SHERIFF APPEAL COURT

[2017] SAC (Civ) 35
PER-F125-14

Sheriff Principal Pyle
Appeal Sheriff Braid
Appeal Sheriff Murphy QC

OPINION OF THE COURT

delivered by SHERIFF PRINCIPAL PYLE

in the appeal by

ALEXANDER BAPTIE

in the cause

ALEXANDER BAPTIE

Pursuer and Appellant

against

MARIANNE ELIZABETH BRATT OR McLEAN OR BAPTIE

Defender and Respondent

Pursuer and Appellant: Stuart QC; Macnabs LLP
Defender and Respondent: Innes; Miller Hendry

6 December 2017

Introduction

[1] This is an appeal from the sheriff at Perth in an action of divorce. In granting decree of divorce, the sheriff also *inter alia* awarded the respondent a capital sum of £119,735.55, payable by agreement in two instalments.

[2] In his note of appeal, the appellant invites this court to recall the sheriff's interlocutor and to refuse the respondent's crave for a capital sum.

Findings in Fact

[3] On most, but not all, of the relevant facts to determine the capital sum crave, parties were in agreement. For present purposes the relevant facts may be summarised as follows:

1. The appellant owned the whole issued share capital of Glencarse Limited. He was also the sole director. The company's trade was the purchase of heritable properties, renovation of them and then letting them on short assured residential tenancies. The appellant regarded the company as a long term investment vehicle;
2. From its incorporation, the company secured finance from the Royal Bank of Scotland. By 2011 the amount borrowed was £850,000. The borrowing was secured by way of standard securities over the company's heritable properties and a bond and floating charge. In addition, before January 2010 the appellant granted further standard securities in favour of the bank over two plots of ground and a personal guarantee for £190,000;
3. In January 2011, the bank wrote to the appellant seeking his proposals for repayment of the borrowings by the end of that year. The bank was unwilling to continue to lend the funds to the company because it, the bank, considered that the 'loan to value ratio' was too high. The management of the borrowings was passed to the bank's global restructuring group. There was monthly contact between the appellant and the bank regarding refinancing;

4. The appellant secured refinancing from Shawbrook Bank Limited in November 2013, when the borrowings from the Royal Bank of Scotland were repaid. Prior to that date, no steps were taken by the latter bank to compel the company to realise any of its heritable properties. Nor did it take any steps to call up the borrowings or to place the company in administration or liquidation. The company continued to service the interest on the borrowings until repayment was made and was able to continue to trade;
5. The agreement with Shawbrook Bank Limited required that in addition to the existing securities standard securities were granted over two other heritable properties, one owned by the appellant; the other owned by the appellant and his mother. The total sum which was secured against all the properties and the company was £852,281.

[4] The sheriff held that the market value of the company assets at the relevant date was £1,063,000. He found that the value of the appellant's shareholding was £198,000. He also made a finding in fact that the company was due the appellant £65,415 by way of a director's loan.

[5] The appellant's grounds of appeal related to two matters: first, the value of the appellant's shareholding and, secondly, the director's loan. We deal with each of these matters in turn.

The Valuation of the Appellant's Shareholding

[6] The correct approach to the valuation of the shares in a private limited company was authoritatively decided by the Inner House in *Sweeney* v *Sweeney* 2004 SC 372. In that case the Lord Ordinary had held that the value of the share portfolio held by the husband on the

relevant date for the purposes of Sections 8, 9 and 10(3) of the Family Law (Scotland) Act 1985 should be assessed net of such capital gains tax as would have been exigible from the husband in the event of a realisation by him of those shares on that date. The Inner House disagreed (at para [15]):

