sale proceeds of a development of flats on the site of Mile End School in Aberdeen. The project did not run smoothly. Unforeseen problems were encountered from the start. There were substantial cost overruns and a six month delay in completion.

[2] In November 2016 the defender terminated the contract on the ground that the development costs exceeded the agreed budget by more than the contractually permitted margin of 5 per cent. The pursuer subsequently raised these proceedings alleging that the termination was in breach of contract and seeking damages. Following proof, the commercial judge held that the defender had not been entitled to terminate the contract; the evidence showed that the defender had in fact approved the expenditure that had caused the budget to be exceeded. The defender was therefore in breach of contract by purporting to terminate when it had not been entitled to do so. No damages were payable for the breach, however. This was because there would have been insufficient profits from the project to entitle the pursuer to receive any of its agreed profit share; the flats failed to sell at the expected prices as a result of the Aberdeen property crash brought about by the downturn in the oil industry in 2018.

[3] In this reclaiming motion (appeal) neither party challenged any of these findings. The focus of the appeal was the commercial judge's decision to award the pursuer £211,831.63 in respect of the alternative claim for reasonable remuneration for its services under clause 3.12 of the contract. The defender argued that the judge had been wrong to do so. He had misunderstood the clause and should have decided that it did not apply where the termination had been in breach of contract. In other words, the clause applied only where the termination had been lawful. If that argument was wrong, the judge should have held that the damages payable under the clause should be calculated so as to reflect an assessment of the quality of the services provided. In that event the works would have been valued, according to the expert evidence accepted by the judge, at 10 per cent of the figure of £211,831.63 and so the relevant sum in damages was £21,183.16.

The relevant terms in the contract

[4] Clause 6.2 provides that the contract could be terminated by either party on the service of thirty days written notice on the other party if:

“6.2.1 the other party is in material breach of this Agreement and fails to rectify such breach within ten working days after being required in writing so to do by the other party;

...

6.2.7 if the Development Costs or any reasonable estimate of same prepared by the Professional Team Quantity Surveyor for the Company (i.e. the defender) from time to time exceed the Budget by 5% or more, and such excess has not been previously approved in writing by the Company.”

[5] Clause 3.12 governs the remuneration payable where there has been termination under clause 6.2.1 or 6.2.7:

“In the event of termination of this Agreement by the Project Manager in terms of clause 6.2.1 or by the Company in terms of clause 6.2.7, the Project Manager shall, in the event that no Project Manager’s Profit Share is due to the Project Manager following the application of any part of this clause 3, be entitled upon completion of the Development, and subject always to the application of Clause 3.9, to such reasonable remuneration for its services up to the Termination Date, such remuneration to be based on the open market rate for a project manager carrying out the management of a development similar to the Development (but which remuneration shall not in any event exceed the amount of the Profit Share A Cap), and failing agreement to be fixed by the Adjudicator.”

[6] Clause 3.9 stipulates as follows:

“For the removal of doubt the Project Manager acknowledges that no Project Manager’s Profit Share shall be payable unless and until (i) all of the Development Costs incurred or to be incurred relative to the Development have been fully accounted or provided for (irrespective of the stage of progress of the Development as at the Termination Date it being the express intention of the parties that where insufficient Net Sale Proceeds have been generated at the Termination Date to cover all Development Costs incurred or to be incurred and the Priority Sum A that no Project Manager’s Profit Share shall be payable) and (ii) the Company has received payment of the Priority Sum A in full. Where at the Termination Date adequate provision has not or cannot reasonably be made for all Development Costs incurred or to be incurred in order to ascertain the Project Manager’s Profit Share the Company shall be entitled to defer determination of the Project Manager’s Profit

Share until completion of the Development by the Company or such earlier date on which adequate provision can reasonably be made for all Development Costs. At the discretion of the Company, provided it is demonstrably prudent to do so, the Company may make payments to account of the Priority Sum A, the Priority Sum B and the Project Manager's Profit Share.”

[7] Clause 3.9 therefore makes clear that no profit share would be due to the pursuer unless and until all the development costs had been accounted or provided for and Priority Sum A had been paid to the defender.

The decision of the commercial judge

[8] As already explained, the commercial judge held that the defender was not entitled to terminate the contract in terms of clause 6.2.7. Accordingly, it was in breach of contract.

[9] His next task was to decide what damages the breach attracted, if any. The pursuer relied for this on the evidence of one of their shareholders and directors, Mr David Suttie, while Mr Jolyon Aldous, a chartered accountant, provided expert evidence on behalf of the defender on this aspect. It is unnecessary, given the scope of the reclaiming motion, to examine in detail the methods of calculation adopted by these witnesses. It is sufficient to note that the commercial judge preferred the method used by Mr Aldous, on whose approach the profits of the development did not exceed Priority Sum A. This was important because of the terms of clause 3.9, which provided for the prioritisation of payments. The result was that there was no profit share for the pursuer because it was absorbed entirely by the defender's entitlement to Priority Sum A, and so there would have been nothing left with which to pay the pursuer if the agreement had not been terminated. The judge therefore held that no damages were payable in respect of the defender's wrongful termination of the contract.

