



SHERIFF APPEAL COURT

[2024] SAC (Civ) 46
PAI-A334-22

Sheriff Principal Murphy KC

OPINION OF THE COURT

delivered by Sheriff Principal S F Murphy KC

in appeal by

EDWARD ALEXANDER LEISHMAN

[Pursuer/Appellant]

in the cause

EDWARD ALEXANDER LEISHMAN

against

ALEXANDER ANTONY NOBLE

[Defender/Respondent]

Pursuer/Appellant: McAndrew, Advocate; Complete Clarity Solicitors & Simplicity Legal
Defender/Respondent: Hankinson; DHM Law

11 November 2024

Introduction

[1] In June 2022 the parties discussed concluding a business deal whereby the pursuer and appellant would sell his shares in a company (“EVC”) to the defender and respondent. A document titled “Heads of Terms” was executed by them on 26 August 2022 in which the respondent agreed to pay £20,000 to the appellant for his shares at which point the appellant would resign as a director of EVC. However, it also proposed that a formal share

purchase/sale agreement be drafted, to include the terms set out in the document. The appellant averred that on the same day the respondent intimated to him that payment of £20,000 had been made and in reliance on that he completed form TM01 to resign as a director of EVC. Subsequently he discovered that only £1000 had been paid to him by the respondent. He raised an action for payment of the balance of £19000. Following debate the sheriff upheld the respondent's preliminary plea to the relevancy and dismissed the action, in an interlocutor dated 20 December 2023. Appeal is taken against that decision.

Grounds of appeal

[2] While the sheriff identified the correct legal principles, he erred in applying them to the present case, in particular by finding that the parties had not intended to be bound by the Heads of Terms document. He ought to have held that the parties had intended it to have immediate effect so that the payment obligation was enforceable and he had erred by refusing to fix proof before answer on the issue of supplementary oral agreement. *Esto* the parties' intention to be bound had not been established by the Heads of Terms document, the sheriff had erred by dismissing evidence of subsequent conduct as irrelevant to the issue of the parties' prior intention to be bound by it.

Submissions for the appellant

[3] The initial issue related to formation of contract. Whether two parties had reached a binding agreement had to be assessed objectively through the lens of honest, sensible businessmen and based upon events before and after the alleged conclusion of the bargain: *Baillie Estates Limited v Du Pont (UK) Limited* 2009 CSOH 95. The performance of the substantive obligations is a significant aspect of subsequent conduct which can be relevant

to that assessment: *G Percy Trantham Limited v Archital Luxfer Limited* [1993] 1 Lloyd's Rep 25; *RTS Ltd v Molkerei Alois Muller GmbH* 2010 1 WLR 753. The bare fact that parties to a completed agreement stipulate that it shall be embodied in a formal contract does not necessarily indicate that they are still at the stage of negotiations: *Stobo Limited v Morrison (Gowns) Limited* 1949 SC 184; *Supaseal Glass Limited v Inverclyde Windows Manufacturing Limited* 2022 SCLR 380. Clear language is required where an agreement is to be conditional upon a further, written contract, particularly where the essential elements of the agreement have been provided for: *Stobo; HT Van Laun and Co v Neilson* 1904 SLT 86. In any event, such a condition may be waived by subsequent conduct: *RTS Limited*. The phrase "Heads of Terms" is not a term of art and cannot of itself exclude an inference that parties intended to be bound immediately: *Pretoria Energy Co (Chittering) Ltd v Blankley Estates Ltd* [2023] L & TR 26.

[4] Parties may agree on the essential elements of their bargain while leaving other aspects to be finalised later: *RTS Ltd*. A contract for the sale of shares will generally involve agreement on the parties, subject matter and price: *Macqueen and Thomson on Contract Law in Scotland*, 15th edition, at 2.15. Other necessary terms would fall to be implied: *Stair Memorial Encyclopaedia, Companies*, at paragraphs 107-8; *Supaseal*.

[5] The sheriff erred in deciding that the Heads of Terms document pointed against an intention to be bound by its terms. His analysis focussed on the preamble and clause 5 of the document which created a misleading interpretation. He failed to construe the document as a whole.

[6] Parties' subsequent conduct indicated their intention to be bound by the terms of the Heads of Terms document. The averments relating to that conduct were capable of

supporting a submission (after evidence) that any condition requiring subsequent formality had been waived.

[7] The sheriff found that the expression “Heads of Terms” was commonly understood to refer to a non-binding agreement without appropriate evidence of commercial practice; accordingly he took account of an irrelevant consideration.

[8] In all the circumstances the sheriff ought to have fixed proof before answer to determine the questions between the parties.

Submissions for the respondent

[9] The grounds of appeal do not address the sheriff’s actual findings. He decided that the Heads of Terms created an obligation to draft a formal share purchase agreement and not an obligation to make payment. Its terms were clear and unambiguous and therefore fell to be applied by the court: *Rainy Sky v Kookmin Bank* [2011] UKSC 50. In the absence of an obligation for payment the appellant’s case was irrelevant, as the sheriff held. The grounds of appeal are irrelevant by failing to recognise the distinction between an agreement to draft a share purchase agreement which would contain a payment obligation and an agreement which creates a payment obligation which may be subject to further contract or conditions before it becomes binding.