> "As a matter of ordinary language 'the value' of [any] property which is realisable for money is the price which a hypothetical willing purchaser would pay, and the hypothetically willing seller receive from him, for that property on a hypothetical sale at the date in question. It is not constituted by that price less any costs (including any liability to tax) which the hypothetical seller would incur in the event of such a sale. The circumstance that sec 10 makes provision for a 'net value' of matrimonial property by deducting outstanding debts but makes no equivalent provision for the deduction of hypothetical liabilities tends to confirm that that ordinary usage is being employed. It is appropriate to bear in mind that one of the principles identified in sec 9(1) is that the net value of matrimonial property should be shared fairly. But that consideration should not be seen in isolation but in the context of the ultimate purpose of the legislation being that any order for payment of a capital sum should meet two criteria, one being that it is justified by the sec 9 principles, the other being that it is reasonable having regard to the resources of the parties (at the time when the order for payment is ultimately made). That time will necessarily be after, and commonly long after, the relevant date, as at which the value of the matrimonial property is to be determined. The fact that the scope of the property, the value of which is to be shared, is identified – in accordance with the statutory objective – as at the relevant date does not of itself entail that, to achieve fair sharing or the ultimate making of an award in accordance with the statutory criteria, it is necessary to suppose (contrary to the fact) that the property has been realised for cash as at that date. That is particularly so where there are other stages at which the actual or foreseeable incidence of tax and other liabilities or costs upon any realisation or other disposal can be brought into account."

[7] As the sheriff records (p 45 of the appeal print), the two expert chartered accountants led by the parties at the proof were both in agreement that the valuation of the appellant's shareholding was dependent upon the valuation of the heritable property owned by the company. Each party in turn led expert evidence from chartered surveyors as to the latter valuation. For the appellant, expert evidence was given by Mr Hall. He valued the properties at £786,000 based upon the hypothesis that each property would be sold individually as at the relevant date, but if sold as a portfolio he considered that the valuation

should be reduced by 20%. The respondent's expert was Mr Davidson who had been instructed by the appellant to value the same properties in support of the company's funding application to Shawbrook Bank Limited. The valuation had been conducted between September and October 2012, but the sheriff accepted that the figures would have been the same as at 1 January 2012, being the agreed 'relevant date' for the purposes of the 1985 Act. His valuation was £1,068,000. He also said that if the properties were sold as a portfolio the valuation would drop by between 40% and 50%. For reasons set out in his judgment, the sheriff preferred the evidence of Mr Davidson in determining the top line valuation. Counsel for the appellant did not dispute that finding.

[8] However, counsel for the appellant made two criticisms of the sheriff's approach. First, he submitted that the sheriff ought to have taken Mr Davidson's valuation of the properties based upon a portfolio sale. Secondly, he submitted that the sheriff had failed to take into account that at the material time the Royal Bank of Scotland had intimated its intention not to renew its funding. Indeed, on being pressed by us, counsel invited us to add two new findings in fact as follows:

> "[19] The Royal Bank of Scotland were not prepared to continue funding the company – hence the refinancing through Shawbrook Bank Limited.
>
> [20] In the absence of such re-financing, the Royal Bank of Scotland would have to be repaid and the company's assets sold. The company would therefore be lost."

Counsel submitted that the correct approach to the valuation of the shareholding based upon the approach in *Sweeney* required the court to make valuation assumptions based upon the economic activities of a party after the relevant date. (*McConnell* v *McConnell* 1997 FamLR 108; *Sweeney* v *Sweeney* (Outer House) 2003 SLT 892)

[9] We observe in passing the rather loose language employed in the proposed findings in fact, such as the company would be "lost" rather than would be placed in administration

or receivership. We also found that counsel, particularly in his written note of argument, conflated the two objections rather than dealing with each in turn. Nevertheless, in our opinion, there are two fundamental difficulties with counsel's approach: first, the evidence when looked at as a whole, rather than selective parts of it, does not on the facts support the proposed findings and secondly, the approach is not in accordance with the rule in *Sweeney*.

