



TC06211

Appeal number: TC/2016/03817

CAPITAL GAINS TAX – disposal – part disposal – property development

**FIRST-TIER TRIBUNAL
TAX CHAMBER**

MR ROBERT WRIGHT

Appellant

- and -

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

TRIBUNAL: JUDGE ABIGAIL MCGREGOR

**Sitting in public at The Royal Courts of Justice, The Strand, London on 9 June
2017**

Mr Robert Wright for the Appellant

Stephen Goulding, presenting officer for the Respondents

DECISION

The appeal

- 5 1. This is an appeal by Mr Robert Wright (“RW”) against a discovery assessment for capital gains tax in the tax year 2012-13 in the amount of £25,760.56.

Evidence

2. RW gave evidence in the hearing and was cross-examined by Mr Goulding.
3. A bundle containing copies of documents and correspondence was also
10 provided to the Tribunal, some of which are referred to in this decision.

Law

4. The general principle of chargeability of capital gains tax is set out in section 1 of the Taxation of Chargeable Gains Act 1992 (TCGA 1992):

15 “Tax shall be charged in accordance with this Act in respect of capital gains, that is to say chargeable gains computed in accordance with this Act and accruing to a person on the disposal of assets.”

5. Under TCGA 1992, s 15(2), the default position is that every gain is chargeable unless it is specifically excluded.

- 20 6. Assets are defined under TCGA 1992, s 21(1):

(1) All forms of property shall be assets for the purposes of this Act, whether situated in the United Kingdom or not, including—

- (a) options, debts and incorporeal property generally, and
25 (b) currency, with the exception (subject to express provision to the contrary) of sterling,
(c) any form of property created by the person disposing of it, or otherwise coming to be owned without being acquired.

7. Disposal is not defined but it is generally accepted that a disposal takes place
30 when an asset is sold, given away, or exchanged for another asset. However, TCGA 1992, s 21(2) specifically includes part disposals:

(2) For the purposes of this Act—

- (a) references to a disposal of an asset include, except
35 where the context otherwise requires, references to a part disposal of an asset, and

5 (b) there is a part disposal of an asset where an interest or right in or over the asset is created by the disposal, as well as where it subsists before the disposal, and generally, there is a part disposal of an asset where, on a person making a disposal, any description of property derived from the asset remains undisposed of.

8. Where there has been a disposal, the gain must be calculated. However, the legislation does not set out a procedure to follow to calculate this gain. The normal approach is to start with the consideration for the disposal, and then to subtract certain costs, notably the original acquisition cost of the asset in accordance with TCGA 1992, s 38. However, TCGA 1992, s 17 provides that market value of the asset disposed of must be used in certain circumstances:

15 (1) Subject to the provisions of this Act, 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—

20 (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, and in particular where he acquires or disposes of it by way of gift or on a transfer into settlement by a settlor or by way of distribution from a company in respect of shares in the company, or

25 (b) where he acquires or, as the case may be, disposes of the asset wholly or partly for a consideration that cannot be valued, or in connection with his own or another's loss of office or employment or diminution of emoluments, or otherwise in consideration for or recognition of his or another's services or past services in any office or employment or of any other service rendered or to be rendered by him or another.

30 (2) Subsection (1) shall not apply to the acquisition of an asset if—

35 (a) there is no corresponding disposal of it, and

(b) there is no consideration in money or money's worth or the consideration is of an amount or value lower than the market value of the asset.

9. There are also general provisions which deem certain sets of circumstances to give rise to a disposal and to treat that disposal as having taken place at market value in section 29, as follows (to the extent relevant):

(1) Without prejudice to the generality of the provisions of this Act as to the transactions which are disposals of assets, any transaction which under the following subsections is to be treated as a disposal of an asset—

5 (a) shall be so treated (with a corresponding acquisition of an interest in the asset) notwithstanding that there is no consideration, and

(b) so far as, on the assumption that the parties to the transaction were at arm's length, the party making the disposal could have obtained consideration, or additional consideration, for the disposal, shall be treated as not being at arm's length and the consideration so obtainable, or the additional consideration so obtainable added to the consideration actually passing, shall be treated as the market value of what is acquired.

...

15 (4) If, after a transaction which results in the owner of land or of any other description of property becoming the lessee of the property there is any adjustment of the rights and liabilities under the lease, whether or not involving the grant of a new lease, which is as a whole favourable to the lessor, that shall be a disposal by the lessee of an interest in the property.

20 **Findings of fact**

10. The facts of this case are not simple and, in some areas, it has been necessary to come to a conclusion on the balance of probabilities based on the statements from RW in evidence and the documents submitted. I find the following facts:

25 11. During the course of 2011, RW was approached by a developer, Chapman Button LLP, with whom he had worked before but otherwise had no connection, to ask him to get involved in a project to develop the upper floors of a building in Hackney Road, London.

