



OUTER HOUSE, COURT OF SESSION

[2024] CSOH 83

P581/24

OPINION OF LORD SANDISON

In the petition

ARBITRATION APPLICATION No 2 OF 2024

Petitioners: McKinlay; Ledingham Chalmers LLP
Respondent: R Sutherland; The McKinstry Company LLP

22 August 2024

Introduction

[1] By way of this application, the petitioners challenge the decision of an arbitrator dated 14 June 2024 on two separate grounds.

[2] The arbitration was governed by the Scottish Arbitration Rules, and the first ground of challenge alleges the existence of a serious irregularity in the conduct of the arbitration in terms of rule 68 thereof. That challenge does not require the court's leave to proceed.

[3] The second ground of challenge is advanced under rules 69 and 70, and alleges that the arbitrator fell into legal error in his determination. Such a challenge requires the leave of the court to proceed unless the proposed respondent in the appeal agrees to it, which he does not.

[4] In terms of rule 70(5), the petitioner's application for leave falls to be determined without a hearing unless I am satisfied that one is required. Having reviewed the papers, I

consider that the relevant issues have been appropriately canvassed there and that a hearing is not required.

Background

[5] The parties are members of a farming partnership conform to a partnership agreement dated 1 April 2012. The partnership agreement provides *inter alia* as follows:

“19.1 Each partner shall at all times ... be just and faithful to the other partners in all matters relating to the firm

...

22.1 If any partner shall:

...

22.1.4 commit any material breach or persistent breach of this agreement;

22.1.6 be guilty of any conduct likely to have a material adverse effect upon the firm’s business or reputation;

...

then, upon the partners becoming aware thereof, and in any such case, the other partners may by notice in writing expel such partner from the firm and upon service of such notice such partner shall forthwith be deemed to have ceased to be a member of the firm.”

[6] On 8 September 2022 a notice of expulsion in terms of clause 22.1 was served by the petitioners on the respondent. The petitioners considered that service of the notice was justified by the respondent’s alleged conduct towards them, including two assaults on the first petitioner in late 2020 and early 2021, which were said to constitute a breach of the duty to be just and faithful in terms of clause 19.1, as well as representing a material breach of the agreement in terms of clause 22.1.4, and by behaviour directed at the firm’s employees and

third parties dating back as far as March 2018, which was said to represent conduct of the kind struck at by clause 22.1.6.

[7] The respondent denied that he had engaged in any conduct falling within the ambit of clauses 19 or 22 and disputed the validity of the expulsion notice.

The arbitration

[8] Clause 28 of the partnership agreement provides for resolution of disputes by arbitration, and the question of the validity of the expulsion notice was accordingly referred to the arbitrator.

[9] The petitioners and the respondent were respectively afforded periods to intimate and adjust their statement of claim and response, to include the factual matters and legal grounds relied upon by them and the orders they sought, which they each duly did. An evidential hearing took place before the arbitrator between 13 and 15 May 2024. It was agreed amongst the arbitrator and the parties that the hearing would be conducted in accordance with the rules of evidence and procedure as they would apply in the Scottish civil courts.

[10] Following completion of the factual evidence, both parties lodged written submissions. The petitioners claim that the respondent's written submissions raised new lines of defence not featuring in his pleadings, in particular that the expulsion notice was invalid due to delay in serving it once the other partners had become aware of the conduct in question, and that there had been a breach of natural justice in the process prior to its issue. Counsel for the petitioners submitted that these matters had not been put in issue in the pleadings or evidence, that the hearing would have been conducted differently had these

issues been perceived to be live ones, and that the petitioners would be prejudiced if these arguments were entertained at the stage which had been reached.

The decision

[11] The arbitrator determined that the respondent had assaulted the first petitioner in late 2020 and that there had been another physical altercation in December of that year during which each assaulted the other. He held that the assaults by the respondent constituted material breaches of his obligation to be just and faithful to the partners of the firm, but that the notice of expulsion had not been issued within a reasonable time following the assaults. He held that an incident in March 2018 had involved the respondent verbally abusing a third party, who had felt threatened thereby, but that there was no evidence that that conduct had actually had a material adverse effect on the business of the firm and thus did not meet the threshold for expulsion under clause 22.1.6, and that in any event the expulsion notice had not been issued within a reasonable time of the other partners becoming aware of the incident.

[12] The respondent's argument based upon breach of natural justice was rejected on its merits and because the arbitrator did not consider that it was open to the respondent to raise that issue for the first time during submissions following conclusion of the evidence. The petitioners' submission that the respondent's argument regarding delay in serving the expulsion notice should be rejected on the basis that it was not open to him to raise this issue for the first time during submissions following conclusion of the evidence was not specifically addressed.

[13] The arbitrator disposed of matters by holding that the notice of expulsion was invalid as it had not been served within a reasonable period of the other partners becoming aware of the conduct which might have justified such service.

The grounds of appeal

[14] The petitioners' serious irregularity appeal under rule 68, with which this opinion is not concerned, proceeds on the basis that the arbitrator decided the case based upon a matter that did not form part of the dispute which had been put in issue by the parties, that the procedure adopted did not provide them with a reasonable opportunity to deal with it, and that they will suffer substantial injustice if those irregularities are not addressed.

[15] In relation to their legal error appeal in terms of rule 69, the petitioners argue, under reference to *Newfield Construction Ltd v Tomlinson* [2004] EWHC 3051 (TCC), 97 Con LR 148 per HHJ Coulson QC at paragraphs [28], [33] and [34], that in deciding the case on an issue which did not feature in the pleadings in the arbitration, the arbitrator erred in law and exceeded his jurisdiction. They further argue that the arbitrator misconstrued clause 22.1.6 of the partnership agreement by treating the actual, rather than the likely, impact of the respondent's conduct as being determinative of any right to expel, and that the conduct in question met the proper test. They ask the court to order the arbitrator to reconsider these matters.

