[2022] UKFTT 00039 (TC)

TC 08391/V

INCOME TAX AND CORPORATION TAX – disposal of a business to a group company – ascertaining market value – intangibles relief – whether payment was a distribution – substitution of market value under Schedule 29 FA 2002 - held – valuation of assets actually transferred was £1 – no chargeable gain realised on disposal – no distribution – market value required to be substituted for purposes of intangibles relief – appeal of first appellant allowed – appeal of second appellant dismissed

FIRST-TIER TRIBUNAL
TAX CHAMBER

Appeal number: TC/2017/01653
TC/2017/01659

BETWEEN

JASPER ALEXANDER THIRLBY CONRAN (1)

JC VISION LTD (2) **Appellants**

-and-

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

TRIBUNAL: JUDGE JEANETTE ZAMAN
JULIAN STAFFORD

The hearing took place on 3 to 10 November 2021. With the consent of the parties, the form of the hearing was a video hearing on the Tribunal video platform. A face to face hearing was not held because of the ongoing restrictions from the COVID-19 pandemic. The documents to which we were referred are described in the decision notice. Prior notice of the hearing had been published on the gov.uk website, with information about how representatives of the media or members of the public could apply to join the hearing remotely in order to observe the proceedings. As such, the hearing was held in public.

Alun James, counsel, instructed by BHG Chartered Accountants, for the Appellants

Sadiya Choudhury, counsel, instructed by the General Counsel and Solicitor to HM Revenue and Customs, for the Respondents

DECISION

INTRODUCTION

1. The appeals of Jasper Alexander Thirlby Conran ("JATC") and JC Vision Ltd ("JCV") arise in the context of the transfer of a business in 2008 by Jasper Conran Optical LLP ("JCO") to JCV. That transfer was effectively the incorporation of the business which had been commenced by JCO in 2007. The consideration for the transfer was £8.25 million.

2. JATC, the majority partner in JCO, brought his share of the proceeds into account as a capital gain, paying CGT of £1,400,464, and JCV treated the consideration paid as an expense which was amortised in its accounts and claimed relief for such amounts under the intangibles regime (which was then in Schedule 29 Finance Act 2002 ("FA 2002")) for the accounting periods ended ("APEs") 31 March 2009 to 31 March 2014.

3. HMRC amended JATC's self-assessment tax return for the tax year 2008-09 by means of a closure notice issued on 8 September 2016, which recorded HMRC's decision that the valuation used had been overstated, the correct figure was nil and the £8.25 million paid to JATC should be treated as a distribution.

4. HMRC amended JCV's corporation tax self-assessment returns for the APEs 31 March 2009, 31 March 2010 and 31 March 2011 pursuant to closure notices issued on 8 September 2016. The closure notices recorded HMRC's decision that there was no debit to be brought into account as the market value of the intangible is nil. HMRC also made consequential amendments to JCV's corporation tax self-assessment returns for the APEs 31 March 2012, 31 March 2013 and 31 March 2014.

5. The issues are described further below. If we accept that the market value of the business transferred to JCV was £8.25 million, the Appellants' appeals succeed. If we conclude that the value is £1 (which is the position now taken by HMRC, rather than nil as set out in the closure notices), the outcome depends on our further conclusions as to the application of the distributions rules (for JATC) and the intangibles rules (for JCV). We have concluded that the market value of the assets actually transferred to JCV was £1, such that JATC did not realise a chargeable gain upon the disposal by JCO. Furthermore, the £8.25 million which had been paid by JCV is not a distribution within the distributions legislation. However, JCV is not entitled to intangibles relief on the £8.25 million which it paid to JCO.

FACTS

6. The parties have prepared a Statement of Agreed Facts (the "SAF") which is set out in the Appendix hereto. The SAF includes some information in relation to the transactions which were undertaken and outlines HMRC's enquiry and the progress of this appeal.

7. We make the additional findings of fact set out below, some of which overlap with matters agreed in the SAF.

8. JATC is the sole shareholder of Jasper Conran Holdings Ltd ("JCHL"), which is the holding company of various companies. JCV is a 100% subsidiary of JCHL.

Jasper Conran Optical LLP

9. JCO was formed on 28 June 2007 with two members, JATC and JC Eyewear Limited ("JCE"). JATC was the sole shareholder of JCE.

10. The LLP Members Agreement dated 14 October 2008 refers to JCO as carrying on the Business, which is defined therein as "entering into operating arrangements with Specsavers International Healthcare Limited in respect of the design, manufacture and marketing of optical products".

11. According to Schedule 2 of that agreement, JATC had a 99.9% share of JCO with the remaining 0.1% held by JCE. JATC contributed capital of £999 and had a profit share of 99%, and JCE contributed capital of £1 and had a profit share of £1. JATC thus had an entitlement to 99.9% of any gains of a capital nature and 99% of other profits.

Licence Agreement from JATC to JCO

12. On 3 September 2007, JATC granted to JCO a non-exclusive licence to sub-license the Trade Marks (as defined) in relation to the Optical Products (as defined) to Specsavers in accordance with the terms of the OPLA (as defined below) (the "JCO 2007 Licence").

13. The JCO 2007 Licence is deemed to have come into force on the commencement date of the OPLA and is royalty-free.

Optical Products Licence Agreement with Specsavers

14. On 3 September 2007, JCO entered into an Agreement for an Optical Product Licence (the "OPLA") with Specsavers International Healthcare Ltd ("Specsavers").

15. The recitals refer to JCO as being licensed to use the Trade Marks, that Specsavers is a leading retailer in the field of Optical Products and that:

> "(C) The Parties have agreed to work together to produce Designs…and that JCO shall provide a licence to [Specsavers] to use the Trade Marks to enable [Specsavers] to manufacture, market and sell the Branded Products…".

16. Key definitions in Clause 1 of the OPLA were as follows:

> ""Designs" were defined as "…the designs…created by the Parties cooperating together defining the general appearance, size, shape and decoration of the Branded Products, but excluding always the Trade Marks;"
>
> "Branded Products" were defined as "…any Optical Products created from a Design and/or bearing the Trade Mark which has been approved by JCO in accordance with Clause 5 hereof;"
>
> "Optical Products" were defined as "…spectacle frames, packaging for cases, cases and cleaning cloths but excluding always sunglasses;"
>
> "Trade Mark" was defined as: the registered trade marks set out at Part 1 of the Schedule hereto and/or the name "Jasper Conran;""

17. The registered trademarks in Part 1 of the Schedule were the trademark "Jasper Conran" registered in the European Community and the same trademark for which registration had been applied for in Norway and Guernsey at the time of the OPLA.

18. The Term of the OPLA was from the Commencement Date of 3 September 2007 to 7 March 2012, and the Territory was defined as the territories of the UK, Ireland, the Channel Islands, the Isle of Man, the Netherlands, Sweden, Norway, Denmark, Spain and such additional territories as might be agreed by the parties from time to time.

19. Clause 2.1 of the OPLA stated:

> "The Parties shall work together to create the Designs for the Branded Products. The Licensee acknowledges and agrees that the number of SKUs to be comprised in the Designs for the launch shall not be less than twenty-four…".

20. Specsavers was responsible for the manufacture, marketing and sale of the Branded Products. Clause 3.2 set out various targets for the quantities of Branded Products to be delivered to warehouses, which target increased each year.

21. Clause 4.1 of the OPLA provided:

> "In consideration of the payment of the Licence Fees…JCO hereby grants to the Licensee during the Term a non-exclusive, non-transferable licence to use the Trade Marks to manufacture, have manufactured and sell the Branded Products either to (i) the Authorised Retailers or (ii) directly to consumers…and to market, promote and advertise the Branded Products and produce Marketing Material in the Territory subject always to the terms of this Agreement."

22. Clause 5 provided that the parties shall consult to agree the terms and scope of the designs, and contains various conditions to ensure quality of the Branded Products.

23. Clause 8.1 provided that Specsavers shall pay to JCO £5 per unit of the Branded Product (except cases, packaging for cases and cleaning cloths), ie frames, manufactured and delivered, this being the Licence Fee.

24. JCO's obligations were set out in clause 10, and at clause 10.3:

> "JCO warrants to the Licensee that it is entitled and shall remain entitled throughout the Term, to grant the rights referred to in clause 4 above and that as far as JCO is aware such grant will not infringe the design right, copyright, trademark or other right of any third party."

25. Clause 17 provided that neither party was entitled to assign the benefit of the OPLA or its obligations thereunder without the prior written consent of the other party, but JCO was entitled to assign the agreement to any member of the JC Group (defined as any company or entity owned or controlled by JATC) without Specsavers' consent.

26. The OPLA was amended on 2 September 2008. The amendments included extending the Term to 31 August 2013, extending the Territory, increasing the number of units of the Branded Products to 48 (such number having previously been increased from 24 to 36 in accordance with the OPLA) and reducing the Licence Fee to £4.50 per frame delivered. The letter amending the OPLA also referred (at clause 9) to JCO's intention to assign the OPLA to JCV and stated that JCO would be entitled to assign the letter to a group company on providing written notice to Specsavers.

Licence to group entities

27. A letter dated 29 July 2008 from JATC to JCHL was said to be for the benefit of all of the JC Group (the "July 2008 Licence").

28. The July 2008 Licence stated that JATC "retain[s] all rights … to the Trade Marks and to any goodwill subsisting therein". It defined "Trade Marks" as those set out in the Schedule to the letter and any trademarks which had existed previously or would be applied for by JATC in the future.

29. Under the July 2008 Licence, JATC agreed to grant licences of the Trade Marks to all of the JC Group (and acknowledged that previous such licences had been granted by JATC) where he deemed it appropriate to do so having regard to the commercial arrangement to be entered into by JCH or any member of the JC Group to exploit the Trade Marks and on the basis that sub-licensing may be permitted on a case-by-case basis.

30. The party to which a licence was granted would pay JATC such sums as may be agreed between them in respect of the grant.

Business Transfer and Novation Agreement

31. On 31 October 2008, JCO entered into a Business Transfer and Novation Agreement ("BTNA") with JCV. The Effective Date of the BTNA was 4 September 2008.

32. The recitals to that agreement record:

"(A) The Vendor carries on the Business…

(B) The Vendor wishes to sell and the Purchaser wishes to purchase the Business with a view to carrying on the Business as a going concern in succession to the Vendor…".

33. Under clause 2.1, the Vendor, JCO, sold and the Purchaser, JCV, purchased the following:

"…with a view to the Purchaser carrying on the Business from the Effective Date as a going concern in succession to the Vendor:-

2.1.1 the benefit (subject to the burden) of the Contract;

2.1.2 the Goodwill;

2.1.3 the Marketing Information;

2.1.4 all records and other documents relating exclusively to the Business."

34. The relevant definitions were as follows:

""Assets" means the several assets to be sold by the Vendor to the Purchaser under this Agreement and described in clause 2;

"Business" means the Vendor's business relating to the operation of the Optical Product Licence Agreement;

"Contract" means the OPLA;

"Goodwill" means the goodwill and all of the intellectual property of the Business with the exclusive right to carry on the Business in succession to the Vendor; and

"Marketing Information" means all information relating to the supply of any products or materials to the Business and to the marketing of any products or services supplied by the Business.""

35. Under clause 3, JCO novated and transferred to JCV all of its rights, obligations and liabilities under the OPLA.

36. Clause 4 provided:

"4.1 The consideration for the sale of Business comprising the Assets and the novation of the Optical Product Licence Agreement shall be the sum of £7,300,000, or such difference sum in accordance with the following:-

4.1.1 To the extent that the valuation of the Business is subsequently agreed with the Shares Valuation division of [HMRC] at a different figure to that contained in Clause 4.1, the consideration shall be adjusted accordingly.

4.1.2 In the event that relief from Corporation Tax under Schedule 29 Finance Act 2002 for any amortisation of the consideration in Clauses 4.1 or 4.1.1 is subsequently denied to the Purchaser by [HMRC], the consideration shall be reduced to £1.

4.2 For the avoidance of doubt, no part of the consideration is attributable to the grant of any licence by Mr Conran to use or sub-licence any of his trade marks. The Purchaser, by virtue of being a wholly-owned Subsidiary of Jasper Conran Holdings Limited (which is entitled to use the trade marks under licence from Mr Conran and make them available to its subsidiaries) is already entitled to use or sub-licence such trade marks."

37. Clause 5.1 is a warranty that JCO has good and marketable title to each Asset.

38. Clause 7.3 requires JCO to execute and do and use its reasonable endeavours to procure to be executed and done by all necessary parties at the request of the Purchaser all such deeds, documents, acts and things as may be necessary or desirable for effectively vesting the Assets in the Purchaser and for giving full effect to the BTNA.

Subsequent events

39. On 18 December 2008, BHG valued the business of JCO upon its sale to JCV at £8.25 million. This figure rather than the value of £7.3 million stated in clause 4.1 of the BTNA was treated as the consideration for this agreement.

40. Clause 4.1.2 of the BTNA was amended on 20 May 2009 to provide that if amortisation relief was subsequently restricted or denied following a determination by HMRC that it was attributable to an asset pre-existing at 1 April 2002, the consideration for the element for which relief was not available would be adjusted to £1 but the consideration for the element for which relief was available would not be adjusted. Any overpayment of consideration was to be refunded.

41. The Licence Fee payable by Specsavers under the OPLA was reduced to £4 per frame delivered as of 1 November 2010 (by way of letter dated 28 October 2010).

42. The OPLA expired on 31 August 2013 and it was not renewed (this having been a decision taken by Specsavers). In their letter of 12 March 2013 explaining their decision not to renew, Specsavers referred to a meeting which had been held with JATC and others in December 2012 at which it was made clear that JCV were not prepared to reduce the range of frames or the amount of the Licence Fee.

Accounts

43. The SAF records the successful launch of the business. This can be seen from both the accounts of JCO before the transfer to JCV and those of JCV afterwards.

44. JCO's accounts for the APE 31 March 2008 record that for the nine months ended 31 March 2008, JCO had turnover of £1,151,915, cost of sales of £158,038, gross profit of £993,877, administrative expenses of £62,765 and an operating profit of £931,112. The note on related party transactions states that JCO paid Jasper Conran Limited ("JCL") design and management fees totalling £153,000. Those fees were within the "cost of sales".

45. JCO's accounts for the APE 31 March 2009 included the results for five months of the business. They record turnover of £569,881, cost of sales of £86,398 and a gross profit of £483,483. The design and management fees payable to JCL were £85,000.

46. JCV's accounts for the APE 31 March 2009 (the "JCV 2009 Accounts") were signed off on behalf of the director on 27 January 2010, and were audited, confirming that they gave a true and fair view in accordance with UK GAAP applicable to smaller entities. The turnover was £927,093, with a cost of sales of £141,042 (which included a design fee payable of £122,500), and thus a gross profit of £786,051. There is then an operating loss, but that is attributable to the amortisation of the consideration paid under the BTNA.

47. JCV continued to amortise the consideration in subsequent years, and the accounts for the APE 31 March 2014 record a net book value of the intangible fixed assets of nil.

Post-transaction valuation check, HMRC enquiries and the closure notices

48. On 15 July 2008, BHG submitted a non-statutory business clearance application on behalf of JCO and JCV to HMRC seeking confirmation that corporation tax relief under Schedule 29 FA 2002 would be available on the amortisation of the goodwill acquired from JCO as it had been created after 1 April 2002.

