SHERIFF APPEAL COURT

[2024] SAC (Civ) 5
HAM-A349-18

Sheriff Principal S F Murphy KC
Sheriff Principal N A Ross
Appeal Sheriff B Mohan

OPINION OF THE COURT

delivered by SHERIFF PRINCIPAL N A ROSS

in the appeal in the cause

CHARLES FINDLAY McINALLY

Pursuer and Appellant

against

ARCHIBALD MILLIGAN McINALLY Jr, as executor nominate of ARCHIBALD MILLIGAN McINALLY Snr

Defender and Respondent

Pursuer and Appellant: Colquhoun, advocate; Hutchesons
Defender and Respondent: MacLean, advocate; Wallace Hodge & Company Limited

6 February 2024

[1] Archibald Milligan McInally Senior was a farmer. He died on 30 October 1983. His estate was regulated by a trust disposition and settlement dated 23 October 1979 (the "Will"). The Will provided for an alimentary liferent of the farm and the farming business for his wife, Helen Rae McInally. His wife died on 11 October 2003. By that date, the respondent was the sole remaining trustee under the Will.

[2] The Will provided that, upon the failure or termination of the liferent to Helen Rae McInally, the trustees were directed to "hold, apply, pay and convey" the residue of the

estate to or for behalf of such of their children as then were surviving and had attained the age of 18 years, equally among them. Provision was made for the event of children pre-deceasing, with or without progeny, or not having attained 18 years. Provision was made for the trustees to deal with the estate prior to conveying to the beneficiaries.

[3] There are six residuary beneficiaries of the estate, including both the appellant and the respondent. For reasons unexplained in averment, findings in fact or submission, the respondent continued to operate the farm business from the date of the truster's death and after the expiry of the liferent, up until 2016, without making any final distribution of the assets to the beneficiaries. The appellant resided in the farmhouse from at least 2003 to 2016 without paying rent, council tax or other household bills, and without any formal lease. In 2016 the respondent sold the farmhouse for £350,000. He also sold an area of ground at the farm for £184,241. He did not distribute the proceeds to the beneficiaries. There is further heritable property as yet unsold.

[4] The appellant raised this action of count, reckoning and payment. The obligation to account was admitted. After sundry procedure, the respondent lodged an account of intromissions. The appellant lodged a note of objections, which the respondent answered. The action was appointed to a proof on the Record of Objections and Answers.

Proof on Objections and Answers

[5] The list of objections to the account is lengthy. The record sets out five challenged items of expenditure in the year 2003-04, including heat and light, council tax, telephone charge and management charge, and a reduction of accrued debt by £10,215.52. The same first four heads are all challenged in 2004-05, 2005-06, 2006-07, and the same first three heads in years 2007-08 to 2014-15. In year 2015-16 further items challenged include an accrued

management charge of £53,339.81. In the following years up to 2017-18 further items are challenged.

[6] Following proof, the sheriff adopted parties' classification of the various heads as falling under: (i) interim payments; (ii) management fees; (iii) accrued debt; (iv) inconsistent entries and (v) legal expenses. In relation to category (iv) he found that there was insufficient evidence to identify any consistency. In relation to category (v), the respondent gave an undertaking which resolved the matter. In relation to categories (i) to (iii) he issued an interlocutor dated 8 August 2022 repelling the appellant's objections to the executry account and ordaining certain deductions be made from the account.

[7] The appellant appeals that interlocutor in relation to six separate heads. Briefly summarised, these related to (i) payment of council tax and services, and (ii) utility bills, both during the period when the appellant occupied the farmhouse; (iii) the cost of clearing rubbish from the farmhouse after the appellant left and prior to sale; (iv) the recovery of sums paid to a bank under a bond of caution in respect of a debt incurred by the appellant; (v) payment of a fee to the farm manager; and (vi) payment of an accrued debt.

Submission for the appellant

[8] Counsel for the appellant submitted that the sheriff had erroneously treated all six items as distributions for the appellant's benefit, rather than expenses of the estate. The result had been to unfairly reduce the appellant's share in favour of the remaining beneficiaries. Some of these payments were for the benefit of the liferentrix, not the appellant. The respondent, as trustee, had extremely limited discretion to intromit with the fund. It was his duty to distribute it.

[9] The precise nature of a beneficiary's interest in the estate depends on the terms of the trust. When the right had vested, the relationship between beneficiary and trustee was akin to that of debtor and creditor. Whether any payment amounted to a distribution was a question of fact. Where a right to trust property had vested in the beneficiaries, any distribution by the trustee required consent. It was not open to the trustee to decide how to spend the fund. In the present case, the respondent was wrong to say that set-off was available, as it did not operate automatically, and in the present case any claims had prescribed. On the wording of the Will, the estate vested in the appellant on 11 October 2003, when the testator's wife died and the liferent ended.

