TC05904

Appeal number:TC/2011/01610

INCOME TAX – relief for gift of shares to charity – shares admitted to dealing on AIM – section 272 TCGA 1992 – whether quoted in The Stock Exchange Daily Official List – if so, whether in consequence of special circumstances quoted price not a proper measure of market value – section 273 TCGA 1992 – information assumed to be available to hypothetical prudent purchaser – market value of shares – appeal allowed in part

FIRST-TIER TRIBUNAL
TAX CHAMBER

JONATHAN NETLEY **Appellant**

- and -

THE COMMISSIONERS FOR HER MAJESTY'S REVENUE & CUSTOMS **Respondents**

TRIBUNAL: JUDGE JONATHAN CANNAN

Sitting in public at the Royal Courts of Justice, Strand, London WC2A 2LL on 20-23, 26-30 September 2016 and 4-5 October 2016

Mr Michael Firth of counsel instructed by Champion Accountants, Manchester for the Appellant

Mr Michael Gibbon QC, Mr James Henderson and Ms Emma Pearce of counsel instructed by HM Revenue & Customs Solicitor's Office and Legal Services for the Respondents

DECISION

Introduction

1. This is a lead case in accordance with Rule 18 of the Tribunal Procedure (First-tier)(Tax Chamber) Rules 2009. The common issue to be determined by the tribunal is as follows:

> "What was the market value of the shares in Frenkel Topping Group Plc which the Lead Appellant disposed of by way of gift to charity on 28 July 2004 as at that date for the purposes of section 587B ICTA 1988 (and on what basis and principles should the market value of such shares be determined)?"

2. The determination of that issue has involved eleven days of evidence and submissions. It requires me to find various facts relevant to valuation, resolve issues of law as to the basis of valuation and resolve issues between the two expert valuers. I shall approach the issues in that order in this decision. First I shall say something about the background.

3. Frenkel Topping Group Plc ("FTG") was the subject of a placing of shares and admission to the Alternative Investment Market ("AIM") on 28 July 2004. At that time the Appellant, Mr Jonathan Netley was one of a number of shareholders who held shares in FTG. On the same date he gifted shares to St Ann's Hospice, a well-known charity. He claimed that the value of his shares on that date was 48p, evidenced by the price at which shares were traded on AIM. More than 50% of the other shareholders in FTG gifted shares to various charities on the same date and more shareholders gifted shares to charity later in the 2004-05 tax year.

4. Mr Netley claimed relief on his gift of FTG shares to charity in his tax return for 2004-05 on the basis that the shares were valued at 48p. The amount of tax relief generated by Mr Netley's gift of shares was greater than the £10,000 cash he had invested to subscribe for the shares in or about June 2004. HMRC amended the return by a closure notice dated 30 September 2010 to reflect their view that the shares were valued at 8p. The effect of this was to reduce the amount of tax relief available from £15,866 to £2,624.

5. HMRC contend that the arrangements surrounding the admission of FTG shares to AIM were designed to allow subscribers to claim income tax relief greater than their cash investments. They contend that the price of 48p per share was in excess of their open market value for tax purposes. Mr Michael Gibbon QC who appeared on behalf of HMRC together with Mr James Henderson and Ms Emma Pearce invited me to find that the market value of the shares for tax purposes on 28 July 2004 was 6.6p per share. Mr Michael Firth who appeared on behalf of the Appellant invited me to find that the market value of the shares was 48p per share. It is not of course a binary choice and subject to issues of law I may find in the light of all the evidence that the value of the shares is anywhere within that range, or indeed outside that range.

6. The evidence before me was wide-ranging. I heard evidence from individuals concerned in the placing of the FTG shares, including corporate financiers and a

financial adviser; evidence from investors including Mr Netley; evidence as to enquiries carried out by AIM's regulation team; expert evidence in relation to the operation of AIM; and expert evidence in relation to the valuation of the shares. I have distilled all that evidence and the equally wide-ranging submissions of counsel into this decision. I could not hope to detail every aspect of the evidence or the submissions but I have endeavoured to set them out in such a way that a reader of this decision will understand the basis on which I have reached a decision. I was greatly assisted in that task by the written and oral closing submissions of counsel.

Statutory Provisions and an Outline of the Issues arising out of those Provisions

7. In 2004-05 certain shares which were qualifying investments were eligible for income tax relief when gifted to charity pursuant to section 587B Income and Corporation Taxes Act 1988 ("ICTA"). Relief was given by reference to the market value of the qualifying investment as follows:

> " (1) Subsections (2) and (3) below apply where, otherwise than by way of a bargain made at arm's length, an individual … disposes of the whole of the beneficial interest in a qualifying investment to a charity.
>
> (2) On a claim made in that behalf to an officer of the Board—
>
> (*a*) the relevant amount shall be allowed—
>
> (i) in the case of a disposal by an individual, as a deduction in calculating his total income for the purposes of income tax for the year of assessment in which the disposal is made;
>
> ...
>
> (4) Subject to subsections (5) to (7) below, the relevant amount is an amount equal to—
>
> (*a*) where the disposal is a gift, the value of the net benefit to the charity at, or immediately after, the time when the disposal is made (whichever time gives the lower value);
>
> …
>
> (8A) The value of the net benefit to the charity is—
>
> *(a)* the market value of the qualifying investment,
>
> …
>
> (9) In this section—
>
> 'qualifying investment' means any of the following—
>
> (*a*) shares or securities which are **listed or dealt in on a recognised stock exchange**;
>
> …

(10) Subject to subsection (11) below, the market value of any qualifying investment shall be determined for the purposes of this section as for the purposes of the 1992 Act."

(Emphasis added)

8. It was common ground in this appeal that the shares in FTG were qualifying investments. Section 587B(10) provided that the market value of any qualifying investment was to be determined as it would be under the Taxation of Chargeable Gains Act 1992 ("TCGA"). The relevant provisions for present purposes are contained in sections 272, 273 TCGA as follows:

> " 272(1) In this Act 'market value' in relation to any assets means the price which those assets might reasonably be expected to fetch on the open market.
>
> (2) In estimating the market value of any assets no reduction shall be made in the estimate on account of the estimate being made on the assumption that the whole of the assets is to be placed on the market at one and the same time.
>
> (3) Subject to subsection (4) below, the market value of shares or securities quoted in The Stock Exchange Daily Official List shall, except where in consequence of special circumstances prices quoted in that List are by themselves not a proper measure of market value, be as follows—
>
> > (a) the lower of the 2 prices shown in the quotations for the shares or securities in The Stock Exchange Daily Official List on the relevant date plus one-quarter of the difference between the 2 figures, or
> >
> > (b) halfway between the highest and lowest prices at which bargains, other than bargains done at special prices, were recorded in the shares or securities for the relevant date,
>
> choosing the amount under paragraph (a), if less than that under paragraph (b), or if no such bargains were recorded for the relevant date, and choosing the amount under paragraph (b) if less than that under paragraph (a).
>
> (4) Subsection (3) shall not apply to shares or securities for which The Stock Exchange provides a more active market elsewhere than on the London trading floor; and, if the London trading floor is closed on the relevant date, the market value shall be ascertained by reference to the latest previous date or earliest subsequent date on which it is open, whichever affords the lower market value.
>
> 273(1) The provisions of subsection (3) below shall have effect in any case where, in relation to an asset to which this section applies, there falls to be determined by virtue of section 272(1) the price which the asset might reasonably be expected to fetch on a sale in the open market.

(2) The assets to which this section applies are shares and securities which are not quoted on a recognised stock exchange at the time as at which their market value for the purposes of tax on chargeable gains falls to be determined.

(3) For the purposes of a determination falling within subsection (1) above, it shall be assumed that, in the open market which is postulated for the purposes of that determination, there is available to any prospective purchaser of the asset in question all the information which a prudent prospective purchaser of the asset might reasonably require if he were proposing to purchase it from a willing vendor by private treaty and at arm's length."

9. A number of issues arise out of the application of these provisions to the valuation of the FTG shares. In outline, and with considerable simplification at this stage those issues are as follows:

(1) Were the FTG shares "quoted in The Stock Exchange Daily Official List" so as to engage section 272(3)?

(2) If so, was the price quoted such that "in consequence of special circumstances" it was not in itself a proper measure of the market value of the FTG shares? The special circumstances relied on by HMRC include what are said to have been tax avoidance motives surrounding the placing of the shares and subsequent gifts to charity made by Mr Netley and other shareholders.

(3) If section 272(3) is not engaged and the FTG shares are to be valued by reference to section 272(1) alone:

(a) What information is deemed to be available to any prospective purchaser of the FTG shares? In particular, were the shares "quoted on a recognised stock exchange" with the effect that section 273 has no application.

(b) What was the value of the shares based on the information available to the prudent purchaser in the light of the evidence of the two expert valuers?

Findings of Fact

10. It is convenient to set out my findings of fact and in so far as necessary my consideration of the evidence on which I have reached those findings under the following headings:

(1) The Flotation of FTG

(2) Background - Zeus Partners, Mr Lundy and WH Ireland

(3) The Frenkel Topping Business

(4) Mr Netley - Purchase and Gifting of Shares

(5) Dr McArthur - Purchase and Gifting of Shares

(6) The Alternative Investment Market and Investigations into Possible Abusive Practices

(7) The Valuation Process

(8) Lock-ins

(9) The Significance of Gift Relief

(1) The Flotation of FTG

11. On 8 April 2003 a company was incorporated with the name WC (Co (4)) Limited. In the period prior to flotation I shall generally use the term “the Company” to describe this company. For the period from the date of flotation onwards I shall use the term “FTG”.

12. On 8 July 2003 the Company changed its name to Forward Link Limited. Its authorised share capital was £1000 divided into 1000 ordinary shares of £1 each of which one subscriber share was in issue, fully paid. On 27 January 2004 the subscriber share was transferred to Mr Richard Hughes of Zeus Partners (“Zeus”), a corporate finance business which was instrumental in the ultimate flotation of the FTG shares.

13. On 27 January 2004 the Company subdivided each £1 share into 20,000 shares of 0.005p each. On the same day it also issued 50,000 redeemable shares of £1 each which were one quarter paid, thereby raising £12,500. The redeemable shares were issued to Zeus and were to be made fully paid immediately following the close of the Offer for Subscription referred to below, at which stage they would be immediately redeemed by the Company out of the proceeds of the Offer for Subscription.

14. The Company re-registered as a public limited company with the name Forward Link Plc on 29 January 2004.

15. On 17 February 2004, it was resolved that the authorised share capital of the company be increased to £350,000, being 2,000,000,000 ordinary shares of 0.005p each. On the same day, the company issued 13,980,000 ordinary shares of 0.005p each at par raising £699 gross.

16. As at 17 February 2004 the Company’s balance sheet therefore showed cash of £13,200 and a debtor of £37,500 in respect of the outstanding subscription monies for the redeemable shares. Of the 14,000,000 issued shares in the Company, 12,884,878 or approximately 92% were held by individuals associated with Zeus as follows:

(1) Mr Richard Hughes - 5,578,683 for which he had paid approximately £278.93. Mr Hughes was also a director of the Company.

(2) Mr Ian Currie - 6,066,488 for which he had paid approximately £303.32.

(3) Mr Keith Salisbury - 1,239,707 for which he had paid approximately £61.98.

17. The remainder of the 14,000,000 shares were owned as follows:

(1) 731,707 were owned by Mr Stephen Lundy of Berkeley Morgan, for which he had paid approximately £36.58. Berkeley Morgan acted as financial advisers to some of the individual investors who later participated in the flotation of the Company as FTG, including Mr Netley.

(2) 383,415 were owned by WH Ireland plc ("WHI") a firm of stockbrokers for which they had paid approximately £19.17. WHI were appointed to act as financial adviser to the company and as Nominated Adviser ("Nomad") which was a requirement of AIM rules in relation to the flotation of the company as FTG.

18. A Prospectus was published on 17 February 2004 ("the February Prospectus") pursuant to which the company offered 23,000,000 shares ("the Subscription Shares") for subscription at 5p each ("the Offer for Subscription"). The gross proceeds of a full subscription would therefore be £1,150,000. The February Prospectus stated that the Company had been formed to be a cash shell to attract companies wishing to seek admission to trading on AIM. The February Prospectus also contained two conditions which are significant in this appeal. The first committed shareholders subscribing for Subscription Shares to make a subsequent cash subscription for new ordinary shares upon the admission of the shares of the company to trading on AIM ("Admission"). The subsequent cash subscription was fixed at 23% of the amount paid for the Subscription Shares. The second condition was that the subscribing shareholders would not transfer legal or beneficial ownership of any Subscription Shares during the period from the date of issue until the second anniversary of Admission except in certain limited circumstances ("the Lock-in"). An exception to the Lock-in was that the Company would consent to a disposal to a registered UK charity if the charity itself agreed to be subject to the Lock-in.

19. The Offer for Subscription was extended beyond the date originally set in the February Prospectus, and finally closed on 2 June 2004. Mr Netley applied under the Offer for Subscription for 200,000 ordinary shares in the company for a subscription price of £10,000. On 3 June 2004 the company issued and allotted the full 23,000,000 Subscription Shares including the shares Mr Netley had applied for.

20. On 3 June 2004 the Company also altered its share capital by means of a bonus issue and a consolidation of share capital. As a result of the bonus issue and consolidation Mr Netley's 200,000 Subscription Shares became 82,000 Subscription Shares. The effect on the company's share capital as a whole was that 9,430,000 Subscription Shares were issued pursuant to the Offer for Subscription.

21. Following closure of the Offer for Subscription, the redeemable shares in the Company were made fully paid up, and then immediately redeemed and cancelled.

22. At that stage the interests in the Company were as follows:

Shareholder	Subscription Shares	% of Company's Share Capital
Richard Hughes	2,287,260	15.08
Ian Currie	2,487,260	16.40
Keith Salisbury	508,280	3.35
Stephen Lundy	300,000	1.98
WHI	157,200	1.04
Retail Investors	9,430,000	62.16
Total:	15,170,000	100

23. On 1 July 2004 James Brearley & Sons Ltd ("JBS") agreed to subscribe for 3,428,572 ordinary shares in the Company ("the JBS Shares") to be issued and allotted by the Company. The total subscription price before expenses was £600,000, equivalent to 17.5p per share. I set out the relationship between Frenkel Topping and JBS in more detail below. The subscription by JBS was conditional only on the Company acquiring FTG, it was not conditional on admission to AIM. The JBS Shares were issued on 26 July 2004.

24. By an agreement dated 8 July 2004 ("the Acquisition Agreement"), the Company agreed to acquire from Richard Fraser, Stephen Ashcroft and Nicholas Leech ("the Vendors") 66.2% of the shares in Frenkel Topping Limited ("FTL") and Frenkel Topping Structured Settlements Limited ("FTSSL"). The Company also acquired the benefit and burden of a share sale and call option agreement in favour of Mr Fraser and Mr Ashcroft to purchase the remainder of the shares from John and Naomi Frenkel and Arrow Nominees (for shorthand "Mr Frenkel"). The consideration for the acquisition was to be 26,450,000 ordinary shares in the Company ("the Consideration Shares"). This represented 58% of the Company's share capital. The Acquisition Agreement identified the consideration for the share sale and the assignment of the option as £2,248,250 which would be equivalent to 8.5p per share in the company.

25. The Acquisition Agreement was not conditional on the shares being admitted to AIM. It was completed on 28 July 2004 and I shall refer to this transaction as "the Acquisition".

26. The share sale and option agreement acquired by the Company required it to purchase 16.6% of the remaining shares in FTL and FTSSL for £600,000 effectively on completion of the Acquisition. The Company also had the benefit of a call option over the remaining 17.2% exercisable in the period June 2004 to July 2006 at a price between £628,646 and £712,500 depending on when the option was exercised.

27. The Acquisition whereby the Company agreed to purchase the shares in FTL and FTSSL was conditional on obtaining an independent valuation report pursuant to

section 103(1) Companies Act 1985. The consideration for the purchase of 66.2% of FTL and FTSSL shares was expressed to be £2,248,250 to be satisfied by the allotment of shares in the Company. Baker Tilly issued a report for those purposes expressing their opinion that the value of the total consideration was not less than £2,645,000, that being the total amount treated as paid up on the shares allotted. The valuation they carried out was on 7 July 2004 and was said to be on the basis of a multiple of projected earnings but no details of the valuation were referred to in evidence.

28. On 9 July 2004 the company published a further prospectus ("the July Prospectus"). The July Prospectus concerned the Acquisition, the placing of shares and Admission of the Company's shares to trading on AIM. The Company was seeking to raise £264,500 by a placing of 551,042 shares ("the Placing Shares") at 48p per share. The Placing Shares were to be issued to the retail investors pursuant to their commitment to subscribe for further shares at a price equivalent to 23% of the amount paid for their Subscription Shares. In effect the retail investors were bound to accept the placing price of 48p. In the case of Mr Netley he committed to subscribe for 4,792 Placing Shares at a cost of £2,300.16.

29. The Company had appointed Baker Tilly to carry out accounting due diligence and to produce a "Short Form Report" for inclusion in the July Prospectus, a confidential "Long Form Report" and a confidential Working Capital Report.