49. As set out at [7] of the SAF, HMRC confirmed on 26 August 2008 that although there was disagreement on some points HMRC did agree that the goodwill (and, if any, IP) of the JCO business constituted assets created after 1 April 2002 for the purposes of paragraph 118(2)(c) of Schedule 29 FA 2002. HMRC have not changed their position on this point.

50. On 14 December 2009, BHG sent form CG34 to HMRC on behalf of JATC to request a post-transaction check of the valuation of JCO's business.

51. HMRC's Shares and Asset Valuation Division ("SAV") initially determined that the market value of the business transferred under the BTNA was nil. The basis for this valuation was that clause 4.2 of the BTNA stated that no part of the consideration was attributable to the grant of any licence by JATC to use or sub-license any of his trademarks. HMRC therefore considered that these trademarks were not transferred under the BTNA. As a hypothetical purchaser would be unable to operate JCO's business under the OPLA without access to the trademarks, the OPLA had no value in the absence of such access. SAV later revised the market value of the consideration under the BTNA to £1, as a nominal sum would have been needed in order to frank the sale of JCO's business under the BTNA.

52. HMRC closed the enquiry into JATC's return for the year 2008-09 on 8 September 2016, amending the return so that the sum received by JATC was treated as a distribution subject to income tax and not as a chargeable gain subject to capital gains tax. The additional tax due as a result of this amendment is £662,036.37.

53. On 8 September 2016, closure notices were issued in respect of the enquiries into JCV's returns. These closure notices amended the returns in question so as to remove the debit for amortisation in the profit and loss account on the grounds that there was no debit to be brought into account under the provisions of Schedule 29 FA 2002, nor was it allowable under any other provision of the Taxes Acts. In addition, consequential amendments were made to the returns for APEs 31 March 2012 to 31 March 2014 under paragraph 34(2A) Schedule 18 Finance Act 1998.

54. The corporation tax due from JCV as a result of the amendments made in respect of each accounting period is as follows:

APE	Tax due after amendment
31/03/2009	£216,030.08
31/03/2010	£441,459.20
31/03/2011	£302,178.24
31/03/2012	£227,232.20
31/03/2013	£192,663.60
31/03/2014	£13,576.67

EVIDENCE

55. The parties provided us with their skeleton arguments, a hearing bundle, a supplemental hearing bundle and a bundle of authorities. As already noted, the parties had agreed a SAF, but there were no witnesses of fact.

56. We had the benefit of expert evidence as to both valuation and accounting. We had the following reports:

(1) for the Appellants:

(a) report from Ian Brewer as to valuation dated 6 June 2019, as amended by a short supplemental note dated 4 November 2021, and

(b) report from Peter Holgate as to accounting dated 5 June 2019;

(2) for HMRC,

(a) report from Joanne Beard as to valuation dated 12 December 2019, and

(b) report from Iain Dickinson as to accounting dated 17 June 2019; and

(3) a joint accountants report dated 26 July 2019 (the "Joint Report"), setting out areas of agreement and disagreement between Mr Holgate and Mr Dickinson.

57. The four experts attended the hearing, were cross-examined and answered questions from the panel. We had the benefit of a transcript of the hearing and we found this particularly helpful when considering the evidence which had been given by the four experts.

ISSUES

58. The appeals involve the determination of the open market value of the assets transferred by JCO to JCV under the BTNA. If we conclude that the value is £8.25 million, then the appeals of both JATC and JCV must be allowed.

59. We note in this regard that although the expert report of Mr Brewer produces a valuation of a higher amount (giving a range of £9.266 million to £9.477 million), the Appellants have not sought to argue that this higher amount should be substituted for the £8.25 million actually paid (and which had been supported by the original valuation report of BHG).

60. HMRC submit that the open market value is £1 and have amended the returns of JATC and JCV accordingly. (This value of £1 was sometimes referred to by the experts as the "SAV valuation".) However, the Appellants' position is that even if we agree with HMRC on valuation their appeals should still succeed. The reasons for this differ as between JATC and JCV, and it is thus possible for the appeals to have different outcomes.

61. If we conclude that the value is £1, then:

(1) JATC – The proceeds received by JATC in the year 2008-09, which have been brought into account by JATC as a capital gain, are not chargeable to CGT. That is common ground.

(a) The issue is then whether they were instead chargeable to income tax as a distribution. JATC's position is that there is no distribution, because the business was worth £8.25 million to JCV, and that the CGT which has been paid should be refunded (although Mr James emphasised that this was JATC's secondary position, as his primary position was that the value declared of £8.25 million was correct and the CGT had been properly declared and accounted for).

(b) If we conclude that the proceeds are to be taken into account as a distribution to JATC, HMRC must then establish that paragraph 92 of Schedule 29 does not apply to treat the distribution as being for market value (of £1). JATC also submit that this paragraph is inapplicable, albeit for different reasons which are particularly relevant in the context of JCV's appeal.

(2) JCV - HMRC argues that no debits are available for the amortisation of expenditure on an intangible asset.

(a) HMRC submit that the market value of £1 should be substituted for the actual accounting treatment, relying on paragraph 5 of Schedule 29, on the basis that the accounts of JCV for the relevant periods were not in accordance with GAAP and therefore fall to be treated as if corrected by the insertion of a fair value of £1. JCV submit that there is no basis for saying that the accounts were not in accordance with GAAP, irrespective of the value determined for tax purposes.

(b) Market value could also be required to be substituted by paragraph 92 of Schedule 29, which applies to transactions between "related parties". The Appellants argue that paragraph 95 does not extend the concept of related parties to LLPs/partnerships and therefore paragraph 92 does not apply to the transaction between JCO and JCV. HMRC submit that the transaction is between JATC and JCV, who are related parties. This reliance on paragraph 92 is not HMRC's primary argument, as they rely (in the context of JATC's appeal) on the transaction being within an exception to paragraph 92.

RELEVANT LEGISLATION

62. The relevant legislation is set out as in force in the year 2008-09.

Taxation of Chargeable Gains Act 1992 ("TCGA 1992")

63. Section 18(1) and (2) TCGA 1992 provide:

> "(1) This section shall apply where a person acquires an asset and the person making the disposal is connected with him.
>
> (2) Without prejudice to the generality of section 17(1) the person acquiring the asset and the person making the disposal shall be treated as parties to a transaction otherwise than by way of a bargain made at arm's length."

64. "Connected persons" are defined in accordance with s286 TCGA 1992. A company is connected with another person if that person has control of it (s286(6)).

65. Section 17(1)(a) provides:

> "… a person's acquisition or disposal of an asset shall for the purposes of this Act be deemed to be for a consideration equal to the market value of the asset—
>
> (a) where he acquires or, as the case may be, disposes of the asset otherwise than by way of a bargain made at arm's length,…"

66. Section 272(1) defines "market value" as:

> "…the price which those assets might reasonably be expected to fetch on a sale in the open market."

67. In addition, s59A provides the following in relation to limited liability partnerships:

> "(1) Where a limited liability partnership carries on a trade or business with a view to profit—
>
> (a) assets held by the limited liability partnership are treated for the purposes of tax in respect of chargeable gains as held by its members as partners, and
>
> (b) any dealings by the limited liability partnership are treated for those purposes as dealings by its members in partnership (and not by the limited liability partnership as such);
>
> and tax in respect of chargeable gains accruing to the members of the limited liability partnership on the disposal of any of its assets shall be assessed and charged on them separately."

Schedule 29 FA 2002

68. The provisions of Schedule 29 FA 2002 applied for the purposes of determining a company's gains and losses in respect of its intangible fixed assets in respect of accounting periods ending before 1 April 2009.

69. Paragraph 4 provided that it applies to goodwill as it does to an intangible fixed asset.

70. Paragraph 5 provided:

> "(1) If a company does not draw up accounts in accordance with generally accepted accounting practice ("correct accounts")—
>
> (a) the provisions of this Schedule apply as if correct accounts had been drawn up, and
>
> (b) the amounts referred to in this Schedule as being recognised for accounting purposes are those that would have been recognised if correct accounts had been drawn up.
>
> (2) If a company draws up accounts that rely to any extent on amounts derived from an earlier period of account for which the company did not draw up correct accounts, the amounts referred to in this Schedule as being recognised for accounting purposes in the later period are those that would have been recognised if correct accounts had been drawn up for the earlier period."

71. Paragraph 9(1) provided:

> "Where in a period of account a loss is recognised in determining the company's profit or loss in respect of capitalised expenditure on an intangible fixed asset—
>
> (a) by way of amortisation,… a corresponding debit shall be brought into account for tax purposes."

72. Paragraph 92 provided:

> "(1) Where there is a transfer of an intangible asset from a company to a related party or to a company from a related party and, in either case, the asset is a chargeable intangible asset—
>
> (a) in relation to the transferor immediately before the transfer, or
>
> (b) in relation to the transferee immediately after the transfer,
>
> the transfer is treated for all purposes of the Taxes Acts (as regards both the transferor and the transferee) as being at market value. This is subject to the following four exceptions…
>
> (4A) The third exception is where—
>
> (a) the asset is transferred from the company at less than its market value, or to the company at more than its market value,
>
> (b) the related party—
>
> (i) is not a company, or
>
> (ii) is a company in relation to which the asset is not a chargeable intangible asset immediately after the transfer to it or (as the case may be) immediately before the transfer from it,
>
> and
>
> (c) by virtue of any provision of—
>
> (i) section 209 of the Taxes Act 1988 (meaning of "distribution"), or
>
> (ii) Part 3 of the Income Tax (Earnings and Pensions) Act 2003 (employment income: earnings and benefits etc treated as earnings),
>
> the transfer gives rise (or would give rise but for sub-paragraph (1)) to an amount to be taken into account in computing any person's income, profits or losses for tax purposes.

> (4B) Where the third exception applies, sub-paragraph (1) does not apply, in relation to the computation mentioned in sub-paragraph (4A)(c), for the purposes of any such provision as is mentioned there.
>
> (5) In sub-paragraph (1) "market value" means the price the asset might reasonably be expected to fetch on a sale in the open market."

73. Paragraph 95 then stated:

> "(1) For the purposes of this Schedule a person ("P) is a "related party" in relation to a company ("C") in the following cases: …
>
> Case Three
>
> C is a close company and P is, or is an associate of—
>
> (a) a participator in C, or
>
> (b) a participator in a company that has control of, or holds a major interest in, C."

74. Paragraph 96(1) defined "control" as follows:

> "(1) For the purposes of this Part "control", in relation to a company, is the power of a person to secure—
>
> (a) by means of the holding of shares or the possession of voting power in or in relation to the company or any other company, or
>
> (b) by virtue of any powers conferred by the articles of association or other document regulating the company or any other company,
>
> that the affairs of the company are conducted in accordance with his wishes."

75. A close company was defined in s414 of the Income and Corporation Taxes Act 1988 ("ICTA 1988") as a company with five or fewer participators. "Participator" was defined in s417(1) and included a shareholder. An associate in relation to a participator was defined as including any partner of the participator in s417(3).

76. Section 118ZA(1) ICTA 1988 was in similar terms to s59A TCGA 1992 and provided:

> "For corporation tax purposes, where a limited liability partnership carries on a trade, profession or other business with a view to profit—
>
> (a) all the activities of the partnership are treated as carried on in partnership by its members (and not by the partnership as such),
>
> (b) anything done by, to or in relation to the partnership for the purposes of, or in connection with, any of its activities is treated as done by, to or in relation to the members as partners, and
>
> (c) the property of the partnership is treated as held by the members as partnership property.
>
> References in this subsection to the activities of the limited liability partnership are to anything that it does, whether or not in the course of carrying on a trade, profession or other business with a view to profit."

Distributions

77. Section 209(2)(b) ICTA 1988 provided as follows:

> "In the Corporation Tax Acts "distribution", in relation to any company, means—
>
> … any other distribution out of assets of the company (whether in cash or otherwise) in respect of shares in the company, except so much of the

distribution, if any, as represents repayment of capital on the shares or is, when it is made, equal in amount or value to any new consideration received by the company for the distribution…".

78. Some of the key phrases were defined in s254 as follows:

> "(1) In this Part, except where the context otherwise requires -
>
> "new consideration" means, subject to subsections (5) and (6) below, consideration not provided directly or indirectly out of the assets of the company, and in particular does not include amounts retained by the company by way of capitalising a distribution;
>
> …
>
> (9) A distribution shall be treated under this Part as made, or consideration as provided, out of assets of a company if the cost falls on the company.
>
> …
>
> (12) For the purposes of this Part a thing is to be regarded as done in respect of a share if it is done to a person as being the holder of the share, or as having at a particular time been the holder, or is done in pursuance of a right granted or offer made in respect of a share; and anything done in respect of shares by reference to share holdings at a particular time is to be regarded as done to the then holders of the shares or the personal representatives of any share holder then dead."

79. Section 383 of the Income Tax (Trading and Other Income) Act 2005 ("ITTOIA 2005") provided that income tax is charged on dividends and other distributions of a UK resident company and that they are treated as income for these purposes. Tax is charged on the amount of the distribution made in the tax year and the person liable for this tax is the person to whom the distribution is made or is treated as made (s384 and s385 ITTOIA 2005).

OPEN MARKET VALUE OF ASSETS TRANSFERRED TO JCV

80. The disposal by JCO to JCV was deemed by s59A TCGA 1992 to be made by the partners in JCO, namely JATC and JCE, to JCV. It was common ground that JATC and JCV are "connected parties" and deemed by s18 to be otherwise than at arm's length for capital gains purposes. The disposal was deemed to be at market value, defined as the price at which those assets might reasonably be expected to fetch on a sale in the market.

81. The approach to be taken to ascertaining market value has been considered in various authorities over the years, and it was common ground that principles expressed in the context of inheritance tax apply equally here. We have considered some of these authorities by reference to their own facts further below, but consider it helpful at the outset to set out a summary of the principles which have been established, before assessing the evidence before us and the submission of the parties. We gratefully adopt Judge Cannan's summary of the key principles which he set out in *McArthur v HMRC* [2021] UKFTT 0237 (TC) at [14]:

> "(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).

(6) The hypothetical purchaser embodies whatever was actually the demand for the asset at the relevant time in the real market (*IRC v Gray* [1994] STC 360 at 372).

(7) The market value is what the highest bidder would have offered for the asset in the hypothetical sale (*re Lynall* at 694B per Lord Reid)."

82. Judge Cannan further stated:

> "165. In my view the correct approach is straightforward. It is a case of identifying the highest price a reasonably prudent purchaser would pay. Not the highest price a range of reasonably prudent purchasers might pay. Expert evidence is a proxy for the reasonably prudent purchaser and different valuers might come up with different estimates. In that case, it is necessary to consider on the balance of probabilities and based on the reasoning of the experts who is right or where in the range the highest price lies.
>
> 166. Mr Henderson made a fair point that the test can be looked at both ways. The valuer is looking for the highest price the hypothetical purchaser would pay and the lowest price the hypothetical vendor would accept. Where they meet, is the market value of the shares. It is also the case that section 272 envisages a single price which is the market value."