[10] The present case should be distinguished on its facts from *Supaseal*. The proposed share purchase agreement in the present case was not a “bells and whistles” exercise but was to be the only basis on which any payment obligation would arise. It was plain from clause 5 of the Heads of Terms that the share purchase agreement which was to be prepared was to be the final agreement. The issue between the parties was truly one of construction and not a question of formation of contract. It followed that the cases of *Supaseal*, *Baillie*

Estates Limited, *RTS* and *G Percy Trentham Limited* were not in point. These cases were ones in which a contract had come into existence not through offer and acceptance but through performance.

[11] The general rule is that a contract cannot be construed with reference to subsequent actings: *McBryde on Contract*, paragraphs 8-30 to 8-33; *L Schuler AG v Wickman Machine Tool Sales Ltd* [1973] 2 WLR 683.

[12] Insofar as the appellant seek to rely on waiver, under reference to *RTS*, no such case is pled on record in the present case. The only expression of a payment obligation would have been contained within the share purchase agreement which was not executed. In its absence there could be nothing to waive.

[13] The present case is similar to *Van Laun* in that the share purchase agreement was to include the only binding expression of a payment obligation. An agreement and a binding agreement are not the same thing. Clauses 2 and 3 of the Heads of Terms document only make practical sense if the expression “this agreement” refers to something subsequent to it.

[14] The sheriff did not rely on the expression “heads of terms” in making his findings but on the contents of the document.

[15] The appeal should be refused as its basis was irrelevant.

Decision

[16] Parties do not challenge the sheriff’s summary of the governing legal principles in this case, nor do I. These are:

- (i) a contract for the sale of shares and resignation as a director does not require to be committed to writing;

- (ii) whether or not parties have reached a binding agreement must be assessed by the court objectively;
- (iii) where parties agree not to be bound until a written agreement has been completed, they will not be bound until that point;
- (iv) even if parties agree that either may withdraw until a formal written contract has been executed, that does not necessarily mean that they are still at the stage of negotiation; and
- (v) while agreement may be reached on the essentials of a contract, parties will not be bound if they do not intend to be and what the essentials are may vary according to the contract under consideration (*Supaseal*).

[17] The sheriff's interpretation of the Heads of Terms is based upon its preamble which states: "It is proposed that a formal Share Purchase/Sale agreement is drafted to include the following terms ..." and clause 5, which states:

"Both parties acknowledge that they have been advised that it is open to them to take independent legal advice before entering into a final share/purchase agreement."

He found that the unambiguous import of these two elements was that parties had agreed to draft a formal share purchase agreement and that no obligation to pay the agreed value of the shares would or could arise until the formal agreement was executed. It followed that the appellant's case was irrelevant as he had not pled on record details of any concluded bargain which could give rise to an obligation for payment.

[18] Support for that position may be found in the case of *Van Laun* which has similarities with the present one. The opinion of the Lord President describes the (unsigned) memorandum of understanding on which the appellant relied in this way:

"This document quite recognises that there is to be a proper legal contract, and that that legal contract is to contain the expression, and the only binding expression, of

the agreement, and in the ordinary case where it is arranged that a legal contract in certain terms is to be entered into, an action *ex contractu* will not lie unless and until that legal contract has been entered into.”

Lord Kinnear agreed:

“Therefore the pursuers’ averment is that the terms of the contract between them and the defenders are those expressly set out in this memorandum. Now, the first of these terms is that the firms agree that that they will enter into a proper legal contract, when prepared, with the pursuers for the purpose of placing in their hands the conduct of the amalgamation of their businesses. That is the first term of their contract, and it appears to me to follow of necessity that no binding obligation had been contracted between the parties, or was intended to be contracted between the parties, until a formal written contract should be executed.”

Despite the apparent similarities between this case and the present one in my view *Van Laun* may be distinguished on its facts for a number of reasons. In *Van Laun* the memorandum of understanding on which the appellants relied, which is the equivalent of the Heads of Terms document in the present case, was never signed, as Lord Adam and Lord Kinnear point out, whereas in the present case there is no dispute that the Heads of Terms document was executed on 26 August and the issue is its significance. The companies themselves in *Van Laun* specifically intimated that they did not see their way to amalgamate in 1900 after discussions with the appellants but did so three years later by themselves. There was therefore no performance of any part of the memorandum on the part of the railway companies established and there had been no relevant averment of *rei interventus* to render the appellant’s case relevant.

[19] The sheriff’s position is that where the language used is unambiguous the court must apply it, as stated in *Rainy Sky SA* at paragraph 23 and in the body of authority quoted by Lord Clarke in the preceding paragraphs. However, the Heads of Terms also included the following:

- “1. Mr Noble will pay Mr Leishman £20, 000 for his share on EVC ...
7. Following Mr Noble’s purchase of Mr Leishman’s share, Mr Leishman will resign as Director of EVC ...”