30. The July Prospectus set out financial information for FTL and FTSSL which when combined showed the following:

Year End:	**31/12/01** **£**	**31/12/02** **£**	**31/12/03** **£**
Turnover	2,729,901	2,729,448	3,168,960
Operating Profit/Loss	(4,276)	(332,529)	407,333
Profit/Loss before tax	(88,817)	(420,961)	326,905
Profit/Loss after tax	(89,278)	(441,869)	302,496

31. At the date of the July Prospectus the actual and prospective position of the Company's share capital was as follows:

(1) There were 15,170,000 ordinary shares in the Company in issue.

(2) The intention was that the 3,428,572 JBS Shares would be issued to JBS.

(3) The intention was that the 26,450,000 Consideration Shares would be issued as consideration for the acquisition of 66.2% of the share capital of FTL and FTSSL.

(4) The intention was that the 551,042 Placing Shares would be issued.

(5) The total prospective number of ordinary shares in the Company in issue following completion of the Acquisition and the Placing would be 45,599,614 assuming full take-up. The July Prospectus recorded that the Placing Shares would represent 1.21% of that figure.

32. Under the heading "Key Statistics" on page 3 of the July Prospectus it was recorded that the gross proceeds of the Placing assuming full subscription would be £264,500. Under the heading "Key Information" on page 7 of the July Prospectus it was stated that the Company "*is seeking to raise £264,500 before expenses by way of a placing of up to 551,042 Placing Shares to fund the costs of the Proposals*". The reference to costs of the Proposals was to the costs of the flotation.

33. The amount being raised from the Placing Shares was intended to pay the fees associated with the placing and admission to AIM. It represented 23% which the investors subscribing for the Subscription Shares had agreed to invest by way of subsequent subscription. At the time of the initial subscription the number of Placing Shares investors would get and the price of those shares was not known. Those matters would depend on the valuation of the business acquired and any changes to the share capital of the company in the meantime.

34. Baker Tilly were instructed to produce accountants' reports on the Company, on FTL and on FTSSL. Those reports dated 9 July 2004 were included in the July Prospectus. Baker Tilly also produced a Working Capital Report for the directors of the Company which was not included in the July Prospectus.

35. The timetable in the July Prospectus anticipated the admission date being 28 July 2004.

36. On 28 July 2004 the transactions went ahead as intended and the ordinary shares in FTG were admitted to trading on AIM. There was no outside marketing to fix the float price. I was provided with a copy of the London Stock Exchange Daily Official List for 28 July 2004. Pages 42 to 108 show entries in relation to "Listed Companies (excluding Investment Trusts)" and pages 129 to 140 show entries in relation to AIM. On page 133 there is an entry for the Company showing a "quotation" of 48.25 – 48.75p. Under the heading "Business done" there is the following narrative:

"[47-49.63 12] 08:49.63 (1) 7(5) 09:49.63(1) 12:47.25(5)"

37. I was told and it was not disputed that this narrative is shorthand for 12,000 shares being traded on the day. Two lots of 1,000 shares were traded at 49.63p, 5,000 shares were traded at 47p and 5,000 shares were traded at 47.25p. Those figures were rounded. In fact there were two trades of 1,000 shares and two trades of 4,972 shares meaning that in total 11,584 shares were traded on the opening day. Winterflood Securities ("Winterflood") purchased at least one lot of 4,972 shares on the opening day. Winterflood is a market maker and was known as making a market in all shares dealt on AIM. As market maker it acted as a middleman between two brokers and it would have needed to purchase a small number of shares on the opening day of trading for the purpose of making a market. Winterflood sold two lots of 1,000 shares

on the same date. Mr Hughes' mother, on his recommendation, had purchased one lot of 1,000 shares.

38. On the date of admission to AIM, the shares in FTG were held as follows:

Shareholder	**Shares**	**% of Company's Share Capital**
The Vendors	26,450,000	58.00
JBS Shares	3,428,572	7.52
Richard Hughes	2,287,260	5.02
Ian Currie	2,287,260	5.02
Keith Salisbury	508,280	1.11
David Southworth	200,000	0.44
Stephen Lundy	300,000	0.66
WHI	157,200	0.34
Retail Investors	9,981,042	21.89
Total:	45,599,614	100

39. Mr Weaver (HMRC's expert valuer) records in his evidence that a maximum of 41,620,000 shares were subject to lock-in arrangements as at 9 July 2004. This referred to the 15,170,000 shares in issue as at 3 June 2004 and the 26,450,000 shares issued as Consideration Shares to the Vendors. These figures were not disputed. They included shares held by persons other than the retail investors who were not formally locked-in but who would not be expected to sell shares in the short term following the flotation. In addition the 3,428,572 JBS Shares issued on 26 July 2004 were also subject to a lock-in. In reality the only shares which might be considered freely tradable on flotation were the Placing Shares which accounted for 1.2% of the issued share capital of FTG.

40. Everybody accepted that on the opening day of trading on 28 July 2004 there was a very thin market in FTG shares. I am satisfied that one of the reasons for that and probably the main reason is that the only shares held by retail investors which could be traded on market were the Placing Shares. The next transaction on market after the opening day of trading was 7,187 shares traded on 26 October 2004 at 45.5p.

Background – Zeus Partners, Mr Lundy and WH Ireland

41. Zeus was established by Mr Ian Currie and Mr Richard Hughes in Manchester in April 2002. Mr Currie studied economics at Manchester University before training with KPMG in Leeds and qualifying as a Chartered Accountant in 1986. He left KPMG to become a stockbroker, initially at Brewin Dolphin and subsequently Peel Hunt and Apax. He was involved in floating many companies. Richard Hughes also

worked at Apax and had many years' experience in flotations, capital raising, mergers and acquisitions. Apax had a reputation in Manchester for successfully establishing cash shell companies with a view to the purchase and flotation of established businesses. Apax later changed its name to Altium at about the same time that Mr Currie and Mr Hughes left to set up Zeus.

42. Zeus acted as a corporate finance house. Mr Currie and Mr Hughes also controlled Zeus Capital Limited which was a financial adviser and which was also approved as a Nomad in relation to the admission of company shares to dealing on AIM. Zeus was established with the intention of acquiring interests in trading businesses with a view to an initial public offering ("IPO"). The intention was that admission to the main market or to AIM, a stronger board of directors and additional cash resources would generate significant additional shareholder value.

43. Zeus would typically set up a cash shell and raise founders' equity shortly before the IPO, known as pre-IPO fundraising. This was attractive to retail investors as they had the opportunity to participate in due course in an expected uplift in value if an attractive business was identified and purchased. There were substantial risks for investors at the point of investment. They would not know what, if any, acquisition would take place or when it would take place. If no acquisition took place the pre-IPO investors could end up losing their investment. The equity funding at this stage was intended to provide additional working capital for a target business. Zeus had to be satisfied that the target business would be able to deliver enhanced shareholder value. Zeus was looking for businesses where they would be confident of realising a significant premium on flotation. The February Prospectus records that in identifying potential targets the directors of the Company focus on small businesses which they believe have the capability to grow rapidly. The July Prospectus records that the directors including Mr Hughes considered FTG to be such a company. Mr Hughes and Mr Currie had a track record in this type of cash shell transaction and in most cases shares on admission traded at a significant premium to the pre-IPO subscription price paid by investors.

44. Zeus had a continuing relationship with WHI and in a number of transactions in or about 2004 Zeus used WHI as the Nomad for the purpose of seeking admission to AIM. Obviously an important aspect of the admission process was setting the price at which shares would be placed on admission to AIM. Mr Hughes' evidence was that this was a matter for negotiation between Zeus and the Nomad and that such negotiations could get quite heated. His evidence gave the impression of a robust almost adversarial process. In relation to the Company Mr Hughes took the lead on behalf of Zeus. I set out below how the price came to be set at 48p on the admission of the FTG shares to AIM.

45. Admission to AIM often involves some shareholders being "locked in" to their shares by way of restrictions on disposal of those shares for a period of time. I deal with lock-ins in more detail below, both generally and specifically in relation to FTG.

46. Mr Lundy was a regional director of Berkeley Morgan from 1993 to 2012. He met with Mr Hughes and Mr Currie in late 2002 whilst they were in the course of

setting up Zeus and it was agreed that Mr Lundy would introduce clients to Zeus' cash shell companies. The agreement was that for clients introduced to cash shells by Mr Lundy he would receive a commission of 3% of funds raised. In most cash shells Mr Lundy was also offered shares in the company for a nominal consideration and that was the case in relation to the Company.

47. Zeus also had other introducers and there were other businesses in the North West doing similar form transactions. Mr Lundy decided not to introduce his clients to those other businesses because he had doubts about the commerciality of what they were doing, although he was not asked in his evidence to explain the nature of those doubts.

48. The attraction for Mr Lundy's clients was to get involved at the early stage of a cash shell company which it was intended would be admitted to AIM by persons with a good track record of making money for investors. The Company was one of those cash shells and followed several earlier successful flotations by Zeus. Two of the directors of FTL and FTSSL were introduced to Mr Lundy by Betesh Fox Solicitors. The directors were seeking advice as to funding a management buy-out from Mr Frenkel and they were already some way down the line of negotiating a buy-out. Mr Lundy introduced them to Mr Hughes of Zeus. Zeus saw potential to float FTG and to introduce new specialist financial products to the company. Mr Lundy had no involvement in setting the price at which shares were issued and he had no involvement in the issue of the JBS Shares.

49. The February Prospectus stated that a number of potential targets had been identified. At that time FTL and FTSSL was Zeus' preferred transaction for the cash shell although there was no mention of either company or Frenkel Topping in the February Prospectus. Mr Lundy advised some 25-30 investors who subscribed for shares in the Company following the February Prospectus.

50. Mr Lundy saw it as part of his duty as a financial adviser to advise his clients as to the possibility of gifting shares to charity, and the associated tax implications. Similarly he advised clients as to the capital gains tax implications of disposing of AIM shares and the inheritance tax implications associated with AIM shares. Some of Mr Lundy's clients who invested in cash shells would gift shares on flotation, others would gift shares subsequently and others would retain their shares. It made no difference to Berkeley Morgan how clients dealt with their shares. He maintained that the transactions were not structured simply to generate gift relief on an inflated flotation price.

51. WHI acted as Nomad on the flotation of most of Zeus' cash shell companies. In relation to FTG they were appointed to act as financial adviser and Nomad by an agreement between the Company and WHI dated 17 February 2004. WHI were subsequently appointed as the Company's broker. By way of remuneration they received various fees and commissions, including success fees and shares in the Company.

(3) The Frenkel Topping Business

52. The Frenkel Topping business commenced in 1980 when John Frenkel and Michael Topping established a chartered accountancy practice in Manchester. The practice specialised in forensic accounting and litigation support, mostly involving personal injury cases. It also introduced financial services to its clients, advising how best to invest personal injury awards.

53. In 1989 FTL was set up to deal with the financial services work. In the same year FTL became the first business in the UK to obtain judicial approval for the establishment of a structured settlement. A structured settlement is an alternative to what was then a conventional award of lump sum damages. All or part of the damages are awarded as a regular tax free payment to the claimant, usually guaranteed to last for the remainder of the claimant's life. Work involving structured settlements grew and in 1996 FTSSL was established to separate the structured settlement business from the general financial services business. The work of FTSSL was referred by solicitors and insurance companies involved in the personal injury field.

54. In 1999 FTL was appointed as an investment adviser by the Court of Protection on a number of cases instead of the usual court approved brokers. From an investment adviser's perspective such funds are regarded as "sticky" in the sense that once obtained they are unlikely to be moved from the adviser's management which would require a Court order. Unlike other areas of investment management therefore, once the initial "sale" has been made the fee income from managing the investment is very likely to continue indefinitely. Funds under management and fee income are likely to increase year on year because current year sales will generate fees on top of continuing fee income.

55. Throughout the 1990's personal injury awards increased in both size and number. An assessment carried out by the Department of Constitutional Affairs estimated that £2.26 billion of personal injury compensation by way of new awards had been paid in the year ended April 2002. Further, in October 2003 CPR Practice Direction 40 introduced the requirement for a structured settlement report to be produced for all claims where future losses were in excess of £500,000. In early 2004 it was expected that this would lead to increased levels of work for FTSSL. At the time FTSSL was regarded as one of the market leaders in the UK in the implementation of structured settlements.

56. The management team at Frenkel Topping included Richard Fraser who was the managing director, Stephen Ashcroft who was responsible for product development and Nick Leech who was the business manager. John Frenkel who was one of the founders of the business was no longer actively involved in the business. In early 2004 shares in FTL and FTSSL were held as follows:

Shareholder	**Shares Held %**
John and Naomi Frenkel and	33.80

Arrow Nominees	
Richard Fraser	30.83
Stephen Ashcroft	32.83
Nick Leech	2.50

57. The holdings of Richard Fraser, Stephen Ashcroft and Nick Leech totalled 66.2% and were the subject of the Acquisition. They also had a contract to purchase 16.6% of the remaining shares and an option to purchase the balance of 17.2%.

58. The management team at FTL and FTSSL were introduced to Zeus by Mr Lundy and there were a number of meetings between Mr Hughes and Mr Fraser. Mr Hughes thought that the business offered a good investment opportunity which could realise value through admission to AIM. In particular he was attracted by the stickiness of the funds under management and the prospect of growing the business, including what he saw as an opportunity to sell loan notes and equity instruments in PFI companies to the funds under management.

59. Mr Hughes negotiated on behalf of the Company to purchase the Vendor's interests in FTL and FTSSL. During the course of this work it became apparent that there was a working capital shortfall. Mr Hughes helped to negotiate additional funding from JBS with whom the Frenkel Topping businesses already had a business relationship. The funding provided by JBS was not conditional on the admission of the Company's shares to AIM.

60. JBS had been managing funds on behalf of FTL since April 2003. In February 2004 there were discussions with JBS about JBS investing in FTL and also making a loan to the company. On or about 30 March 2004 FTL agreed to appoint JBS exclusively to manage funds for a further period of 2 years. The income arising was to be split between FTL and JBS in an agreed way. Further, JBS agreed to advance £500,000 to FTL on account of FTL's share of that income. The July Prospectus stated that FTL had set up a discretionary fund management service with JBS. As at 31 May 2004 there were funds of approximately £102m being managed using that service.

61. On 1 July 2004 JBS agreed to subscribe for 3,428,572 shares in the Company for £600,000. The consideration was satisfied by an assignment to the Company of the debt of £500,000 owed by FTL to JBS. JBS paid the remaining £100,000 by 4 July 2004. The result was that the new funds raised for the business by this subscription amounted to £100,000. The balance of £500,000 was effectively a debt/equity swap.

62. I have set out above financial information taken from the July Prospectus for the combined businesses in the 3 years to 31 December 2003. The financial results of the Frenkel Topping business for the 7 month period from 1 January 2004 to 28 July 2004 were not in the public domain at the time of the flotation, but they were as follows:

	FTL £	FTSSL £
Turnover	913,073	203,642
Operating Profit	85,770	(278,209)
Profit/(Loss) before taxation	69,025	(300,370)
Taxation	-	-
Profit/(Loss) after taxation	69,025	(300,370)

(4) Mr Netley **-** *Purchase and Gifting of Shares*

63. Mr Netley was at all material times a partner in Tushingham Moore, a firm of chartered surveyors based in Manchester. He was introduced to Mr Lundy by Mr Moore who was a senior partner in the firm. Three of the partners had invested in a previous cash shell through Mr Lundy and Mr Moore suggested that all six partners be given the opportunity to invest in another cash shell. Following that suggestion in or about May 2004 all six partners were given the opportunity to invest in the Company.

64. Initially Mr Moore presented the key features of the opportunity to the other five partners orally, including Mr Netley. It seemed to me from Mr Netley's evidence that in relation to the soundness of the investment he was simply following Mr Moore's lead. He did not really give much consideration to the detail of the investment. Mr Netley described his understanding of the key features of the investment as follows:

> "… so it was a shell company, there is an opportunity to invest in that company, but there was also an opportunity to gift the shares."

65. Mr Lundy had a meeting with all six partners in order to complete identity checks and to get their signatures on relevant documentation including an application form to subscribe for shares. Documentation including the February Prospectus would have been sent to Mr Moore beforehand and was available to the other partners. There was no presentation as such by Mr Lundy, but the partners had an opportunity at that meeting to ask any questions they might have. The February Prospectus included a commitment to subscribe a further 23% of the amount paid for the Subscription Shares. The application form included a commitment to subscribe for the Placing Shares and an undertaking not to dispose of the Subscription Shares as follows:

> " **Commitment to Further Subscription**
>
> It is a term of the Offer for Subscription that a New Shareholder agrees to make or procure the making of a further subscription for new Ordinary Shares upon Admission at the price at which any new Ordinary Shares are placed at that time.
>
> …
>
> **Lock-in**

> It is a term of the Offer for Subscription that a New Shareholder undertakes to the Company that … the New Shareholder will not directly or indirectly transfer, sell or otherwise dispose of the legal or beneficial ownership of any of the Subscription Shares or any shares which may accrue to the New Shareholder as a result of the New Shareholder's holding of such shares … until the second anniversary of Admission EXCEPT:
>
> 1. with the prior written consent of the Company (such consent to be given or withheld in its sole discretion), the Company will consent to a disposal to a registered United Kingdom charity provided that:
>
> (i) [provision for 3 days notice]; and
>
> (ii) such charity shall agree in a form acceptable to the Company not to dispose of such shares during the remaining period of the Lock-in as if such charity was the original New Shareholder."

