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 COURT OF APPEAL—17, 18 AND 19 APRIL AND 12 MAY 1978
 

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 HOUSE OF LORDS—2 AND 3 JULY AND 25 OCTOBER 1979
 

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**O'Brien (H.M. Inspector of Taxes) v.  
Benson's Hosiery (Holdings) Ltd.<sup>(1)</sup>**

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*Corporation tax—Chargeable gains—Meaning of “property” and “assets” under Part III of Finance Act 1965 (c 25)—Whether £50,000 received from director to secure release from service agreement a chargeable gain—Finance Act 1965, s 22(1), (3) and (4)(b).*

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In September 1968 the Company, a holding company, acquired the total issued share capital in a company which marketed hosiery (“Hosiery”) and B, the sales and marketing director of Hosiery, entered into a seven-year service agreement with the holding company to act for it in the same capacity. Under that agreement B carried out sales and merchandising duties for Hosiery and another subsidiary of the Company with conspicuous success. In April 1970, following negotiations, B and the Company entered into a supplemental agreement whereby B paid the Company a capital sum of £50,000 for the release of his obligations under the service agreement. The Company, appealing to the Special Commissioners against a corporation tax assessment raised on the basis that the £50,000 was a chargeable gain, contended (i) that the right of an employer under a service contract to the employee’s services was not a chargeable asset; (ii) alternatively, if it was, that it was acquired for a consideration which could not be valued within the meaning of s 22(4)(b), Finance Act 1965, (i.e. the asset was deemed to be acquired for a consideration then equal to its market value); (iii) alternatively, that under s 22(3) the £50,000 was derived from the shares in Hosiery and the other subsidiary, the values of which were diminished by virtue of B’s departure, so that the chargeable gain fell to be computed by reference to those shares. It was contended on behalf of the Crown that the Company’s rights under the service agreement constituted an asset for the purposes of s 22(3), and that the £50,000 was a capital sum “received in return for . . . surrender of rights” within s 22(3)(c). The Commissioners allowed the Company’s appeal, holding that an employer’s rights under a personal service contract were not “property” within the meaning of s 22(1). The Crown demanded a Case.

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The Chancery Division, allowing the Crown’s appeal held (1) that the £50,000 was a capital sum received in return for forfeiture or surrender of rights within the meaning of s 22(3)(c); (2) that the Company’s contractual rights were “property” and “assets” for the purposes of s 22(1); and the said sum was “derived from” the service agreement alone and there was no justification to look

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(1) Reported (Ch D) [1977] 3 WLR 206; [1977] 3 All ER 352; [1977] STC 262; [1977] Ch 348; 121 SJ 376; (CA) [1978] 3 WLR 609; [1978] 3 All ER 1057; [1978] STC 549; [1979] Ch 152; 122 SJ 439; (HL) [1979] 3 WLR 572; [1979] 3 All ER 652; [1979] STC 735; [1980] AC 562; 123 SJ 752.

behind it to the underlying value of the shares in Hosiery and the other subsidiary (*Commissioners of Inland Revenue v. Montgomery* 49 TC 679; [1975] Ch 266 applied); (3) that the matter should be remitted to the Special Commissioners to hear evidence and argument on, and determine whether the said rights could be valued, and if so, the value thereof. The Company appealed. A

The Court of Appeal, allowing the Company's appeal extracted from *Nokes v. Doncaster Amalgamated Collieries Ltd.* [1940] AC 1014 a general principle that contracts of employment were not assignable and so were not property or assets. The Crown appealed and the House of Lords unanimously reversed the Court of Appeal and held, *per curiam*, that: (1) the *Nokes* case provided no guidance for capital gains tax purposes, being in any event concerned only with the transfer or assignment of rights under an employment contract whereas the capital gains tax legislation was concerned with disposals; (2) the employer's rights to obtain a substantial sum for the release of B from his contract sufficiently bore the mark of an asset of the employer, being something which he could turn to account; (3) s 22(3)(a) would be apt to cover a case of damages recovered by an employer from a third party for wrongful procurement of breach of contract by the employee; (4) it was erroneous to deduce from s 22(4), which had no application to the present appeal, a principle that for capital gains tax purposes an asset must have a market value; *Inland Revenue Commissioners v. Crossman* [1937] AC 26 distinguished; (5) (as had been held in the Courts below) the £50,000 was not derived from the employer's shareholding in its subsidiaries. B C D

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CASE E

Stated under s 56 of the Taxes Management Act 1970 by the Commissioners for the Special Purposes of the Income Tax Acts for the opinion of the High Court of Justice.