The sheriff erred in my view by focussing too narrowly on the question of the strict construction of the Heads of Terms document. He stated, at paragraph [24] of his judgment, that: “‘Heads of Terms’ is commonly understood to refer to a non-binding agreement, with a view to a contract subsequently being concluded.” However, in the English Court of Appeal decision in *Pretoria Energy Co (Chittering) Limited* it was said (within paragraph 28):

“Nor is the label ‘Heads of Terms’ conclusive: a document labelled ‘heads of terms’ may be intended to be a non-binding record of the broad principle of an agreement to be made in formal written documents subsequently negotiated, or may be intended, in whole or in part, to be a binding contract governing the parties’ relations until a more detailed agreement is drawn up ...”

[20] The sheriff noted, within paragraph [30] of his judgment, that the respondent had paid a sum of money to the appellant who had resigned as a director of the company conform to Form TMO1 which he had completed on 26 August 2022. While the general rule is that a contract should not be construed by reference to the parties’ subsequent actings, that is not absolute. Paragraph 8-30 of *McBryde on Contract* (3rd edn) begins:

“Although in some cases a contract has been construed with reference to what happened after the contract was made, it is thought that as a general rule a contract should not be construed with reference to the subsequent conduct of parties or a change in circumstances.”

The case of *L Schuler AG* contains similar reasoning, while in *RTS Ltd* the court stated, at paragraph 35:

“Even if certain terms of economic or other significance to the parties have not been finalised, an objective appraisal of their words and conduct may lead to the conclusion that they did not intend agreement of such terms to be a precondition to a concluded and legally binding agreement.”

In the present case the appellant pled within article of condescendence 2 the following:

“Thereafter the parties intended to implement the terms of the document (i.e. the Heads of Terms) and the Defender confirmed to the Pursuer that he had transferred the Pursuer the sum due in clause 1 of the document (£20, 000) by bank transfer. Thereafter, the Pursuer completed the TM01 form (Termination of Appointment as Director). The Defender then scanned a copy of the executed (sic) and TM01

Pursuer's agent under cover of an email confirming agreement had been reached and implemented."

In answer 2 the respondent states: "The Heads of Terms as produced by the Pursuer do not comprise the entire agreement between the parties." There follow averments relating to funds from EVC which are said to have been in the possession of the parties, including a sum of £19,000 said to have been held by the appellant, before the conclusion:

"On 26 August 2022, at 94 Hope Street, Glasgow – the parties agreed that payment of the Consideration would be discharged by payment by the Defender to the Pursuer of £1, 000 and retention by the Pursuer of the Funds. The Defender subsequently paid the Pursuer £1,000.00"

[21] These answers are in turn denied by the appellant. However, in their pleadings both parties aver that significant steps were taken by both sides on or about 26 August 2022 in relation to the transfer of ownership of EVC. Performance on both sides "will often make it unrealistic to argue that that there was no intention to enter into legal relations" (*G Percy Trentham Limited, RTS Ltd*). Both parties aver that the steps they took were taken in furtherance of an agreement reached at a meeting in 94 Hope Street on that date. They diverge on the terms of the bargain which each avers was made. Neither party claims that any formal share purchase/sale agreement was executed. The appellant's pleadings state that parties intended to implement the terms of the "Heads of Terms" document. The respondent's pleadings state that the "Heads of Terms" document did not comprise the entire agreement between the parties. In support of that position it is averred that a specific arrangement for payment of the consideration was agreed at that meeting.

[22] It is significant in my view that both parties aver that they proceeded in furtherance of what they perceived the agreement to be without producing or executing any more formal document than the "Heads of Terms". Accordingly in my view it is not possible to determine what the contractual basis, if any, of the actions taken by either party was,

without hearing evidence of what occurred at the meeting on 26 August 2022. It follows that I consider this to be a classic case for proof before answer to have been fixed. What is clear from their pleadings concerning their actions is that both parties obviously thought that an agreement had been reached at the meeting on 26 August: the respondent transferred funds to the appellant; and the appellant resigned as director of EVC. While these subsequent actings may not serve to identify the terms of the bargain in any detail, they clearly allow an inference that each party believed that agreement had been reached and one which was based on terms contained within the “Heads of Terms” document executed on that day. The sheriff erred in my view in failing to take account of these considerations and in basing his decision exclusively on a strict interpretation of the preamble and paragraph 5 of the Heads of Terms document.

[23] I shall therefore allow this appeal and recall the judgment of the sheriff in terms of the interlocutors dated 20 December 2023 and 19 February 2024; and I shall remit the case to the sheriff at Paisley with a direction to fix proof before answer in relation to whether a binding contract was agreed by parties on or about 26 August 2022.

[24] I grant sanction for the use of junior counsel in this appeal and shall invite written submissions of the question of expenses to be received within 21 days of the date of the interlocutor accompanying this opinion.