[10] The commercial judge went on to consider whether there was remuneration payable to the pursuer in terms of clause 3.12. It was not contended that the finding that the termination was unlawful precluded the pursuer from seeking reasonable remuneration. The judge observed that it would be odd to interpret the agreement as providing for such a claim to be made where the termination was lawful, but not where it was unlawful. The clause was sufficiently wide to apply to either a lawful or an unlawful termination.

[11] Parties led expert evidence from two chartered surveyors as to the open market rate for a project manager: Mr Douglas Garden testified for the pursuer and Mr Keith Strutt for the defender. Mr Garden's calculation produced a fee of £383,422.58, based on a percentage of 3.25% plus a further 1.95% for the services provided by the pursuer in addition to project management.

[12] Mr Strutt produced the figure of £211,831.63, based on a fee percentage of 2.5%. Mr Strutt's calculation, in contrast to Mr Garden's, also considered the quality of the services actually provided by the pursuer. Mr Strutt's rating for the most critical activities – cost plan and budget; programme and progress tracking; and monitoring the team was either "low" or "none". The pursuer, in Mr Strutt's opinion, had not taken the systematic approach required in project management, but had rather worked on an *ad hoc* basis. He considered that the quality of the services delivered was on average no more than 10% of what was required and so reasonable remuneration, applying that percentage to the overall fee, would be £21,183.16.

[13] The commercial judge found no reason to reject Mr Strutt's opinion as to the quality of services provided by the pursuer. However, whether the services were carried out to a high standard or not played no part in assessing remuneration under clause 3.12. Project management services are normally remunerated by applying a fee percentage to the project

value. It was not suggested in the clause that the calculation required an assessment of the standard of service delivered. It accorded with commercial common sense to construe the word “reasonable” in clause 3.12 as a reference to the rate to be applied, rather than the quality of the services. If the parties had intended that the standard of the project management service provision was to be taken into account in determining the fee, then the contract would have said so expressly. In any event, assessment of quality would be an enormously laborious exercise with almost unlimited scope for disagreement. Such an exercise would introduce unacceptable uncertainty.

[14] That being so, the only issue which remained was which expert’s evidence as to the level of remuneration was to be preferred. The commercial judge preferred Mr Strutt’s approach. There was no contractual basis for Mr Garden’s application of an additional fee and the rate of 3.25% could not be justified, given that the comparators relied upon related to much larger projects and in any event did not support the application of that percentage. Mr Garden produced no reasoning or evidence to support the figure and failed to confirm the sources of construction costs used in his calculation.

The issues in the reclaiming motion

[15] In the appeal the defender advanced three short points which were said to amount to errors of law on the part of the commercial judge: (i) clause 3.12 did not apply because the contract had been terminated by the defender in breach of contract (this point had not been taken in the Outer House); (ii) if the clause did apply it required the quality of the services to be taken into account; and (iii) the reference in clause 3.12 to clause 3.9 meant that no remuneration was due to the pursuer since the development costs had not been provided for and Priority Sum A had not been paid to the defender.

[16] In the next section we will address each of these points in turn.

Analysis

(i) *Did clause 3.12 apply?*

[17] The relevant part of the clause reads: “In the event of termination of this Agreement by ... the Company in terms of clause 6.2.7... (the pursuer) shall ... be entitled ... to ... reasonable remuneration ...”. The defender argued that this meant that the clause applied only if the termination at its hand was lawful or valid. Here it had been in breach of contract. So the clause simply did not apply. Valid termination was a condition precedent to the clause being engaged. This argument raises a question of contractual interpretation.

[18] In recent times this territory has been extensively explored. The approach is now clear. As Lord Hodge explained in the Supreme Court in *Wood v Capita Insurance Services Ltd* [2017] AC 1173, paras 8 to 15, interpreting a contract involves an iterative process; the text and the context are equally important, as are the real-world consequences of the competing constructions. This court took the same approach in *Ardmair Bay Holdings Ltd v Craig* 2020 SLT 549 (Lord Drummond Young delivering the opinion of the court at paras [47] to [49]). There are four key points. (1) A contract must be construed objectively; what one party may subjectively have taken its terms to mean is irrelevant. (2) The words of the contract must be understood in their proper context; this extends to the totality of the contract itself and to the surrounding circumstances known to the parties when they entered into it. (3) The contractual terms must be read in a purposive sense so that the basic aims of the contract are fulfilled and not frustrated. (4) In the case of a commercial contract, what makes common sense in business terms may often be a useful interpretative tool.

[19] Applying these principles to the present case we have no difficulty in holding that clause 3.12 applied in the circumstances which arose. The starting point (and also the end point) is that the clause does not say that the termination has to be valid or lawful. It states only that termination has to be in terms of clause 6.2.7. That is in fact what happened in November 2016 when the defender sent the termination notice; it did so in terms of clause 6.2.7. The fact that it was not entitled to terminate on that ground does not detract from the fact that it sought to do so. In other words the defender's reliance on clause 6.2.7 for the purpose of terminating the contract was sufficient to engage clause 3.12.