66. Mr Netley described his understanding of the risks involved in the investment as follows:

> "… it was presented as an opportunity to invest but the flip side of that is that you could have gifted the shares and got tax relief from that, so, yes, it was speculative but it was relatively risk-free in the sense that you had an out if you did not want to progress with it."

67. At this stage Mr Lundy knew that FTL and FTSSL was the intended target and if asked he would have divulged that information to Mr Netley. It seems that he was not asked by Mr Netley because Mr Netley was not aware of the intended target at the date of his investment in the Subscription Shares.

68. All six partners discussed the investment and decided together that they would gift their Subscription Shares to charity on the date of flotation, although not necessarily to the same charity. Mr Netley chose St Ann's Hospice having discussed the gift with his sister.

69. Mr Lundy and Mr Hughes referred in evidence to the commitment to subscribe for the Placing Shares as being unenforceable. In practice they considered that there would be little Zeus could do about it if an investor failed to subscribe for the Placing Shares. I am not sure why they considered it to be unenforceable but nothing really turns on that. Investors were clearly making a commitment to subscribe for the Placing Shares on Admission to the extent of 23% of their initial investment.

70. The documentation available to Mr Netley did not refer to the tax consequences of gifting shares to charity. Mr Lundy stated that he had a duty to investors as a financial adviser to explain the potential tax consequences of their actions. He had no specific recollection but his evidence was to the effect that he would have explained that tax relief was available on a gift to charity. Mr Lundy also told Mr Netley that Berkeley Morgan could handle the formalities of any gift.

71. Mr Netley along with his partners all invested in the Company. Mr Netley invested £10,000 for 200,000 Subscription Shares. Following the bonus issue and consolidation these became 82,000 shares. All six partners invested in the Company and all six partners gifted their Subscription Shares on the date of Admission.

72. In administrative terms the gift by Mr Netley of his Subscription Shares proceeded as follows. At some stage Mr Netley indicated to Berkeley Morgan that he wished to gift his shares to St Ann's Hospice. On 17 June 2004 Berkeley Morgan wrote to Mr Netley as follows:

> " Further to your application to purchase shares in Forward Link plc. I understand that you are considering gifting your shares to the St Ann's Hospice. If you would like to go ahead please sign the enclosed Consent Request letter and Stock Transfer form and return them to me as soon as possible. Please do not date either of the forms."

73. The draft consent request was also dated 17 June 2004 and was in the form of a letter from Mr Netley to the Company. At some stage, before he had any information as to the intended acquisition by the Company, Mr Netley signed the consent request and it was sent to the Company asking for consent pursuant to the Lock-in arrangements to transfer the entirety of his 82,000 Subscription Shares to a charity. Mr Netley's letter was in a standard form.

74. The share transfer form included the details of St Ann's Hospice which Berkeley Morgan retained on file from previous cash shell transactions where investors had gifted to the same charity. Berkeley Morgan would have contacted St Ann's Hospice to ensure that they would accept a gift of the shares. Mr Lundy's experience was that some charities were reluctant to accept such gifts of shares.

75. The intention was that Berkeley Morgan would hold the signed consent request letter and the stock transfer forms to await Mr Netley's further instructions. At this stage Mr Netley might have known that the intended target was FTL and FTSSL but the final form of the transaction would not have been known. The letter from Berkeley Morgan clearly states "if you would like to go ahead", in other words Mr Netley was being asked to confirm that he <u>did</u> wish to gift his Subscription Shares. However the consent letter which he signed stated "*I am considering disposing by way of gift 82,000 Ordinary 0.5p shares in Forward Link Plc …*".

76. It was assumed by Mr Lundy and Mr Netley that the directors of the Company would consent to a gift to charity if the charity agreed to the Lock-in. Mr Currie's evidence was that if a charity subject to a lock-in requested consent to sell shares in a company then consent would be given. He said that he was not aware of a charity ever being refused such consent. I accept that evidence.

77. On 30 June 2004 the Company wrote to Mr Netley consenting to the transfer of his shares to St Ann's Hospice subject to the Hospice being bound by the Lock-in agreement. The letter was in standard form. It was signed by Mr Hughes and also had provision for signature by the charity.

78. On or about 9 July 2004 Mr Netley would have received a copy of the July Prospectus. The prospectus contained information about taxation including capital gains tax on disposals, inheritance tax, income tax and stamp duty. It did not contain any information about relief for gifts of shares to charity. I do not consider that the omission was significant.

79. In a standard form letter dated 12 July 2004 Catherine Glendinning of Berkeley Morgan wrote to a Mr McCarthy of St Ann's Hospice stating: "*Our clients would like to gift some of their shareholding in Forward Link Plc to the St Anne's Hospice (sic). The shares are subject to a two-year lock in period, which means you would not be able to sell them within a two year period. Before the shares are gifted to you the directors of the company involved, Forward Link Plc, require written confirmation from yourselves that you agree not to dispose of the shares within the lock in period.*" The letter enclosed a consent from the Company dated 30 June 2004 for signature by the charity and further stated: "*It is essential that this is returned urgently*".

80. At that point in time the charity would not have known the intended target business and Mr Lundy said that charities would not generally ask.

81. On 28 July 2004 Mr Lundy said that one of his assistants would have telephoned Mr Netley and other investors gifting on the same date to confirm his instructions for the gift to charity. On the same date Mr Netley received 4,792 Placing Shares for which he paid £2,300. Mr Netley gifted all 82,000 of his Subscription Shares in favour of St Ann's Hospice on the same day, as did over 50% of the other retail investors who had taken up the Offer of Subscription.

82. On 2 August 2004 Mr Lundy wrote to Mr Netley referring to his gift of shares to St Ann's Hospice and stating that the closing price on the Daily Official List was 48.25p – 48.75p. The market value of Mr Netley's shares was stated to be £39,667.50 and Mr Netley was said to be eligible for tax relief at 40% amounting to £15,867. Mr Netley subsequently claimed that gift relief on his tax return for 2004-05. At his marginal rate of 40% the amount of relief was £15,867 on an investment of £10,000. In the closure notice HMRC reduced the relief to £2,624 based on a share price of 8p per share. I understand that Mr Netley retained his 4,792 Placing Shares.

83. Zeus did not have direct contact with Mr Netley or with any of the other individuals who subscribed for Subscription Shares and Placing Shares in the Company, save in relation to consent to the gifting of shares to various charities.

(5) Dr McArthur - Purchase and Gifting of Shares

84. Dr McArthur has enjoyed a very successful career in business. He has made very significant donations to a charitable trust which he established called the Hamilton Davies Trust. He has an investment portfolio which is managed by Brewin Dolphin on a discretionary basis. In 2004 he was consulted by Brewin Dolphin about an investment in the Company and agreed to purchase Subscription Shares and thereafter Placing Shares. Dr McArthur had previously invested in similar cash shell transactions carried out by Zeus and has previously gifted some of those shares.

85. The evidence as to Dr McArthur's investment was not entirely clear and was not supported by reference to any documentation. It seems that he bought some 3,497,126 shares in the Company by way of Subscription Shares and Placing Shares. He gifted 1,308,860 shares on 10 September 2004 and 439,998 shares on 21 March 2005. I understand that both gifts were made to the Hamilton Davies Trust. At that stage he retained 1,748,268 shares. Subsequently, some of the retained shares were sold on the market but Dr McArthur retains over 1m shares in FTG. Dr McArthur told me and I accept that he has retained this holding because he believes in the long term value of the shares.

86. It was clear from his evidence that Dr McArthur has strong views about the way in which HMRC have dealt with his tax affairs in relation to gifts of shares in FTG. Those views are not relevant to the issues I must decide on this appeal and it would not be appropriate for me to explore them any further.

(6) The Alternative Investment Market and Investigations in Possible Abusive Practices

87. AIM is part of the London Stock Exchange ("LSE"). It was established in 1995 in place of the Unlisted Securities Market ("USM") and gives an opportunity for smaller companies to float on a market which is more flexible and less regulated than the LSE main market.

88. AIM covers a broad range of companies from start ups to mature businesses worth hundreds of millions of pounds. It is a "disclosure based market" with fewer rules and a lighter regulatory framework than the main market. It relies on the presence of Nomads to ensure that companies admitted to AIM are "appropriate" and that proper disclosures are made in admission documents and market announcements. This approach is intended to guard against unscrupulous behaviour involving attempts to manipulate the market which could occur on smaller company share markets anywhere in the world. The AIM rules are not intended to be construed in a legalistic way. The spirit of the rules and market integrity are equally if not more important. Regulation is often informal and low key and might simply involve conversations with a particular Nomad or Nomads if AIM had any cause for concern. Amending the Rules and indeed suspending a share are the ultimate sanctions for market abuse.

89. Companies will seek admission to AIM for a variety of reasons. Mostly they are seeking to raise capital, but there may be other reasons. For example to provide opportunities to raise capital in the future; to place an objective market value on the company shares; to create a market in the company shares for the benefit of shareholders generally or for the purposes of an employee incentive scheme; or broadly to enhance the status of the company. Admission to AIM can in itself increase the market value of a company.

90. AIM companies are required to have at least one market maker. The market maker will move the price of the share up or down according to either market demand or their view of the value of the company.

91. It is a requirement of the AIM rules that any company admitted to AIM must have a Nomad. Nomads are approved by the LSE to manage admission of companies to AIM. Typically Nomads are corporate finance houses and brokers with experience of equity capital market transactions. The Nomad will advise and guide a company in relation to the admission process. It was common ground that the role of a Nomad in 2004 was as follows:

(1) To undertake due diligence to ensure a company is suitable for AIM;

(2) To provide guidance to companies through the flotation process;

(3) To prepare the company for being on a public market;

(4) To assist in preparation of the AIM admission document;

(5) To confirm to AIM that the company is appropriate to be admitted to AIM;

(6) To act as a regulator whilst the company is on AIM.

92. Mr Ray Knowles was employed by the LSE between 2000 and 2007. From 2004 onwards he was head of the AIM regulation team. He is presently a director of risk management at Citigroup Global Markets.

93. In 2004 the LSE became aware of concerns expressed by HMRC that certain admissions to AIM involved an improper use of AIM and the gift relief provisions. As a result, Mr Knowles met with HMRC and the Financial Services Authority in September 2004 although the notes of that meeting were not in evidence. There was a further meeting in November 2004. There may also have been a further meeting in January 2005 but again the notes of any such meeting were not in evidence. For the purposes of those meetings Mr Knowles had been looking at recent admissions to AIM including FTG. Certain companies were identified which involved the use of cash shells, pre-admission subscriptions for shares, followed shortly afterwards by a placing of shares on admission at a significant premium to the initial subscription price. They also involved what Mr Knowles considered to be excessive lock-in arrangements, going beyond the AIM rules and market practice. The Nomads acting in relation to admissions involving these characteristics were identified, including WHI.

94. In December 2004 Mr Knowles visited WHI to discuss WHI's role as Nomad in relation to the companies he had identified, and to consider whether a valuation analysis had been carried out. There was no note of that visit but in May 2005 Mr Knowles is recorded as having not seen the "detailed valuation information" that he would have expected to see. Mr Youngman who was then the managing director and head of corporate finance at WHI recalled that Mr Knowles had expected to see more documentation on valuation. What Mr Knowles had seen was information which suggested to him that Zeus would consider the balance sheet value including goodwill. That would form the basis of a valuation in respect of shares to be issued to the vendors of the business. Zeus would then do a valuation based on price / earnings ratios ("p/e ratios") for quoted companies assuming future income streams which

would form the basis of the price at admission. He also noted that whilst WHI would discount that valuation to some extent "*whatever happened the outside subscribers would always get their four times uplift on investment*".

95. The Respondents intended to call as a witness Mr David Hannis who was an executive director of JBS. In the event he did not give evidence but the Respondents did seek to place some reliance on a document he had exhibited to his witness statement. It was headed "Frenkel Topping – Update" and appeared to have his typed signature together with the date 4 March 2004. The document referred to the financial dealings between Frenkel Topping and JBS. Mr Gibbon placed some reliance on the following extract:

> "At a meeting with Richard Fraser on Monday 23rd February, Richard Fraser outlined how the company had been approached by a Venture Capitalist (Zeus Capital) with a proposal leading to their decision to list on the AIM market. The tax advantages of a side "gift aid" scheme, allow the stock to be listed at a price of up to four times their true worth. This comes hand in hand with the raising of some £1m or so to pay off John Frenkel …"

96. The document was put to Mr Hughes and he noted a number of inaccuracies in the passage quoted. Firstly, Zeus was not venture capitalists. Secondly, the £1m being raised was not to pay off John Frenkel. Thirdly he disputed that the shares were to be floated at four times their true worth. I should say that it was not part of the Respondents' case that anyone deliberately intended the float price to be more than the true worth of the shares.

97. There was no reliable evidence before me that subscribers to Zeus cash shells would always get a four times uplift on their initial investment. I am not satisfied that Mr Knowles' notes of his meeting with Mr Youngman either alone or together with the Hannis note is a sufficient evidential basis to make such a finding. Mr Knowles accepted that it was not unusual for there to be a gain on admission to AIM for pre-IPO investors reflecting the risk such investors were taking in making their initial investment. His view back in 2004 may well have been that retail subscribers would get a four times uplift but the evidence on which he formed that view was not available to me.

98. Mr Knowles' suspicion, which Mr Youngman recalled had been expressed to him at the time, was that valuation was driven by Zeus and that WHI played little or no role in determining the valuation. In his evidence Mr Youngman maintained that WHI had been involved in the valuation process and in the absence of any action by AIM in 2005 he assumed that AIM had been satisfied with what it had seen in relation to valuation. He recalled a letter sent to all Nomads in 2005 by Mr Martin Graham the then Head of AIM following Mr Knowles' enquiries. The letter set out concerns the LSE had about flotations linked to gift relief claims. Mr Graham described the common features of such companies as follows:

> (1) a cash shell that makes an acquisition of a trading entity on, or shortly before, admission to AIM;

(2) the involvement of private investors for whom a key motive for investing in such companies pre-admission is the availability of “Gift Aid relief”;

(3) an initial offer for subscription pre-admission followed shortly after by a placing on admission at a price significantly higher than the subscription price; and

(4) lock-in arrangements in place for most shareholders that go well beyond those usually required by the AIM rules.

99. Mr Lundy was reluctant to accept that FTG shared these characteristics, but Mr Youngman accepted that it did, together with 11 other cash shells promoted by Zeus for which WHI acted as Nomad. Given the close involvement of Mr Youngman, together with the supporting evidence of Mr Netley in relation to the significance of gift relief to him, I accept that the admission of FTG to AIM did share these characteristics. Having said that it does not follow that FTG was in some way unsuitable for admission to AIM or that the flotation of FTG was in any way abusive. Mr Gibbon did not suggest that it was.

100. Mr Knowles’ evidence in chief was that it was unclear to him why a pre-IPO fundraising was necessary, other than to produce a gain to the investors. In cross examination however he accepted that if the founders were not willing to fund a cash shell initially then a pre-IPO fund raising would be necessary at least to fund the costs of admission if the admission to AIM was aborted. Some but not all of those costs would be success based. His evidence was that the FTG flotation was not typical in that it was unusual for retail investors to be involved prior to the admission of the company to AIM. He would expect either institutional investors or a small number of high net worth individuals to contribute the initial equity funds. The costs of admission would be funded by subscription for shares placed on admission and if the admission was aborted then by the initial equity funders.

101. In cross-examination Mr Knowles accepted and I find that institutional investors would be unlikely to invest in a placing such as FTG which raised only £264,500. It was also unlikely therefore that there would be a book building process. A book building process involves identifying institutional investors who wish to invest in the company being floated. It might be relied upon to some extent to fix the value of the shares on admission because the institutional investors involved would carry out their own valuation of the business.

102. There was evidence before me from two experts on the workings of AIM. Mr Brickles had been head of the AIM regulatory team from its launch in 1995. Between 2001 and 2003 he was head of AIM. He left AIM in 2003 and since then has been involved in other exchanges and markets around the world. He was instructed by the Appellant and his evidence was directed towards the role of Nomads and the general market practice in relation to lock-ins when companies were admitted to AIM.

103. Mrs Kennedy is a solicitor and until recently was a partner in Kergan Stewart LLP solicitors. She is a member of the AIM Advisory Group of the LSE and chaired that group in 2001 and 2002. In 2004 Mrs Kennedy was a qualified executive and a director in the corporate finance department of Brewin Dolphin. Being a qualified

executive meant that she was recognised by the LSE as being qualified to carry out the work of a Nomad. A Nomad must have a number of "qualified executives" in order to act as such. After 2007 Mrs Kennedy was Head of Compliance for Brewin Dolphin or an associated firm. Mrs Kennedy was instructed by the Respondents and her evidence was specifically directed towards the admission of FTG to AIM, in particular the role of WHI and the lock-in provisions.