83. In the present appeals, the parties do not seek to argue that the market value is at different points within a range. Instead, the Appellants, relying on the evidence of Mr Brewer, argue that the value is £8.25 million whereas HMRC rely on the evidence of Ms Beard and submit that the value is £1. HMRC have challenged some aspects of Mr Brewer's approach to valuation (whilst acknowledging that his discounted cashflow ("DCF") methodology is otherwise broadly appropriate) but the key issue underpinning the different positions of the parties is the basis on which the valuers have produced their valuations. Put shortly, Mr Brewer considers that the right to use the trademark is implicit in the deal, whereas Ms Beard acknowledged that she had looked to value the OPLA.

Evidence of Ian Brewer

84. Mr Brewer had prepared a report (references to which are to that report as amended) and gave evidence to the Tribunal. It was on his evidence that the Appellants relied. There were three further valuation reports which had been prepared on behalf of the Appellants at various stages, and we were taken to those by Mr James. These reports were not their expert evidence.

85. We set out some key points from these valuations:

(1) BHG report dated 18 December 2008 (the "BHG 2008 Report") – The purpose of this report was stated to be to calculate the UK tax market value of the business of JCO upon the sale of that business to JCV. That report recommended that the business was transferred at a purchase price of £8.25 million (and it was this conclusion that informed the increase in the purchase price payable under the BTNA). This price was based on a DCF valuation model in light of the following:

(a) it noted that it is possible that the OPLA would be renewed once it expired but made no assumption to that effect;

(b) it referred to JCL supplying design services for a fixed fee of £17,500 per month, and that JCL also supplies all administrative services to JCV for a fixed fee of £2,000 per month. Those costs were believed to equate to open market rates; and

(c) when forecasting profit and loss over the term of the OPLA, no expense was applied for payment by the purchaser of any royalty for use of the trademark.

(2) BHG report dated 24 January 2013 (the "BHG 2013 Report") – This was said to have been commissioned to cross-check the earlier valuation report and was provided to HMRC during the course of the enquiry. It supersedes the BHG 2008 Report, and values the business at £11.65 million. That was also based on a DCF valuation model:

(a) It considered it "probable" that the OPLA would be renewed for a further term of five years, and assumed such a renewal for investment appraisal purposes. (This assumption was also adopted in subsequent valuations.)

(b) It also allowed a terminal value for the business. (Subsequent valuation reports do not.)

(c) It assumed that a purchaser of the business would pay a royalty to JATC of 30% of business turnover for design input and the right to use the trademark.

(3) Valuation Solutions report dated 16 October 2013 (the "Valuation Solutions Report") – This also approached the valuation using a DCF model, cross-checked using an EBITDA multiple and valued the business at £10.165 million. The methodology:

(a) assumed the purchaser would need to pay an arm's length royalty for the right to use the trademark. They had conducted various research, which they referred to in the report, and summarised the ranges of royalty rates identified and what they considered the closest comparables, and applied an 8% royalty rate; and

(b) assumed that the OPLA would be renewed once, but that the application of a terminal value was not appropriate.

86. In describing his approach, Mr Brewer explained:

(1) He considered that the right to use the trademark was "implicit in the deal but in any event there were plenty of entities around with the right to use the trademark to whom the business was worth its full value and this would, in turn, drive the market in a real world scenario".

(2) It would not make economic sense for a willing but not anxious vendor to give away a profitable business.

(3) It would also not make sense for a third party purchaser to enter into an agreement where JATC would demand "the lion's share of the profits" in return for a licence to use his name when they would be bearing all the costs and most, if not all, of the risks associated with the business.

87. He had adopted an income approach using DCF methodology which means first of all establishing the cashflows to be used and then the discount that needs to be applied to arrive at the net present value. He has then considered the EBITDA implied as a cross-check.

(1) In arriving at the cashflows he has assumed that sales would be in line with the forecasts for the ten year period to 31 August 2018 produced in the BHG 2013 Report and the Valuation Solutions Report (which were based on Specsavers' growth forecasts). He considered these to be a reasonable set of figures.

(2) He has used alternative royalty rates of 6% and 8% which he considers to be more commercial (based on his own research as to royalty rates in the ophthalmic industry and that of Valuation Solutions) rather than the 30% used in the BHG 2013 Report. He has applied the royalty rate to the net sales of the licensee, ie to the fees received by JCO under the OPLA.

(3) He took account of design input costs of £210,000 pa.

(4) He calculated the weighted average cost of capital ("WACC") using a 40/60 weighting for equity/debt and applied a discount rate of 13%.

88. Using a 6% royalty rate gives an open market value of the business as of 4 September 2008 of £9.477 million and an 8% royalty rate gives a value of £9.266 million.

89. Mr Brewer disagreed with the approach taken by Ms Beard, which (in her terms) concluded that allowing for the cost of a royalty to JATC plus a design fee would "effectively cancel out any profits and leave little, if any value in the business". He doubted any purchaser would enter into such an arrangement. He said he had adjusted for a commercial royalty rate, applying it to the payments received from Specsavers, saying that these were the net sales of the business, and denied that this was a "royalty on a royalty" (again, this having been the phrase used by Ms Beard). Mr Brewer did not accept that the £4.50 being paid by Specsavers to JCV under the OPLA was a good benchmark for illustrating what would be paid for the right to use the Conran name, such that this would be the level of fees that JATC would expect to charge anyone else.

90. HMRC's main challenge to Mr Brewer's evidence was that his approach rests on a flawed assumption that access would be provided to the trademarks under the terms of the BTNA (as he states that the right to use the trademark is implicit in the deal) and a hypothetical purchaser would not need to make a further payment in order to obtain access to them from a third party, namely JATC. Mr Brewer did acknowledge that if JCV did not have access to the trademark then the value of the business would be "severely undermined", but emphasised that JCV did have the right to use the trademark, was able to perform the obligations under the OPLA and generated significant profits each year from this business.

91. Ms Choudhury did put further challenges to Mr Brewer:

(1) She submitted that there were potential deficiencies in his report as, eg, there was a reference in the letter of engagement to his having produced an indicative valuation (but Mr Brewer could not recall what that had been and which was not produced in evidence), and his report referred to his having spoken to and obtained information from BHG and JCL, but he couldn't fully explain what this had been.

(2) On royalty rate:

(a) There was no evidence of other licences between JATC (or JC Group companies) and third parties, other than one dating from 1991 when JATC had apparently agreed a 5% royalty with the German clothing producer Beiderman.

(b) Mr Brewer had looked at royalty rates applicable to trademarks in the ophthalmic industry, but the table of data did not include the OPLA between Specsavers and JCO. Mr Brewer explained his opinion that the amount payable by Specsavers under the OPLA was not a royalty, it was a flat fee per frame.

(c) The table of royalty rates showed, eg, a licence from Warner Bros to Gargoyles of 10% on net sales. This royalty was payable on the net sales of Gargoyles, as that was the body making the sales. Here, Specsavers was making the sales so surely any royalty should be calculated by reference to those sales.

Taking Mr Brewer's approach, namely that JCV would pay a royalty of 6-8% of the £4.50 it received from Specsavers to JATC, this begged the question as to what the remaining 94-96% was being received for, as Mr Brewer's approach recognised that the design services could be bought for £210,000 pa. Mr Brewer's response was that this represented the profitability of a trading company.

(3) Mr Brewer had looked at ratings of quoted UK companies in similar sectors to JCO/JCV (eg Burberry Group, Hugo Boss), but these are substantially larger than JCO; Ms Chaudhury challenged whether the discount was sufficient.

(4) When calculating the WACC, Mr Brewer had based this on a 40/60 equity/debt ratio, based on the information in the BHG 2013 Report. He had not carried out his own assessment.

Evidence of Joanne Beard

92. HMRC relied on the evidence of Ms Beard. Her evidence was:

(1) Absent the appropriate design services and, more specifically, a trademark licence agreement, the business would be unable to operate and the value of the goodwill would be nominal, say £1, a sum sufficient only to frank the sale of the assets transferred.

(2) If it were to be assumed a service agreement were in place with JATC, an appropriate arm's length fee would have to be paid. The BHG 2008 Report said that the design service fee paid by JCO to JCL of £17,500 per month was believed to be an arm's length rate so a payment of at least this amount would have to be paid by the hypothetical purchaser.

(3) Similarly, to ensure access to the trademarks for use within the business, the hypothetical purchaser would have to negotiate an arm's length royalty with JATC. It is clear that he is very keen to keep control over his marks and the protection of his name and reputation.

(4) The cost calculated in the BHG 2013 Report and the Valuation Solutions Report for the royalty rate a purchaser would have had to pay for use of the Conran trademark was not an open market royalty rate because it was based on the turnover of the JCO business which itself represented the royalty fees received from Specsavers for use of the trademark – it is a "royalty on a royalty".

(5) The agreed royalty fee at the date of the valuation of £4.50 per branded product delivered to Specsavers' warehouses equated to a royalty rate of 7.2% (based on the sale price of completed glasses by Specsavers). As this was agreed at arm's length between unconnected parties as part of the OPLA it seems reasonable that this was the rate that JATC would demand of the hypothetical purchaser. This cost, as well as any design fee, would effectively cancel out any profits and leave little, if any, value in the business.

(6) There is no evidence to suggest that any other members of the JC Group were in the market with a special reason for wanting to acquire the business and it seems extremely unlikely that different members of the group would bid against one another to increase the price. Therefore, any potential influence of such a purchaser cannot be taken into consideration.

93. Ms Beard acknowledged that JCO had been able to exploit the OPLA successfully (referring to the operating profits made prior to disposal), but considered that a hypothetical purchaser would be concerned to establish whether it would be in a position to fulfil the obligations under the OPLA. In fulfilling its obligations, JCO did not itself provide any of the

design or management functions nor did they own the trademark. A purchaser would have to gain access to these and negotiate a price with JATC.

94. Mr James challenged the evidence of Ms Beard, including:

(1) The decision to look at the £4.50 paid by Specsavers as a percentage of the sales by Specsavers of completed glasses. He submitted that this was contrary to the data set out by Mr Brewer on royalty rates which showed that the rate was applied to the net sales of the licensee; in this situation the licensee of the trademark would be JCO or JCV. Ms Beard's explanation was that the licensee in each comparable put forward by Mr Brewer was able to exploit the trademark and was using it on products they make.

(2) Mr James contested the outcome of Ms Beard's reasoning which was that JCO would pay away all of its earnings as a licence fee; this was a surprising commercial outcome. Ms Beard's explanation was that she would looking at the position of JATC and what he would require as payment; her rationale was that he would expect nothing less than this.

(3) Mr James put it that Ms Beard was valuing an "inoperable OPLA" and destroying the business of JCO. Ms Beard acknowledged that the basis on which she was valuing the business, the hypothetical situation she was envisaging, was that there was no mark being transferred under the BTNA. However, she considered that the BTNA was clear as to what was being sold, this is what she was valuing and she was not making additional assumptions as to the position of the hypothetical purchaser.

(4) Her report did not address the position of a hypothetical vendor, ie Mr Brewer's position that a hypothetical vendor, running a profitable business, would not sell that business for £1. Ms Beard agreed that a hypothetical vendor would not sell for £1; but what JCO is selling is not what it is making its money from. JCO had been exploiting the OPLA together with the trademark, whereas we only know that the hypothetical vendor is selling the OPLA.

(5) Ms Beard had not provided any evidence as to what the business was worth to another Conran company, ie a purchaser which has the right to use the JATC name. On special purchasers, Ms Beard had said that the Appellants' argument was that there were special purchasers in the form of members of the JC Group who would pay full value, being at least the value for which it was sold, by virtue of them having access to the trademark. She accepted that in a hypothetical sale all likely purchasers are deemed to be in the market, but said that for a special purchaser argument to succeed the special purchaser must have existed in reality and actively been in the market at the date of valuation. There was no evidence that other members of the JC Group were in the market and it was extremely unlikely that they were bidding against each other.

Consideration of expert valuation evidence

95. There were some areas where we considered that Mr Brewer's evidence was unsatisfactory, in particular in relation to royalty rates. We were troubled by the absence of detailed evidence of other (recent) licences which had been entered into by members of the JC Group, as we considered that this would have been very helpful to our consideration. It was also apparent that Mr Brewer had not focused on the details of the BTNA. When explaining his position that it was implied that the trademark was available, he acknowledged that the trademark was not formally transferred under the BTNA, but said that Specsavers must have known that access was there for JCV. This may well have been the case, but the BTNA did not require that JCO obtain Specsavers' consent to an assignment to another member of the JC Group.

96. However, the different approaches taken by Mr Brewer and Ms Beard meant that although Ms Chaudhury put various challenges to Mr Brewer as to the details of his approach, (eg his decision to assume a 40/60 equity/debt split when calculating the WACC), there was no competing evidence adduced on behalf of HMRC on such matters on which we could reach a conclusion that a different ratio was appropriate.

97. Ms Beard acknowledged that she was essentially valuing the OPLA, and treating the fee payable by Specsavers under that agreement as a proxy for what JATC would expect to receive as an arm's length royalty in the market. We were not convinced by her approach to special purchasers (which we considered to be unrealistic and unworkable given that there can never be active potential purchasers in the context of an intra-group transaction where there is no public auction or marketing) and place no weight on this part of her evidence.

98. Having considered the evidence of both experts we concluded that the decision as to whose evidence to prefer required us first to decide the basis on which the valuation was to be made. Having reached such a conclusion, the evidence of both Mr Brewer and Ms Beard was sufficiently credible to support the valuation which they had each reached (proceeding on their different bases).

Summary of Appellants' submissions

99. In submitting that we should conclude, relying on the evidence of Mr Brewer, that the market value of the business transferred by JCO to JCV was £8.25 million, Mr James put forward various arguments in the alternative (albeit that there was an element of overlap in the approach so far as it related to access to the trademark):

> (1) The starting point is to identify the asset sold. The asset sold under the BTNA was the business including the OPLA with Specsavers, and that did include access to the trademark. This was apparent from the terms of the BTNA (eg clauses 4.2 and 7.3). This access to the trademark by both vendor and purchaser were key features of the factual nexus that could not be disregarded. For capital gains purposes, the actual sale that took place then informs the hypothetical disposal. In contrast, HMRC were valuing what Mr James described as an inoperable business, one under which JCV would not be able to grant the continuous sub-licence to Specsavers. HMRC had not adduced valuation evidence of this business and had thus not put forward evidence which could be preferred to that of Mr Brewer.
>
> (2) Alternatively, look at the position of the hypothetical vendor of this business:
>
> > (a) It is a profitable business, as agreed in the SAF; why would such a vendor sell for just £1. In *Gray,* Hoffmann LJ referred to the hypothetical vendor as "a prudent man of business", negotiating seriously without giving the impression of being either over-anxious or unduly reluctant. (Full case citations are included in our discussion of the authorities below.)
> >
> > (b) In *Clay* Pickford LJ had said that the seller is not one who is prepared to sell at any price; he is not anxious. It is therefore not a forced sale; the hypothetical vendor is willing but not anxious. Such a person would want appropriate value for their business.
>
> (3) Looking at the situation of a hypothetical purchaser, it is accepted that such person is not JCV itself. However:
>
> > (a) The question is then whether a hypothetical purchaser has access to the mark, and this comes back to the identification of the asset transferred, ie an operational OPLA. It is necessary to assume the sale of that asset and anything necessary to enable that sale to occur. Mr James relied on Viscount Hailsham in *Crossman*,

submitting that this demonstrates that restrictions around assignment cannot be used to depress value; you must look at the inherent value of the asset. This has since been confirmed by the House of Lords in *Lynall*. This principle is not confined to valuing shares in private companies (as confirmed by *Alexander*). *Dyer*, which did concern shares, is distinguishable as the shares sold in that case were freely transferable and the Upper Tribunal rejected the submission that the value of that asset, ie those shares, should be treated as improved by the company having put in place a contract with the key individual. Here, the OPLA cannot be transferred without access to the trademark.