12. Robert Wright, alongside his son Symon Wright (“SW”), decided to proceed with this project, which involved:

30 (1) RW and SW jointly acquiring a 999 year lease (the “headlease”) over the upper floors and airspace of the Hackney Road property, completing on 4 July 2011 for the sum of £990,000;

(2) RW and SW providing funds to Chapman Button LLP to undertake the development work; and

35 (3) Chapman Button LLP undertaking all the development work, including paying all sub-contractors;

13. RW provided a total sum of £743,780, made up of:

(1) £495,000 for the half share in the acquisition of the headlease; and

(2) additional funds provided in cash of £248,780.

14. At the end of the development, the upstairs of the Hackney Road property consisted of four residential flats, each being granted a new long leasehold title under the headlease:

5 (1) Two of the flats (1 and 4) were sold to independent third parties on the open market, both being long leaseholds of 125 years;

(2) One of the flats (3) was acquired, at full market value by David Button, one of the partners in Chapman Button, also being a long leasehold of 125 years; and

10 (3) The final flat ("Flat 2") was transferred into the name of RW, on a long leasehold of 999 years (less the period of the headlease that had already expired during the building project).

15. Completion statements were provided for:

(1) Flat 1 showing a disposal value of £590,000;

(2) Flat 3 showing a disposal value of £590,000; and

15 (3) Flat 4 showing a disposal value of £525,000.

16. Throughout the development period, RW and SW continued to be legal owners of the headlease. There was considerable uncertainty about the beneficial ownership of this headlease and whether, and to what extent Chapman Button LLP had a beneficial interest in the property:

20 (1) RW had, in a letter to HMRC dated 21 October 2015, stated that:

(a) RW and SW's names were on the "title deed...to protect us financially", and

25 (b) "A Deed of Trust was set up on 4 July 2011 which showed that [SW and RW] held a beneficial interest in the property as Trustees for the parties [RW, SW and Chapman Button LLP];

(2) In a further letter to HMRC dated 18 December 2015, RW enclosed a copy of a Deed of Trust, dated 4 July 2011, but not signed, which provided that:

30 (a) the contributions towards the acquisition of the Hackney Road property on 4 July 2011 were one third RW and SW and two thirds Chapman Button LLP;

(b) RW and SW were to hold the property on trust for RW, SW and Chapman Button in the same proportions; and

(c) RW, SW and Chapman Button were to bear the cost of development in the same proportions;

35 (3) In a third letter dated 6 February 2016, RW stated that he was unable to find a signed copy of the Deed of Trust and that the one sent with the earlier letter did not reflect the eventual agreement, in particular because it referred to Chapman Button LLP providing the bulk of the funding, which was not what happened;

(4) In the Tribunal hearing, RW asserted that this Deed of Trust was never signed because he and SW had been advised not to sign it and that when he said in the letter to HMRC that the Deed of Trust was “set up”, he should have said “drawn up”;

5 (5) HMRC produced an official copy of the register of title to the Freehold (not the headlease) of the Hackney Road property dated 4 November 2015, which showed (to the extent relevant) that:

10 (a) The freehold to the Hackney Road property was owned (from 17 June 2011) by two companies, apparently independent from any of RW, SW and Chapman Button LLP;

(b) The freehold had the benefit of the rights reserved under a 125 year lease dated 8 June 2012 between RW and SW as one party and David Button on the other; and

15 (c) There was a 999 year lease, commencing 4 July 2011 over the second floor, roof and airspace of the property (although no record of the proprietors of that lease are included in the register of the freehold title)

(6) Given the level of confusion over the beneficial ownership, caused in great part by RW’s inconsistent statements regarding it, and that RW’s final assertion at the hearing was that there was no deed of trust, which is, in relation to the tax question arising in this appeal, RW’s weakest position, I find, on the balance of probabilities, that RW and SW remained beneficial owners of the headlease throughout the period in question and that Chapman Button’s financial interest in the project was limited to the profits they made on the development work itself and a contractual right to buy one of the flats at the end of the development;

(7) I also find that the lease referred to in paragraph 5(b) above was not, as HMRC asserted, the new lease over Flat 2; while it is not clear which leasehold title it refers to, the information does not match with a 999 year lease granted to RW alone.

30 17. At the end of the project RW had received:

(1) Ownership of Flat 2, and

(2) £294,362 in cash.