104. I am satisfied that Mr Brickles and Mrs Kennedy are both highly experienced experts in relation to the flotation of companies on AIM. It is unfortunate that there were differences in the nature and extent of their instructions. That is not a criticism of either expert, but it created unnecessary difficulties in assessing their evidence. In the event there were many more points of agreement between the two experts than there were points of disagreement. There was a joint statement of experts. The points of disagreement generally stemmed from the fact that Mr Brickles had not been instructed to consider the specific transaction involving FTG. Further, Mrs Kennedy was instructed by HMRC to comment "upon the circumstances relevant to the AIM price of shares in [FTG] on 28 July 2004". As a result her evidence at times strayed into aspects of the transaction which did not assist. In particular, in relation to valuation she went beyond expressing an opinion on the role of Nomad's generally and of WHI in particular. Her evidence also contained certain comments on other witness statements which were not helpful. Mrs Kennedy's written reports did not clearly identify the specific role of Nomads in relation to valuation. In cross-examination however she accepted that Nomads should look at valuation as part of their duty to assess appropriateness.

105. In short, it would have been better if both parties had been able to agree the scope of the expert evidence beforehand and then given clear and consistent instructions to their respective experts.

106. There was no AIM rule that specifically required a Nomad to perform a valuation analysis. The reason for this was because the information in the AIM admission document was intended to be sufficient for investors to form their own view as to valuation and to make their own investment decisions. Rule 37 of the AIM rules sets out the duties of a Nomad which include, pursuant to Schedule 6 a requirement for the Nomad to confirm that:

> " … in its opinion, it is satisfied that the applicant [for admission] and the securities which are the subject of the application are appropriate to be admitted to AIM."

107. Both experts agreed and I find that a duty in relation to valuation arose as part of the Nomad's wider duty to AIM to ensure that only appropriate companies were admitted to AIM. Further, I find that in the absence of institutional investors the Nomad had a duty to perform some analysis to ensure that it was comfortable with the valuation on admission. I accept Mr Brickles' summary of the position that "if [the company was] coming up with a valuation that no reasonable adviser can possibly have come up with, that would go to suitability".

108. Mr Knowles accepted that AIM did not reach any conclusion that shares in FTG had been over-valued. Following his investigation the LSE remained concerned that certain companies had been admitted to AIM primarily to secure gift relief. The letter from Mr Graham to Nomads in 2005 referred to above, suggested that companies possessing some or all of the features he had identified may be unsuitable for admission. Mr Knowles stated that following that letter what he described as the "abusive practice" appeared to cease. He accepted that one consideration in sending that letter was retaining the tax advantages available to AIM companies. Mr Firth suggested that the principal reason this letter was sent was that AIM had to be seen by HMRC to be doing something. I do not accept that was the position. I am satisfied that AIM had concerns about certain flotations in which WHI and others acted as Nomads, but Mr Knowles was not able to conclude on the evidence available to him that the flotations were abusive or that the valuations of such companies on admission and the lock-in provisions were inappropriate.

109. Mr Knowles' evidence in chief very briefly referred to methods of valuation, the absence of a liquid market in the shares of FTG and other matters. In the evidence before me those matters were covered in much more detail by other witnesses and therefore I do not place any reliance on Mr Knowles' observations in relation thereto.

(7) The Valuation Process

110. Mr Youngman was managing director and head of corporate finance at WHI between 1995 and 2009. He has 35 years of experience in stockbroking and corporate finance and has been involved in the admission to AIM of a large number of companies. Mr Youngman was the main contact for Zeus at WHI and WHI acted as Nomad on a number of admissions to AIM promoted by Zeus. In relation to the valuation of shares on admission, effectively the price paid for new shares being issued at the time of admission, Zeus would present their outline of the valuation. He would ask Zeus to explain and justify their valuation and the assumptions used. Valuations would be discussed at WHI amongst its executive directors and at meetings of its corporate finance committee. Mr Youngman recalled that on a number of occasions WHI rejected valuations on the basis that they were over-optimistic. Mr Youngman's evidence was that the internal procedures at WHI would not have allowed valuations put forward by Zeus to be accepted too readily. He described the ultimate valuation as being "negotiated". I accept Mr Youngman's general description of this process.

111. Mr Youngman's recollection was that in relation to FTG he considered that the Zeus valuation was "on the high side". He did not regard the projections for revenue growth as being very exciting. However Zeus provided information in relation to additional revenue streams from PFI projects that made him feel "comfortable " with the valuation. I accept that evidence.

112. In oral evidence Mr Youngman said that he had a recollection in relation to FTG of doing a discounted cashflow calculation, looking at price/earnings multiples based on forecasts from both Zeus and Baker Tilly, looking for comparables and considering general market conditions. He recalled considering the impact of a new

Canada Life product and potential PFI income. Unfortunately Mr Youngman did not have access to WHI files in relation to FTG for the purpose of giving his evidence. The contemporary documentation in evidence was therefore limited and Mr Youngman was relying to a large extent on recollection of events more than 10 years ago.

113. The documentary evidence that is available shows that in or about February 2004 Zeus produced a 3 page Valuation Paper in relation to Frenkel Topping. In relation to the market for structured settlements it referred to a new type of annuity expected to be available in March 2004. That was from Canada Life although it was not named in the Valuation Paper. At the time of the Valuation Paper there were two other life offices involved in the market for structured settlements although they were described as being "not particularly competitive". Amendments to the civil procedure rules and the Courts Act 2003 were also expected to benefit FTG. The conclusion in the Valuation Paper was as follows:

> "We are currently finalising a transaction with the vendors and have agreed a deal of circa £1m cash for working capital, with the vendors retaining 65% interest in the company post flotation.
>
> There is a massive opportunity in selling the pfi product through to the claims market which could massively improve the underlying performance of the business.
>
> Conservatively, we believe the company can deliver the numbers and as such believe a market capitalisation of circa £22m, is credible."

114. The Valuation Paper was sent to Mr Youngman at WHI by Mr Hughes in an email dated 3 February 2004. This was followed by email correspondence and there may also have been face to face meetings although there was no record of such meetings before me and no witness had any specific recollection of what might have been discussed. On 3 February 2004 Mr Youngman replied to Mr Hughes questioning the valuation. He asked whether the projections included in the Valuation Paper included the PFI income. He then asked:

> "On what basis do you believe a valuation of £22 million is credible? 2003 historic p/e 55x; 2004 est p/e 30+x; 2005 est p/e 22x; 2006 est p/e 17/18x"

115. Mr Hughes replied on the same date to say that he had included "£250k in 2005 that is all". He then sought to justify the valuation by reference to the Canada Life product, the PFI revenue, the nature of the funds under management and the possibility of bringing fund management in-house from JBS.

116. On 4 February 2004 Mr Youngman emailed Mr Hughes again questioning the valuation. The email commences:

> "Once again we are struggling with valuation."

117. Mr Youngman went on to question comparables used by Zeus, he described the projections as "not wildly exciting in terms of turnover growth". He suggested that if

the vendors of the business were insisting on 65% of the enlarged group then they should be prepared to warrant £1m of earnings in the current year which would substantially support the proposed valuation.

118. Mr Hughes replied seeking to justify his stance. Mr Youngman was able to secure a comfort letter in relation to potential PFI income which in part led to him being comfortable on the valuation. This was a letter from Mr Hughes to WHI dated 10 February 2004 which explained that Mr Hughes was a shareholder in Education Solutions Speke Ltd which was a special purpose vehicle involved in the design, build, finance and operation under PFI of Speke Forward Learning Centre. He indicated that there had been discussions between the shareholders and FTG on the possibility of realising the investment to an insurance company which would use the cashflow generated by the investment to support a structured settlement annuity. It was said that this would generate a one off commission for FTG of £400-600,000 and annual commission of approximately £60,000. He also referred to the possibility of involvement in other PFI projects which he identified.

119. The Valuation Paper appears to have been updated or at least prepared in an amended form in or about April 2004. Mr Hughes could not recall who had produced this version or why and Mr Youngman did not recall ever seeing it. The document concluded:

> "Based on these statistics [as to publicly quoted p/e ratios] a conservative P/E ratio of say 15x could easily be justified and based on historical PAT of £300k which easily look maintainable a valuation of £4.5 million appears sensible and prudent."

120. Mr Hughes could not explain how that valuation of £4.5m came about other than that it was historic profit after tax of £300,000 with a p/e ratio of 15.

121. Mr Hughes' evidence was that in this type of negotiation the power lies with the Nomad and the negotiation was robust. Mr Youngman accepted that whilst Zeus would be pushing for a high valuation, WHI were not pushing for a low valuation as such. He put it in these terms:

> "What we were looking for was a fair and reasonable valuation and an appropriate valuation so that when this company was admitted to AIM, it would not bring AIM into disrepute. It would not be ridiculed for [being] too high a valuation or indeed too low a valuation."

122. It is also the case that if the valuation was too high or too low then it would cause reputational damage to WHI as well as giving rise to the possibility of informal or formal sanctions from AIM. In light of all the evidence it seems to me that Zeus were understandably looking for a high valuation and WHI were looking to be comfortable that the valuation was not outside the bounds of what might be considered reasonable. That was the extent of their duty as a Nomad.

123. I accept that Nomads must be satisfied that the valuation is justified. However they do not undertake a robust valuation exercise and to a large extent it is a matter of impression, instinct and experience. Mr Currie was right when he said that valuation

is an art, not a science. There is an element of negotiation between the company and the Nomad, with the company and its advisers generally pressing for the highest price that can be justified and the Nomad operating as a moderating influence.

124. Mr Youngman recalled the compliance visit to WHI by Mr Knowles in late 2004/early 2005. He recalled producing documentation to Mr Knowles to support the valuations of various companies selected by Mr Knowles including FTG. The documentation included business plans, cashflow forecasts, financial projections and valuation papers presented to WHI by Zeus. As far as Mr Youngman was concerned Mr Knowles was satisfied with what he had seen.

125. Given the passage of time and the absence of documentation I cannot rely on Mr Youngman's recollection of doing a discounted cashflow calculation or any detailed valuation exercise. I find that WHI took a relatively broad brush approach to valuation that was consistent with the extent of its responsibilities as a Nomad. It was more akin to a broad credibility check than a rigorous valuation.

126. There is no reason to consider that WHI's remuneration from the Company affected their approach to valuation and it was not seriously suggested that it did.

(8) Lock-ins

127. Lock-ins on flotation generally restrict sales of shares by directors, senior employees, substantial shareholders and others for a lock-in period. This reflects the fact that it is undesirable for certain investors to sell their shares within a short period of admission to AIM. The purpose of a lock-in is broadly to ensure that those closely connected with the company cannot exploit information they might have as to the company's performance before such information is published following admission. I accept Mr Brickles' evidence that lock-ins are also intended to restrict "all those who may have advantages over the market as a whole by getting into a stock at either a different price and/or at an earlier occasion".

128. In 2004 AIM Rule 7 was the only rule which specifically required a lock-in for certain shares on flotation. At the material time it provided as follows:

> " **Lock-ins for new businesses**
>
> 7. Where an applicant's … main activity is a business which has not been independent and revenue earning for at least two years, it must ensure that all related parties and applicable employees as at the date of admission agree not to dispose of any interest in its securities for one year from the admission of its securities.
>
> This rule will not apply in the event of an intervening court order, the death of a party who has been subject to this rule or in respect of an acceptance of a takeover offer for the AIM company which is open to all shareholders."

129. For these purposes a "related party" was defined to include directors and their family members, shadow directors and substantial shareholders. Substantial shareholders were those holding more than 10% of the company's shares. Applicable

employees were employees who together with family members held 0.5% of the company's shares.

130. Published Guidance Notes to the AIM rules stated as follows:

> "The Exchange will not require a substantial shareholder to be the subject of a lock-in under rule 7 where that shareholder became a substantial shareholder at the time of an AIM company's admission and at a price which was more widely available."

131. The scope of a lock-in was a matter of the discretion for the Nomad and negotiation with the company being admitted to AIM and its advisers. The experts agreed that a Nomad would not want to apply a lock-in to a shareholder unless there was a reason to do so. During his investigation, if Mr Knowles as the AIM regulator had concluded that the lock-ins for those cash shells he looked at were inappropriate, it was an option for AIM to insist that the Nomad and/or the company should release the lock-ins.

132. It was common ground between all witnesses that the AIM rules in relation to lock-ins were a minimum requirement and that in any particular case a more substantial lock-in may be required, either in terms of the shareholders locked-in or the period of a lock-in.

133. Various witnesses referred in their evidence to a "hard lock-in" and a "soft lock-in" but with slightly different meanings. For the purposes of this decision I refer to a hard lock-in as a lock-in required by the AIM rules. A soft lock-in is a lock-in that goes beyond what the AIM rules require and would be negotiated between the Nomad and the company. A soft lock-in might be subject to exceptions, such as transfers to family members. There are also "orderly marketing arrangements" which do not prevent a shareholder from selling shares, but which might for example require any sale to be made through the company's broker. Companies admitted to AIM were required to have a nominated broker. Such sales might also be subject to the consent of the Nomad or nominated broker, with consent not to be unreasonably withheld. All these arrangements would be a matter for negotiation between the Nomad and the company, but the Nomad would not want to impose a lock-in on a particular shareholder or class of shareholders unless there was a reason to do so.

134. The experts agreed that for companies to which Rule 7 did not apply, a lock-in of one year or slightly more was common. Release from such lock-ins would usually be based on the effluxion of a set period of time or a corporate event such as an announcement of results.

135. AIM Rule 7 did not apply to FTG because the business was an established revenue earning business. Any lock-in therefore would be a soft lock-in which would typically be applied to existing shareholdings of:

(1) Directors, their families and other connected parties together with any new shares subscribed for on admission;

(2) Major individual or family shareholdings;

(3) A vendor who had sold the business to the company shortly before or conditional on an IPO;

(4) Major shareholders, often when selling part of their holding as part of the IPO; and

(5) Employees who were part of the management team.

136. Mrs Kennedy's evidence was that the lock-in in the FTG transaction was unusual in that:

(1) It was for a period of 2 years. One year was usual, perhaps followed by orderly marketing arrangements;

(2) It applied to small retail shareholders who she considered had effectively subscribed as part of the IPO process;

(3) It applied to a large percentage of FTG's share capital;

(4) It included a charity exemption which was used only in respect of companies promoted by Zeus.

137. At the time of her report Mrs Kennedy was not aware of any admissions to AIM which included all these characteristics other than those promoted by Zeus. It subsequently appeared that in fact there may have been two admissions to AIM sharing these characteristics which were not promoted by Zeus but the details were not in evidence.

138. Mr Brickles' evidence was that it was unusual for retail investors to be the subject of a lock-in, but it would depend on the circumstances and circumstances could vary considerably. The period of a lock-in would generally be geared to "reporting milestones" such as publication of interim or final accounts. In other words locked in shareholders could only sell once subsequent performance was disclosed.

139. Mrs Kennedy's evidence was that a two year lock-in was very unusual, but in cross examination she appeared to agree that it is logical to have a two year lock-in to cover release of financial results. Her evidence however remained that a two year lock-in for retail investors was extremely unusual. Mr Brickles broadly agreed that the more shares locked in the more unusual it was, and the more undesirable it was from the point of view of the market in shares.

140. Mrs Kennedy produced evidence in relation to a number of companies admitted to AIM in or about 2004 and the associated lock-ins. Mr Brickles agreed that the examples were representative. In cross-examination Mr Firth made various criticisms of the sample but in light of the evidence of Mrs Kennedy and Mr Brickles I am satisfied that it was representative. There was no example of a two year lock-in for retail investors.

141. There was some evidence before me of an admission to AIM of Proton Power Systems in 2006 where all the existing shareholders were locked-in. It was suggested in cross-examination of Mrs Kennedy that a holder or holders of 0.4% of the pre-IPO shares were locked in. Even if that is right, and the calculation of 0.4% was not

explained, in my judgment it cannot be inferred from that example that there was any market practice to lock-in small retail investors or that it was usual.

142. Mr Currie's evidence was that the idea for a lock-in for pre-IPO investors came following the flotation on AIM of a company called Debt Free Direct in about 2002. Mr Currie was involved in that flotation and it did not have a lock-in. The pre-IPO investors paid 10p per share and it floated at 40p. Mr Currie described the investors as "being out like rabbits" and described having to place the shares again, in other words find replacement investors. The reason he would become involved at that stage is that in smaller AIM companies the market for shares is effectively on a matched bargain basis. If a shareholder wants to sell say £10,000 of shares, the broker will not be able to do that on the market. Instead the broker will often contact the company to see if it knows of any potential buyers. If buyers cannot be found that in turn might damage the reputation of the financial advisers involved in the flotation. As a result Mr Currie decided that in future cash shell transactions he would include soft lock-in provisions going beyond Rule 7, such as those in FTG. Mr Currie's evidence as to the circumstances in which the FTG lock-in was imposed was not disputed and I accept it.

143. Mr Hughes' evidence was that currently and going back to 2004 he would want to lock-in all the investors that he could identify who had subscribed prior to the placing and admission to AIM. He said that in 2004 a two year lock-in was essential and was the market practice. It was put to Mr Currie that the 2 year lock-in for pre-IPO retail investors with a specific carve out for gifts to charities was unusual and was included so as to attract retail investors who wanted to realise gift relief on flotation. Mr Currie did not accept that such a lock-in was unusual. He suggested that such a lock-in was best practice in the market at that time and that there had been a long history of discussions with the LSE about the need for such lock-ins.