[10] In relation to the first two heads, the sheriff erred in accepting that the respondent as trustee had power to spend the money and reclaim it. The sheriff identified that the appellant had benefited from the payments, but the payments would have to be made anyway. They related to the farmhouse, which was trust property, and in any event were at least partly attributable to other purposes. There was no contract under which they could be recovered.

[11] For the third claim, it arose as the appellant left a quantity of rubbish behind when he quit the farmhouse. The fact that £10,850.72 in clearance works was spent was not disputed. There was no legal basis, however, on which the respondent could recover that sum from the appellant, which was the effect of the deduction from the account. No entitlement to do so had been identified. In any event, prescription operated.

[12] For the fourth claim, the sum of £10,215.52 was paid by the respondent to the bank under a cautionary obligation, itself entered into in respect of a debt between bank and the appellant. It was accepted the appellant had not paid the debt, thereby triggering the obligation. It was not, however, a payment made on behalf of the appellant. It was a direct

obligation on the trustor, and therefore on the trust estate. It could not be deducted from the appellant's share without prior agreement.

[13] The fifth claim related to a management fee paid to one of the family, to run the farm during the period of the liferent, ending in 2003. The sheriff erred in treating this as a capital expense on the estate. The evidence showed that it was an income expense. Under the Will, the respondent was not entitled to encroach on capital, and had therefore made an impermissible capital distribution. The sum of £53,339.81 required to be repaid by the respondent to the trust estate.

[14] The sixth claim was resolved by agreement during the appeal hearing.

Submission for the respondent

[15] Counsel for the respondent submitted that, in relation to the first two heads, the sheriff was correct to find that the respondent was entitled to use trust funds to pay the various utility and other bills, to regard these as directly connected to the appellant's use and occupation of the farmhouse, and to recover them from the appellant's share of the fund. The appellant would otherwise have had to pay these bills himself. They served to reduce the fund available to the other residuary legatees. It did not matter that the appellant had no contractual or other liability to the providers.

[16] The matter depended on the terms of the Will. On a proper construction of the trust, the trustee had wide discretionary powers to divide the residue either by paying or conveying it, or by applying it for the benefit of the beneficiaries. While "[an] executor is nothing else than a debtor to the legatees" (*Jamieson* v *Clark* 1872 10 M 399 at 405 (IH), the respondent as trustee had much wider powers. The respondent had enduring directions to hold and administer the estate over time in accordance with the liferent purpose and the

residuary purpose. In doing so, he was able to realise and distribute portions of income or capital of the trust estate from time to time.

[17] The relevant provision was a direction to the trustees to "hold, apply, pay and convey the…residue to or for behalf of…the children of my marriage with [the liferentrix]…equally among them". The word "apply" incorporated a power to use the residue to pay or obtain benefits for a beneficiary, including from third parties. It was a discretionary power, and included relieving the beneficiaries of debts. This incorporated the costs of running the farmhouse in which the appellant lived without paying the bills. In an action of accounting, in the event of doubt, the persuasive or legal burden of proof rests on the objector (*McGivney Construction Ltd* v *Kaminski* 2015 CSOH 107 at paras 13, 14; *Gray* v *Cape* [2021] SAC (Civ) 32 at paras 35, 40).

[18] In respect of ground 3, it was not disputed that the appellant had left the farmhouse in such a state that the site required to be cleared of accumulated waste prior to sale. The terms of the trust made clear that the trustee would have discretionary power to apply residuary funds for the benefit of the pursuer, including the payment of third parties for services. That was irrespective of any legal liability to do so. If the trustee considered this to be for the sole benefit of the appellant, then it was reasonable to deduct this from his share to ensure all beneficiaries received an equal share.

[19] In relation to ground 4, the respondent required to make a payment to a bank under a bond of caution. The caution had been granted in respect of the appellant's personal debt to the bank, which had not been repaid. The cautionary obligation, and payment thereunder, was therefore for the benefit of the appellant. The preceding points applied. While this payment had been made prior to the termination of the liferent, that made no difference. The power existed from the point of death, as the appellant's share of the residue

vested *a morte testatoris*, subject to defeasance only in the event of his predeceasing the termination of the liferent.

[20] Ground 5 was a management fee paid to a farm manager during the term of the liferent. The sheriff correctly found that no election had been made to treat this fee as an income expense. The services had been required to manage the farm business. The fee had been unpaid and accumulated, and paid from the realised funds upon sale of the farm. It was a payment from capital of the estate.

[21] Ground 6 was resolved by agreement.