1. At a meeting of the Commissioners for the Special Purposes of the Income Tax Acts held on 22 and 23 September 1975 Benson's Hosiery (Holdings) Ltd. ("the Company") appealed against an assessment to corporation tax in the sum of £50,000. F

2. Shortly stated the question for our decision was whether for the purposes of Part III, Finance Act 1965 ("the Act") a chargeable gain arose on the receipt by the Company in its accounting period ended 31 July 1970 of £50,000 paid by an employee and director of the Company to secure his release from his service contract with the Company. G

3. The following witnesses gave evidence before us: Peter Brian James ("Mr. James"), chartered accountant, partner in David Kroll & Co., the Company's auditors; John Michael Wariner, ("Mr. Wariner"), chartered accountant and since 1 October 1970, financial director of the Company.

4. Copies, which are available for inspection by the Court if required, of the following documents were proved or admitted before us: H

(1) the Company's annual report and accounts for year ended 31 July 1970;

(2) the Company's prospectus dated 25 September 1968;

(3) service agreement dated 23 September 1968 ("the service agreement") between the Company and Mr. Robert Solomon Behar ("Mr. Behar");

(4) agreement dated 2 April 1970 ("the supplemental agreement") supplemental to the service agreement. I

A 5. As a result of the evidence both oral and documentary adduced before us we find the following facts proved or admitted:

(1) The Company is a holding company and does not itself trade. On 25 September 1968 the Company acquired the whole of the issued share capital of Benson's Hosiery Ltd. ("Hosiery") in exchange for 7,850 ordinary shares of 2s. each of the Company credited as fully paid up. The share capital of Hosiery was taken into the Company's books at a value of £124,785. A figure of £49,851, being the excess of the said value of £124,785 over £74,934 (which was taken to be the value of the net tangible assets of Hosiery) was included in the value of "goodwill" in the consolidated accounts of the Company and its subsidiaries. Goodwill was not, however, shown in the balance sheets of the Company or of any of its separate subsidiary companies. Also on 25 September 1968 the Company, by way of capitalization of the sum standing to the credit of share premium account, which arose from the acquisition of Hosiery, issued to its members 124 fully paid ordinary shares of 2s. each for each 2s. share already held.

(2) At about the same time as the Company acquired Hosiery, it also acquired for cash the whole of the issued share capital of South Coast Warehousemen Ltd. ("South Coast").

(3) Hosiery and South Coast were the first two subsidiaries which the Company acquired.

(4) At the time of its acquisition by the Company, Hosiery carried on the business of marketing of hosiery. One quarter of Hosiery's share capital was owned by Mr. Behar, who for some years had been Hosiery's sales and merchandise director and who had pioneered successful new methods of marketing. Following the Company's acquisition of Hosiery and the share issue referred to in sub-para (1) above, Mr. Behar became entitled to 245,250 ordinary shares of 2s. each in the Company.

(5) By the service agreement Mr. Behar was appointed sales and merchandise director of the Company for seven years at a salary of £4,000 per annum. The material clauses of the agreement are:

"1. Mr Behar shall be and he is hereby appointed Sales and Merchandise Director of the Company upon the terms hereinafter appearing for the term of Seven Years from the 23 day of September 1968 and thereafter unless and until determined by not less than 3 months notice in writing given by either party to the other and as such Sales and Merchandise Director Mr Behar will perform the duties and exercise the powers which may from time to time be assigned to or vested in him by the Board of Directors of the Company or any Managing Director of the Company including rendering services to any Subsidiary of the Company. 2. Mr Behar shall devote the whole of his time attention and abilities to his duties hereunder (including the business of such of its Subsidiary Companies as the Board may from time to time require) and shall comply with the directions from time to time given and made by the Board and shall well and faithfully serve the Company and use his utmost endeavours to promote the interests thereof . . . 4. There shall be paid to Mr Behar as such Sales and Merchandise Director (to include any remuneration payable to him as a Director of the Company or of any of its Subsidiary or associated companies) a salary payable monthly in arrear on the first of each month but to be deemed to accrue from day to day from the said 23rd day of September One thousand nine hundred and sixty-eight at the rate of Four thousand pounds per annum such salary to be the subject of review by

Agreement between the parties from time to time . . . 8. The Board shall be at liberty from time to time to appoint any other person or persons to be a Sales and Merchandise Director of the company jointly with Mr Behar and to appoint such Assistant Sales and Merchandise Director of the Company as they may think fit. 9. The reconstruction or amalgamation of the Company during the continuance of this Agreement whereunder Mr Behar shall be offered comparable employment on terms not less favourable to him than those herein contained shall not give rise to any claim by Mr Behar for damages against the Company.”