144. The expert evidence did not support the description given by Mr Hughes and Mr Currie as to what was usual. I consider that Mr Currie and Mr Hughes were mistaken when they said that such lock-ins were required by the LSE, reflected best practice or were otherwise usual. It may be that they were usual for the cash shells promoted by Zeus but that is a different point.

145. As to the carve out for gifts to charity, that was clearly aimed at investors who might want to gift their shares to charity. However it was not specifically put to Mr Hughes or Mr Currie that the intention was to attract investors who simply wished to obtain relief on gifts of shares to charity regardless of the investment prospects of the company being floated. I am not satisfied on the evidence before me that was the intention of the Company or its advisers.

146. Mr Youngman's evidence in chief did not deal with lock-ins. In cross examination his evidence was that a two year lock-in applicable to retail investors was not unusual. He could not recall that it was Mr Currie who had suggested a lock-in for retail investors in cash shells. He did say however that a lock-in for retail investors on a flotation such as FTG "protects investors in the after-market". If shares had been issued at 10p and six months later there was a placing at 40p then investors of any

description would expect those people to be locked-in. That is not consistent with the expert evidence and I prefer the evidence of the experts. Mr Youngman had not come across a charity exception to a lock-in until his dealings with Zeus.

147. Based on all the evidence before me I find that:

(1) There was no market practice to lock-in small retail investors for any period of time, whether investing at an IPO or pre-IPO.

(2) A two year lock-in for small retail investors such as those who invested in Subscription Shares of FTG was unusual.

(3) The charity exception from the lock-in was also unusual.

(4) I am satisfied that Mr Netley for these purposes was a small retail investor.

(5) I am satisfied that the lock-in for retail investors in FTG was imposed so as to prevent an exodus of retail investors on Admission and for a period thereafter.

(9) The Significance of Gift Relief

148. The special circumstances relied on by the Respondents in relation to section 272(3) are said to arise primarily from aspects of the flotation which it is said were "in large measure designed to facilitate the tax advantages to be derived from gifting the shares to charity by individuals who had …[subscribed] under the Offer for Subscription". In addition it was submitted that it was inherent in the design of the flotation that retail investors would be offered shares pre-IPO; that there would be a significant price uplift on flotation; and that unusual lock-in arrangements prevented investors being "out like rabbits". The combination of those factors meant that the market in the shares of FTG was highly illiquid.

149. Mr Lundy was asked whether the investment in the Company was ever described to investors as a form of tax shelter. His response was "I don't think so", on the basis that gift relief was a relief created by the Government. The question of whether investors were encouraged to invest on the basis that they would receive relief greater than the amount of their investment was not put in terms to Mr Lundy. Mr Lundy emphasised, on more than one occasion and sometimes in response to a different question that it was a matter for individual investors whether they gifted the shares to charity and some investors retained their shares. I gained the impression that Mr Lundy was seeking to distance himself and the transaction from any suggestion of an understanding that investors would obtain gift relief.

150. It was put to Mr Lundy that a key motive for the investment by private investors such as the partners in Tushingham Moore, including Mr Netley, was the availability of gift relief. Mr Lundy did not accept that in so many words. He did accept that by gifting the Subscription Shares, the Placing Shares effectively became free shares. There was therefore no risk in continuing to hold the Placing Shares. Mr Netley gave similar evidence to the effect that the opportunity to obtain gift relief on a gift to charity made the transaction "relatively risk-free".

151. Mr Hughes' evidence was that Zeus' motivation throughout the transaction was to realise the equity value of the investment, and not to create an opportunity for investors to obtain tax relief. He only knew one of the investors, Dr McArthur, and he had no concern with whether the investors intended to gift their shares. He was aware from the consent letters which he signed on or about 30 June 2004 that an appreciable number of investors were intending to gift their shares to charity because he signed standard form consent letters on that date.

152. It was put to Mr Hughes in cross-examination that it would have been clear to him that the structure of the transaction would give investors the opportunity to obtain gift relief. To the extent that past performance was a guide, I find that there was clearly a prospect that there would be a substantial uplift on admission which would give individual investors the opportunity to gift their shares. That would give gift relief ostensibly at the AIM quoted price which provided an opportunity to remove or reduce any risk of an overall loss, including the risk associated with being locked-in to the shares for 2 years.

153. I am not satisfied that the Company or Zeus intended retail investors to take advantage of gift relief. The opportunity to do so was simply the result of a significant premium arising on admission to AIM. I am not satisfied that the flotation was structured so as to provide such an opportunity. The intention of the Company and Zeus was to float FTG at the highest price obtainable.

Issues of Law

154. There are two issues of law relevant to the question of valuation which I have identified above. For convenience I shall repeat them here:

(1) Were FTG shares "quoted in The Stock Exchange Daily Official List" so as to engage section 272(3)?

(2) Were FTG shares "quoted on a recognised stock exchange" with the effect that section 273 has no application in defining the information available to a prospective purchaser.

155. I shall deal with each issue in turn.

156. The Appellant's submission that the FTG shares were quoted in The Stock Exchange Daily Official List ("SEDOL") was straightforward. Essentially Mr Firth produced an extract from SEDOL which included under AIM an entry for the FTG shares including a quotation.

157. Mr Gibbon's submission as to why the Appellant is wrong depends on some understanding of the operation of various markets by the LSE over time and a purposive construction of various statutory provisions. His submissions in relation to the various markets may be summarised as follows:

(1) AIM was a successor to the USM. The USM had been set up in 1980 as a market for shares and securities in smaller companies. At that time there was a

clear distinction between listed and unlisted shares. The market for shares on the USM was generally far less liquid than for listed shares.

(2) USM shares appeared in SEDOL but under the heading "Unlisted Securities Market".

(3) Section 150 Capital Gains Tax Act 1979 ("CGTA 1979") was the predecessor to section 272 TCGA 1992. It is clear that USM shares did not fall within section 150 or section 272(3) because they were not "listed" in SEDOL. I explore that submission further below. Further, Council Directive 97/279/EEC ("the Admission Directive") which coordinated the conditions for the admission of securities to official stock exchange listing required at least 25% of shares in a listed company to be in public hands whereas the requirement of the USM was for only 10% of shares to be in public hands. The USM rules also avoided any language associated with listing.

(4) In 1984 the Stock Exchange (Listing) Regulations 1984 ("the 1984 Regulations") were brought into effect. Amongst other directives designed to harmonise the listing of securities across the European Community, the 1984 Regulations brought into effect the Admission Directive. The 1984 Regulations designated The Council of the Stock Exchange as the competent authority for the purpose of the directives and defined "admission to official listing" and "official listing" as the admission of securities to the Official List of the Stock Exchange.

(5) From 1984 onwards USM shares were included in SEDOL under the heading "USM Appendix" with the following narrative:

> "The Council of the Stock Exchange has granted permission for dealings to take place in the following securities in the Unlisted Securities Market. The securities in the Appendix have not been admitted to official listing on the Stock Exchange."

(6) Further, Part IV of the Financial Services Act 1986 ("FSA 1986") dealt with the official listing of securities. No investments were to be admitted to the Official List of The Stock Exchange save in accordance with the provisions of Part IV.

(7) On 19 June 1995 AIM came into existence in place of the USM. AIM rules were broadly less onerous than USM rules and were intended to comply with the Public Offer of Securities Regulations 1995 ("the POS Regs") which came into force on the same date. As the name implies the POS Regs regulated public offers of securities, for example in relation to the form and content of prospectuses. They applied to "Public Offers of Unlisted Securities" which were investments "not admitted to official listing, nor the subject of an application for listing".

(8) When AIM came into existence, shares on AIM were clearly "unlisted securities". They were not admitted to the Official List of The Stock Exchange in accordance with Part IV FSA 1986 and public offers of such shares were designed to comply with the POS Regs.

(9) AIM shares had a heading in SEDOL separate from “Listed Companies” with the following narrative:

> “These securities have been admitted to trading on the Alternative Investment Market of the London Stock Exchange (AIM). It is emphasised that these securities are not admitted to the Official List. AIM is a market designed primarily for emerging or smaller companies. The rules of the market are less demanding than those of the Official List.”

158. Mr Firth did not take issue with this historical and legislative context. He submitted that it was irrelevant, and that HMRC had failed properly to distinguish between SEDOL and the Official List. I shall return to that distinction below. Before doing so I shall summarise Mr Gibbon’s submissions in relation to the background to section 272(3):

(1) The purpose of section 272(3) is to provide a reliable proxy for the open market value of shares and requires a quotation in a sufficiently liquid market to give such a proxy.

(2) Section 150 CGTA 1979 was the predecessor to section 272(3) and applied to:

> “…shares **listed** in The Stock Exchange Daily Official List …”

(3) Background Notes to the Finance Bill 1996 referred to forthcoming Stock Exchange changes. Those changes were put forward in November 1995 and involved what was described by the Stock Exchange as a “historic decision” to move away from a quote driven system of trading to a matched bargain system. Pursuant to the quote driven system, market makers would display the best price at which they would buy or sell shares – the quote. Dealing was by telephone possibly involving the negotiation of a better price. The alternative of an electronic matched bargain facility was to be introduced whereby firm prices would be displayed for a specific number of shares. The proposals were controversial and they were still being debated in March 1996.

(4) The Background Notes to the 1996 Finance Bill read as follows:

> “Clause 185 and [Schedule 38] ensure that various provisions which refer to the Stock Exchange treatment of shares and securities, retain their intended meaning in the light of forthcoming Stock Exchange changes. Price quotes for some shares and securities will, from 1 April 1996, no longer be included in the Stock Exchange Official List. This clause and schedule by changing the statutory wording where necessary from that date, ensure that the tax treatment of such shares and securities remains unchanged.”

(5) The effect of Finance Act 1996 (“FA 1996”) was to amend what had originally been section 150 CGTA 1979 to the form that now appears in section 272(3). In particular paragraph 12 Schedule 38 FA 1996 provided as follows:

> “ 12(1) In section 272(3) [TCGA 1992] (market value of **certain listed shares or securities**), for ‘listed’ there shall be substituted ‘quoted’.”

(emphasis added)

159. In response to Mr Gibbon's submissions as to the legislative history of section 272(3), Mr Firth relied on the established rule that in construing a consolidating statute such as TCGA 1992 there should not be any need to refer back to the same provisions in earlier legislative versions (see *Farrell v Alexander [1977] AC 59; IRC v Joiner [1975] 1 WLR 1701*). The position was recently summarised by the Upper Tribunal in *Eclipse Film Partners (No.35) LLP v HMRC [2013] UKUT 639 (TC)*:

> " 97. The law regarding the approach to construction of a consolidating statute was explained by the House of Lords in *Farrell v Alexander* [1977] AC 59 and is well settled. When construing a consolidating statute, which is intended to operate as a coherent code or scheme governing some subject matter, the principal inference as to the intention of Parliament is that it should be construed as a single integrated body of law, without any need for reference back to the same provisions as they appeared in earlier legislative versions: see *Farrell v Alexander* [1977] AC 59, 73B-C (Lord Wilberforce), 82B-D and 83D-H (Lord Simon of Glaisdale) and 97B-E (Lord Edmund-Davies). An important part of the objective of a consolidating statute or a project like the Tax Law Rewrite Project is to gather disparate provisions into a single, easily accessible code. That objective would be undermined if, in order to interpret the consolidating legislation, there was a constant need to refer back to the previous disparate provisions and construe them. Therefore the court's main task in this case must be to construe the ITTOIA without reference back to section 18 ICTA and Schedule D. However, where, after undertaking such an exercise, a provision which falls to be applied is found to be ambiguous, a subordinate presumption comes into play, namely that it is presumed that there was no intention to change the meaning of the provision which has been repeated in the same language in the consolidated code. In such circumstances, it may be relevant to try to determine the meaning of the relevant provision by looking to see what it meant when it was previously enacted: see [1977] AC 59 at 73B (Lord Wilberforce), 84D-H (Lord Simon of Glaisdale) and 97B (Lord Edmund-Davies)."

160. Mr Gibbon relied on various passages from the House of Lords judgments in *R v Environment Secretary (ex p Spath Holme Ltd) [2001] 2 AC 349* at p388 C-E where Lord Bingham stated:

> " From these authorities, it is plain that courts should not routinely investigate the statutory predecessors of provisions in a consolidation statute, particularly where (as in *Maunsell v. Olins,* and *Farrell v. Alexander*) the issue concerns the construction of a single word or expression. Such a practice would reduce the benefit to be derived from the process of consolidation (although the advantage of gathering scattered, and often amended and re-amended, provisions together in a coherent sequence in a single statute should not be underrated). But the overriding aim of the court must always be to give effect to the intention of Parliament as expressed in the words used. If, even in the absence of overt ambiguity, the court finds itself unable, in construing the later provision in isolation, to place itself in the draftsman's chair and interpret the provision in the social and factual context which originally led to its enactment, it seems to me legitimate for the court - even, as Lord Simon said, incumbent on it - to consider the earlier, consolidated, provision in its social and factual context for such help as it may give, the assumption, of course, being (in the absence of amendment) that no change in the law was intended. I agree with the Court of Appeal that it is, in the present case, appropriate to consider the statutory predecessor of section 31."

161. Mr Gibbon further relied on *Mangin v Inland Revenue Commissioner [1971] AC 739* at p746E where Lord Donovan giving a majority judgment of the Privy Council set out various rules of statutory construction including, fourthly:

> "… the history of an enactment and the reasons which led to it being passed may be used as an aid to its construction."

162. Mr Gibbon relied on the Background Notes to FA 1996 as part of the contextual scene, rather than directly as to the meaning of the words used. In support of such reliance he referred me to the Judgment of Lord Steyn in *R (otao Westminster City Council) v National Asylum Support Service [2002] UKHL 38*:

> " 5. The question is whether in aid of the interpretation of a statute the court may take into account the Explanatory Notes and, if so, to what extent. The starting point is that language in all legal texts conveys meaning according to the circumstances in which it was used. It follows that the context must always be identified and considered before the process of construction or during it. It is therefore wrong to say that the court may only resort to evidence of the contextual scene when an ambiguity has arisen… [I]n his important judgment in *Investors Compensation Scheme Ltd v West Bromwich Building Society* [1998] 1 WLR 896, 912-913, Lord Hoffmann made crystal clear that an ambiguity need not be established before the surrounding circumstances may be taken into account. The same applies to statutory construction. In *River Wear Commissioners v Adamson* (1877) 2 App Cas 743, 763, Lord Blackburn explained the position as follows:
>
> > ' I shall . . . state, as precisely as I can, what I understand from the decided cases to be the principles on which the courts of law act in construing instruments in writing; and a statute is an instrument in writing. In all cases the object is to see what is the intention expressed by the words used. But, from the imperfection of language, it is impossible to know what that intention is without inquiring farther, and seeing what the circumstances were with reference to which the words were used, and what was the object, appearing from those circumstances, which the person using them had in view; for the meaning of words varies according to the circumstances with respect to which they were used.'
>
> Again, there is no need to establish an ambiguity before taking into account the objective circumstances to which the language relates. Applied to the subject under consideration the result is as follows. Insofar as the Explanatory Notes cast light on the objective setting or contextual scene of the statute, and the mischief at which it is aimed, such materials are therefore always admissible aids to construction. They may be admitted for what logical value they have…
>
> 6. If exceptionally there is found in Explanatory Notes a clear assurance by the executive to Parliament about the meaning of a clause, or the circumstances in which a power will or will not be used, that assurance may in principle be admitted against the executive in proceedings in which the executive places a contrary contention before a court. This reflects the actual decision in *Pepper v Hart* [1993] AC 593. What is impermissible is to treat the wishes and desires of the Government about the scope of the statutory language as reflecting the will of Parliament. The aims of the Government in respect of the meaning of clauses as revealed in Explanatory Notes cannot be

> attributed to Parliament. The object is to see what is the intention expressed by the words enacted."

163. Mr Firth did not disagree with the approach described in the authorities relied on by Mr Gibbon. His principal submission was that it is not permissible to treat the wishes of government about the scope of statutory language described in extra-statutory material as reflecting the will of Parliament. However Mr Gibbon did not seek to place reliance on the material for that purpose. He relied upon the extra statutory material to demonstrate the context in which the statute was enacted which in my view is unobjectionable.

164. Mr Firth did submit that there must be an ambiguity before you can look at context. Any such ambiguity must be in the current law as stated in 1992, and amended in 1996. There was no ambiguity in TCGA 1992 or the 1996 amendment and AIM shares were clearly listed in SEDOL and quoted in SEDOL. It is not permissible to go back to the previous law to find an ambiguity. I do not accept that submission. Firstly the historical and legislative context relied on by Mr Gibbon is part of the objective setting or contextual scene of section 272(3). Secondly, as set out below I consider that against that background there is ambiguity in section 272(3).

165. There is undoubtedly a distinction between the Official List and SEDOL. The Official List is a list of securities maintained by the United Kingdom Listing Authority which is part of the Financial Conduct Authority. At the time of FA 1996 and prior to de-mutualisation of the LSE it was the LSE which was the competent authority for the purpose of maintaining the Official List. The Official List is simply that, a list of shares and securities although in 2004 it was not formally published as such. It was also common ground that it does not contain any information as to the price of those shares and securities. It can be contrasted with SEDOL, which is a daily publication published by the LSE showing all shares traded on the LSE, including AIM shares, together with a quotation based on the price at which those shares were traded on the day.