Decision

[22] The appellant's description of the respondent's approach was that it unwarrantedly overcomplicated matters. We agree with that characterisation. The Will has a simple structure and the trust it creates is not a complex one. In our view the sheriff, in allowing these deductions to be made only from the appellant's share of the trust estate, paid undue regard to the equitable considerations arising as a result of the payments made, and insufficient regard to the limits to the underlying powers which the respondent purported to exercise.

[23] The respondent could only act in accordance with the powers awarded in the trust created by the Will. The relevant provision stated:

> "(AND LASTLY) on the failure or termination for any cause whatever of the foregoing liferent provision in favour of my wife I direct my Trustees to hold, apply, pay and convey the said residue to or for behalf of such of the children of my marriage with the said Mrs. Helen Rae McInally as shall then survive and have attained or may thereafter attain the age of Eighteen years, equally among them…."

[24] We do not accept the respondent's characterisation of this as creating a discretionary trust. The only trust purpose is the conveyance of the estate to the beneficiaries. The reason for the creation of the trust is plain: it is to allow the deceased's wife to enjoy the liferent of the farm business and the farmhouse accommodation.

[25] The respondent's case rests on identifying a power to hold the funds and to apply them, on a discretionary basis, for the benefit of the beneficiaries, without limit of time. The wording grants no such power. The words "hold, apply, pay and convey" do not create a discretionary trust. There is no suspensive or other condition which would delay the respondent's obligation to convey the residue. Following death the only permitted period of delay of the obligation was the duration of the liferent. That ended in 2003. Counsel for the respondent appeared to suggest that it was for the beneficiaries to demand performance, and that distribution could be withheld until such an event. We find no support in the authorities for such an approach, and we do not agree with that proposition. It fails to recognise the clear duty on the respondent. Despite questioning during the appeal, no reason was given, or even suggested, to explain the many years' delay in the respondent carrying out his duties of distribution as executor-nominate and trustee. It is difficult to anticipate that any satisfactory answer could have been forthcoming. He seems simply to have failed to act. Failure to act in accordance with lawful duty carries inevitable personal risk.

[26] And so it was here. In our view, although equitable principles about offsetting payments were woven through the submission for the respondent, and the decision of the sheriff, this case has no requirement of them. Rather, the starting point is to identify what duties were imposed on the trustee. The question is whether the respondent was entitled to make deductions from the account of the estate, while refusing or failing to make payment

of the residue. The answer is to be found in the powers granted under the Will. These, as discussed, were extremely limited. Against that background, we turn to consider each of the heads of objection.

[27] Ground 1 relates to services and council tax payable in respect of the farm house, which were incurred during the appellant's residence there and for which he did not pay. Ground 2 relates to the utility bills similarly incurred. The sheriff found both of these to have been properly deducted from the account tendered by the respondent. In our view, they did not properly form expenditure which the respondent was entitled to attribute only to the appellant's share of estate funds.

[28] The principal reason is that the trust did not confer upon the respondent power to do so. The respondent did not have power to administer the estate as if it were a going concern. His sole duty and power was to distribute the estate following the termination of the liferent in 2003. He either elected not to do so, or neglected his duty. Under ordinary principles of accountability, he became responsible and accountable for his stewardship of the trust property. He required to preserve trust assets until such time as they were distributed. If he retained beneficial ownership, as trustee, of the farm house, he required to meet the expenses of so doing. Three points arise as a result.

[29] The first is that the expenses of maintaining the trust property required to be met. If these were rightfully incurred in the exercise of the trustee's duty, these would be payable from the trust estate. They accordingly were a direct liability on the trust and for respondent as trustee to pay, not the appellant.

[30] The second is that, if the appellant enjoyed an illicit benefit, or increased the burden on the trust property through his own use of the farm house, the respondent would no doubt be able to seek a remedy, whether under the law of restitution or otherwise. That

remedy, whatever it may be, was for the respondent to establish. It did not arise automatically. He could, had he chosen, demand payment from the appellant, and if necessary, raise an action. It might be that he had a duty to do so, although that was not part of counsel's submissions. However, he did not. These claims arose during the years 2003 to 2016, and it may be that the law of prescription poses a challenge. Were the respondent to manage successfully to prosecute such a claim, the trust estate would be enlarged. However, he has no entitlement to assume success and to make such a deduction. It remains a hypothetical claim. It is unknown whether the appellant might have a defence to such a claim. The sheriff referred to the "justice and fairness" of allowing the respondent to reclaim these amounts. This is not a claim in equity and those considerations are not engaged.