[16] Rule 70 provides:

- “(1) This rule applies only where rule 69 applies.
- (2) A legal error appeal may be made only –
 - (a) with the agreement of the parties, or
 - (b) with the leave of the Outer House

- (3) Leave to make a legal error appeal may be given only if the Outer House is satisfied –
- (a) that deciding the point will substantially affect a party's rights,
 - (b) that the tribunal was asked to decide the point, and
 - (c) that, on the basis of the findings of fact in the award (including any facts which the tribunal treated as established for the purpose of deciding the point), the tribunal's decision on the point –
 - (i) was obviously wrong, or
 - (ii) where the court considers the point to be of general importance, is open to serious doubt ..."

[17] The petitioners maintain that the arbitrator's decision substantially affects their rights, in that, had the alleged legal error not been committed, they would have been successful in the arbitration. They contend that the arbitrator's approach to the interpretation of the scope of the dispute was obviously wrong in law, as was his approach to the interpretation of clause 22.1.6, or in any event that both issues are points of general importance in relation to which the arbitrator's approach is open to serious doubt. They finally claim that, given the close relationship between the grounds of their serious irregularity appeal and the proposed legal error appeal, it would be in the interests of justice, and not inconvenient, for the issues raised on both fronts to be heard and determined together.

Respondent's position

[18] The respondent draws attention to clause 28.2 of the partnership agreement, which provides that:

“The decision or award of such arbiter shall be final and binding upon all the partners. No appeal shall be competent to any court of law in terms of the Administration of Justice (Scotland) Act 1972.”

Although that statute (and in particular section 3 thereof) had been repealed by the time the agreement was entered into, the language of the clause was sufficiently clear to indicate that the parties had agreed to exclude any right of appeal on an error of law.

[19] Further, the petitioner’s statement of claim in the arbitration referred to an earlier notice of expulsion served on the respondent in August 2021, and averred that, they having decided not to insist on that notice, his conduct had again thereafter deteriorated, causing the service of the further notice in September 2022. The respondent had understood from those averments that the petitioners proposed to lead evidence of events occurring after August 2021, but in the event they had not done so. It was their failure to lead any such evidence that caused the submission on his behalf that there was no evidence justifying his expulsion on a proper construction of the expulsion clause. As the only relevant evidence before the arbitrator related to events up to August 2021, that was all that he was able to consider when making his decision. The petitioners’ counsel had accepted that the arbitrator had the right to determine the proper construction of the expulsion clause, which he had then done.

Decision

[20] Rule 69 of the Scottish Arbitration Rules is a “default” rule within the meaning of section 9 of the Arbitration (Scotland) Act 2010. That means that it applies to the arbitration in question only in so far as the parties have not agreed to modify or disapply it in whole or in part in relation to the arbitration: section 9(2). Parties are to be treated as having agreed to modify or disapply a default rule if or to the extent that it is inconsistent with or

disapplied by, *inter alia*, the arbitration agreement: section 9(4). In the present case, the arbitration clause in the partnership agreement makes it clear that the arbitrator's decision is to be "final and binding" on the parties. The reference to the Administration of Justice (Scotland) Act 1972, though otiose given the repeal of section 3 of that statute by the 2010 Act, further indicates that the parties' intention was not to permit a case to be stated by the arbitrator for the opinion of this court on any question of law which might arise in the arbitration. Although the parties were not entitled to contract out of the mandatory provisions of the Rules relating to serious irregularity appeals, the stipulations made by them in clause 28 of the partnership agreement are inconsistent with the existence of a legal error appeal to this court from a decision of the arbitrator in terms of rule 69. The application in terms of that rule is accordingly incompetent and leave to make such an appeal must be refused.

[21] I would not in any event have granted leave to appeal even had the application for such leave been competent. Briefly stated, the points which the petitioners sought to place under review were matters which the arbitrator was asked to decide and their determination may substantially affect the petitioners' rights (thus satisfying the requirements of rule 70(3)(a) and (b)). However, they are not points of general importance within the meaning of rule 70(c)(i), being respectively issues of the relationship between the true import of the arbitral pleadings and the conduct of the arbitral process, and of construction of the terms of a particular partnership agreement, both of which are highly situation-specific issues with little or no reach beyond the facts of this individual case. Therefore, although I might have been inclined to regard the arbitrator's construction of clause 22.1.6, at least, as open to serious doubt, that is not the test which falls to be applied.

[22] Rather, the appropriate criterion for granting leave for the proposed legal error appeal would have been that posited by rule 70(c)(ii), ie that the tribunal's decision on the points in issue was "obviously wrong". That is a very high hurdle to surmount. The issue concerning the true import of the arbitral pleadings and its relationship with the conduct of the arbitral process is paradigmatically one for the arbitrator to assess and determine within that necessarily wide ambit of discretion which attends the superintendence of virtually any formal dispute resolution process. That was not quite the issue which arose in *Newfield Construction*, which involved the arbiter failing to take into account matters which he ought to have taken into account in determining the scope of the dispute put before him. No such suggestion appears to be made in this case. The question of the proper construction of clause 22.1.6 in context is likewise one upon which reasonable minds may properly differ without one or other opinion being obviously wrong. The test for granting leave would not have been satisfied even had the proposed legal error appeal been competent.

Disposal

[23] Leave to appeal on the ground of legal error is refused for the foregoing reasons. The case will be put out by order to discuss further procedure in respect of the petitioners' ground of challenge alleging serious irregularity.