166. Mr Firth noted that in 1992, at the time of consolidation in TCGA 1992, USM shares were not quoted in SEDOL, in the sense that the shares were included in the USM Appendix but there was no quotation column as there was in relation to listed companies. Thus USM shares could not on any view fall within section 272(3). Mr Gibbon did not dissent from that result, although he submitted that it was nothing to do with USM shares being included in an appendix of SEDOL. It was the fact that they were never "listed" in the Official List that meant they did not fall within section 272(3).

167. Mr Firth distinguished AIM shares which from the outset of AIM in 1995 were contained in the main body of SEDOL albeit under a heading separate from Listed Companies. AIM shares also had a quotation column. So, if it was necessary to look at whether a share was listed in SEDOL it was simply necessary to look at SEDOL and see the share in the list. Similarly, if it was necessary to see if a share was quoted on SEDOL it is simply necessary to see the share listed in SEDOL with a quotation.

168. Mr Firth submitted that the statutory provisions were clear and that the tribunal cannot attach a meaning to the words used which they cannot reasonably bear. He submitted that is what HMRC are trying to do when they interpret "quoted in SEDOL" as effectively meaning "listed on the Official List and quoted on SEDOL". Mr Gibbon accepted that was HMRC's construction of section 272(3), and submitted that the reason that terminology was not used in the section was because the section was concerned with finding the price of a share. For that reason, it simply directs the reader to the document where prices for listed shares are to be found, namely SEDOL. Mr Gibbon submitted that between 1992 and 1996 "listed" was not an apt word to catch USM shares, or AIM shares after 19 June 1995.

169. Mr Firth's submission was that if Parliament had intended in 1992 to refer to only shares on the Official List then it would have said so. Parliament must be presumed to understand the distinction between the Official List and SEDOL. He illustrated this by reference to section 288 TCGA 1992 which was an interpretation section repealed by FA 1996. Section 288(4) provided that:

> " References in this Act to quotation on a stock exchange in the United Kingdom or a recognised stock exchange in the United Kingdom shall be construed as reference to listing in the Official List of The Stock Exchange."

170. Mr Firth made the point that where Parliament wished to refer to the Official List it did so. In similar vein Mr Firth also referred to various other amendments introduced by Schedule 38 FA 1996. He gave as an example section 735 ICTA 1988 where a reference to "listed in the Stock Exchange Daily Official List" was replaced by "listed in the Official List of the Stock Exchange".

171. Mr Firth submitted that the amendments in 1996 did not materially affect the position of AIM shares. He submitted that AIM shares were from the inception of AIM in 1995 both listed in SEDOL and quoted on SEDOL. He described HMRC's arguments to the contrary as impermissible statutory amendment rather than statutory construction.

172. Mr Gibbon acknowledged that many amendments in Schedule 38 substituted the word "listed" for the word "quoted". However, in relation to section 735 and other amendments he made what I consider to be a good point that in those amendments Parliament was principally concerned with the status of shares, whether they are listed or not, rather than the price of the share at any particular time.

173. In relation to section 288(4) Mr Gibbon submitted that it was simply a confirmation of what would already have been understood. I agree. It seems to me that it was intended to be a clarifying provision and does not assist in construing section 272(3). Nor indeed do references to the other amendments made by Schedule 38 in various different contexts.

174. Mr Firth also made the point that section 272(3) expressly contemplates that it should apply to shares which lacked liquidity because it made express provision for days on which no bargains are recorded. It does not seem to me that the absence of

bargains on a particular day necessarily implies an absence of liquidity generally in the market for a particular share. I do not consider that Mr Firth's submission supports an argument that section 272(3) is not generally concerned with identifying a price for shares in a liquid market.

175. Mr Gibbon submitted that the word "quote" had a protean quality in the sense that it could mean different things in different contexts. Effectively, the fact that SEDOL contained a price for an AIM share did not mean that it was a quote for the purposes of section 272(3). He relied by way of context on market terminology and the stock exchange changes in 1996. He relied also on the words of paragraph 12(1) Schedule 38 FA 1996 highlighted above and the intention to maintain the status quo expressed in the Background Notes. In the light of all that material he submitted that the reference to "quoted" was intended to mean "officially listed at a price". If Parliament had intended a fundamental change to the way AIM shares had been dealt with then it would have made such a change clear.

176. In the light of the arguments on this appeal it is a matter of some irony that an Inland Revenue Press Release at the time of the budget statement in November 1995 prior to FA 1996 stated that it was proposed to "clarify the use of the terms 'listed' and 'quoted' securities in tax legislation". That clarification was said to be necessary in the light of forthcoming changes at the Stock Exchange but it was stated that it would not affect the tax treatment of shares.

177. The change in terminology from "listed" to "quoted" seems odd at first sight given that the stock exchange changes in 1996 involved moving away from a quote driven system to a matched bargain system. Newspaper articles in late 1995 and early 1996 indicate that the matched bargain facility would apply to some but not all listed shares. Mr Gibbon submitted that there must have been concerns that "listed in The Stock Exchange Daily Official List" might no longer be an apt description if shares of some listed companies were being dealt in on a quotation basis and some on a matched bargain basis. The intention behind the amendment to section 272(3) was therefore to identify listed companies for which SEDOL contained a price without the risk of losing listed companies which were not traded by reference to a quote. As I understand the submission it was the "quotation" in SEDOL that was relevant, but without intending to remove the requirement that the share must still be listed in the sense of being in the Official List.

178. Mr Firth questioned why, if that is the case Parliament would not simply say "listed in the Official List". I agree with Mr Gibbon that the answer may be that section 272(3) directs to SEDOL because that is the document where prices for listed shares are to be found. It would undoubtedly have been clearer if the reference was to shares listed in the Official List and quoted in SEDOL. I do consider however that there is some ambiguity as to what is meant by "quoted" in SEDOL. That ambiguity arises from the market terminology described above and the possibility that in the context of share prices it has a different meaning from the quotation included in SEDOL.

179. The July Prospectus of the Company illustrates that ambiguity. It contained the following statement in relation to AIM, which I take to be a standard statement for prospectuses on admission to AIM:

> "Admission to AIM should not be taken as implying that there will be a liquid market for the Ordinary Shares. It may be more difficult for an investor to realise an investment in the Company than in a company whose shares are **quoted on the Official List**."

180. It is the case that HMRC have interpreted section 272(3) and its predecessor as excluding reference to shares on the USM and AIM. That interpretation goes back to 1980 when the USM was first established and the Inland Revenue issued a statement of practice to that effect (SP 18/80). The interpretation continued after AIM was established in 1995. I accept that HMRC's view of the law in itself is irrelevant to the proper construction of section 272(3), but there was no material before me to suggest that HMRC's view has ever been challenged.

181. Mr Gibbon described the Appellant's approach to this issue as "literalist" and as having a "prima facie logic". He emphasised however that what section 272(1) was aiming at was a fair basis of valuation (see Widgery LJ in *re Lynall [1970] 1 Ch 138* at p153). I agree that the construction to be given to section 272(3) must take into account that overarching concept.

182. In my view the ambiguity is resolved by considering the context in which the changes were made. I am satisfied that Parliament was reacting to stock exchange changes and did not intend to effect any significant change to the tax treatment of AIM shares. The reference in section 272(3) is to shares in the Official List for which a price is quoted in SEDOL. If Parliament had intended the amendment to effect a significant change then it would have made it clear that it was doing so. The position is similar to *Ye Olde Cheshire Cheese v Daily Telegraph Plc [1988] 1 WLR 1173* where at 1180B Sir Nicolas Browne-Wilkinson V-C held that it would have been most improbable that Parliament intended to change the substantive rights of tenants in the course of making merely a procedural modification.

183. I accept Mr Gibbon's submission that the intention of Parliament must have been that USM shares and AIM shares were to be treated in the same way. Both comprised unlisted shares not in the Official List, involved a lesser degree of regulation that shares in the Official List, and involved a generally far less liquid market. The fact that USM shares were included only in an appendix to SEDOL was not relevant to their exclusion from section 272(3). Nor was it relevant that there was a quotation column for AIM shares in SEDOL. Between June 1995 when AIM came into existence and 1996 when the provision was amended, section 272(3) was looking for a share that was "listed" rather than "quoted".

184. For the reasons given above I am satisfied that section 272(3) does not apply in calculating the market value of Mr Netley's shares in FTG for the purposes of gift relief.

185. The second issue of law is similar to the first. It is whether the FTG shares were “quoted on a recognised stock exchange” for the purposes of section 273 TCGA 1992. This affects the information available to a prospective purchaser of the shares in ascertaining their market value for the purposes of section 272(1). If the shares are quoted on a recognised stock exchange then section 273(3) does not apply.

186. This issue was first raised by the Appellant in Mr Firth’s skeleton argument dated 5 September 2016. He submitted that FTG was quoted on a recognised stock exchange, although having said that he also submitted that there was no difference in the information that should be treated as being available. I return to that submission below in considering valuation, and the information assumed to be available for the purpose of valuation.

187. Section 288(4) TCGA 1992 originally provided as follows:

> “References in this Act to quotation on a stock exchange in the United Kingdom or a recognised stock exchange in the United Kingdom shall be construed as references to listing in the Official List of The Stock Exchange.”

188. This section was repealed by Schedule 41 FA 1996. In the light of that repeal, the Appellant’s argument is essentially that AIM is part of the London Stock Exchange and therefore the Company’s shares are quoted on a recognised stock exchange. Mr Firth submitted that if HMRC are right that the ordinary meaning of the words “quoted on a recognised stock exchange” in the context of UK shares meant listed in the Official List then there would have been no need for section 288(4) in the first place.

189. It is clear that when AIM was introduced in June 1995 it was not a recognised stock exchange for the purposes of section 273(2). It was expressly excluded from that definition by section 288(4) because on any view the shares of AIM companies were not listed in the Official List.

190. Mr Gibbon put forward an explanation for the repeal of section 288(4). He submitted that in light of the stock exchange changes in 1996 the draftsman may have been concerned that leaving this provision in place could cause confusion. It is not really clear to me how that confusion might have arisen, but again I accept Mr Gibbon’s further submission that there is no indication that Parliament was intending what would have been a fundamental change.

191. Mr Gibbon also submitted that it has never been suggested since 1996 that AIM shares are quoted on a recognised stock exchange, and Mr Firth did not challenge that submission. The terminology of the market relied on by Mr Gibbon was that shares were admitted to dealing on AIM. They were not properly described as listed on AIM and they were not properly described as quoted on AIM. Hence shares admitted to dealing on AIM were not quoted on a recognised stock exchange. I accept Mr Gibbon’s submission, which is supported by the distinction in section 587B(9) ICTA. For the purposes of gift relief a qualifying investment is defined as any “shares or securities which are listed or dealt in on a recognised stock exchange …”. It is

because the FTG shares are dealt in on AIM that they qualify for gift relief, but they are not listed or quoted on a recognised stock exchange.

192. Such a distinction is consistent with the July Prospectus for FTG and in documentation in evidence before me relating to other companies admitted to dealing on AIM. In relation to taxation the July Prospectus stated as follows:

> "On issue, the Ordinary Shares will not be treated as either "listed" or "quoted" securities for tax purposes. Provided that the Company remains one which does not have any of its shares quoted on a recognised stock exchange (which for these purposes does not include AIM) … the Ordinary Shares should continue to be treated as unquoted securities …"

193. Further, the Appellant's own expert evidence proceeded on what may be described as the conventional basis that for AIM shares the information available is the public information supplemented by section 273.

194. Mr Gibbon indicated during the hearing that he wished in effect to reserve the right to make further submissions on this issue in relation to other aspects of the tax code where reliefs were given for shares which were not quoted on a recognised stock exchange. In the event it has not been necessary for me to receive any further submissions.

195. The absence of any controversy over a long period of time as to whether AIM shares fall within section 272(3) and 273(2) suggests that there has been a well-established and common understanding that AIM shares are not "quoted" either in SEDOL or on a recognised stock exchange. I am also satisfied that the interpretation I have given to sections 272(3) and 273(2) is consistent with the dicta of Widgery LJ in *re Lynall* at p153H in relation to valuation, in that case for estate duty purposes:

> "The intention underlying section 7(5) is to produce a fair basis of valuation between the Crown and the subject."

196. It is accepted that the market for AIM shares may be illiquid, and FTG is clearly a case in point. The price at which the small volumes of shares were traded on 28 July 2004 cannot, without more, be viewed as a reliable proxy for the open market value of those shares.

Special Circumstances

197. In light of my decision that the FTG shares are not quoted in SEDOL the question of whether the price quoted in SEDOL is not a proper measure of market value in consequence of special circumstances does not arise. I shall therefore set out my conclusions only briefly.

198. The meaning of "special circumstances" in this context was considered by the House of Lords in *Crabtree v Hinchcliffe [1972] AC 707*. In that case the taxpayer was arguing for special circumstances because he considered that the shares were worth more than the quoted price. Lord Reid stated at 731B as follows:

> “ Now I must turn to the interpretation of section 44 (3). As might be expected it takes the Stock Exchange quotation as reflecting market value in all normal cases. Stock Exchange prices are more liable than most open market prices to large and rapid fluctuations. But the taxpayer must take the risk of that unless there are "special circumstances." "Special" must mean unusual or uncommon - perhaps the nearest word to it in this context is "abnormal." I see no reason to exclude any kind of abnormality. "Rigging the market" was discussed in argument. This exception of cases where there are special circumstances must be intended to provide that a fair value is to be taken where they exist: generally a fair value could only be reached by inquiring what the market value would have been if the special circumstances had not existed. I think that that is what the section is contemplating when it says that in consequence of special circumstances the Stock Exchange quotation is not by itself a proper measure of market value. If it is not then some other measure must be found.”

199. The Respondents submitted that the arrangements were designed in large measure to facilitate the tax advantages to be derived from gifting shares to charity. The design included ensuring that there was a very significant uplift in the value of the shares between the price paid for the Subscription Shares and the flotation price. It was not suggested that there was any manipulation of the price on flotation, but that unusual lock-in arrangements were necessary to ensure that investors were not “out like rabbits” on flotation. Further, that the two stage subscription arrangement involving the Subscription Shares with a commitment to purchase the Placing Shares was also unusual.

200. I have made findings of fact in relation to the significance of gift relief on the flotation of FTG. In particular, I am not satisfied that the flotation as a whole was structured in order to obtain the tax advantages of gift relief. The evidence leads me to a conclusion that the transaction was not structured with the intention of giving an opportunity for gift relief to retail investors. The availability of gift relief was simply an incident of a successful flotation. It is inherent in the Respondents’ submission that the evidence of at least Mr Hughes and Mr Currie as to why they structured the transaction as they did was untrue. In my judgment the evidence does not justify such a finding.

201. I have found that the lock-in arrangements were unusual and were not in accordance with market practice at the time. I am satisfied that those arrangements at least contributed to a very illiquid market in the shares of FTG in which effectively only 1.2% of the shares were available to trade. In my view that is sufficient to amount to special circumstances. I must then consider as a matter of causation whether in consequence of that the price quoted in SEDOL would not in itself be a proper measure of market value. The price quoted on SEDOL for FTG shares on 28 July 2004 was derived from the dealings on that date. The circumstances in which those transactions took place and the volume of those dealings leads me to conclude that they do not give a proper measure of market value. In a more liquid market the dealings would have been a proper measure of market value. The unusual lock-in provisions contributed to the absence of liquidity. It is therefore a consequence of the lock-in that the price quoted is not a proper measure of market value.

Valuation Principles and the Valuation Evidence

202. Section 272(1) defines market value for present purposes as the price which Mr Netley’s shares might reasonably be expected to fetch on a sale in the open market. For that purpose section 273(3) requires it to be assumed that in the open market any prospective purchaser has available the information which a prudent prospective purchaser might reasonably require if he were purchasing the shares from a willing vendor, by private treaty and at arm’s length.

203. The following principles of valuation are not controversial:

(1) The sale is hypothetical. It is assumed that the relevant property is sold on the relevant day (see *Duke of Buccleuch v IRC [1967] AC 506* at 543 per Lord Guest).

(2) The hypothetical vendor is anonymous and a willing vendor, in other words prepared to sell provided a fair price is obtained (see *IRC v Clay [1914] 3 KB 466* at 473, 478).

(3) It is assumed that the relevant property has been exposed for sale with such marketing as would have been reasonable (*Duke of Buccleuch v IRC* at 525B per Lord Reid).

(4) All potential purchasers have an equal opportunity to make an offer (*re Lynall [1972] AC 680* at 699B per Lord Morris).

(5) The hypothetical purchaser is a reasonably prudent purchaser who has informed himself as to all relevant facts such as the history of the business, its present position and its future prospects (see *Findlay’s Trustees v CIR (1938) ATC 437* at 440).

204. The matters of valuation principle which are in dispute in the present appeal concern:

(1) The information available to the hypothetical prudent purchaser.

(2) The significance of experts taking different views as to the market value of the shares.

(3) The extent to which a subsequent comparable transaction can be taken into account.