[20] We are fortified in this reading of the clause by the fact that it makes commercial common sense. We can see no reason why the parties would have agreed that an entitlement to reasonable remuneration would arise where there was a valid termination but not where termination was in breach of contract. That would mean that the defender would be left better off in circumstances where its termination of the contract was unjustified. It is unlikely that the parties would have chosen to create the potential for such an anomalous outcome, which would run contrary to the well-known rule of construction that a party should not be entitled to rely on its own breach of contract to obtain a benefit under the contract (*Alghussein Establishment v Eton College* [1988] 1 WLR 587, Lord Jauncey at 595; *BDW Trading Limited (t/a Barratt North London) v JM Rowe (Investments) Limited* [2011] EWCA Civ 548, Patten LJ at paras 29-31).

[21] We conclude that clause 3.12 was worded so as to apply to the termination of the contract by the defender in November 2016.

[22] Having answered the first issue in the affirmative, we turn now to the question of reasonable remuneration.

(ii) *Does reasonable remuneration involve an assessment of the quality of the pursuer's services?*

[23] Clause 3.12 provides for payment to the pursuer of "reasonable remuneration for its services up to the Termination Date". It continues by stating that such remuneration is to be "based on" the open market rate for a project manager carrying out the management of a development similar to the Mile End development.

[24] The defender submitted that the use of the words "based on" implied that the open market rate for a similar project was no more than a starting point in a process of qualitative evaluation of the services provided. The quality of the work had to be taken into account. Otherwise the pursuer could insist on payment even if it had done no work. That defied commercial common sense. The reference to such reasonable remuneration meant that the pursuer was not entitled to payment for work done negligently or in a substandard fashion.

[25] The defender's approach is misconceived. There is nothing said in clause 3.12 about reasonable remuneration being based on the quality of the services provided by the pursuer. There is no mechanism in the clause for carrying out an exercise of evaluating the quality of the pursuer's services. What the clause does contain is a definition of reasonable remuneration. It is to be based on the open market rate for a project manager engaged on a similar development. In other words the basis of the remuneration is to be what would be the going rate in the open market for similar services. This does not justify wider factors extending to the quality of the services or the time spent on them having to be factored in. We agree with the commercial judge that assessment of quality would be a laborious exercise with substantial scope for disagreement. As he observed, it would introduce unacceptable uncertainty as well as a need for the application of subjective judgement in relation to every aspect of the service provision. The task faced by an adjudicator appointed

to fix the remuneration in the absence of agreement would, in the absence of any agreed methodology, be an exceptionally difficult and controversial one.

[26] As to the argument that this interpretation would allow the pursuer to carry out no work, but nonetheless insist on payment of reasonable remuneration, this is unrealistic. In the real world the likelihood that the pursuer would decline to provide any services under the contract is implausible. It was in the pursuer's financial interests to maximise its profit share from the development; inevitably it would do this by carrying out the project management services for which it was appointed. Moreover, clause 3.12 makes clear that the pursuer is entitled to reasonable remuneration "for its services". In the event that it provided none there would be no entitlement to such remuneration.

[27] In conclusion on this branch of the case, the commercial judge did not err in holding that the quality of the pursuer's services did not require to be taken into account.

(iii) What is meant by "subject always to the application of Clause 3.9"?

[28] The defender submitted that the proper construction of this phrase in clause 3.12 is that any claim for reasonable remuneration only arises once the development costs have been provided for and the defender has been paid Priority Sum A in full. Since the latter had not been paid, the pursuer had no entitlement to reasonable remuneration.

[29] We note that clause 3.12 specifically states that it applies in the event that no manager's profit share is payable to the pursuer. Clause 3.9 is concerned with a different scenario, namely the conditions which require to be satisfied before the manager's profit share becomes payable. The latter provision does not place any limitation on the circumstances in which the former applies. As the pursuer submitted, the two clauses are concerned with two different types of payment, arising in distinct sets of circumstances. We

reject the defender's contention that payment under clause 3.12 only falls due once the conditions set out in clause 3.9 have been fulfilled. Such a construction would require there to be read into clause 3.9 the words "or reasonable remuneration under clause 3.12" between "no Project Manager's Profit Share" and "shall be payable". There is no justification for rewriting the contract in this way.

[30] Even if that is wrong, the defender's approach makes no commercial sense and would cut across the whole purpose of clause 3.12, which applies where no project manager's profit share is payable to the pursuer. The position would, on the defender's argument, be entirely circular. We agree with the commercial judge that the more sensible construction is that the phrase refers to the second part of clause 3.9 which provided for the deferral of any payment to the pursuer until all development costs had been ascertained and paid or provided for. This is consistent with commercial common sense and gives content to the phrase. There is no suggestion that the development costs remain unascertained or unprovided for. In the circumstances the phrase has no practical application.

Decision

[31] For the reasons we have given, the reclaiming motion is refused. We have reserved all questions as to expenses.