(b) The statutory hypothesis requires the assumption that a sale of the business as a going concern did in fact take place and, as such a sale cannot take place without the purchaser having access to the trademark, it is assumed that the hypothetical purchaser has access to the mark; clause 10.3 of the BTNA required JCO to ensure access to the necessary licence to support the sub-licence to Specsavers at all times.

(c) HMRC are contending for a different transaction, and the sale of a different asset.

(d) On the royalty rate, Mr Brewer's evidence was based on research, and applies the rate to net sales of JCV. Ms Beard's approach ignores the existence of JCO, and fails to recognise that JCV would not pay away its entire profits by way of a licence fee.

(4) Alternatively, even if the business sold and to be valued is the business without access to the trademark, there were special purchasers in the form of members of the JC Group who would pay full value, being at least the value for which it was sold, by virtue of them having access themselves to the trademark and therefore access to the full value of the business, and this therefore remains the full market value. HMRC are wrong to say that these special purchasers could acquire the business from the hypothetical vendor for £0 or £1 because they could fulfil the terms of the OPLA and the hypothetical vendor could not. This is because the hypothetical vendor has a valuable design business with the benefit of a lucrative contract and therefore, by definition, access to the trademark.

100. In short, Mr James submitted that HMRC's approach was completely unrealistic. It takes the concept of a hypothetical sale to a place where reality ceases to operate.

Summary of HMRC's submissions

101. HMRC's primary contention is that the valuation used by the Appellants was overstated. The correct valuation was £1, which was the price that the asset might reasonably be expected to fetch on a sale in the open market.

(1) Access to the trademarks owned by JATC was not sold to JCV under the BTNA and the market value has to be determined on that basis.

(2) The argument that a vendor would not sell a profitable business for £1 relies upon the asset(s) generating that income and the asset(s) sold to be the same. In the present case, the assets in question were different with the trademarks being held separately. The asset being sold here was the OPLA but without the all-important access to the trademarks. There is no authority to the effect that it ought to be assumed that another asset is held/transferred at the same time as the asset being valued. Furthermore, the BTNA itself contemplates that the consideration may be reduced to £1 in certain circumstances.

(3) The continuing availability of the licence to use the JATC trademark resulted from the facts of the actual transaction, which involved a sale to someone who already held a licence to use the trademark. The statutory fiction requires consideration of a hypothetical vendor and purchaser, but everyone else is real, and that includes JATC. The transfer and sub-licensing of the mark under the July 2008 Licence would have required JATC's consent, and he is fiercely protective of the use of his mark.

(4) Even if the Tribunal were to find that it must be assumed that the OPLA would be transferred with access to the trademark, it is still necessary to determine the royalty payable. There is no evidence that JATC would have provided a licence to a hypothetical purchaser at anything other than an arm's length rate, a matter which is addressed in Ms Beard's evidence. HMRC submit that the amount of the royalty would be the amount payable by Specsavers under the OPLA, and this would eliminate any profits under the OPLA and render it commercially worthless.

(5) The absence of the right to use the trademark affects the value of the OPLA to a hypothetical purchaser, but not the ability to assign the contract. The authorities relating to restrictions on transfer did not assist the Appellants.

(6) There is no evidence that any of the other companies controlled by JATC were in the position of a special purchaser. Moreover, as recognised by Ms Beard, this would suggest that each of these companies would be trying to beat the price offered by any other (and thus drive it up between them) which is extremely unlikely. Furthermore, even if purchasers for JCO's business existed, any such purchaser would not need to offer more than £1 to frank the sale of JCO's business to it. This is because no other party would be in a position to satisfy those obligations and this would therefore represent the best price available to a vendor which itself did not have access to the trademarks or the design team.

(7) Valuation has to be determined on the basis of an anonymous vendor and purchaser and the Appellants' argument seeks to ascribe characteristics to the hypothetical vendor which it would not necessarily have. The actual vendor, JCO, obtained design input as well as management and administrative support from other group companies on an informal basis and without any contractual arrangements for the provision of those services. Its "business" therefore simply comprised holding the OPLA. In those circumstances, HMRC submit that their valuation of the business transferred by JCO is realistic.

Discussion and conclusions

102. We have carefully considered the authorities to which we were taken by both parties in the light of all of their submissions. We look first at some of those authorities and then explain the conclusions we have reached on the present facts.

103. In *IRC v Gray* [1994] STC 360 the question was whether property comprising two or more component parts (in that case a majority interest in a farming partnership and the reversionary interest in the land let to that partnership) could be treated as one unit of property if that was the course that a prudent hypothetical vendor would have adopted in order to obtain the most favourable price without undue expenditure of time and effort.

104. In the Court of Appeal Hoffmann LJ set out the following:

> "…Certain things are necessarily entailed by the statutory hypothesis. The property must be assumed to have been capable of sale in the open market, even if in fact it was inherently unassignable or held subject to restrictions on sale. The question is what a purchaser in the open market would have paid to

> enjoy whatever rights attached to the property at the relevant date (see IRC v Crossman [1937] AC 26). Furthermore, the hypothesis must be applied to the property as it actually existed and not to some other property, even if in real life a vendor would have been likely to make some changes or improvements before putting it on the market (see Duke of Buccleuch v IRC [1967] 1 AC 506 at 525). To this extent, but only to this extent, the express terms of the statute may introduce an element of artificiality into the hypothesis.
>
> In all other respects, the theme which runs through the authorities is that one assumes that the hypothetical vendor and purchaser did whatever reasonable people buying and selling such property would be likely to have done in real life. The hypothetical vendor is an anonymous but reasonable vendor, who goes about the sale as a prudent man of business, negotiating seriously without giving the impression of being either over-anxious or unduly reluctant. The hypothetical buyer is slightly less anonymous. He too is assumed to have behaved reasonably, making proper inquiries about the property and not appearing too eager to buy. But he also reflects reality in that he embodies whatever was actually the demand for that property at the relevant time. It cannot be too strongly emphasised that although the sale is hypothetical, there is nothing hypothetical about the open market in which it is supposed to have taken place. The concept of the open market involves assuming that the whole world was free to bid, and then forming a view about what in those circumstances would in real life have been the best price reasonably obtainable.
>
> …
>
> It is often said that the hypothetical vendor and purchaser must be assumed to have been 'willing', but I doubt whether this adds anything to the assumption that they must have behaved as one would reasonably expect of prudent parties who had in fact agreed a sale on the relevant date. It certainly does not mean that having calculated the price which the property might reasonably have been expected to fetch…, one then asks whether the hypothetical parties would have been pleased or disappointed with the result…"

105. This decision was reached in the context of capital transfer taxes on death. There was thus no actual transaction. Nevertheless, we find this decision to be particularly helpful in emphasising that the property must be assumed to have been capable of sale in the open market and that the question is what a purchaser would have paid to enjoy whatever rights attached to the property at the relevant date. Hoffmann LJ also reiterated the characteristics which are to be assumed of the hypothetical vendor and purchaser.

106. Whilst there is typically some reference to the characteristics of the hypothetical vendor in the authorities, the guidance is somewhat scant. In *IRC v Clay* [1914] 3 KB 466 at 478, Pickford LJ stated:

> "I think a willing seller means one who is prepared to sell, provided a fair price is obtained under all the circumstances of the case. I do not think it means only a seller who is prepared to sell at any price and on any terms, and who is actually at the time wishing to sell. In other words, I do not think it means an anxious seller."

107. *Clay* concerned the valuation of a house where its value as a private residence was considered to be £750, but it was next door to a nurses' home and the trustees of that home wanted to extend their premises. They bought the house for £1,000. The decision in *Clay* thus involved an actual transaction which had occurred (albeit that the sale was in 1910 whereas the valuation was being determined as at April 1909). *Clay* was also referred to as an illustration

of the principle of special purchasers, as the house was worth more to the trustees than to others in the market because of the characteristics of the trustees.

108. There is wider authority on the difficulties posed by restrictions on transfer. This was initially considered by the Irish Court of Appeal in *Attorney-General for Ireland v Jameson* [1905] 2 IR 218, but was then considered by the House of Lords in *IRC v Crossman* [1937] AC 26. In *Crossman*, a testator at the time of his death owned a number of shares in a company, the articles of association of which imposed rigid restrictions on the alienation and transfer of the shares. It was contended for the personal representatives of the testator that the value of the shares was limited to the restricted price fixed by the articles to be paid by any existing shareholder exercising his right of pre-emption under the articles.

109. The contention of the personal representatives was rejected by a majority decision of the House of Lords. Viscount Hailsham LC stated (at p39) "…it seems to me essential to determine what is the property which has to be valued", and then set out (at p41-42):

> "... it seems to me that this construction [contended for by the personal representatives] involves treating the provisions of s 7, sub-s 5, as if their true effect were to make the existence of an open market a condition of liability instead of merely to prescribe the open market price as the measure of value. The right to receive the price fixed by the articles in the event of a sale…is only one of the elements which went to make up the value of the shares. In addition to that right, the ownership of the share gave a number of other valuable rights to the holder, including the right to receive the dividends, the right to transmit the share…and the right to have the shares of other holders who wished to realize offered…All these various rights and privileges go to make up a share and form ingredients in its value
>
> ... the purpose of s 7, sub-s 5, is not to define the property in respect of which estate duty is to be levied but merely to afford a method of ascertaining its value."

110. The House of Lords later followed *Crossman* in *Re Lynall* 47 TC 375, where Lord Reid held as follows (at p406):

> "The Appellants urged your Lordships to accept the view of the minority in *Crossman*'s case. They appear to assume that there could be a sale by a shareholder of shares subject to a right of pre-emption [at par]. In my view it is legally impossible for the shareholder to sell such shares in the open market or otherwise without first obtaining from the holder of the right of pre-emption an agreement not to exercise that right. I agree with Lord Roche that sale means a transaction which passes the property in the thing sold. All that the shareholder could offer would be an undertaking that if the right of pre-emption was exercised he would assign to the "purchaser" his right to receive the pre-emption price, and that if the right of pre-emption was not exercised he would transfer the shares to the purchaser, so that if the directors registered the transfer the property in the shares would pass but if they did not he would hold the shares in trust for the purchaser. In my view that would not be a sale. I support the view of the majority on the ground that s. 7(5) is merely machinery for estimating value, that it will not work if s. 7(5) is read literally, that it must be made to work, and that the only way of doing that is the way adopted in *Crossman*'s case."

111. Lord Morris of Borth-y-Gest agreed, setting his position out as follows (at p408):

> "But, having considered the arguments attractively presented on behalf of the Appellants, 1 have not been persuaded that the decision in *Crossman*'s case was erroneous. Section 7(5) requires an estimate to be made of the price which

> the property would fetch if sold" in the open market. So a sale in the open market must be assumed, and this in some cases will involve an assumption of the satisfaction of such conditions as would have to be satisfied to enable such a sale to take place."

112. Similarly, Viscount Dilhorn said at (p412):

> "The House was invited to reconsider the majority decision in *Crossman* and to depart from it. In my view the decision in that case was right. Parliament has enacted that the price the shares would fetch if sold in the open market has to be assessed. There could be no sale on the open market on 21st May 1962 unless the directors agreed to the registration of the transfer of the shares and Mr. Lynall refused to purchase the shares at £1 a share. Therefore, for the price the shares would fetch if sold in the open market to be assessed, it must be assumed that the directors had so agreed and Mr. Lynall had refused to buy. As Mr. Harman said in the course of his argument for the Crown, if property is only saleable in the open market in certain circumstances, then when the Act requires the property to be valued at the price which it would fetch if sold in the open market, one must proceed on the basis that those circumstances exist. This does not mean that the shares change their character. The shares bought by the hypothetical purchaser will be subject to the restrictions imposed by article 8."

113. The House of Lords in *Lynall* thus refused to overturn *Crossman* and held that the hypothesis of a sale of the shares in the open market required the assumption that on the occasion of that sale the right of pre-emption under the articles had been waived and the board's consent given, ie that the conditions required to be met were satisfied.

114. The Court of Appeal has since confirmed (in *Alexander v IRC* [1991] STC 112) that these principles apply generally and are not restricted to shares in a company - in that case, to a lease the disposal of which within five years of grant would trigger the payment to the landlord of a "right to buy" discount which had been obtained when the leasehold interest was acquired under the Housing Act 1980.

115. We were also referred to two recent decisions on improvements or changes to the assets, *Spring Capital Ltd v HMRC* [2015] UKFTT 66 (TC) and *Dyer v HMRC* [2016] UKUT 381 (TCC).

116. In *Spring Capital* a company's claim for a deduction for amortisation of goodwill was rejected because it was decided that no purchase of goodwill had taken place. However, the Judge set out his conclusions (obiter) on the valuation of goodwill and stated that he agreed with the taxpayer's view that the business should be valued on the basis that he (and his brother) would remain with the business on a sale, and that employment contracts and non-competition covenants would have been entered into. The Tribunal stated (at [251]) that:

> "It seems to me that this method of valuation gives effect to what Hoffman LJ described as the 'reality principle' to be derived from Buccleuch. In other words, it must be supposed that Messrs Thomas would take the necessary reasonable steps to sell the trade for the highest price. As regards the caveat in Buccleuch that this must not entail 'undue expenditure of time and effort', it seems to me that entering into employment contracts and non-competition covenants would not have involved undue time and effort, or, indeed, expense."

117. However, *Dyer* was decided by the Upper Tribunal the following year and in that case shares were held to be worthless at the point of acquisition (thereby precluding a claim by the appellant that they had later become of negligible value for CGT purposes) because the

company in question had no contract of employment or non-competition agreements with the key individual director working in the company's business.

118. The Upper Tribunal concluded that, in the absence of a contract of employment or services between the director and the company (who relied on her services) and an assignment or licence of her IP rights, the company's shares were worthless. This was despite the fact that the taxpayers contended (relying on *Gray* and *Lynall*) that arrangements which would satisfy an intending investor could easily have been put in place and the company would have been valuable if they had been.

119. The Upper Tribunal stated at [46]:

> "Mr Dyer's argument that the shares should be valued by reference to the arrangements which would have been put in place had Mr Ho or some other investor been prepared to proceed must fail because the question is not, what would have been the value of the company, structured in a manner which would have attracted an investment from Mr Ho (that is, a company with suitable binding arrangements with Miss Dyer for the provision of her services and the continuing use of her IP rights)? The proper question is, what was the value of the company as it was on 31 October 2007? At that date JDDL, for the reasons we have given, had no contractual rights over Miss Dyer's services, her trademarks or her designs. Rather, it had an unsuccessful trading history which had led to a substantial level of indebtedness. It had no assets of substance and quite clearly had no value. The F-tT's conclusion that the shares Mr and Mrs Dyer acquired on that date were worthless is in our view unassailable."