(6) Mr. Behar acted as marketing director for both Hosiery and South Coast. As such he was responsible for finding new outlets for marketing (which were vital to replace those which were lost by wastage), engaging and controlling the direct salesmen, overseeing the stocks held and for formulating the purchasing policy of both companies. As far as his responsibilities to the Company were concerned, he reported to the main board of directors on the marketing activities of the Company's subsidiaries. The duties of Mr. Behar's appointment required special skills and energy and he carried out his duties with conspicuous success. His remuneration from the Company and its subsidiaries, including his remuneration under the service agreement and annual bonuses was about £5,000 or £5,500 per annum.

(7) Early in March 1970 Mr. Behar approached the directors of the Company and asked to be released from his obligations under the service contract. The Company agreed to Mr. Behar's release on the terms set out in the supplemental agreement between the Company of the first part, Mr. Behar of the second part, two directors of the Company ("the directors") of the third part and Mr. J. J. Norton ("Mr. Norton"), a director and shareholder in the Company, of the fourth part. The material clauses of the agreement are:

"Now This Agreement Witnesseth as follows: 1. In consideration of the sum of Fifty thousand pounds to be paid by Mr Behar to the Company in the manner hereinafter appearing the Company hereby release Mr Behar from the Agreement with effect from the first day of May One thousand nine hundred and seventy. 2. Mr Behar hereby agrees with the Company as follows: (a) To pay to the Company the said sum of Fifty thousand pounds on or before the thirtieth day of June One thousand nine hundred and seventy. (b) (i) Not prior to the twenty-second day of September One thousand nine hundred and seventy five (hereinafter called 'the restricted period') without the consent of either of the Directors to sell more than One hundred thousand Ordinary Shares or such larger number of shares as may represent One hundred thousand Ordinary Shares by reason of any bonus issues allotted by the Company after the date hereof in the Company in any period of one year commencing on the sixth day of April One thousand nine hundred and seventy apart from any shares sold for the purpose of realising the said sum of Fifty thousand pounds. (ii) To sell in the manner provided by this Deed not less than fifty thousand Ordinary Shares in the Company in any one fiscal year during the restricted period. (c) To authorise the Bank having custody of the Share Certificates relating to Mr Behar's holding in the Company to notify the Company of any direction by Mr Behar to deliver Share Certificates to meet any sale of shares in the Company by Mr Behar during the restricted period. (d) To give to either of the Directors four weeks notice of his intention to sell any shares in the Company during the restricted period specifying the number of shares he intends selling in order to give to either of the Directors an opportunity of finding a purchaser through the London Stock Exchange at the middle market ruling on the day on which such notice is given at



A the opening of the London Stock Exchange after which period of four weeks in the event of the shares still remaining unsold then Mr Behar may dispose of such shares in such manner as he thinks fit... 4. In the event of Mr Norton or the Directors collectively or individually selling more than three hundred thousand shares held by them in the Company varied in accordance with Clause 2(b) hereof in any one year during the restricted period then Mr Behar shall be entitled to dispose in manner provided in this Deed of one third of the excess number of shares sold by Mr Norton or the Directors over three hundred thousand shares 5. Mr Norton and the Directors will on the date of any sale of shares by all or any of them in the Company in excess of Three hundred thousand offered in any one year give immediate written notice of such sale to Mr Behar 6. Mr Behar will as from the 1st day of May 1970 resign his directorships in the Company its subsidiary and its associated Companies and immediately thereafter the following statement only shall be released to the press: 'Mr Robert Behar has for personal reasons resigned his office of Director of Benson's Hosiery (Holdings) Limited and its associated Companies.'