[10] For the first proposed finding in fact, counsel relied on the letter dated 10 January 2011 from the Royal Bank of Scotland to the appellant. (This was not included in the appendix, but we allowed counsel to produce it during the hearing.) The letter certainly provides that the "term loan is due to be repaid by 31/12/2011" and that "in the circumstances it would be prudent to begin to consider how this will be achieved and I would be grateful if you could provide me with an update on your intentions/proposals by 30th April 2011". But it does not say what the bank would do if the loan was not repaid by that date. Nor was parole evidence led by the writer of the letter which might have shed light on that question. Counsel relied upon the evidence of the appellant (p 14ff of appendix):

> "Q: So what did the Royal Bank of Scotland do as a result of… this letter…?
>
> A: Very little apart from chase us quite hard just to, well, the letter says it all, we had no alternative, they weren't for changing their mind, they weren't for giving us a chance to change anything so we had to find alternative funding from another lender.
>
> Q: They were going to give you one more year, is that what you said?
>
> A: A reasonable time frame, yes.
>
> Q: A reasonable time frame to re-finance the company?
>
> A: Yes…"

There then followed, *inter alia*, a discussion about a reduction in the value of the properties in the company's balance sheet and, according to the appellant, that if there was no

acknowledgement of the poorer state of the housing market the bank might carry out a full valuation and that it might have given the bank "an opportunity to wish to just take control of the company and to liquidate it or do as they pleased but the Director would have no choice, if they called in the loans." (p 17 of appendix) In particular, counsel relied upon two answers. The first (on the same page) was:

> "Q: What was the last thing you said about the Directors?
>
> A: The Director would have no choice, no option if the Royal Bank of Scotland called [*sic*] the loan"

And, on p18 of the appendix:

> "Q… that if you felt, that if your accounts did not acknowledge to at least some extent this decline in the property market that that might invoke a more critical line?
>
> A: Exactly right.
>
> Q: From the Royal Bank of Scotland?
>
> A: Yes.
>
> Q: And did you have concerns about the consequences of that happening?
>
> A: Very much.
>
> Q: Okay, very much, and what were your concerns?
>
> A: That the Royal Bank of Scotland would liquidate the company or withdraw their credit facilities and take re-possession of the properties.
>
> Q: And would that be the end of the company?
>
> A: Yes, 100%."

In our opinion, all that can be taken from these passages of evidence are that the appellant understood the terms of the bank's letter and that on one scenario, namely a failure to recognise the then property market in the company's balance sheet, the bank *might* take certain steps. But counsel was unable to point to any evidence from the bank about what it would have done – and indeed on the evidence of the appellant himself the circumstance which he was concerned about did not arise because the company *did* alter the balance sheet.

[11] Counsel also relied upon the evidence of Mr McLeod, the expert chartered accountant led on behalf of the appellant. Counsel submitted that the sheriff failed to have regard to the fact that in reaching his view that the appellant's shareholding had a nil value Mr McLeod was aware of the financial circumstances of the company which, in particular, had the Royal Bank of Scotland intimating that it no longer wished to provide funds to the company and, in the event, the re-financing by Shawbrook Bank Limited required the appellant to provide additional security over properties not in the company's ownership. However, Mr McLeod expressly said both in his report and his evidence that he did not carry out a valuation of the shares on the basis of those surrounding circumstances because the valuation of the properties by Mr Hall already showed that the assets were worth less than the then borrowings (p 211ff of appendix). Counsel put a hypothesis to Mr McLeod after referring to a passage from his report (p 212ff of appendix):

> "Q: … Let's just proceed on the assumption that at some point somebody is going to say that the J & E Shepherd [Mr Hall] valuations are too low…?
>
> A: If there is a forced sale by the finance company, whether it be a bank or otherwise, the marketplace reacts to that, and they tend to keep in within the lower price paid for the assets, than market value, or even the depressed value for the valuation. I have experience of someone just now with the Royal Bank of Scotland. The value of the properties they achieve are significantly lower than within a portfolio valuation.
>
> Q: Is that in a situation where the bank has stepped in and is selling or is the company?
>
> A: The company is selling.
>
> Q: And the market knows that?
>
> A: Yes.
>
> Q: And, as a result of that, uses that knowledge to drive a harder bargain, in effect?
>
> A: Okay, indeed.
>
> Q: You think that the position that the bank were taking in this case, at around that time, if a purchaser was sought for the shares of Glencarse, is that something that might well have been a factor?

A: It may well have been a factor."