120. This decision of the Upper Tribunal is binding upon us, and we prefer the reasoning therein to that in *Spring Capital*.

121. The starting-point for our decision in this appeal must be the identification of the assets transferred by JCO to JCV. It is those assets which are required to be valued, and in respect of which the valuation principles must be applied.

122. The transfer in question was by JCO to JCV under the terms of the BTNA, the provisions of which we have already described. That agreement is framed as the transfer of a business, namely JCO's business relating to the OPLA. However, this does not detract from the identification of the assets which were actually transferred thereunder, which whilst including the assignment of the OPLA itself and the goodwill of the business, did not include the right to use the trademark. That such a right was not amongst the assets transferred is evident, not only from its absence from the "Assets" as defined in the BTNA, but also this was an asset which JCO did not have the right to assign (at least without consent) and also JCV did not need JCO to transfer this right to it, as JCV already had the right to use the trademark (by virtue of the July 2008 Licence).

123. We are not persuaded by the (admittedly elegant) submissions of Mr James:

(1) Whilst it is apparent that the parties to the BTNA contemplated that JCV would continue to conduct the business of JCO, ie perform the obligation under the OPLA, this cannot change the identity of what was actually transferred.

(2) There is merit in Mr James' submission that JCO could have sought to transfer to JCV the rights under the JCO 2007 Licence, and if it had done so, then this would have made it clear that JCO was transferring both the OPLA and the right to use the trademark. Mr James submitted that this was not done as there was no need for such step, as JCV already had the right to use the trademark. However, not only was there no evidence of fact before us as to the reasons why such transfer did not occur, that is not the actual

transaction, and in any event the JCO 2007 Licence is royalty-free but does not permit assignment and thus consent would have been required from JATC for such transfer.

(3) The principles established in *Crossman* and *Lynall*, that the assumption that there is a sale in the open market will also sometimes require an assumption that conditions are satisfied or restrictions are removed, do not assist. The OPLA was freely assignable to other members of the JC Group; this remains the case even if an assignment to someone who did not have the right to the trademark and to grant a sub-licence to Specsavers would mean that the assignee was immediately in breach of the terms of the OPLA (including in breach of clause 10.3).

(4) We accept that there is a form of "marriage value" in the transfer of the OPLA to a person with the right to use the trademark; but that characteristic does not exist in a hypothetical sale of the asset, where Mr Brewer acknowledged that it is still necessary to calculate an appropriate arm's length royalty (even though no such royalty was payable in fact by JCV).

(5) The authorities do provide some support for the role of special purchasers. We do not agree with Ms Beard's position that for a special purchaser to be found to exist there must be evidence that they were actively in the market – that is a scenario that will be factually impossible in most instances of intra-group transactions about which there is no public knowledge. However, the fact that purchasers may exist who already have the right to use the trademark should not be used to change the identity of what was actually transferred, namely the OPLA.

124. Considering the expert evidence of Mr Brewer and Ms Beard in the light of these conclusions, we accept the evidence of Ms Beard that the value of the assets transferred, having regard to the need to value only the assets transferred ie the OPLA, and the inability to make assumptions as to the characteristics of the hypothetical purchaser (ie we cannot assume they held their own right to use the trademark) means that the market value was £1.

125. Mr James submitted that such a conclusion is artificial, or assumes that the profitable business of JCO is destroyed. However, we agree with Ms Chaudhury that the valuation of £1 reflects the identification of the asset which is being transferred (and thus valued) as the OPLA and other defined assets without the right to use the trademark, and that the BTNA itself (at clause 4.1.2) provided for the possibility of a transfer for just £1 in the scenario (which did not materialise) that HMRC did not accept that the BTNA involved the transfer of post-2002 assets (ie assets within the new intangibles regime).

JATC'S APPEAL AND DISTRIBUTIONS

126. HMRC submitted that the sum received by JATC on the sale of JCO's business to JCV does not constitute payment in exchange for the disposal of an asset. It is instead a distribution to him from JCV within the meaning of s209(2)(b) ICTA 1988, and is therefore chargeable to income tax; the sum represents value from a company of which he has control.

127. In contrast, JATC's alternative ground of appeal was that even if a £1 valuation is appropriate for CGT purposes based on a hypothetical purchaser, this does not mean that the £8.25 million which was paid for the business by JCV was a distribution for income tax purposes. This is because it could only be a distribution insofar as it exceeded the value to JCV itself of the business acquired (ie the position of the hypothetical purchaser does not arise) and, on any view (including HMRC's), the business was worth that amount to JCV because JCV had access to the trademark. Furthermore, it was not "in respect of" shares in JCV; neither JATC nor JCO are shareholders in JCV. There is no connection to shareholdings, and those words must be given a meaning rather than ignored.

128. JATC is the sole shareholder of JCHL, which is the sole shareholder of JCV. It was common ground that JATC has control over JCV through this indirect shareholding. We have considered whether the payment of £8.25 million by JCV is a distribution within s209(2)(b) and whether the amount of such distribution must be treated as being at market value (which we have found to be £1) by reason of paragraph 92 of Schedule 29 or whether, as HMRC submit, the market value rule does not apply (relying on paragraph 92(4A)).

129. There are various limbs to the meaning of a distribution under s209(2)(b), namely that it is "out of assets of the company" and "in respect of shares in the company", and that it does not include so much of the distribution (if any) which "is, when it is made, equal in amount or value to any new consideration received by the company for the distribution". Section 254 then sets out the interpretation to be given to these phrases.

130. At the outset we note that the JCV 2009 Accounts did not treat the payment as a distribution and that the Joint Report records (at [10b]) that Mr Holgate and Mr Dickinson agree that if the appropriate valuation for accounting purposes was £1 then the payment of £8.25m should have been treated by JCV as a distribution. They explain that this is on the grounds that JCV has paid to JCO (and thus, in substance to JATC) £8.25m and gained nothing of value in return. The payment to JCO is equivalent in its effect to JCV paying a dividend distribution to its parent, JCHL, which is owned by JATC. The Joint Report does not address the absence of sufficient distributable reserves. In any event, we do not consider that either of these points (ie the actual accounting treatment or what the accountants now agree that it should have been) is of itself relevant in determining whether the payment was a distribution within s209(2)(b). That provision contains its own definition of distribution, and that needs to be applied to the facts before us.

131. We are satisfied that the payment of £8.25 million was made "out of assets of" JCV for this purpose.

132. Section 254(9) provides simply that a distribution is treated as made, or consideration as provided, out of assets of a company if the cost falls on the company. The £8.25 million was a cost to JCV, whether viewed in terms of cash (as SAF [11] records that it did actually make a payment of that amount) or its accounts, which record the acquisition of goodwill for a cost of £8.25 million (albeit that this then begs the question as to new consideration, but we consider that separately).

133. As to whether this was "in respect of shares in the company", Ms Chaudhury contrasted this language with that used in, eg, s209(4) ICTA 1988 which refers to a payment being made "to a member" and submitted that the indirect nature of the shareholding cannot prevent the payment being "in respect of shares" in JCV where JATC was the sole indirect shareholder.

134. Section 254(12) provides that a thing is to be regarded as done in respect of a share if it is done "to a person as being the holder of the share". We consider that this does require that something is done to a person in their capacity as shareholder, albeit that this can extend to capture acts done to indirect shareholders. But the fact that the recipient is a shareholder, whether direct or indirect, is not of itself sufficient to mean that it was necessarily in respect of shares in the company.

135. The business of JCO was treated by s118ZA(1) ICTA 1988 as being carried on in partnership by its partners, ie JCE and JATC, anything done to or in relation to the partnership in connection with its activities is treated as done to the members as partners, and the property of the partnership is treated as held by the members as partnership property. The BTNA is between JCO and JCV, but this transparency for corporation tax purposes means that the amount stated to be payable as consideration was payable to JCE and JATC as partners in JCO. There was no submission by HMRC that the valuation had been made otherwise than in good

faith, and it is notable that although the expert evidence before us as to valuation for the Appellants was the report of Mr Brewer, there had been three earlier reports (albeit that two were prepared by BHG) concluding that the business had substantial value (the lowest being £8.25 million).

136. JATC received £8.25 million as he was the majority partner in JCO which conducted the business, in the form of the OPLA with Specsavers. We do not accept HMRC's submission that this payment was made by JCV to JATC as the (indirect) holder of the shares in JCV, ie in respect of shares in JCV. For this reason, the payment was not a distribution within s209(2)(b).

137. This is sufficient to allow JATC's appeal, but we have also set out our conclusions on whether the payment is excluded from being a distribution as being equal in amount or value to any new consideration received by JCV.

138. Section 254(1) provides that "new consideration" means consideration not provided directly or indirectly out of the assets of the company. The only consideration received by JCV capable of potentially being such new consideration was the assets transferred under the BTNA. Given that we have decided that the market value of such assets for capital gains purposes is £1, this immediately raises the question as to whether a different valuation methodology should apply here.

139. Mr James submitted that the statutory fiction did not apply in this context and that, as JCV had the right to use the trademark (under the July 2008 Licence), the consideration received by JCV, ie the assets under the BTNA, were worth £8.25 million to JCV (even if they would not have been worth more than £1 to a hypothetical purchaser). He rejected Ms Chaudhury's argument that this sought to apply a purely subjective valuation for which, she submitted, there was no authority, but instead Mr James submitted that it was an objective valuation to the company, but having regard to its own characteristics.

140. We consider there is some merit in looking at the position of JCV itself in this context, as we are being asked to assess whether it has received new consideration at least equal to the £8.25 million paid. We are conscious that there was no witness evidence of fact on behalf of JCV. We do, however, have the accounts of JCV, and the JCV 2009 Accounts recognise assets acquired from JCO of £8.25 million. That implies that they did constitute new consideration of that amount. However, HMRC challenge those accounts, submitting that they are not in accordance with GAAP (albeit that this submission was not made in the context of HMRC's submissions on distributions but only in relation to whether JCV is entitled to amortise the £8.25 million paid under the BTNA).

141. We address the accounting treatment in the context of JCV. The difficulty we have with Mr James' argument is that whilst it may well be said that the business has a greater value to JCV than to a purchaser which does not already have a licence, the definition looks at the new consideration received, ie the assets transferred. Whilst we consider the point finely balanced, we have concluded that we should not allow a marriage value concept here. The consequence of this is that JCV has not received new consideration of £8.25 million.

142. If we had concluded that there is a distribution from JCV to JATC, Mr James contended that it is for HMRC to explain why such distribution is not treated as being made at market value, ie £1, given HMRC's position that paragraph 92 applies to the transfer under the BTNA, with the transfer being treated as being between JATC and JCE (on the one hand) and JCV. We set out below our conclusion that paragraph 92 does apply in this manner. However, we also agree with HMRC that, if there was a distribution within s209, then the third exception in paragraph 92(4A) would apply, such that the transaction would not be treated as a distribution

by JCV of £1. The market value rule would therefore not override the amount actually received by JATC.

143. JATC's appeal is thus not only allowed (in that we have concluded that the £8.25 million is not chargeable to income tax as a distribution), but also we have concluded that no CGT was payable on this amount as disposal proceeds. We note Mr James' position that this was not the primary submission on behalf of JATC, albeit that it is one of the range of outcomes contemplated by his alternative submissions.

JCV AND INTANGIBLES RELIEF

144. Mr James submitted that even if the market value is £1, then there is no basis for imposing a market value figure in the accounts of JCV; the valuation of £8.25m could only be amended if either paragraph 92 or paragraph 5 of Schedule 29 applied and, he submitted, neither paragraph is in point.

145. We consider paragraph 92 first then paragraph 5 and, in the context of the latter, the expert evidence as to accounting which was before us.

Paragraph 92 Schedule 29

146. Where paragraph 92 applies, the transfer is treated "for all purposes of the Taxes Acts (as regards both the transferor and the transferee) as being at market value":

(1) Paragraph 92 applies where there is a transfer of an intangible asset from a related party to a company (paragraph 92(1)), subject to four exceptions.

(2) The only potentially relevant exception is the third exception in paragraph 92(4A), which applies where (a) the asset is transferred to the company at more than its market value, (b) the related party is not a company and (c) the transfer gives rise (or would give rise but for paragraph 92(1)) to an amount to be taken into account in computing any person's income, profits or losses for tax purposes by virtue of s209 ICTA 1988.

147. HMRC's primary submission was that this third exception does apply, such that the market value rule in paragraph 92 does not apply to JCV, this being the reason for their decision that the £8.25 million is taxable in JATC's hands as a distribution. (HMRC relied on paragraph 5 in support of their submission that JCV is not entitled to intangibles relief for the £8.25 million.) However, as we have decided that this amount is not a distribution, this exception in paragraph 92(4A) cannot apply and we therefore address the parties' submissions as to whether the transfer of the intangible assets under the BTNA was within paragraph 92(1).

148. Mr James submitted that JCO and JCV were not related parties for the purposes of paragraph 92 because JCO was not a participator in JCV nor an associate of one within the meaning of paragraph 95. Mr James did accept that JATC and JCV are related parties within paragraph 95. HMRC's position is that this is all that is required and that paragraph 92(1) thus applies. JCV's position is that the relevant transfer is from JCO to JCV, ie that the LLP is not transparent for this purpose. Mr James submitted that this proposition was clear from the decision of the Tribunal in *Armajaro*, and that if there was any doubt this was removed by changes in legislation which were introduced in 2016 to address the lacuna which resulted from this interpretation.

149. Related parties are defined in paragraph 95, Case Three of which is that a person ("P") is a related party in relation to a company ("C") if C is a close company and P is or is an associate of a participator in C or a participator in a company that has control of or holds a major interest in C. JATC is a related party in relation to JCV as JATC is a participator in a company (JCHL) that has control of JCV. JCE is also a related party to JCV as it is a partner of JATC and thus an associate of JATC. However, we agree with Mr James that there is no

provision which enables JCO, as an LLP, to be a participator in JCV or an associate of a participator in JCV. The question is therefore whether for the purposes of paragraph 92 we need to treat the transfer as being between JATC and JCE (as partners in JCO) and JCV (as HMRC submit) or between JCO and JCV (as JCV submit).

150. Section 118ZA(1) ICTA 1988 provides that LLPs are transparent "for corporation tax purposes" as regards the activities of the LLP, anything done by, to or in relation to the LLP and the property of the LLP. We consider that this is very clear and that the consequence of this is that the transfer of the Assets under the BTNA for the purposes of paragraph 92 is from JATC to JCV, and that the market value rule therefore applies.

151. We are not persuaded by Mr James' submissions to the contrary.

152. Mr James submitted that it has been clear since the decision in *Armajaro Holdings Ltd v HMRC* [2013] UKFTT 571 that LLPs cannot be looked through for intangibles purposes because intangibles relief follows the accounts and LLPs in particular are separate entities for accounting purposes.

153. In *Armajaro* AHL had claimed intangibles relief in respect of its acquisition of other members' interest in AAM LLP, arguing that it had acquired an interest in the underlying goodwill of the LLP. The Tribunal decided that AHL was not entitled to intangibles relief in respect of its acquisition of the interests of other members in AAM. In that decision:

(1) The Tribunal stated it was not directly concerned with the provisions of paragraph 95 and the concept of related parties, and declined to express a view on the submission that an LLP cannot be a related party (at [28]).