D (8) We were not told what the Company did with the £50,000 which it received from Mr. Behar but the following adjustments were made in drawing up the Company's accounts as at 31 July 1970: (a) In the consolidated balance sheet for the Company and its subsidiaries £50,000 was deducted in arriving at the value attributed to goodwill. A note on the accounts reads:

"6 GOODWILL

E Goodwill consists of the excess cost of shares in subsidiaries over the book value of the net assets of those companies at the dates of acquisition, and is made up as follows:

	£
Balance 31st July, 1969	1,084,670
Add: In respect of the acquisition of subsidiaries completed during the year	<u>222,733</u>
	1,307,403
Less: Amount received from Mr R S Behar, a Director who resigned by agreement dated 18th May, 1970	<u>50,000</u>
	<u>£1,257,403."</u>

G (b) In the Company's balance sheet £50,000 was deducted in arriving at the value of subsidiary companies. A note on the accounts reads:

"15 SUBSIDIARY COMPANIES

H This is made up of shares at cost including expenses of acquisition less dividends received out of preacquisition profits and amounts due on current account."

(9) After Mr. Behar's resignation from the Company and its subsidiaries, he was replaced as marketing director of Hosiery—his replacement being paid about £5,500 or £6,000 per annum. Mr. Behar was not replaced on the Company's main board but his duties in relation to the whole group were taken over by other directors.

I 6. It was contended on behalf of the Company that:

(i) at some time before the supplemental agreement the service contract was terminated by repudiation by Mr. Behar, thereby giving the Company a right to damages for breach of contract;

(ii) the Company's right to such damages or, if there was no repudiation of the service contract by Mr. Behar, the Company's right under the contract to Mr. Behar's services was not (a) a right or asset that was capable of being transferred or (b) a right affecting an asset or right that was capable of being transferred and is therefore not a chargeable asset within Part III of the Act; A

(iii) the corporation tax assessment should be discharged; or alternatively,

(iv) the Company was obliged by the terms of the service contract to provide Mr. Behar with appropriate duties; B

(v) the Company's rights were therefore acquired partly for a consideration that cannot be valued;

(vi) the chargeable gain therefore falls to be computed under s 22(4)(b) of the Act; or alternatively

(vii) the £50,000 paid under the supplemental agreement was paid in part to compensate the Company for a possible diminution as a result of the termination of Mr. Behar's services of the value of its shares in Hosiery and South Coast; C

(viii) the Company's shares in Hosiery and South Coast were, therefore, the assets from which, for the purposes of s 22(3) of the Act, the said £50,000 was derived; D

(ix) the chargeable gain therefore falls to be computed on that basis.

7. It was contended by the Inspector of Taxes that:

(i) the sum of £50,000 paid under the supplemental agreement was paid wholly to secure Mr. Behar's release from the service agreement;

(ii) the said sum of £50,000 was not, within the meaning of s 22(3) of the Act, derived from the Company's shares in Hosiery and South Coast; E

(iii) the Company rights whether under the service agreement or to damages for its breach were chargeable assets within the meaning of Part III of the Act;

(iv) the surrender of the said rights by the Company for payment falls to be treated as a disposal of assets within the meaning of s 22(3) of the Act and, in particular, within the meaning of sub-para (c) of that subsection;

(v) no deduction fell to be made in computing the chargeable gain; F

(vi) the consideration of £50,000 received by the Company for such deemed disposal is therefore the chargeable gain within the meaning of Part III of the Act;

(vii) the Company's rights were not acquired wholly or partly for a consideration that cannot be valued and that s 22(4)(b) therefore has no application to this appeal. G

8. The following authorities were cited before us: *Collier v. Sunday Referee Publishing Co., Ltd.* [1940] 2 KB 647; *Commissioners of Inland Revenue v. Montgomery* 49 TC 679; [1975] 2 WLR 326; *London & Thames Haven Oil Wharves Ltd. v. Attwooll* 43 TC 491; [1967] Ch 772.

9. We, the Commissioners who heard the appeal, took time to consider our decision and gave it in writing on 24 October 1975 as follows: H

(1) The question for our decision is whether for the purposes of Part III of the Act a chargeable gain arose on the receipt by the Company of £50,000 paid by Mr. Behar, an employee and director of the Company, in connection with the termination of his service contract.

A (2) Evidence was adduced before us of the circumstances in which the service contract was terminated. In our view there was insufficient evidence that it was terminated by repudiation by Mr. Behar and we find that the termination resulted from the supplemental agreement.