In our opinion, this evidence does not assist the appellant. It proceeds upon a hypothesis which is not consistent with the evidence: there was no forced sale, the bank had not "stepped in", there was no evidence that the market "knew", and in any event Mr McLeod goes no further than to say all of that "might" be a factor.

[12] Counsel also submitted that the evidence of the respondent's expert, Mr Ritchie, showed that he had proceeded upon a valuation of the properties rather than the shareholding. Counsel referred to Mr Ritchie's evidence in cross-examination at pp 422 to 435 of the appendix. For the sake of brevity we do not refer to those passages in detail. Suffice it to say that in our opinion Mr Ritchie made it perfectly clear that he understood that he was valuing the shareholding, but that in doing so he agreed with Mr McLeod that the value would be determined by the valuation of the properties by a chartered surveyor. During that part of the cross-examination, counsel put to Mr Ritchie the surrounding circumstances of the Royal Bank's position and the requirements of the funding from Shawbrook Bank Limited. But, as Mr Ritchie pointed out, the company did ultimately find the finance to replace the Royal Bank of Scotland's loan. In any event, as he made clear, both he and Mr McLeod proceeded upon the basis that the value of the shareholding of a company like the appellant's would be realised by selling the properties and then to drawing the value out of the company (p 437 of appendix).

[13] But even if the evidence supported the appellant's position, in our opinion counsel's criticism of the sheriff's approach proceeds upon a misunderstanding of the rule in *Sweeney*. That is because counsel fell into the trap of looking for evidence which in effect would, if proved, establish that there was no actual willing buyer, rather than the hypothetical one. As counsel for the respondent submitted, the exercise involves having no regard to the factors

surrounding what might be an actual sale. Counsel for the respondent also recognised that there could be circumstances where, as a matter of known fact, the shareholding or, more likely, the underlying company assets would be valued at rock bottom prices, such as where an administrator or liquidator had been appointed. To the layman that all might look as potentially unjust if for example insolvency occurred a few days after the relevant date, but that would be to ignore the other provisions of the 1985 Act, as discussed in *Sweeney*, whereby, for example, the appointment after the relevant date of an administrator or liquidator will be a relevant factor for the court to take into account when considering the resources of the parties at the date the award is to be made. Moreover, the fact of refinancing, even with additional security from non-company assets, logically has no effect on the valuation of the shareholding because the hypothetical purchaser would by definition be replacing one form of finance with another – a point made by Mr Ritchie (p 388 of appendix).

[14] Before we leave this ground of appeal, we should deal with further submissions made by counsel for the appellant. The first was that the sheriff ignored the evidence of the company's accountant, Mr Crichton, to the effect that the correct method for the shareholding valuation was based on the yield, that is to say the return on the investment. But that submission ignores the fact that Mr Crichton was not instructed by the appellant to value the assets. While he is a chartered accountant he was not for the purposes of the proof called as an expert witness. His method of valuation flied in the face of the appellant's own position before the sheriff and on record, namely that the valuation was on a net asset basis, per the evidence of Mr McLeod. Counsel criticised the sheriff for failing to take into consideration Mr Crichton's evidence, but the reason for that was the appellant did not found on Mr Crichton's basis of valuation. Rather, he founded on Mr McLeod's.

[15] Secondly, counsel criticised the sheriff for not taking into account the evidence of Mr Crichton on the surrounding financial circumstances of the company. It is true that he was able to give detailed evidence on the company accounts which he himself had prepared and that he frequently described the company's financial position as "perilous", but the factual basis of that opinion was no more than we have earlier described. Accordingly, we also reject that criticism of the sheriff's approach.