(2) Entitlement to relief under Schedule 29 is dependent on the expenditure being reflected in the accounts of the company claiming entitlement to relief ([31]).

(3) In accordance with GAAP, AHL could not include AAM's goodwill in AHL's accounts. AHL showed its interest in AAM as a subsidiary undertaking. Nothing in s118ZA requires or permits a corporate member of an LLP to treat the assets of the LLP as is own for accounting purposes. Section 118ZA does not change the accounting rules or practice or deem the accounts to include something that they do not include (see [32]).

154. We are not bound by the decision in *Armajaro* but in any event we do not consider that our conclusion is inconsistent therewith. *Armajaro* concerned a refusal by the Tribunal to apply s118ZA to treat intangible assets of an LLP as those of the corporate partner for accounting purposes, and thus denied relief under Schedule 29 in circumstances where no expenditure on intangible assets was reflected in the accounts of the person claiming relief. The Tribunal did not conclude that LLPs are never transparent for the purposes of Schedule 29.

155. In the alternative, Mr James referred to the legislation introduced in Finance Act 2016 ("FA 2016"), submitting that if HMRC's argument is correct in this case, it is unclear why it was necessary to legislate to this effect at all in 2016; and if HMRC are correct that LLPs are looked through and are not parties to a transaction for intangibles purposes, then the legislative amendments simply do not work (which, he submits, cannot be correct).

156. Section 845(1) Corporation Tax Act 2009 ("CTA 2009") is in identical terms to paragraph 92(1). Section 845(4A) and (4B), which were inserted by FA 2016, then state:

> "(4A) References in subsection (1) to a related party in relation to a company are to be read as including references to a person in circumstances where the participation condition is met as between that person and the company.

> (4B) References in subsection (4A) to a company include a firm in a case where, for section 1259 purposes, references in subsection (1) to a company are read as references to the firm."

157. According to the Explanatory Notes to clause 49 of FA 2016, which introduced sections 845(A) to (F):

> "1. The clause confirms that transfers of assets between companies and other bodies, such as partnerships or Limited Liability Partnerships (LLPs), in respect of which the participation condition is satisfied are brought into account at their market value.
>
> …
>
> 3. New Section 845(4A) enables section 845 to apply to transfers between companies and other bodies, such as partnerships or LLPs, in relation to whom the "participation condition" is met…
>
> Background note
>
> …
>
> 12. …HM Revenue and Customs (HMRC) has identified arrangements that use entities such as partnerships or LLPs to transfer assets in ways that aim to bring the assets within the new rules without an effective change of economic ownership. These arrangements also seek to disapply the rules that ensure that these transfers are brought into account at market value for tax purposes.
>
> 13. HMRC does not consider that these arrangements work in the way that they are claimed to work. This measure confirms that these arrangements are not effective in preventing the correct value being used when assets within the Part 8 regime are transferred between companies and other bodies such as partnerships or LLPs, where the participation condition is satisfied."

158. The amendment made by the introduction of s845(4A) is somewhat neutral in the present context; it extends the range of potential related parties and does not of itself address the prior question as to the parties to a transfer. However, we do note that the Explanatory Notes cited above do appear to pre-suppose that a transfer may be made between a company and another body such as an LLP, and that it is the relationship between those entities that needs to be considered rather than between the company and the partners in the LLP. This flows through into the approach taken in s845(4B) which extends the meaning of company to include a firm (and references to a firm include an LLP), and therefore contemplates that an LLP may itself be a party to the transfer referred to in s845(1). We also note that the Explanatory Notes set out HMRC's position that the arrangements which had been seeking to exploit the rules do not work, albeit that we recognise that this language is routinely used in the context of changes which are being introduced to seek to counter what HMRC perceives as tax avoidance arrangements.

159. There was no equivalent to s845(4A) or (4B) in the years under appeal, and Mr James submits that such provisions would have been necessary and their subsequent introduction supports his submission that, in their absence, the transfer in question was between JCO and JCV and they are not related parties. We have considered the changes which were introduced, and the Explanatory Notes which accompanied their introduction, but are not persuaded by Mr James' submissions. We recognise that Parliament was seeking to ensure that certain arrangements did not fall outside s845(1), in circumstances where HMRC's published position was that the arrangements did not work in any event, ie that the changes were not required. We cannot comment on the range of transactions which were in the mind of the draftsman of these new provisions, or which were being referred to in the Explanatory Notes. We have before us

the facts of the present appeal, the drafting of paragraph 92(1) and s118ZA and, even taking account of the decision to introduce changes in 2016, we remain of the opinion that the transfer to which paragraph 92(1) must be applied is treated by s118ZA as between JATC and JCE (on the one hand) and JCV. Those parties are related parties within the meaning of paragraph 95 and accordingly the transfer is treated for all purposes of the Taxes Acts, including for the purposes of Schedule 29, as being at market value, ie £1.

160. JCV's appeal is dismissed.

Paragraph 5 of Schedule 29

161. HMRC's primary submission had relied on paragraph 5 of Schedule 29 to deny intangibles relief to JCV. We address this in full as not only did we hear submissions from both parties but we also had expert evidence as to accounting and in relation to which we should make our findings.

162. Paragraph 5 provided as follows:

> "(1) If a company does not draw up accounts in accordance with generally accepted accounting practice ("correct accounts")—
>
> (a) the provisions of this Schedule apply as if correct accounts had been drawn up, and
>
> (b) the amounts referred to in this Schedule as being recognised for accounting purposes are those that would have been recognised if correct accounts had been drawn up.
>
> (2) If a company draws up accounts that rely to any extent on amounts derived from an earlier period of account for which the company did not draw up correct accounts, the amounts referred to in this Schedule as being recognised for accounting purposes in the later period are those that would have been recognised if correct accounts had been drawn up for the earlier period."

163. Mr James submitted that:

(1) The JCV 2009 Accounts were drawn up in accordance with GAAP, as were the accounts for all relevant accounting periods.

(2) Even if the market value of the assets transferred is determined by the Tribunal to be £1, that is new information, a change of estimate. It is not an error. In any event, paragraph 5 only applies where the accounts were wrong, or not in accordance with GAAP, at the time they were prepared, not if they are subsequently determined to be in error, or where the accounts in a subsequent accounting period take into account the correction of an error.

(3) Even if the value is £1 for tax purposes, this is not the fair value for accounting purposes.

164. Ms Chaudhury submitted that the recognition of £8.25m of goodwill and its amortisation in JCV's accounts means that JCV has not drawn up its accounts in accordance with GAAP because the value of JCO's business was £1. No intangible assets should have been recognised and no amortisation charge expensed. Under paragraph 5(1), the provisions of Schedule 29 apply as if the accounts had been drawn up correctly, which in this context means that the accounts have to be adjusted as if the acquired goodwill is recognised at fair value, which is the same as its market value.

Expert evidence as to accounting treatment

165. The Appellants relied on the expert evidence of Peter Holgate. HMRC relied on the expert evidence of Iain Dickinson. Mr Holgate and Mr Dickinson had also agreed a Joint Report, which we found very helpful.

166. The Joint Report sets out various areas of agreement and identifies the points on which Mr Holgate and Mr Dickinson disagree, setting out their respective positions. We consider that Joint Report first, before then considering the evidence of each expert on the areas of disagreement (both as set out in their report and given at the hearing).

Joint Report

167. The Joint Report identifies the following areas of agreement (and we note that FRSSE is the Financial reporting standard for smaller entities):

> "6. The key issue is whether the amount of £8.25m paid by JCV to JCO should have been accounted for as (a) goodwill which was amortised over a useful economic life of five years; or (b) a distribution to owners.
>
> 7. We agree that a business, including the contract with Specsavers, was acquired by JCV.
>
> 8. We agree that the valuation of this business "for tax purposes" is a matter to be determined by the Tribunal, on the basis of expert evidence. However, we disagree as to whether this has any accounting implications for the 2009 accounts of JCV.
>
> 9. We agree that the appropriate valuation of the acquired business would be the one which measured the cost of the business at the "fair value" of the consideration given in accordance with the FRSSE and FRS 7. We agree that valuation is not a precise science. For example, in the context of the BHG valuation, figures of £7.25m or £9.25m might well have been appropriate for the valuation of the business and thus the transaction price, rather than £8.25m. We agree the accounts should report the substance of transactions in accordance with the FRSSE and FRS 5 and the appropriate valuation of the business acquired should reflect the commercial effect of the arrangements and not merely their legal form.
>
> 10. We agree on the appropriate accounting treatment, as follows:
>
> a. If the appropriate valuation for accounting purposes, was £8.25m ("BHG valuation") (or in the order of £8.25m), we agree that the payment of £8.25m should have been treated by JCV as goodwill. This goodwill should have been amortised over its useful economic life of five years. This is on the grounds that JCV acquired a valuable asset being the business including the contract with Specsavers. This is the accounting treatment that was adopted by JCV.
>
> b. If the appropriate valuation for accounting purposes, was £1 ("SAV valuation"), we agree that the payment of £8.25m should have been treated by JCV as a distribution. This is on the grounds that JCV has paid to JCO (and thus, in substance to Mr Conran) £8.25m and gained nothing of value in return. The payment to JCO is equivalent in its effect to JCV paying a dividend distribution to its parent, JCH, which is owned by Mr Conran.
>
> c. If the appropriate valuation of the business for accounting purposes were determined to be, say, £5m ("Alternative valuation"), that would be outside the reasonable range of valuations and in our view the appropriate accounting treatment would be a combination of the two methods described above, that is: £5m of the payment would be treated as the cost of acquisition and would appear as goodwill; £3.25m of the payment would be treated as a distribution.

> 11. We agree that Mr Conran's licence of the trademarks is, as is appropriate within GAAP, not recognised in the financial statements of JCV or JCO.
>
> …
>
> 17. On the question of a potential prior year adjustment, we agree as follows. If the BHG valuation of the business is determined by the Tribunal to be £8.25m for tax purposes, no further consideration of the accounting treatment adopted by JCV would be required. However, if the SAV valuation of £1 is determined by the Tribunal to be appropriate for tax purposes, the question arises as to whether and, if so, how this new information should be reflected in the next accounts of JCV. As with other unusual or judgmental matters, the director should take appropriate accounting advice and seek to agree the treatment with the auditors. There is no requirement or suggestion that the director should adopt the determination of the tax Tribunal and revise the filed 2009 to 2014 accounts. In practice, since the goodwill is fully amortised, the difference in accounting treatment between a change of estimate and prior period adjustment, as described below, is minimal. We also note that the distinction between what is an "error" and what is an "estimate" is clear in principle but sometimes the categorisation can be difficult in practice. This is a matter of judgment for the director so we believe the choice of accounting treatment depends on the view of JATC in his capacity as director of JCV as to whether he considers the previous accounts were in accordance with GAAP at the time they were prepared:
>
> a. If JATC believes that, despite the ruling of the Tribunal on the taxation of JCV, the 2009 (and subsequent) accounts of JCV were appropriate and gave a true and fair view, he would leave those years' accounts unchanged and would treat any tax payable as an expense in the profit and loss account of the 31 March 2020 accounts. This treatment would be classified by accountants as a 'change of estimate'.
>
> b. If JATC takes the view that the ruling of the Tribunal on tax matters should also be understood to imply that the 2009 (and subsequent) accounts of JCV did not give a true and fair view, he would, in the 31 March 2020 accounts, restate the opening balances, which is how accountants deal with the correction of errors in earlier years. This would involve amending the numbers to reflect (a) no goodwill recognised, no amortisation of goodwill and any tax implications arising; and (b) a debit to retained earnings in respect of a payment that is now regarded as a distribution. Thus any tax payment that might arise would be pushed back, in accounting terms, to the period 2009-2014; and therefore does not affect the results for the year to 31 March 2020 or the comparative period. This treatment would be classified by accountants as a prior year adjustment (PYA) (or prior period adjustment)."

168. We accept these agreed conclusions of Mr Holgate and Mr Dickinson.

169. The Joint Report identified two areas of disagreement, namely:

(1) on "the central accounting question" of the appropriate valuation of the business acquired by JCV; and

(2) if the Tribunal determines that the SAV valuation of £1 is correct, whether to regard this new information as (a) coming to light now and so deal with any consequences of it in the JCV 2020 financial statements (or, now, the JCV 2022 financial statements given the time that has elapsed since preparation of the Joint Report) as a change of estimate; or (b) whether to regard it as a correction of a 2009 error and therefore treat it in the JCV 2022 financial statements as a prior period adjustment.

170. We were repeatedly taken back to the points of agreement expressed at [10] and [17] above during the hearing. Given our decision that the market value of the assets transferred was £1, [10b] then records the agreement that the payment of £8.25 million should have been treated by JCV as a distribution. The agreement at [17] relates to potential prior period adjustments and records two alternative approaches which could be taken by the director of JCV. Mr Holgate would advise JATC, as director of JCV, to adopt the approach in [17(a)], ie change of estimate, and Mr Dickinson would advise the director to adopt the approach in [17(b)], ie correction of an error.

Evidence of Peter Holgate

171. Mr Holgate's evidence was that:

(1) The JCV 2009 Accounts are in compliance with GAAP; and that this is the same for the accounts in subsequent years, with a possible caveat about whether an impairment of goodwill should have been recorded in the 2013 Accounts, and possibly also in the 2012 Accounts. This possible reservation (which he did not want to put too strongly) did not affect his opinion that the earlier accounts gave a true and fair view.

(2) He considered that the accounts show a true and fair view, his reasons for which include that the purchase price was rational, being based on a valuation which was appropriate. A "proper valuation" was carried out, and, on the basis of that valuation, the transaction took place at £8.25m. During cross-examination he added that he had been puzzled by the clauses dealing with adjustments to the consideration (at clauses 4.1.1 and 4.1.2 of the BTNA).

(3) His report dealt with fair value (at [4.18]), stating "In recent years, "fair value" has been used increasingly in accounting, particularly in International Accounting Standards, and in the new UK GAAP…The use of a model is commonly used in the absence of a quoted price and involves asking, hypothetically, what a knowledgeable, willing party would receive or would pay." His report says (at [4.22]) that "fair value has to be a price that makes sense commercially". The only approach to determining fair value that is commercially rational (and not pointless or, worse, inoperable) and stays as close as possible to the circumstances of the actual transaction is to assume that the buyer either has or is granted, as part of the transaction, the right to use the trademarks for the purposes of the Specsavers contract. On this basis, the fair value would be in the order of £8.25m. He accepted that £8.25m makes no commercial sense if the buyer has no access to the trademark or cannot get it at no cost.

(4) Mr Holgate was taken to PwC's accounting manual which, in the section dealing with the meaning of fair value (for the purposes of FRS 7), included at [25.243] that "The standard requires that fair values of assets and liabilities should be based on conditions at the date of acquisition. They should not generally be affected by matters arising after this date…" He said the accounts were not wrong at the time; it is a change in estimate.