B (3) The Inspector of Taxes contended that by virtue of s 22(1) of the Act, the Company's rights under the service contract were assets for the purposes of Part III of the Act, that the sum of £50,000 which the Company received from Mr. Behar ("the £50,000") under the supplemental agreement was a capital sum derived from such assets and that there was accordingly a deemed disposal of assets within the meaning of s 22(3) of the Act and, in particular, within the meaning of sub-para (c) of that subsection. He did not advance the contention that there was a disposal (within the natural meaning of that word) independently of the said subsection and the point was not argued before us.

C (4) As we understand it, it is common ground between the Company and the Inspector of Taxes that the receipt of the £50,000 could not give rise to a deemed disposal under s 22(3) of the Act unless it was derived from assets which were themselves "chargeable assets"—in the sense that if there had been a disposal thereof a chargeable gain or loss could have arisen.

D (5) We considered whether the rights to Mr. Behar's services under the service contract could be such a "chargeable asset". It was contended for the Company that it is inherent in the scheme of Part III of the Act that there are two tests of what is a "chargeable asset": first, whether the right or asset is one that by its nature is capable of being transferred and second, whether the right is one which affects an asset that is capable of being transferred. It was further contended for the Company that a contractual right to personal services satisfied neither of these tests. We noted that s 22(1) of the Act, which provides that "all forms of property" (including certain specific examples) shall be assets for the purposes of Part III of the Act, is drawn in very wide terms and that s 27 of the Act specifically excludes certain types of assets from the category of "chargeable assets" in the sense in which we have used that term in para 4 above. Section 27 deals in different ways with various kinds of property and rights. In some cases (savings certificates, for example) it provides that they shall not be "chargeable assets" (a term which is not defined in the Act). In other cases (as, for example, currency which has been acquired in certain circumstances) it provides that the gain shall not be a "chargeable gain". It is, however, "declared" by subs (7) and (8) that gambling winnings and certain forms of compensation respectively "are not chargeable gains". The Act itself thus recognizes that certain rights are not in the nature of "property" within the scope of s 22(1). We see no reason to suppose that these declaratory provisions are exhaustive of the rights which are not such property. Having regard to the general scheme of Part III of the Act (and in particular to the structure of ss 22 and 27) for the taxation of capital gains, we think that the tests propounded on behalf of the Company of what is a "chargeable asset" are well founded. An employer's right to the services of his employee is no doubt a form of property for certain purposes, so that, for example, an injury to his employee may give the employer a right of action for damages. But rights to an employee's services under a service contract are not capable of being transferred nor do they affect an asset that is capable of being transferred. In our view, and we so hold, an employer's rights under a bona fide contract for personal services (such as we are concerned with in these proceedings) are not "property" for the purposes of Part III of the Act.

I (6) If we are wrong in our decision on the construction of Part III of the Act, it is necessary to consider the first alternative contention advanced on behalf of the Company, namely, that the Company's rights under the service contract were acquired "partly for a consideration that cannot be valued"

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within the meaning of s 22(4)(b) of the Act. We have reviewed the circumstances in which the service contract was entered into (paying particular regard to the office which Mr. Behar held in Hosiery and the interest which he formerly had in that Company) and to the terms of the service contract (in particular Mr. Behar's appointment for 7 years to a specific post requiring his special skills and energy, which he appears to have exercised with conspicuous success, and the Company's obligation under clause 9 in the event of its reconstruction or amalgamation to offer Mr. Behar "comparable employment on terms not less favourable to him"). In this connexion we have also considered the application of the decision in *Collier v. Sunday Referee Publishing Co., Ltd.* [1940] 2 KB 647. In our view Mr. Behar's contract with the Company was founded on his appointment to perform specific duties, that the Company was under an obligation to provide him with corresponding employment during the term of the service contract and that this obligation formed part of the consideration for the rights which the Company acquired under the service contract. But we do not accept that the obligation cannot be valued. While valuation is not an exact science and to assign a value to this obligation would no doubt be difficult and, more than with most valuations, open to subjective opinion ranging over a fairly broad band, we think that the words "cannot be valued" apply only to something much more nebulous than this. The Inspector did not hazard any opinion as to what the value was and asked only for a decision in principle. If, therefore, the value is relevant (e.g. for the purposes of para 4(1)(a) of Sch 6 to the Act) and no agreement on it can be reached between the Company and the Inspector of Taxes, the matter will require to be argued before us.