35 18. RW had submitted to HMRC in an undated letter (which is expressed to be in response to HMRC’s letter of 5 August 2015 and is stated in a subsequent letter to have been received by HMRC on 7 September 2015) that the value of Flat 2 at the time he acquired it was £610,000. He subsequently suggested that this was an inappropriate valuation for the flat because it was higher than the other flats that were sold on the open market and that Flat 2 was in a less good position in the block. We had no evidence to support either position and on balance take RW’s original response to HMRC as to the valuation as the most appropriate one to use as the market value of Flat 2, not least because the leasehold of Flat 2 was considerably longer than the leaseholds granted over flats 1, 3 and 4, which would justify a higher value, even if Flat 2 was otherwise in a less good position.

Parties arguments

19. RW submitted that:

- (1) the granting of the lease of Flat 2 to RW was part of his return on the capital invested in the development project;
- 5 (2) there is no gain to tax because he has not disposed of anything;
- (3) he still owns Flat 2 and therefore the gain cannot have arisen to be taxed, but rather should be taxed when he disposes of it;
- (4) any gain is a paper gain, like a gain on stock market shares before they are disposed of; and
- 10 (5) HMRC is trying to bring forward the time for obtaining capital gains tax.

20. HMRC submitted that it is entitled to make a discovery assessment in accordance with section 29 of the Taxes Management Act 1970 because it made a discovery in relation to the 2012-13 tax year and no information was provided in the relevant tax return that prevents the discovery.

15 21. HMRC submitted that the intention of the capital gains legislation is for it not to be possible for a development of this nature to avoid tax by virtue of retaining a part of an asset and that RW has received money or money's worth in the form of the retained flat and that this therefore must be taken into account for capital gains purpose. The specific arguments raised to support this contention were that:

- 20 (1) RW had an asset that fell within section 21(1)(c) of TCGA 1992, being "any form of property created by the person disposing of it, or otherwise coming to be owned without being acquired", being RW's interest in the whole property, not just the flat retained at the end;
- 25 (2) RW made a part disposal under TCGA 1992, s 21(2)(b), which is set out in full above, but Mr Goulding drew particular attention to the statutory language that includes the circumstances where 'an interest or right in or over the asset is created by the disposal';
- 30 (3) The value to be attributed to the disposal should be the market value of the part disposed of in accordance with TCGA 1992, s 29(1)(b) because RW admitted that 'everything was done on the basis of a handshake' and there had been a transfer of value that was favourable to the lessor under TCGA 1992, s 29(4);
- 35 (4) In any event RW had himself provided the figure of £610,000 for the transfer of Flat 2 and referred to that transaction as the flat having been 'sold to me'; and
- (5) The property register obtained from the Land Registry showed a transfer of the retained flat to RW.

Discussion

Discovery

22. There is no dispute in this case that:

- (1) RW submitted a tax return for 2012-13;
- 5 (2) The return did not include any information relating to the Hackney Road property;
- (3) HMRC made a discovery during the course of 2015 regarding RW's involvement in the Hackney Road property development; and
- 10 (4) The assessment under appeal was made within 4 years of the end of the tax year in question (i.e. within the normal time limit in section 34 of TMA 1970).

23. Where a tax return has been submitted, HMRC can only raise discovery assessments if certain other conditions are met. In this case, HMRC rely on the condition in section 29(5) of TMA 1970, i.e. that at the time when an officer of the
15 Board ceased to be entitled to give notice of his intention to enquire into the return, the officer could not reasonably be expected, on the basis of information available to him before that time, to be aware of the circumstances giving rise to the chargeable gain not having been assessed.

24. On the basis that RW did not include any information about his involvement in the Hackney Road property development or any of the flat disposals in his tax return
20 or any subsequent correspondence with HMRC until the question was raised in 2015, I find that this condition was met.

25. Finally HMRC must show that there has been a loss of tax, i.e. chargeable gains that were not assessed. As set out in the remainder of this decision, I find that there
25 has been a loss of tax.

26. Therefore I find that the discovery assessment was validly made.

HMRC's factual assertions

27. Leaving aside for the moment, the main arguments relating to the disposal or part disposal, HMRC made two assertions of fact to support its arguments and I will
30 reiterate here the findings of fact in relation to those assertions:

- (1) I have found, as a matter of fact, that the market value of the 999 year lease over Flat 2 was £610,000 at the relevant time; and
- (2) I have also found, as a matter of fact, that the property register obtained from the Land Registry by HMRC did not show a transfer of Flat 2 to RW.

Was there a disposal?

28. The question at the heart of this case is whether RW made a disposal that generated a chargeable gain.

29. HMRC submitted that the transaction for the granting of the lease over Flat 2 to RW was a transaction falling within TCGA 1992, s 29(4) (set out in full above) and therefore a deemed disposal under that provision. It is clear from the presence of the word ‘after’ in that sub-section, that it requires a sequence of events as follows:

- (1) First a transaction which involves the owner of land becoming the lessee of that property; and
- (2) Subsequently, there being an adjustment of rights and liabilities under the lease, which is as a whole favourable to the lessor.