(5) The question whether JCV and its auditors were entitled to rely upon the BHG 2008 Valuation when preparing/auditing the JCV 2009 Accounts was not strictly an accounting question, more in the area of directors' responsibilities and auditing procedures. That valuation was "for tax purposes" and that is not automatically the same for accounting purposes.

(6) If the Tribunal now determined the value was £1, this was "for tax purposes". That decision would need to be reflected in JCV's 2022 accounts in some way (with narrative); but that does not mean that the JCV 2009 Accounts were wrong or not in accordance with GAAP.

(7) His report states that there would not need to be a prior year adjustment. Prior year adjustments are defined (in Section C, Definitions, of FRSSE) as "Material adjustments applicable to prior periods arising from changes in accounting policies or from the correction of fundamental errors. They do not include normal recurring adjustments or corrections of accounting estimates made in prior periods." Mr Holgate considered that the circumstances do not amount to a fundamental error, because a fundamental error refers to a major error that was made at the time: a particular set of accounts were wrong at the time they were prepared. In contrast, if the position changes subsequently, albeit in relation to a matter originating in 2009, the effect is booked in the later accounts, with relevant disclosures. The information available at the time of preparing the JCV 2009 Accounts was the BHG 2008 Valuation. The ruling of the Tribunal was not available at the time. Mr Holgate thus supports the treatment outlined in [17(a)] of the Joint Report and, if asked, would advise the director of JCV to that effect.

(8) Irrespective of whether JCV (following a conclusion of the Tribunal that the value was £1) decided to adopt the approach of a change of estimate or a correction of an error, the JCV 2009 Accounts had still been drawn up in accordance with GAAP. So, although he and Mr Dickinson disagreed as to this matter (as set out at [17] of the Joint Report), this difference between them did not determine the question as to whether the accounts were in accordance with GAAP.

172. The above summary incorporates the relevant evidence given by Mr Holgate in cross-examination and in answering questions from the panel.

Evidence of Iain Dickinson

173. Mr Dickinson's evidence was that:

(1) The appropriate valuation is a matter for the Tribunal to determine on the basis of expert valuation evidence. The Tribunal's valuation decision would have the implications for the 2009 accounts of JCV as set out in [10] of the Joint Report.

(2) He disagrees with the distinction Mr Holgate draws between a valuation of the acquired business for "accounting purposes" and a valuation for "tax purposes" and considers that no such distinction is necessary in this case. Both the BHG 2008 Report and the SAV valuation are valuing the same business, at the same point in time and are professional valuations of the cost of the acquired business at the "fair value" of the consideration given in accordance with the FRSSE and FRS 7. They are, accordingly, to use Mr Holgate's terminology, valuations for both "tax purposes" and "accounting purposes" in this case.

(3) In response to the question posed in his instructions "Was the recognition of £8.25m of goodwill and the related amortisation in Vision's accounts in accordance with GAAP, assuming that the SAV valuation of £1 for the transfer of the business is correct?", his opinion in the report is that if the Tribunal determines that the SAV valuation of £1 is the correct valuation then the JCV 2009 Accounts are not in accordance with GAAP because goodwill is overstated (at [3.2] of his report). He relies on two key reasons for this conclusion:

(a) The cost of the acquired business was in fact £1 and therefore the accounts prepared using a valuation of £8.25m and recognising £8.25m of goodwill do not give a true and fair view.

(b) His understanding of the BTNA is that consideration is adjusted to £1, although he notes that the interpretation of the BTNA clauses is a legal matter.

(4) Addressing what the payment from JCV to JCO can best be classified as in accordance with GAAP, he says:

> "3.4 If the SAV valuation is correct, my understanding of the BTNA is that JCV has a legal right to recover the overpayment of £8.25m from JCO. If JCV had sufficient evidence that the overpayment was expected to be recoverable then JCV should have recognised a debt from JCO in the 2009 accounts of JCV in accordance with GAAP.
>
> 3.5 If the overpayment was not recoverable from JCO then JCV should record the payment as a distribution. This opinion is subject to the availability of distributable reserves in JCV."

(5) In his report Mr Dickinson refers to Mr Holgate's draft report and addresses points of agreement and disagreement between them. In the context of the section in Mr Holgate's report on prior period adjustments, Mr Dickinson sets out the following:

> "5.8 The Holgate report is not clear on the technical basis for his opinion in this part of the report however, I assume, that it is Mr Holgate's view that any change in the valuation is booked in the period that the valuation uncertainty is resolved because it is a change of estimate. I note that Mr Holgate also states that "…a fundamental error refers to a major error that was made at the time: a particular set of accounts were wrong at the time they were prepared." Mr Holgate refers to a "fundamental error" a term from FRS 3 'Reporting Financial Performance' ("FRS 3").
>
> 5.9 I disagree, it is my opinion, that if the SAV was correct, then the 2009 accounts of JCV were not in accordance with GAAP. Under GAAP, relying on the BHG valuation of £8.25m rather than the correct SAV valuation of £1 for the fair value of consideration caused a fundamental error in the 2009 accounts that materially understated goodwill.
>
> 5.10 As I have set out above, GAAP required the consideration to be measured at fair value. The directors were correct to obtain the valuation work of BHG in drawing up the 2009 accounts of JCV for accounting purposes. The BHG valuation was a valuation opinion available to the directors at the time they signed and approved the 2009 accounts. There was a known valuation uncertainty for the business transferred as evidenced by the clearance and the post transaction check which was unresolved when the 2009 accounts were approved on 27 January 2010. This valuation uncertainty for tax was the same valuation uncertainty that applied to the measurement of fair value of consideration in the accounts. A disclosure could have been made in the accounts given the potential uncertainty over the goodwill recognised. I note that a disclosure has been included in the 2016 accounts of JCV.
>
> 5.11 If and when the directors accept the valuation work was not correct, either because they accept the SAV valuation, or the Tribunal directs a valuation of £1 (or some alternative figure) then the 2009 accounts will be in error.
>
> …
>
> 5.14 In summary, if the SAV valuation is correct, the material error arose in 2009 from the wrong valuation being used for the business transferred."

(6) A decision of the Tribunal that the valuation is £1 should be dealt with in the 2022 accounts as the correction of an error. Accordingly, Mr Dickinson believes the way to treat the new information is in accordance with the treatment outlined at [17(b)] of the Joint Report and, if asked, would advise the director of JCV to that effect.

(7) The decision taken as to whether to follow the treatment in [17(a)] or [17(b)] of the Joint Report has no bearing on whether the JCV 2009 Accounts are in accordance with GAAP.

174. We have considered carefully Mr Dickinson's oral evidence, some of which is reflected above. Particular exchanges during the hearing are set out below:

Mr James	[Referred to evidence of Mr Holgate] "…going back to 2009, 2010, 2011 and 2012, so at the time, in terms of whether the accounts at that point were drawn up in accordance with GAAP, I understand you to be in agreement with Mr Holgate that at the time the accounts were drawn up in accordance with GAAP based on the information available?
Mr Dickinson	In relation to that, what I would say is the accounts were drawn up based on the BHG valuation. Then that was believed to be the correct valuation at the time by the directors. I think if this Tribunal were to find that the SAV valuation is correct, then that would be a valuation in accordance with GAAP…
Mr James	But that would impact the current year's accounts…Just to be clear, you are saying that at the time in 2009 and 2010 etc, the accounts being based on what they believe to be a correct valuation do not, according to normal principles by BHG, that's what the directors have to go on, and the accounts at that point and as submitted were in accordance with GAAP?
Mr Dickinson	No. They were drawn up based on the BHG valuation, but if we subsequently find the BHG valuation is in error, then those accounts are not in accordance with GAAP…
Mr James	[Any error] would require to be recognised in some way now, but at the time in 2009 when the accounts were submitted, they were submitted in accordance with GAAP at that point?
Mr Dickinson	Yes, and in – yes. So they were drawn up and based on the VAT valuation at the time. We've now subsequently – If the Tribunal were to adopt the SAV valuation we would be – the uncertainty in relation to valuation of the goodwill would mean that those accounts are not in accordance with GAAP now. …
Judge Zaman	[If the Tribunal finds the SAV valuation is correct, and the directors decide in 2022 to treat this as an error] does that necessarily mean that the 2009 accounts were wrong?
Mr Dickinson	So, I don't think it does. So I know that sounds odd, but I think actually each set of accounts is drawn up in its own – independently. I know that sounds odd. …
Judge Zaman	…does that mean that the 2009 accounts are not GAAP compliant?
Mr Dickinson	No, as I say, the separate determination, they are independent. …
Mr Dickinson	Yes. So my position on the 2009 accounts would be what is set out in the joint report in paragraphs 10(a), (b) and (c).

Judge Zaman	[Referred to [10] of the Joint Report]…paragraph [10(b)] is then silent as to whether that means what was actually done was GAAP compliant or not.
Mr Dickinson	Yes, as I would say, and actually I think this is in my first report, in the joint report, if you link that up to paragraph 9, we agreed appropriate valuation for the acquired business to be one which [recorded] the costs of the business at fair value in the consideration given in accordance with FRSSE and FRS7. … So if the fair value of consideration given is £1, that's the bit that means that the accounts aren't in accordance in GAAP, because they've shown goodwill of 8.25 million when they should have shown goodwill of £1 and a distribution of 8.25 million for the cash [paid]. So it's actually linking the agreement in 9 with the words in 10(b) I guess.
	…[Re-examination by Ms Chaudhury]…
Ms Chaudhury	[Referred to 5.8-5.10]
Mr Dickinson	[Confirmed he did not depart from these paragraphs]
Ms Chaudhury	Q. Right. I'm hoping this hasn't got lost in your evidence, but in 5.9 you do say that if the SAV valuation was correct, then the 2009 accounts were not in accordance with GAAP and I did ask you to confirm your report and I take it you haven't departed from that view?
Mr Dickinson	No.
Ms Chaudhury	And just on this point about a new valuation, because it was put to you following 2009, the value of the business was 8.25 million, but if the Tribunal now finds that the value was a pound, when if ever was the valuation, the value of the business 8.25 million?
Mr Dickinson	A. Well, I would say that it wasn't. So there was only one requirement and that was to identify fair value of the business, the cost of acquisition at the time the acquisition happened and, if the correct valuation of the business was £1, then to use 8.25 million and right there, material over-stated goodwill and the accounts in 2009 were wrong …
Judge Zaman	[Referring back to 5.9]… my understanding of this was that you did say something different when you answered my questions earlier … and yet you have just said to Ms Choudhury that you are not changing your opinion, so… are you saying that you stand by that first sentence of 5.9 that the 2009 accounts were not in accordance with GAAP?
Mr Dickinson	A. Yes, I am sorry if I have given other evidence. …
Judge Zaman	So again, going back to one of my earlier questions, does that mean that your position is that wherever after the event an error is identified, that always means that the original accounts were not GAAP compliant?

Mr Dickinson	So, no, because some errors would not be significant enough in the 2009 accounts.

Discussion and conclusions

175. We need to reach a decision as to whether paragraph 5 applies on the basis that the JCV 2009 Accounts (and those for the APEs 31 March 2010 to 31 March 2014) were not drawn up in accordance with GAAP, ie were not "correct accounts".

176. One difficulty we have with the expert evidence relates to the questions posed to the experts and addressed by them in their reports. They were asked various questions, overlapping but slightly different, and although we have considered the whole of their reports, it is pertinent to note that:

(1) Mr Holgate was asked "Are the accounts of JCV, and in particular those for 2009 (document A4), in accordance with UK GAAP? Please address in particular Clauses 57 and 58 of HMRC's Statement of Case."

(2) Mr Dickinson was asked (as amended following his request for further clarification with his instructing lawyer) "Was the recognition of £8.25m of goodwill and the related amortisation in Vision's accounts in accordance with GAAP, assuming that the SAV valuation of [£1] for the transfer of the business is correct? Further to this, please provide your conclusions/comments on what the payment made by JC Vision to JCO LLP can best be classified as in accordance with GAAP."

177. Neither of these questions asked the experts to comment on the language used in paragraph 5(1) relating to whether the accounts were *drawn up* in accordance with GAAP. We are wary of overstating the significance of these words, but given that one interpretation of Mr Dickinson's evidence was that the accounts may become in error only if the Tribunal determined the valuation was £1, ie that no such error may have existed prior to that time, there was potential for these words to be construed as significant. We are aware that this language in paragraph 5(1) contrasts with, eg, that used for loan relationships, another area where the tax treatment follows the accounts, where s307(2) CTA 2009 provides "amounts to be brought into account…are those that are recognised in determining the company's profit or loss for the period in accordance with [GAAP]". It was this language that prompted some of the panel's questions to the experts at the hearing, in particular to Mr Dickinson, and we take this into account in reaching our conclusions.

178. There were significant areas of agreement between the experts, notably at [9], [10] and [17] of their Joint Report; but the issues we need to determine were at the heart of their concisely expressed areas of disagreement.

179. We had some concerns about the evidence given by both experts, although that is not to suggest that we doubted that they were giving their evidence in good faith and having regard to their duties as experts.

180. Mr Holgate's credentials are clearly excellent, and he was able to give clear, thoughtful explanations of provisions of FRSSE, and indicate areas that were not addressed by that standard and where guidance needed to be sought from FRS7. His evidence was consistent (which is in part why we have been able to set it out fairly briefly above). Mr Holgate had thought carefully about the situation of the hypothetical purchaser; but he was not an expert on valuation. He readily acknowledged areas where he had not fully comprehended details of the legal agreements (saying that the consideration adjustment clauses in the BTNA were puzzling).

181. In closing Ms Chaudhury submitted that Mr Holgate had conceded that if the valuation adopted by JCV had been conducted on an incorrect basis, then using that valuation would be

an error and would mean that the accounts were not in accordance with GAAP. However, that was not Mr Holgate's evidence. Judge Zaman had referred Mr Holgate to the difference between the experts as to whether, when looking at prior year adjustments, there was a correction of an error or a change of estimate and asked Mr Holgate to give an example, relevant in the context of this transaction, of something that he would regard as an error. Mr Holgate suggested capitalising the goodwill at £8.25 million and then not amortising it would be an error. In re-examination Ms Chaudhury indicated that she had a question arising from the question from the panel as to what would be an error, and asked whether, if the valuation used for the accounts had valued the wrong asset, that would that be an error. She then expanded on this, asking if BHG had valued the business with the right to use the trademarks implicit in it but it was then found that they had valued the wrong thing, would that constitute an error. Mr Holgate said "I suppose it would be an error". However, the only question from the panel to which Ms Chaudhury could have been referring was that related to prior year adjustments and Mr Holgate's evidence as to error must be considered in that context.

182. Nevertheless, whilst Mr Holgate did consistently and clearly explain his opinion that the accounts had been prepared in accordance with GAAP, showing a true and fair view based on a valuation which was appropriate (and thus, we considered, did address the language of paragraph 5(1)), we had some doubt as to whether this fully engaged with the issue that might arise if, as Ms Chaudhury put it in the context of prior year adjustments, the valuation had been of the wrong asset.

183. We considered that Mr Dickinson had not properly understood the adjustment mechanism in the BTNA, and the fact that it related to a denial of relief for pre-2002 intangible assets, rather than dealing with a situation where relief was denied for other reasons. This was potentially a significant weakness in his evidence given that it was this adjustment mechanism that was referred to as one (of two) key reasons for his conclusion that the accounts were not in accordance with GAAP. His oral evidence was more reassuring in this regard, as his explanation focused on the directors having relied on a valuation which was subsequently determined by the Tribunal to be incorrect.