Director's Loan

[16] The sheriff found in fact that Glencarse Limited was due the sum of £65,415 to the appellant by way of a director's loan. The evidence in support of that was contained in the unaudited accounts of the company to 31 January 2012 in the sum of £68,265. The parties were agreed that this sum was overstated by £2,850. The appellant's position at the proof was that this net figure was an error and should not have been included in those accounts. The sheriff noted that the information provided for the accounts to record sums as due to the appellant must have come either from the appellant himself or from papers provided to the accountant, Mr Crichton, for the purpose of preparing the accounts. Moreover, the sheriff noted that the figures were not only in the above accounts but also in accounts for previous years, which accounts must have been approved by the appellant. The sheriff recorded that the explanation offered by the appellant was that a figure of £65,000 in the accounts represented an increase in value of assets owned by another company in which he had an interest, namely WMB Properties Limited. The evidence from the director's loan account for the relevant period was that the payments in respect of a shed erected on ground owned by WMB Properties Limited were made by the appellant to Glencarse Limited. The sheriff was plainly unimpressed by the evidence of the appellant and his witnesses,

particularly Mr Crichton. He discusses invoices which had been produced and which were said to be evidence of the true nature of the transactions and the manner in which the accounting ought to have been done but had not been because of the error. In the event, the sheriff was not persuaded by the evidence for the appellant that the figure in the director's loan account should be modified, save as to the limited extent agreed.

[17] Counsel for the appellant was critical of the sheriff's approach. The sheriff, he said, had made no adverse finding in respect of the evidence of Mr Crichton. Counsel submitted that Mr Crichton's evidence was clear and material: there had been a misunderstanding on cost and value regarding the shed. The consequence was an overstatement in the director's loan account of £47,084, together with further minor amendments, which in turn would reduce the sum due to the appellant to £18,330. Mr Crichton was the independent accountant for both companies and was best placed to give an explanation of the errors. Moreover, Mr Crichton's explanation had been put to Mr McLeod and Mr Ritchie and they both accepted that Mr Crichton's treatment of the reconciliation to the director's loan account was correct.

[18] In our opinion, this ground of appeal also fails. Counsel referred to passages from the evidence of Mr Crichton (p 291ff of appendix). His evidence was that there was a misunderstanding that the figure of £65,000 in the accounts for WMB Properties Limited was for the actual costs incurred, rather than the value of the shed, which was the true position. In fact, all that had been paid by Glencarse Limited on behalf of WMB Properties Limited was £17,915. Three invoices addressed to WMB Properties Limited were produced and put to Mr Crichton in examination-in-chief. They were not, however, then referred to when he came to explain his revised workings for the loan account reconciliation. Counsel submitted that the sheriff fell into error in discussing these invoices (counsel described them

as "a red herring") when it was plain that Mr Crichton was referring to only one payment by Glencarse Limited on behalf of WMB Properties Limited of one invoice. There are a number of difficulties with that submission. First, Mr Crichton did not say that there was only one payment. He referred to "payments" (p 293 of appendix). Secondly, the "red herring" was a set of three invoices produced not by the respondent but by the appellant. When pressed on the reason for that, counsel eventually said it was "a mistake". But he could offer no explanation for him putting those invoices to Mr Crichton in examination-in-chief. Thirdly, as Mr Crichton recognised, the costs for the shed were subject to Value Added Tax. They would therefore be included in the VAT returns for WMB Properties Limited and would require to be vouched (p 293-294 of appendix). It should therefore have been a straightforward exercise for the relevant invoice or invoices paid by Glencarse Limited to be found and produced. Counsel was unable to explain why that had not been done. When pressed in cross-examination to vouch the figure of £17,915, Mr Crichton's somewhat weak response was "I don't have the information to hand but if you want it I can get it". (p 346 of appendix)

[19] We do not agree that the evidence of Mr Ritchie was of assistance. All that he was prepared to accept was that if what Mr Crichton said was true then in accounting terms he had dealt with it correctly. But that begged the question of whether there was evidence of sufficient quality for the sheriff to accept Mr Crichton's judgment that an accounting error had taken place and what the arithmetical consequences were. Again, Mr McLeod was unable to add any material evidence on this matter, other than to record Mr Crichton's explanation.

[20] In essence, counsel was submitting that Mr Crichton was an independent chartered accountant who admitted an error. He ought to be believed. But that ignores the fact that the

sheriff was required to consider all of the evidence. It is plain that the credibility of Mr Crichton was not in question, but his reliability was. We cannot fault the sheriff's approach to the evidence on this issue. There is no basis in law which would entitle us to interfere.

Decision

[21] The appeal is refused. Parties were agreed that we should reserve the question of expenses.