(7) It was also contended, in the further alternative, by the Company that the £50,000 was paid in part to compensate the Company for a possible diminution as a result of Mr. Behar's departure in the value of its shares in its two subsidiary companies, Hosiery and South Coast and that the Company's shares in these subsidiaries were, therefore, the assets from which, for the purposes of s 22(3) of the Act, the £50,000 was derived. While we would be prepared to infer from the evidence that this was the main factor which influenced the Company to exact such a large sum from Mr. Behar to release him from the service contract, we feel prohibited by the decision in *Commissioners of Inland Revenue v. Montgomery*(1) [1975] 2 WLR 326 from tracing the derivation of the £50,000 beyond the rights which the Company acquired under the service contract.

(8) For the reasons given in para 5 above the appeal succeeds and we discharge the corporation tax assessment in question.

10. The Appellant, immediately after the determination of the appeal, declared to us his dissatisfaction therewith as being erroneous in point of law and on 17 November 1975 required us to state a Case for the opinion of the High Court pursuant to s 56 of the Taxes Management Act 1970 which Case I have stated and do sign accordingly. Mr. H. G. Watson who determined the appeal with me has since retired from the Public Service.

11. The question of law for the opinion of the Court is whether on the facts set out in para 5 above our decision was correct.

J. G. Lewis { Commissioner for the Special Purposes of the  
Income Tax Acts

Turnstile House  
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London WC1V 6LQ

5 August 1976

(1) 49 TC 679.

A The case was heard in the Chancery Division by Fox J. on 14 and 15 February 1977 when judgment was reserved. On 17 February 1977 judgment was given in favour of the Crown, with costs.

*Brian Davenport* for the Crown.

*A. R. Thornhill* for the Company.

B The following cases were cited in argument in addition to those referred to in the judgment:—*Commissioners of Inland Revenue v. Carron Co.* 45 TC 18; 1968 SC (HL) 47; *Harrison v. Nairn Williamson Ltd.* 51 TC 135; [1976] 1 WLR 1161; *Sharkey v. Wernher* 36 TC 275; [1956] AC 58.

C Fox J.—This is an appeal by the Crown from a decision of the Special Commissioners. The question is whether, for the purposes of Part III of the Finance Act 1965, a chargeable capital gain arose on the receipt by Benson's Hosiery (Holdings) Ltd. (which I shall call "the Company") of the sum of £50,000 paid by an employee and director of the Company to secure his release from his service contract with the Company.

D The Company is a holding company, and does not trade. On 25 September 1968 the Company acquired the whole of the issued share capital of Benson's Hosiery Ltd. (which I shall call "Hosiery") in exchange for ordinary shares of the Company credited as fully paid up. The share capital of Hosiery was taken into the Company's books at a value of £124,785. A figure of £49,851, being the excess of the value of £124,785 over £74,934 (which was taken to be the value of the net tangible assets of Hosiery), was included in the value of goodwill in the consolidated accounts of the Company and its subsidiaries. At about the same time as the Company acquired Hosiery, it also acquired for cash the whole of the issued share capital of South Coast Warehousemen Ltd. (which I shall call "South Coast"). Hosiery and South Coast were the first two subsidiaries which the Company acquired. At the time when Hosiery was acquired by the Company Hosiery carried on the business of marketing hosiery. One-quarter of Hosiery's share capital was owned by Mr. Behar, who for some years had been Hosiery's sales and merchandise director. He had pioneered successful methods of marketing. By a service agreement of 23 September 1968 Mr. Behar was appointed sales and merchandise director of the Company for seven years at a salary of £4,000 per annum. The service agreement provided (*inter alia*) that Mr. Behar should

G "devote the whole of his time attention and abilities to his duties . . . (including the business of such of [the Company's] Subsidiary Companies as the Board may from time to time require) and shall comply with the directions from time to time given and made by the Board."

H Mr. Behar acted as sales and merchandise director for both Hosiery and South Coast. As such, he was responsible for finding new outlets for marketing (which were vital to replace those lost by wastage), engaging and controlling the direct salesmen, overseeing the stocks held and formulating the purchasing policy of both companies. There is no doubt that Mr. Behar's duties required special skills and energy, and that he carried out his duties with conspicuous success. Early in March 1970, Mr. Behar approached the directors of the Company and asked to be released from his obligations under the service agreement. The Company agreed to Mr. Behar's release upon terms which are set out in a supplemental agreement dated 2 April 1970 and made between the Company, of the first part; Mr. Behar, of the second part; two directors of the Company, of the