184. We also had concerns as to the consistency of Mr Dickinson's evidence, and this was apparent from the questions which the panel put to Mr Dickinson at the hearing (with both members of the panel asking questions and following-up both on questions put by way of cross-examination and in re-examination). Mr James and Ms Chaudhury made submissions in closing as to whether or not Mr Dickinson had changed his evidence. Ms Chaudhury submitted that Mr Dickinson's expert opinion was set out in section 3 of his report, and that he had not changed that evidence; his opinions in section 5 were his comments on a draft of Mr Holgate's report, and his oral evidence, if different, was because he was asked different questions.

185. Mr Dickinson's report, addressing the question as to whether the recognition of goodwill of £8.25 million was in accordance with GAAP if we find that the SAV valuation is correct, clearly stated (at [3.2]) that in this situation "the 2009 accounts are not in accordance with UK GAAP". Later, addressing Mr Holgate's discussion of prior period adjustments, he said (at [5.11]) that "if and when…[the Tribunal determines that the SAV valuation is correct]…then the 2009 accounts will be in error". Having regard to the fact that paragraph 5(1) applies "if a company does not draw up accounts in accordance with [GAAP]", a question we had identified with Mr Dickinson's evidence in his report was whether he was expressing an opinion (notwithstanding the apparent clarity of [3.2]) that the accounts only became in error, or not in accordance with GAAP, when the Tribunal determined the valuation was £1.

186. Having considered the evidence of both experts, we conclude:

(1) The Joint Report at [17] sets out two different approaches to prior year adjustments, and records that the distinction between what is an "error" and what is an "estimate" is clear in principle but can be difficult in practice. Mr Dickinson would advise the director to take the former approach whilst Mr Holgate the latter. However, we accept the evidence which both experts gave at the hearing that the decision which is taken in 2022 as to the preferred approach, ie following the decision of the Tribunal, does not determine the answer to the question whether the accounts as drawn up were in accordance with GAAP.

(2) Our decision that the market value of the assets transferred under the BTNA was £1 is made for relevant tax purposes. Nevertheless, we accept, based on Mr Dickinson's evidence, that this should also be fair value for accounting purposes. In accepting this evidence we are conscious that a reason for our decision to prefer the expert evidence as to valuation of Ms Beard over that of Mr Brewer was the identification of the assets which are to be valued. Mr Holgate acknowledged that the accounts should show a true and fair view of the transaction, and reflect a price that makes sense commercially; he accepted that £8.25 million makes no commercial sense if the purchaser has no access to the trademark (or cannot get such access at no cost).

(3) Mr Holgate's evidence was that, irrespective of the position which is taken now as to prior year adjustments, and as to what we now know about the appropriate valuation, JCV's accounts were, when they were drawn up, prepared in accordance with GAAP for the reasons he gave. There were parts of Mr Dickinson's oral evidence that appeared to agree with this – he stated that each set of accounts is drawn up independently, and had to be considered separately; that they were submitted in accordance with GAAP in 2010; but that they are not now in accordance with GAAP given the decision on valuation. However, when considering the interpretation of paragraph 5(1), we reject an approach which looks only at the GAAP-compliance (or otherwise) at the moment the accounts are finalised and signed-off by the director. To take such an approach would mean that intangibles relief would be available by reference to the accounts as filed, if they could be said to have been thought to be in accordance with GAAP at that time, even if it is subsequently shown that they were not in accordance with GAAP, ie that they should have been prepared on a different basis. This conclusion is supported by Mr Dickinson's evidence when viewed as a whole, including not only his whole report but also his evidence given at the hearing.

187. We therefore conclude that paragraph 5 applies, and JCV is only entitled to such relief under Schedule 29 as if its accounts had been prepared reflecting the acquisition of intangible assets with a fair value of £1.

DISPENSATION

188. For the reasons given above, JATC's appeal is allowed (with the amendments required to give effect to the repayment of CGT on the proceeds of the disposal) and JCV's appeal is dismissed.

RIGHT TO APPLY FOR PERMISSION TO APPEAL

189. 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.

JEANETTE ZAMAN
TRIBUNAL JUDGE

Release date: 03 FEBRUARY 2022

APPENDIX

Statement of Agreed Facts

1. Mr Jasper A.T. Conran, OBE ("JATC") is a British fashion designer who commenced business in 1977, aged 18, designing womenswear collections. He subsequently expanded his business into other fashion categories including menswear, childrenswear, men's and women's accessories, tableware and homewares. JATC commenced charging fees to his group companies for the right to use his trademarks in the tax year ended 5 April 2002.

2. In 2007, he contemplated a further diversification into a new product category, eyewear (i.e. the design of spectacles). He had initial discussions with industry specialists including Mr Tony Harris, who ran his own optical business and had extensive connections with a number of retailers. Mr Harris introduced JATC to representatives of Specsavers International Healthcare Limited ("Specsavers"), a Guernsey-based optical group. The parties agreed to go into business together.

3. Jasper Conran Optical LLP ("JCO") was formed on 28 June 2007 and commenced trading on the same date. It was owned 99.9% by JATC, the remaining 0.1% ownership being with JC Eyewear Limited, of which JATC had 100% ownership.

4. On 3 September 2007, JCO and Specsavers signed a five-year Optical Product Licence Agreement ("OPLA"). JCO was to work with Specsavers to design a range of spectacle frames bearing the trademarked name "Jasper Conran". Specsavers were to control the manufacture and sale of the frames, paying a licence fee to JCO of £5 per pair in respect of spectacles manufactured and delivered to Specsavers' warehousing, prior to distribution.

5. Deliveries of the initial "Jasper Conran" frames (24 options) in the period to 31 March 2008 exceeded the target set out in clause 3.2 of the OPLA by approximately 20%. In JCO's first accounting period to 31 March 2008, 230,383 frames were delivered generating turnover from licence fees of £1,151,915 and operating profit of £931,112. In the subsequent five month trading period to 31 August 2008, JCO recorded turnover of £569,882 and operating profit of £430,551.

6. The optical business was subsequently incorporated as a subsidiary of JATC's fashion design group (see para 10 below). According to the Appellants, this was pursuant to advice given to JATC by his accountants BHG Chartered Accountants ("BHG") in spring 2008 following the successful launch of the optical business.

7. On 15 July 2008, BHG submitted a non-statutory business clearance application to HMRC under Code of Practice 10 (COP10), on behalf of JCO and JC Vision Limited ("JCV"), a wholly-owned subsidiary of Jasper Conran Holdings Limited ("JCH"), seeking confirmation that, inter alia, corporation tax relief under Schedule 29, Finance Act 2002 would be available on the amortisation of the business acquired by JCV on the grounds that the goodwill in the business of JCO had been created after 1 April 2002. HMRC confirmed, in a letter dated 26 August 2008, that based on the information provided in the application, the goodwill of the JCO business constituted assets created after 1 April 2002 and, "..to the extent that the value of the goodwill being acquired is attributable to the development of the LLP business since its inception (but not the trade mark licence) does qualify for Schedule 29 relief.

8. On 29 July 2008, JATC wrote to JCH, of which he has 100% ownership, confirming that he "retain(s) all rights....to the trademarks and any goodwill subsisting therein”. The letter also confirmed his agreement to the use of “Jasper Conran” trademarks by any members of the JCH group and/or all other legal entities under his control, reserving the right to charge for use of the trademarks.

9. On 2 September 2008, the Specsavers Licence Fee was contractually reduced to £4.50 per pair of manufactured spectacle frames in exchange for agreeing to increase the Jasper Conran range to 48 options and extending the duration of the OPLA to 31 August 2013. The geographical coverage of the agreement was also extended.

10. On 31 October 2008, JCV signed a Business Transfer and Novation Agreement (“BTNA”) with JCO, under which the partnership sold the business relating to the operation of the OPLA for consideration of £7.3 million, with the 'effective date' of the BTNA backdated to 4 September 2008.

11. BHG prepared a valuation of the business of JCO on 18 December 2008 in the sum of £8.25 million and, as a result, the consideration in Clause 4.1 of the BTNA was increased to this figure. This was paid to the partners in JCO by JCV and included in the relevant partners' tax returns to reflect their respective interests in JCO.

12. JCV recognised the consideration of £8.25m as goodwill in its accounts for the year ended 31 March 2009 and amortised this figure on a straight-line basis over a five-year period to 31 August 2013, being the date of the extended OPLA. JCV claimed corporation tax relief on the amortisation of this goodwill in all accounting periods from 31 March 2009 to 31 March 2014.

13. On 14 December 2009, BHG sent form CG34 to HMRC on behalf of JATC to request a post-transaction check of the valuation of JCO's business. JATC's proportion of the proceeds of sale of JCO's business was included in his tax return for the year 2008/09 as a chargeable gain subject to capital gains tax. JATC submitted this return on 21 December 2009. An enquiry was subsequently opened by HMRC into this return on 2 December 2010. As the parties (JCO and JCV) were connected, the valuation request was referred to Shares and Assets Valuation (“SAV") within HMRC.

14. On 23 April 2010 the SAV valuer requested further information:
(i) A copy of the original agreement between JCO and Specsavers signed in September 2007;
(ii) A copy of the renewal agreement signed in September 2009, plus any documentation relating to the novation of the agreement from JCO to JCV
(iii) A copy of the licence agreement between JATC and JCH;
(iv) Confirmation of exact roles and responsibilities placed on JCO via the Specsavers agreement;
(v) Copies of information supplied by Specsavers to JCO showing the anticipated growth rate of 19% per annum over the five years of the arrangement.

15. This information was provided on 19 May 2010, and, following review, the SAV valuer responded on 25 June 2010, in relation to the capital gains check underway, stating that he considered the open market value of the business to be £nil.

16. Enquiries under paragraph 24(1) Schedule 18 of Finance Act 1998 were opened into JCV's company tax returns for the accounting periods ended 31 March 2009 and 31 March 2010 on 24 February 2011, and for the accounting period ended 31 March 2011 on 28 January 2013.

17. A meeting was held with BHG, the Finance Director of JCH, certain HMRC caseworkers and the valuer from SAV on 1 August 2013. No agreement was reached at that meeting and, accordingly, JATC's representatives decided to engage an independent third-party specialist to review critically the valuation and to negotiate with HMRC on behalf of JATC and JCV.

18. That specialist, Mr. Tony Hindley of Valuation Solutions Limited, concluded, in his report dated 16 October 2013, that the asset had been undervalued and was, in his view, more correctly valued in 2008 at a sum in excess of £10 million. The primary reason for the difference was the expert's view that the trademark fee "pay away" which BHG had, in a revised 2013 valuation, set at 30% of turnover would, in a real-world transaction between unconnected parties, have been more in the region of 8%. HMRC had taken, and continues to take, the view that JATC would seek a trademark royalty equal to 100% of the turnover of the acquired business or, at the very least, 100% of the profit, thereby rendering the business worthless.

19. Mr. Hindley attended a meeting with HMRC in December 2013 at which he discussed his report with SAV. No agreement on valuation was reached at that meeting, nor following a subsequent exchange of correspondence.

20. In June 2014, HMRC sought approval from JATC to the issue of a third-party notice to Specsavers to provide information and documents relating to the "contribution made by JCO to the design of optical products bearing a Jasper Conran trademark". This request was rejected, with detailed reasoning. Nevertheless, HMRC proceeded in advance of JATC's response to contact Specsavers. A complaint was subsequently made by BHG to HMRC in September 2014 to which HMRC responded on 24 October 2014. No further communication was received from HMRC until 5 May 2015 when a change of officer at SAV was notified. There was no change in SAV's position on valuation following this change of personnel.

21. BHG and the Finance Director of JCH met with HMRC mediators on 11 December 2015 as a precursor to a mediation hearing which was set for 15 March 2016.

22. Prior to the hearing, the Appellants were notified by Specsavers that HMRC (SAV) had invoked the Tax Information Exchange Agreement between Guernsey and the UK in order to request the Guernsey Income Tax Office to issue a notice to Specsavers requiring the production of documents and information for the period 27 November 2009 to 17 January 2012. Specsavers had notified the Appellants of this approach because of concerns over the breaching of confidentiality provisions within the OPLA. After responding to this notice, Specsavers received a second such demand on 21 April 2016 for information covering the period from 2012 to 17 March 2016. BHG took the view that this step was neither appropriate nor reasonable and endeavoured to contact the lead HMRC mediator in order to complain about this approach and to seek further explanations, via the mediator, from SAV but, no response was received. BHG subsequently cancelled the hearing scheduled for 15 March 2016 after HMRC informed them that HMRC would not commit in advance to modifying their position in relation to the valuation.

23. On 11 March 2016, BHG formally requested HMRC to issue closure notices in respect of all open enquiries in this case.

24. On 8 September 2016, HMRC closed the enquiry into JATC's tax return for the year ended 5 April 2009, stating that "…the valuation used in respect of the disposal of Jasper Conran Optical LLP to JC Vision was overstated. The correct figure was nil and the £8.25m paid to you in respect of this transaction should be treated as a distribution". The return was amended giving rise to an additional tax liability of £662,036.37.

25. On 8 September 2016, HMRC issued closure notices in respect of the enquiries into JCV's company tax returns for the accounting periods ended 31 March 2009, 31 March 2010, and 31 March 2011. These notices stated that "…the market value of the intangible asset, shown as an addition of £8.25m during the 2009 accounting period, is £nil…". Accordingly, all the amortisation debits claimed in the above-noted accounting periods were reduced to £nil. Consequential amendments were also made to the amortisation debits in the accounting periods ending 31 March 2012 to 31 March 2014, reducing them all to £nil. In view of the valuation opinion, HMRC considered that the consequences were that no amortisation relief would be available and amortisation that had been claimed would be disallowed, leaving the £8.25m received by JCO to be treated, in HMRC's view, as a distribution.

26. JATC and JCV appealed the closure notices on 15 September 2016.

27. On 3 October 2016, HMRC wrote to JATC and JCV offering a statutory review of the amendments made by the closure notices in accordance with a commitment given to Ministers that the statutory review to which customers are entitled will be conducted by someone outside of the line management chain of the decision maker. Such a review must therefore be carried out by review officers who have experience of the subject matter of the appeal but are nevertheless independent of the decision maker and the decision maker's line management thus allowing the review officer to remain as objective as possible.

28. On 21 October 2016, JATC and JCV wrote to HMRC accepting the offer of a statutory review.

29. The reviewing HMRC officer issued, after two time extensions, her conclusion letters to JATC and JCV on 27 January 2017 upholding all the closure notices. The reviewing officer also introduced a new point in respect of JCV, namely that "…the company has not drawn up its accounts in accordance with UK GAAP" and that "I consider that the open market value for capital gains tax purposes and the fair value for accountancy purposes are the same, that is £1"

30. Both Appellants appealed to the First-tier Tribunal on 15 February 2017.

31. HMRC served and filed their Statement of Case on 26 May 2017.

32. The Appellants applied to amend their grounds of appeal on 28 June 2017 to address the argument that had been raised in the review decision and included in HMRC's Statement of Case, which was granted by the Tribunal.