[31] The third point is that, even if there were an entitlement to make deductions against the appellant to reflect these expenses, the respondent led no evidence, and the sheriff made no findings, as to apportionment. Empty buildings still require services and utilities. The appellant was not a tenant. The respondent, not the appellant, was the legal occupier of the farm house and therefore, in the absence of agreement, liable for all bills. The trust and the appellant were liable jointly and severally for payment of the council tax. On the evidence, part of the electricity supply was required for milking the cows in furtherance of the farm business. The respondent required to show, upon challenge to this deduction, that the appellant was liable to make payment of a proportion of the expenses, and to identify what proportion. He failed on both, and has therefore failed to avert the appellant's challenge to those items. He has not shown that these invoices were incurred solely for the appellant's own benefit, or as a result of the appellant's actions.

[32] There may be a question whether the trust estate has a remedy against the respondent for incurring unwarranted expenditure while failing to distribute the estate property. That is not a question to be resolved in this litigation. It is enough that the appellant has demonstrated these proposed deductions from the sum ultimately due to him to be unjustified.

[33] Ground 3 related to the cost of site clearance following the appellant relinquishing possession of the farmhouse. The respondent purported to deduct this cost from the account. In our view, he was not entitled to do so, for two reasons. The first reason mirrors what is set out above. There was no contractual or other duty upon the appellant to perform site clearance upon departure. It is possible that the respondent could establish an equitable or legal remedy against the appellant. However, the respondent has not done so, and did not make any demand for payment, or legal claim. In the absence of such demand, the appellant had no duty to make payment, and the respondent has no entitlement to make deductions from the appellant's share of the estate. The respondent's claim may now be complicated by prescription, but the fact remains that no claim has been advanced. Whether the appellant might have a defence to such a claim is unknown.

[34] Secondly, there is no evidence that the trust estate incurred any loss or deduction. The farm house was sold. There is no evidence that the sale was dependent on, or the sale price influenced by, site clearance. The respondent has not demonstrated that the expenditure was necessary in furtherance of the trustee's duty. The appellant has demonstrated that this deduction is unjustified.

[35] Ground 4 is in similar vein. It is the cost to the estate of meeting a cautionary obligation. The estate was cautioner for debt incurred by the appellant. Payment was, however, demanded and made direct to the trust, in terms of a direct obligation incurred by

the deceased. It required to be paid, irrespective of any right of relief. Again, while a claim might be established against the appellant in respect of the underlying debt or right of relief, no such claim has been advanced. Whether or not the appellant would have a defence to such a claim is unknown. It may be that such a claim has prescribed. The appellant has demonstrated that this deduction is unjustified. Again, the sheriff referred to the making of the cautionary payment being of benefit to the pursuer. This is not a claim in equity and the question of benefit is not engaged.

[36] Grounds 5 and 6 are different in nature. Ground 6 has been resolved by agreement, and the sum to be deducted is agreed in the sum of £2,644.71.

[37] Ground 5 challenges the sheriff's findings that a cattle management fee of £53,339.81 was a capital expense of the estate. The sheriff took the view that the defender was entitled to treat the fee as capital expenditure notwithstanding that the evidence suggested the payments, made to the farm manager, were treated in the accounts as income expenses. The appellant submitted that the fee should have been charged against the income of the liferentrix.

[38] In our view, the sheriff's reasoning is sound. The relevant terms of the Will provide;

> "…and the decision of my Trustees as to what constitutes income or capital shall be final and binding on all concerned".

The sheriff noted that, whatever the accounting treatment, no deduction of fees from the income of the liferent had been made. There were insufficient funds. The sheriff accepted evidence that it was always the intent that the fees be paid from the trust estate. That decision was in accordance with the power given under the Will, and it cannot be disputed by any party. Accordingly, the deduction of £53,339.81 is a legitimate deduction from the estate.

Disposal

[39] We will recall the interlocutor of 8 August 2022, sustain the appellant's objections to the executry account lodged by the defender in respect of the estate of Archibald Milligan McInally senior, who died on 30 October 1983, and sustain the first, second, third, fifth, sixth and seventh pleas-in-law for the appellant but only to the following extent, namely: (i) that the sums expended by the estate on the utility bills for the duration of the appellant's occupation of High Cleughearn Farmhouse, namely £34,920.29; together with (ii) the sum paid by the trustees to Bank of Scotland under a bond of caution, namely £10,215.52; together with (iii) the site clearance costs of £10,850.72 incurred in respect of the said farmhouse, be included as outlays to be borne by the said estate before distribution of the residue to the beneficiaries. Further, we will sustain the respondent's plea-in-law only to the extent of (i) finding that the management fee of £53,339.81 paid by the trustees to Mr Frank McInally be treated as an outlay from the capital of the estate, and (ii) ordaining that the figure of £2,644.71 in respect of accrued debt remains in the account as a charge against the estate. We will thereafter, in respect that the final net value of the estate has not yet been ascertained, remit to the sheriff to proceed as accords.

[40] Parties moved for a hearing on expenses. They should attempt to agree expenses, failing which within 21 days of this decision, they should contact the clerk to arrange a hearing.