205. I deal with items (2) and (3) below in the course of considering the expert evidence. At this stage I focus on the approach to be taken to the information available to the prudent purchaser. In *re Lynall*, the House of Lords identified that a sale in the open market would not involve release of any confidential information to prospective purchasers. The confidential information in that case included the fact that a flotation of part of the company’s capital was being considered. It was not to be taken into account in ascertaining the market value of the shares. A sale in the open market was contrasted with a sale by private treaty, where such confidential information might be available.

206. The House of Lords also identified that the most a reasonable director might do would be to disclose confidential information that could not possibly prejudice the interests of the company. Having said that, Viscount Dilhorne at least did not treat as

confidential information accounts of the company already prepared and awaiting presentation to the shareholders.

207. The Court of Appeal in *re Lynall* had held that it should be assumed that the prudent purchaser would make all reasonable enquiries and that he would receive true and factual answers to reasonable enquiries. Hence, information as to the flotation would have been available. The test was by reference to what a reasonable board of directors would disclose, and not what the particular board of directors would have disclosed.

208. It was the House of Lords decision in *re Lynall* which led to the introduction of what is now section 273, for shares which are not quoted on a recognised stock exchange. Section 273(3) provides that the prudent purchaser is to be assumed as having available all information which he might reasonably require from the vendor if the sale were a sale by private treaty.

209. The effect of section 273(3) and the context in which it came to be enacted were considered by Dr Brice, Special Commissioner in *Caton's Administrators v Couch [1995] STC (SCD) 34*. She concluded as follows:

> " …in my view, s 152(3) [now section 273(3)] is effective to provide that any information, including unpublished confidential information, and even information which might prejudice the interests of the company, is assumed to be available in the hypothetical sale if it would be reasonably required by a prudent prospective purchaser of the asset in question. It is therefore necessary to consider, in each case, what information a prudent prospective purchaser of the asset in question would reasonably require. In the context of s 152(3) I understand the word 'require' to mean 'demand as a condition of buying'; information is 'required' if the purchase would not proceed without it."

210. The question of what a prudent purchaser would reasonably require is essentially a value judgment, informed by the expert evidence. In *Caton's Administrators*, Dr Brice also had regard to an observation in *Dymond's Capital Taxes*. At page 51a Dr Brice stated as follows:

> " *Dymond*, para 23.328 also says that where the holding is less than 25% it may be that the buyer will expect less information but this is a matter for expert evidence. The size of the company is important and a buyer investing £200,000 would obviously be entitled to know more than one investing £2,000. Where the holding was small, say less than £50,000 and less than 5% of the capital, the buyer would not normally be expected to have more than the information which was published or which he could find out without questioning the directors."

211. I respectfully agree with the approach of Dr Brice. It is difficult to see why, in relation to a holding in an AIM company which is small both in terms of value and percentage, a reasonable board of directors would be concerned to reveal any information which was not otherwise public information.

212. I mention above Mr Firth's submission that in relation to FTG, section 273(3) has no effect on the information available for the purposes of valuation. As I

understand the submission, contained in Mr Firth's skeleton argument, price sensitive information available to a purchaser in the open market would be the same as that available in a sale by way of private treaty because the law against insider dealing applied to AIM shares. Neither of the experts addressed this point and in the event Mr Firth did not pursue the point in his closing submissions.

213. Mr Hughes said that if he had been asked by a prospective investor he would have provided profit and cashflow forecasts relating to FTG, including the Working Capital Report which he regarded as a very conservative estimate of future prospects. It is clear from the authorities however that the test is objective. It is not what a particular director or board of directors would have done at the time.

214. In relation to valuation I had the benefit of expert evidence from Mr David Houghton on behalf of the Appellant and Mr Michael Weaver on behalf of the Respondents. Both are chartered accountants and experienced valuers. Mr Houghton considered the open market value of the shares on the basis that section 273(3) applied. Mr Weaver considered the open market value of the shares on three bases: public information, full information and prudent buyer information. Prudent buyer information was on the basis of public information supplemented by information to be assumed pursuant to section 273(3). For the reasons given above, I am satisfied that it is the latter which is the appropriate basis to value the Company's shares in this appeal and I shall focus on the information which was available on that basis.

215. Both experts agreed that in considering what information was available, consideration had to be given to the size and influence of the holding, and to the cost of the investment. Mr Houghton accepted that the general view of valuers was that the information available in respect of small, uninfluential shareholdings with limited outlay is essentially public information.

216. The experts were agreed that the following company information would be available to the prudent purchaser:

(1) The July Prospectus.

(2) The February Prospectus.

(3) The Acquisition Agreement and the share sale and option agreement in favour of Mr Fraser and Mr Ashcroft to purchase the shares of John and Naomi Frenkel and Arrow Nominees.

(4) The financial results of FTL and FTSSL for the period 1 January 2004 to 28 July 2004.

217. The first three items were publicly available at the valuation date. The last item is to some extent surprising because it would only be available under section 273(3). Mr Netley's shareholding of 82,000 shares in FTG was modest. It was 0.18% of the Company's issued share capital and had cost just £10,000 a few weeks prior to the valuation date. It is not clear to me why it would be reasonable for the purchaser of a relatively small tranche of shares by way of private treaty to require such information, and why a reasonable board of directors would provide it. However both experts have

agreed it would be available and I shall proceed on that basis, notwithstanding Mr Firth's submission to the contrary.

218. The experts disagreed as to what further information would be available. Mr Houghton considered that the following information would also be available:

(1) The Baker Tilly Working Capital Report.

(2) The Baker Tilly Long Form Report.

(3) The agreement whereby WHI and the Company agreed that WHI would act as financial adviser and Nomad to the Company.

(4) The brokership agreement between WHI and the Company.

219. In the event there was very little of significance in the Long Form Report which Mr Houghton relied upon, and no basis was put forward to support its availability to the prudent purchaser. Further, the experts agreed that the existence and generic form of the agreements between WHI and the Company would be information available to the prudent purchaser.

220. The Working Capital Report contained detailed forecasts of the Company's future performance up to December 2006. It included forecasts of turnover, operating profit and cashflow based on assumptions in relation to increased business from the new Canada Life product, recruitment of two new consultants and from an increase in funds under management.

221. Mr Houghton considered that this information would be reasonably required by a prudent purchaser on the basis that the Company's shares were "growth shares". He relied on a Guidance Note in the HMRC Share Valuation Manual at SVM114040 which states as follows:

> " There will be cases where the size and cost of the investment may appear small but due to the nature of the investment any prudent purchaser would require further information and 'demand as a condition of buying'. An example of such an investment would be where the value is wholly dependent on the company achieving a growth target and where there is some provision for an early exit. Such arrangements are commonly called 'Growth Shares'. Clearly in such circumstances the growth prospects are intrinsic to the investment and no sale would proceed without access to additional information such as company forecasts."

222. Mr Houghton's evidence was that any investor looking to acquire shares in an AIM company would assume growth because AIM is generally a market for smaller, growing companies. Investors would therefore reasonably require the provision of growth forecasts prior to making an investment decision. In cross examination he retreated from such a general principle and limited such an approach to the particular circumstances of particular companies, especially at or about the time of flotation on AIM. He maintained that the approach would apply to shares in FTG because it was "a very immature business" with a very small market share and the ability to grow into that market. As such, in his report he considered that it was a "growth share".

223. Mr Houghton also relied on references in a book on valuation to support his view as to growth shares. An extract was produced just before the hearing commenced but it was notable that Mr Houghton seemed unfamiliar both with the author of the book and its title. Mr Gibbon's researches established that it was *The Dark Side of Valuation 2nd ed by Aswath Damodaran*.

224. It seemed from Mr Houghton's evidence in cross examination that he was not relying on any specific definition of "growth share", either by reference to the HMRC Share Valuation Manual or indeed any textbook definition. Rather he considered that each company had to be looked at by reference to its own particular circumstances. If the value of the shares depended upon growth then the prudent purchaser would require additional information as to the prospects of growth.

225. I am satisfied that the reference to growth shares in the Share Valuation Manual is to a particular type of share. Those are shares which obtain rights or are relieved of restrictions on the occurrence of some future event related to growth. The value of such shares is wholly or mainly defined by the occurrence of that event and therefore by the prospect of future growth. No-one would purchase such shares without having information about future growth prospects.

226. The July Prospectus said very little about the growth prospects of the Company. Mr Houghton's approach was that investors would require information as to its growth prospects before investing. That begs the question, if true, as to why such information was not provided in the July Prospectus, and yet the retail investors were prepared to buy the shares.

227. Both experts took an approach that the default position is that information as to future prospects is not available. There was no support for Mr Houghton's opinion that the shares of FTG were growth shares, either by reference to decided cases or to valuation practice. Mr Weaver was firmly of the view that FTG shares were not growth shares and that no information as to the future prospects of FTG would be available beyond that in the July Prospectus.

228. In the circumstances I consider that the default position applies. FTG's shares are to be valued on the basis of the information which the experts were agreed would be available to the prudent prospective purchaser. I do not accept Mr Houghton's view that any additional information would be available. On that basis, Mr Houghton valued the shares at 42p per share as at 28 July 2004 and Mr Weaver valued the shares at 6.6p. There is clearly a considerable divergence between the two valuations and I shall explore below the reasons for that divergence.

229. Mr Firth submitted that in ascertaining the open market value of FTG shares one was seeking to identify the highest price a purchaser would pay for the shares. In the case of two experts who take a different view as to the prospects and value of a company, unless one takes an unreasonable view it is the more optimistic view that will prevail. He described that as a logical conclusion from the fact that it is the highest bidder who gets the prize.

230. I do not consider that is the right approach to expert evidence on valuation. The experts are not saying what they would pay for the shares if they were a prospective purchaser. Their evidence is directed to what, in their reasoned opinion, the hypothetical prudent purchaser would pay based on the information available. The market value is a single price, ascertained through a process of valuation. Mr Firth's approach seeks to place a burden on HMRC to satisfy the tribunal that the Appellant's expert has been unreasonable. In my view there is no justification for such an approach. The ultimate question based on all the evidence, including that of both experts, is what the hypothetical prudent purchaser would pay in the open market.

231. Both expert reports contained certain errors and omissions. Where errors were identified I have discounted them for the purposes of this decision. Further, whilst I have had regard to the opinions expressed by Mr Weaver and Mr Houghton, it is the underlying evidence referred to in their evidence which is more significant.

232. Mr Houghton's valuation took into account the following matters:

(1) The admission price of 48p per share and WHI's role as the Nomad on admission of the shares to AIM. He considered this was corroborated by dealings in the shares over the 12 months following admission at an average price of 42.6p per share.

(2) A comparable transaction on admission to AIM on 11 March 2005 of Brooks MacDonald plc, an asset management and private client advisory group. He used a multiple of earnings before interest and tax from the transaction to give a price for FTG of 31.5p per share, or 50.3p per share after various adjustments were made.

(3) A discounted cashflow ("DCF") exercise using the results for y/e 31 December 2003 and forecasts from the Working Capital Report for 2004, 2005 and 2006. These were adjusted to give net cashflows for five years from 1 July 2004 and making various assumptions as to the required rate of return gave a net present value of those cashflows. This was then adjusted to reflect a premium for the fact the shares were admitted to AIM, giving a value of 38.9p per share.

(4) The issue of JBS Shares at a price of 17.5p per share. He considered this to be a sale of shares in FTL and FTSSL whilst in a distressed situation. The businesses had a combined balance sheet at 31 December 2003 showing net liabilities of £471,000 and there were PAYE arrears of £325,000, derived from the Long Form Report. The Working Capital Report showed that the business' cash requirements would exceed their banking facilities in each month between June 2004 and October 2004.

(5) The sale by Mr Frenkel of 16.6% of the shares in FTL and FTSSL for £600,000, equating to 7.93p per share. He considered this reflected the fact that FTL and FTSSL were in a distressed situation.

233. Mr Houghton did not place any reliance in his report on the price indicated in the Acquisition Agreement. He accepted that it was an arm's length transaction but considered that the business was close to insolvency at the time of the transaction. As

a result the Vendors had a weak bargaining position. However he accepted that there was no evidence as to the Vendors' other resources or the availability to the Vendors of other deals.

234. Mr Houghton considered that the most compelling evidence was the comparable transaction with and without adjustments, the DCF and the admission price. The average of these prices was 42.17p. He discounted this for the effect of a 2 year lock-in giving a value of 38.97p per share. Mr Firth conceded however that such a discount was not appropriate because the lock in was personal to Mr Netley and did not attach to the shares.

235. In considering Mr Weaver's evidence I shall focus on his valuation based on prudent buyer information. Mr Weaver's approach to valuing the shares was based on identifying historic p/e ratios. In the absence of prospective forecasts he used historic profits after tax of £302,496 for y/e 31 December 2003 for FTL and FTSSL as a proxy for maintainable earnings. Mr Weaver placed particular reliance on the following matters:

(1) The Acquisition Agreement for 66.2% of FTL and FTSSL on 28 July 2004 implied a share price of 8.5p per share and a p/e ratio for the Company's shares of 11.2. This was based on the value of £2,248,250 attributed to that interest in the Acquisition Agreement for which 26,450,000 shares were issued, with maintainable earnings of approximately £200,000, being 66.2% of £302,496.

(2) The benefit of the share sale agreement whereby the Company acquired 16.6% of FTL and FTSSL for £600,000. Pro rata this suggests that a 100% interest would be worth £3,614,458, equating to a p/e ratio of 11.9 for the whole business based on maintainable earnings of £302,496. Mr Weaver and Mr Houghton went on to calculate a share price of 7.9p, dividing £3,614,458 by 45,599,614 shares. This assumes that FTG exercised its option over the remaining 17.2% of the shares in FTL and FTSSL and that there was no intrinsic value in the option, although those assumptions were not stated.

(3) A p/e ratio of 13.0 by reference to comparable companies in the FTSE Actuaries Speciality and Other Finance Index as at 28 July 2004.

(4) A p/e ratio of 14.0 by reference to the BDO Private Company Price Index for Q2 2004.

(5) Mr Weaver did not consider the issue of the JBS Shares at 17.5p to be representative of the market value at that time because JBS's investment decision could have been motivated by other strategic considerations.

(6) The weighted average price paid by the retail investors for Subscription Shares and Placing Shares was 14.2p per share. In his reports Mr Weaver did not consider that this represented a good indication of market value as at 28 July 2004. As appears later, he changed his view as to the significance of this information.

(7) The price at which shares were traded on AIM on 28 July 2004 did not amount to significant evidence of market value on that date because such a small number were traded.

236. Mr Weaver accepted that a company with higher growth prospects than another company would tend to have a higher p/e ratio, other things being equal, and therefore a higher share price.

237. Taking those matters into account, together with the operating losses and profits in 2001-2003 and in the 7 months to 28 July 2004, Mr Weaver considered that an appropriate p/e ratio was 10.0. He applied that to the maintainable earnings of £302,496 giving a value of 6.6p per share. The existence of the loss for the 7 months to 28 July 2004 was a significant factor in discounting the p/e ratio and the share price.

Principal Areas of Disagreement between the Experts

238. Both experts produced supplementary reports following service of their initial reports. A number of areas of disagreement were identified.

239. Mr Houghton did not consider that the BDO PCP Index was a reliable comparator. It was based on private company transactions which could be distorted for various reasons. It also covered a large cross section of business sectors, types and sizes of businesses. At best he considered it might show a trend and indicate market sentiment. Similarly use of the FTSE Actuaries Speciality and Other Finance Index was not a reliable comparator because it did not reflect the growth potential of smaller companies.

240. Mr Weaver's opinion was that in the absence of the Working Capital Report it is not possible to carry out a DCF exercise, although he did attempt one on the basis of full information. Mr Houghton accepted that without the Working Capital Report it was not possible to carry out a DCF.

241. Further, in Mr Weaver's opinion it is not possible to take into account Brooks MacDonald plc as a comparable transaction because it was not announced until 7 months after the valuation date. He considered that Mr Houghton gave too much weight to the market deals in the Company's shares on the valuation date and gave no or insufficient weight to the terms of the Acquisition Agreement, the results for the 7 months to 28 July 2004 and p/e ratios derived from listed and private company indices.

242. The divergence in the opinions of Mr Houghton and Mr Weaver arises principally from differences as to:

(1) the information available to the prospective purchaser;

(2) the weight to be attached to the flotation price, given the involvement of WHI as Nomad;

(3) the relevance of the comparable transaction in shares of Brooks MacDonald;

(4) The weight to be attached to p/e ratios derived from the two indices relied on by Mr Weaver; and

(5) the weight to be attached to the terms of the Acquisition Agreement.

243. I should add that neither expert regarded the purchase of the JBS shares as being a reliable indicator of market value, although for different reasons. Mr Houghton because FTL and FTSSL were in a distressed state at the time of the transaction and Mr Weaver because there may have been other strategic considerations for the transaction.

244. In relation to the available information, Mr Houghton proceeded on the basis that the Working Capital Report and the Long Form Report would be available. He did not take into account details of the Acquisition Agreement or the trading results for the 7 months to 28 July 2004.