30. When RW and SW granted RW a long lease over Flat 2, RW had indeed become lessee of the property. However, there was no evidence presented to the Tribunal that indicated there had been a subsequent variation of the rights and liabilities under that lease that were favourable to the lessor (being RW and SW jointly) in a manner that shifted value to the lessor. I therefore find that section 29 is not in point at all.

31. Having concluded that there is no deemed disposal under TCGA 1992, s 29, I must consider whether there is a disposal under any other provision. As set out above the term ‘disposal’ is not exhaustively defined in TCGA 1992. However there are certain types of disposal that are specifically included within the definition, most notably in the context of this case in TCGA 1992, s 21(2)(b), which provides:

“there is a part disposal of an asset where an interest or right in or over the asset is created by the disposal, as well as where it subsists before the disposal, and generally, there is a part disposal of an asset where, on a person making a disposal, any description of property derived from the asset remains undisposed of.”

32. Based on the findings of fact set out above, I find that:

- (1) RW commenced the project with an asset, being his joint ownership, with SW, in the whole of the headlease; and
- (2) at the end of the project, RW continued to hold that asset but it had been eroded by the carving out from it of:
 - (a) three 125 year leaseholds that were sold outright to third parties for the combined total of £1,705,000; and
 - (b) one 999 year lease over Flat 2 which was held solely by RW and which had a market value of £610,000.

33. In respect of the three 125 year leaseholds flats, it is quite clear there each transaction was a disposal, in the normal interpretation of that word, to third parties and I find that each of these disposals represents a part-disposal in accordance with

the terms of the statutory language in TCGA 1992, s 21(2)(b), because an interest (being in each case the 125 year lease) in the asset was created by the disposal.

5 34. The question of whether there has been a disposal in relation to the 999 year lease over Flat 2 is less obvious. At the beginning of the project RW owned a half share in the property interest that included Flat 2 (the headlease) and at the end of the project he owned all of the lease in Flat 2. While a person clearly cannot dispose of an asset to themselves, what has happened here is that RW and SW as joint owners of the headlease have created a new asset, the 999 year lease over Flat 2, and transferred that to RW in his own right. Therefore I find that the Flat 2 transaction was also a part
10 disposal.

15 35. For the sake of completeness, I find that RW's submission that he cannot have disposed of Flat 2 because he still owns it is a misunderstanding of the principle by RW. The disposal that has taken place is the carving out of Flat 2 from the headlease and RW's lease over Flat 2 is the asset acquired under that disposal. His submission also ignores the effect of the disposals of the other three flats.

How is the capital gain to be calculated?

36. Having established that RW has made part disposals in relation to all 4 flats, the next question is how the gain is to be calculated for tax purposes.

20 37. The consideration given for the disposal of the three flats to third parties was the combined sale price of £1,705,000.

25 38. I agree with HMRC that the transaction between RW and SW as joint owners of the headlease and RW as acquirer of Flat 2 cannot be said to have taken place at 'arm's length' and therefore the general market value rule in TCGA 1992, s 17 would apply in determining the consideration for the disposal of Flat 2, which was, as found above, £610,000.

39. The general principles of deducting allowable expenditure from the consideration in calculating the gain are set out in TCGA 1992, s 38 and include, broadly, the costs of acquiring the asset, the amount spent on enhancing the value of the asset and the incidental costs of disposal.

30 40. Where there is a part disposal, the amounts allowable as costs of acquisition and enhancement under general principles must be apportioned under TCGA 1992, s 42(2) as follows:

(2) The apportionment shall be made by reference—

35 (a) to the amount or value of the consideration for the disposal on the one hand (call that amount or value A), and

(b) to the market value of the property which remains undisposed of on the other hand (call that market value B),

and accordingly the fraction of the said sums allowable as a deduction in the computation of the gain accruing on the disposal shall be—

$$A/(A+B)$$

5 and the remainder shall be attributed to the property which remains undisposed of.

41. Based on the facts presented to the Tribunal and the findings above, it is possible to determine value A as £1,157,500 (being 50% of £1,705,000 + £610,000). However, the parties did not present any evidence, or indeed provide any indication
10 that they had previously discussed, the market value of the reversionary headlease and therefore it is not possible to determine value B. Therefore I make this decision in principle, with the expectation that the parties can agree on the quantum between themselves, or, if necessary, with the assistance of a professional valuation.

Decision

15 42. For the reasons set out above, I dismiss the taxpayer's appeal in principle.

43. 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
20 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.

25 **ABIGAIL MCGREGOR**
TRIBUNAL JUDGE

RELEASE DATE: 9 NOVEMBER 2017

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