245. I have found that the Working Capital Report was not information which would be deemed to be available to the prudent purchaser. It was therefore not possible to carry out any meaningful DCF. Mr Weaver criticised the basis on which Mr Houghton had carried out his DCF exercise and in turn was subject to criticism of his own approach in cross examination. In the light of my finding that it is not possible to carry out a meaningful DCF on the basis of the information assumed to be available I need not consider those criticisms further.

246. Mr Houghton stated in cross examination that if he could not do a DCF and could not use Brooks MacDonald as a comparator, then there was still the flotation price, supported by the involvement of WHI. It was only in the absence of any such evidence that it would be necessary to do some exercise based on p/e ratios derived from quoted companies or indices.

247. I have made findings of fact in relation to the role of a Nomad in valuations for the purpose of an admission to AIM. It is important to note that HMRC do not suggest that that there was anything in the way in which the various transactions proceeded that was in any way dishonest, or a breach of any market rules. I consider that whilst some weight is to be attached to the fact that WHI acted as Nomad on the flotation, less weight is to be given to it than that attributed by Mr Houghton. Mr Houghton also used as a cross-check the fact that there were trades on AIM in the period from 28 July 2004 to April 2005 at prices between 40p and 48p. That information was not available at the date of valuation and in any event in my judgment it demonstrates a very thin market on which little reliance can be placed.

248. Mr Firth relied upon the actual trades recorded in FTG shares on 28 July 2004. He said that was direct evidence of the value of the shares and that it was not necessary for me to go any further by way of expert evidence. For the reasons I have set out in relation to special circumstances I am not satisfied that any weight can be given to those dealings.

249. The value proposed by Zeus and accepted by WHI as well as the directors of the Company was not subject to a robust valuation process. It is apparent that no exercise equivalent to that undertaken by Mr Houghton and Mr Weaver was undertaken at the time of the placing. In the light of all the evidence I have no reason to doubt that the valuation was sufficient for the purposes of admission to AIM, but it is not sufficient for purposes of this appeal.

250. Mr Houghton maintained that the terms of the Brooks Macdonald flotation was evidence that could be taken into account. He considered that as a business it was "incredibly closely aligned" to the Company and was evidence of "market sentiment" at the valuation date. He said that if it is not used, there is very little to fall back on by way of evidence to support a valuation.

251. Mr Weaver's evidence was firmly that information as to the sale of Brooks MacDonald was not to be taken into account, either as a comparable or as an indicator of market sentiment at the valuation date. He indicated that various international valuation standards bodies regarded that as a generally accepted principle, although there was no equivalent in the UK at the moment. He regarded it as a matter of valuation practice. I accept that is the case in relation to comparables which seems to me to be a logical result. It was not information that was available at 28 July 2004. Mr Houghton could point to no guidance or valuation practice that would support his reliance on Brooks MacDonald. Indeed in *re Holt [1953] 1 WLR 1488* Danckwerts J stated that "*it is necessary…firmly to reject the wisdom which might be provided by the knowledge of subsequent events*".

252. In *Buckingham v Francis [1986] 2 All ER 738* the court was concerned with valuing a company with high returns but little or no assets. It arrived at a valuation based on p/e ratios but speculated whether when businessmen are deciding on a price "*business acumen or hunch does not play a far larger part than the calculations of accountants*". That is in line with Mr Currie's observations that valuation is an art and not a science. Staughton J set out various principles of valuation including at p740a:

> " The company must be valued in the light of facts that existed at [the valuation date]. (Little or nothing turns on the question whether facts which existed but were not then ascertained or ascertainable should be taken into account.) But regard may be had to later events for the purpose only of deciding what forecasts for the future could reasonably have been made on [the valuation date]"

253. It may be that the last sentence was referring to matters such as "market sentiment". I can see that market sentiment might be bullish, bearish or neutral as to the prospects for fund management companies on the valuation date. I can further see that evidence after the valuation date may be taken into account so that the market sentiment, which is public information, can be attributed to the prudent purchaser. However, evidence relied on by the Appellant as to the Brooks MacDonald transaction goes well beyond market sentiment. I do not consider that knowledge of the Brooks MacDonald transaction is to be attributed to the prudent purchaser, or that it says anything about the market sentiment for fund management companies at the valuation date.

254. Mr Weaver relied on the p/e ratio of 13.0 for companies in the FTSE Actuaries Speciality and Other Finance Index as at 28 July 2004. He regarded these companies as the most comparable to the Company and evidence as to p/e ratios suggested that the larger the company the higher the p/e ratio. In fact it turned out that the relationship was more complicated than that, and that Mr Weaver had not stripped out exceptional items which affected the calculation of p/e ratios. I do not accept that those companies are really comparable to FTG. These were much larger diversified companies with market capitalisations between £100 million and £1.8 billion. Mr Weaver suggested that these were the best comparables. He may be right, but I am not satisfied that they offer a good comparison to FTG because of undoubted differences in size, including funds under management, and more importantly the lack of any quantitative evidence about comparative growth prospects. The evidence available as to the growth prospects of FTG contained in the July Prospectus was only qualitative. Mr Weaver suggested that the alternative was to use p/e ratios from AIM companies, but that there were no financial services companies on AIM at the valuation date.

255. The BDO PCP index relied on by Mr Weaver has significant limitations in the present exercise. In particular it is not sector specific and there is no information as to what transactions are included within it. Also it is based on private company transactions rather public company transactions, so will involve a discount for lack of marketability. Mr Weaver accepted that he had never used it to value a public company before, principally because with public companies there would be other more reliable evidence available. It was however a measure of the value of smaller companies. I accept that it is a relevant metric, but in my judgment because of those limitations it has little weight in the context of the present valuation exercise. Further it relates to private companies, and therefore involves a discount when compared to public companies. It also represents the value of a 100% interest, and therefore commands a premium compared to the valuation of a minority interest. Mr Weaver suggested that these two factors cancelled one another out, but it seems to me that such an approach involves too broad a brush.

256. Mr Firth submitted that Mr Weaver's reliance on the transactions covered by the Acquisition Agreement was wrong, principally for the following reasons:

(1) The shares in FTL and FTSSL were in private companies whereas FTG was a public company.

(2) The sale of 66.2% of FTL and FTSSL was a share for share exchange and Mr Weaver was wrong to rely on a nominal consideration of £2,248,250 identified in that agreement.

(3) That transaction was for a majority stake which implied a value for the combined business less than the share sale price for 16.6% of the shares which was for a minority stake. He submitted it was implausible that a minority interest could command proportionately more than a majority interest.

(4) At the time of those transactions the businesses were in a distressed state, whereas on flotation the business was not in a distressed state.

(5) Nothing was known about the relative bargaining positions of the parties.

257. In the circumstances Mr Firth submitted that these transactions should not be given any weight in the valuation exercise. Alternatively, he suggested that significant adjustments were required to the p/e ratios calculated by Mr Weaver.

258. Mr Weaver clearly accepted in cross-examination that the valuation of a minority interest in a private company involved a discount from the value of the same interest in a publicly quoted company. The discount arises because there is a lack of marketability in the case of an interest in a private company. His evidence was that it was rare for the discount to be more than 25%, but details of an academic study which was in evidence suggested a mean discount of 50%.

259. Mr Weaver also accepted in cross examination that where he had identified a value of 8.5p per share, based on the value attributed in the Acquisition Agreement to a 66.2% interest in the business, that was the value of the business as a private company and not as a public company. Similarly in relation to the call option for a 16.6% interest. If Mr Weaver's p/e ratio of 11.9 derived from the 16.6% transaction is adjusted to reflect a 50% discount the p/e ratio for a public company would be approximately 24.

260. This criticism of Mr Weaver's evidence based on the distinction between the p/e ratio of private and public companies was not a point that had been raised by Mr Houghton. Mr Firth acknowledged that it was a point raised for the first time in cross-examination. Mr Weaver was therefore dealing with the issue without warning. Mr Gibbon submitted that it was "an abstract mathematical exercise … without the support of an expert". Further it ignored the fact that the parties to the Acquisition Agreement had placed a value of £2,248,250 on 66.2% of the business. There is force in that submission and it echoes criticisms made by the deputy High Court Judge in *Smith v Tesco Plc & Royal Free London NHS Foundation Trust [2016] EWHC 3252 (QB)* who said:

> " It defeats the purpose of exchange of expert evidence and joint discussions between experts if experts raise new theories shortly before trial."

261. The observation applies with greater force to a new approach advocated not by an expert but by counsel without the support of an expert report. There is potential unfairness not only to Mr Weaver as an expert witness but also to counsel having to deal with the point and re-examine with little or no notice. Having said that Mr Weaver's cross-examination lasted two days in all and he did have an opportunity to consider the point raised by Mr Firth overnight. In the light of Mr Weaver's evidence I am satisfied that the p/e ratio derived from the Acquisition Agreement should be adjusted to 24 to reflect the fact that FTG was a public company.

262. Mr Firth cross-examined Mr Weaver on the basis that it was necessary to gross up the p/e ratio of 24 calculated above on the basis that FTL and FTSSL were in a distressed state at the time of the transaction to give a p/e ratio of 42 for the business in an undistressed state at flotation.

263. Both Mr Firth and Mr Weaver produced examples as illustrations as to the effect of the businesses being in a distressed state. Effectively Mr Firth's point was a simple one, even if his examples and the cross-examination based on those examples were far from straightforward. His point as I understand it was that £2,248,250, even if it was negotiated, reflected the fact that the owners of FTL and FTSSL were in a weak bargaining position, or at least may have reflected that fact. Mr Weaver did not accept that any adjustment was necessary.

264. Mr Firth produced a calculation which gave a share price of 28p based on that p/e ratio, calculated as 42 x £302,496 (maintainable earnings) / 45,599,614 (shares in issue). It was not suggested that any adjustment was necessary to take into account the assets or liabilities of FTG. Mr Firth justified his calculation on the basis that it was an approximation and neither party had sought to value the call option over the 17.2% of shares in FTL and FTSSL that FTG did not own. He suggested that taking 100% of the maintainable earnings balanced the fact that no value had been attached to the call option. That was also the implicit approach adopted by Mr Weaver and Mr Houghton and I too shall adopt it.

265. However, I am not satisfied that it is appropriate to make any adjustment to the p/e ratio to reflect the fact that FTL and FTSSL were in a distressed state. The transaction involved a sale of the shares in FTL and FTSSL. Making an adjustment assumes that the shareholders of FTL and FTSSL had no access to alternative funding and were in a weak bargaining position.

266. I do not consider that there is any reliable evidence, still less any public information, to support a conclusion that the sale of the 16.6% holding was the result of a weak bargaining position on the part of Mr Frenkel. Nor that the Vendors were forced sellers in relation to their 66.2% holding. The available information does not indicate anything about their bargaining position. In the circumstances of this case where the available information is limited, I consider that these transactions are to be taken into account and given some weight, albeit with the caveat that nothing is known about the relative strength of the bargaining positions.

267. Mr Firth suggested that the consideration of £2,248,250 identified in the Acquisition Agreement was not necessarily a negotiated figure. He submitted that the percentage shareholding in the Company that the vendors would receive would have been more important to the parties negotiating the Acquisition. Mr Weaver maintained that both parties would have a view as to the value of the underlying business going forward and there was no reason to doubt the figure included in the Acquisition Agreement as a negotiated figure.

268. In support of his submission that the consideration was not an important figure, Mr Firth compared the share sale agreement whereby the Company purchased on the same day a further 16.6% of FTL and FTSSL for £600,000. That implied a value of the businesses of £3.6m whereas the sale of 66.2% for £2,248,250 implied a value for the businesses of £3.4m. Mr Firth suggested that it was implausible that Mr Frenkel would be able to negotiate a higher price per share than the Vendors for their majority holding. I do not accept that it is implausible. The comparison is between transactions

involving different parties who may have different views as to valuation and different bargaining positions.

269. Mr Weaver did not place reliance on the JBS transaction because of the existing and continuing business relationship between JBS and the Company. I accept that no information is known about that business relationship and how it might impact on the price paid for the shares. However, in the absence of very much more reliable information available to a prudent purchaser I do consider that it carries some weight. I do not consider that Mr Houghton is right to ignore it altogether because the business was distressed at the time of the transaction, when nothing is known as to the relative bargaining positions of the parties and the shareholders.

270. Mr Weaver did not take into account the role of WHI as a Nomad, in particular in relation to valuation. It was not disputed that WHI, as Nomad, had access to the Working Capital Report. That fact would have been public information even if the content of the report was not. I have found that the Nomad had a duty to consider valuation as part of considering whether the Company as appropriate for AIM. Mr Weaver accepted in cross-examination that some reliance could be placed on the presence of the Nomad, but not "exclusive reliance". In light of the duties of WHI as Nomad, Mr Weaver also changed his view as to the relevance of the weighted average price paid for shares by the retail investors.

271. I accept that weight should be placed on the involvement of WHI as Nomad, together with the existence of their limited duty in relation to valuation. I do not consider that the dealings on 28 July 2004 add any weight given the nature and extent of those trades. Mr Firth argued that the willingness of Winterflood, the market maker, to pay 48p per share meant that the highest offer in the open market would be 48p. I do not accept that submission in the context of a valuation of 82,000 shares. In particular I am not satisfied that it follows that Winterflood would have paid 48p for a holding that size.

272. It appears that the operating loss in the 7 months to 28 July 2004 was at least in part due to FTSSL being unable to write new business because it was waiting for the new Canada Life product to come on stream. That knowledge derives from the Working Capital Report which is not available to the prudent purchaser. Having said that, it was put to Mr Weaver that the fact FTSSL was unable to offer settlement products until the Canada Life product came on stream in September 2004 would have been public information because that must have been what prospective clients were told. However there was no material from which the prudent purchaser could assess what effect FTSSL being unable to write new business might have had on the results for the 7 months to 28 July 2004 or on the future prospects of the business of FTSSL. In those circumstances it seems to me that the loss of £231,345 for the 7 months to 28 July 2004 does carry weight in the valuation exercise. Information as to the amount of the loss was available, and whilst there were possible explanations there was no definitive explanation for that loss. The absence of any clear explanation would give rise to risk which would lead to a discount in the price a prudent purchaser would pay.

Decision on Valuation

273. To put the competing share prices into perspective, the market capitalisation of FTG derived from the various share prices identified would be as follows:

Share Price (p)	**Source**	**Market Capitalisation (£m)**
6.6	Mr Weaver based on a p/e ratio of 10	3
8.5	Acquisition Agreement	3.9
14.2	Weighted average paid by Mr Netley	6.5
17.5	JBS Shares	8.0
42	Mr Houghton based on admission price, DCF and comparable	19.2
48	SEDOL – 28 July 2004	21.9

274. I was also told during the evidence that the share price in SEDOL for shares in FTG on 20 September 2016 was 62p, but had gone as low as 14p in the interim. Counsel did not suggest this was relevant evidence that I could take into account as to the value of the shares on 28 July 2004 and I discount it completely.

275. I consider that the most relevant information for the purposes of valuation, taking into account my discussion in relation to the available information, is as follows:

(1) The retail investors had invested a weighted average of 14.2p per share with the prospect of an uplift on flotation. They committed to doing so without knowing the target company or the other information available after 2 June 2004. They knew that Zeus was promoting the Company, and that Zeus and the people behind Zeus had a successful track record of floating companies which had potential for growth.

(2) The Company had a recent history involving losses and profits for the years 2001 to 2003 together with losses for the 7 months to 28 July 2004. The explanation for the latter loss was not clear but it may have arisen because FTSSL was between products and unable to write new business. Despite this Zeus clearly considered that there were prospects for growth and in early 2004 FTSSL was a market leader in structured settlements, the market for which was likely to increase.

(3) P/e ratios derived from the transactions covered by the Acquisition Agreement for 66.2% and 16.6% of the shares of FTL and FTSSL were 11.2 and 11.9. These should be adjusted to approximately 22 and 24 to reflect the fact that FTG was to be a public company. Those p/e ratios imply a share price of 14.6p and 15.9p respectively based on 100% of maintainable earnings, although nothing was known as to the relative bargaining positions of the parties.

(4) The JBS Shares were allotted at 17.5p very shortly before the flotation, without knowing what effect the relationship between JBS and FTL/FTSSL might have had on the price for that deal.

(5) The flotation price of 48p per share, knowing that WHI as Nomad had a duty to AIM to ensure that FTG was an appropriate company for flotation which involved a duty to consider valuation but without undertaking a robust valuation exercise.

276. Share valuation is in many respects an art not a science and in some cases has been described as "intelligent guesswork". Doing the best I can, I consider that a reasonably prudent purchaser with the information available might reasonably be expected to pay 17.5p per share on the open market on 28 July 2004.

Conclusion

277. For all the reasons given above I am satisfied that the market value of Mr Netley's shares on 28 July 2004 was 17.5p per share. To that extent the appeal is allowed. I have set out above the basis and principles which I have applied in arriving at that valuation.

278. This document contains full findings of fact and reasons for the decision. Any party dissatisfied with this decision has a right to apply for permission to appeal against it pursuant to Rule 39 of the Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules 2009. The application must be received by this Tribunal not later than 56 days after this decision is sent to that party. The parties are referred to "Guidance to accompany a Decision from the First-tier Tribunal (Tax Chamber)" which accompanies and forms part of this decision notice.

JONATHAN CANNAN
TRIBUNAL JUDGE

RELEASE DATE: 26 MAY 2017