(Fox J.)

third part; and a Mr. Norton, a director and shareholder of the Company, of the fourth part. The material provisions of the supplemental agreement are as follows: A

“Now This Agreement witnesseth as follows: 1. In consideration of the sum of Fifty thousand pounds to be paid by Mr Behar to the Company in the manner hereinafter appearing the Company hereby release Mr Behar from the Agreement” [that is to say, the service agreement] “with effect from the first day of May One thousand nine hundred and seventy. 2. Mr Behar hereby agrees with the Company as follows: (a) To pay to the Company the said sum of Fifty thousand pounds on or before the thirtieth day of June One thousand nine hundred and seventy.” B

There then follow various provisions regarding the disposal by Mr. Behar and any of the directors of shares in the Company. C

The Company was assessed to corporation tax in respect of the receipt of the £50,000 and appealed against that assessment. The Special Commissioners held that the Company’s rights under the service agreement were not assets for the purposes of s 22 of the Finance Act 1965. The material provisions of the Finance Act 1965 are as follows:

“19(1) 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 . . . 19(3) Subject to the said provisions, a tax, to be called capital gains tax, shall be assessed and charged for the year 1965–66 and for subsequent years of assessment in respect of chargeable gains accruing in those years, and shall be so charged in accordance with the following provisions of this Part of this Act . . . 22(1) All forms of property shall be assets for the purposes of this Part of this Act, whether situated in the United Kingdom or not, including—(a) options, debts and incorporeal property generally, and (b) any currency other than sterling, and (c) any form of property created by the person disposing of it, or otherwise coming to be owned without being acquired. (2) For the purposes of this Part of this Act—(a) references to a disposal of an asset include, except where the context otherwise requires, references to a part disposal of an asset, and (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 . . . 22(3) Subject to subsection (6) of this section, and to the exceptions in this Part of this Act, there is for the purposes of this Part of this Act a disposal of assets by their owner where any capital sum is derived from assets notwithstanding that no asset is acquired by the person paying the capital sum, and this subsection applies in particular to—(a) capital sums received by way of compensation for any kind of damage or injury to assets or for the loss, destruction or dissipation of assets or for any depreciation or risk of depreciation of an asset, (b) capital sums received under a policy of insurance of the risk of any kind of damage or injury to, or the loss or depreciation of, assets, (c) capital sums received in return for forfeiture or surrender of rights, or for refraining from exercising rights, and (d) capital sums received as consideration for use or exploitation of assets.” D  
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On behalf of the Crown it is contended that the Company’s rights under the service agreement constituted an asset for the purposes of s 22. More particularly, it is contended that the £50,000 was a capital sum “received in return for . . . surrender of rights” within s 22(3)(c). I may say that it is common ground that the £50,000 was a capital sum. I

(Fox J.)

- A On behalf of the Company, the following submissions are made: (i) that the right of an employer under a contract of service to the services of the employee is not a chargeable asset; (ii) if that is wrong, that the chargeable asset was acquired for a consideration which cannot be valued, and that accordingly the provisions of s 22(4) apply, with the result that the asset was acquired for a consideration equal to its market value when acquired; (iii) alternatively, that on the facts
- B found by the Special Commissioners the £50,000 was derived from the shares in Hosiery and South Coast, the values of which were affected by Mr. Behar's departure, so that the chargeable gain falls to be computed by reference to those shares.

C I come, then, to the construction of s 22. Section 22(1) provides that "All forms of property shall be assets for the purposes of . . . this Act". The first question is whether the Company's rights under the service agreement are property for the purposes of s 22(1). The word "property" is not, I think, a precise term. Its meaning may vary with its context. Lord Porter, in *Nokes v. Doncaster Amalgamated Collieries, Ltd.* [1940] AC 1014, at page 1051, put the position thus:

- D "In truth the word 'property' is not a term of art but takes its meaning from its context and from its collocation in the document or Act of Parliament in which it is found and from the mischief with which that Act or document is intended to deal."

E In the *Nokes* case itself, I may say, the majority of the House of Lords took the view that a contract of service was not property for the purposes of the relevant Statute in that case. Now reading s 22(1) I am left with the impression, as I think was Walton J. in *Commissioners of Inland Revenue v. Montgomery*<sup>(1)</sup> [1975] 2 WLR 326, that the concept of what are "assets" for the purposes of the section is one of very great width. It seems to me that the draftsman was intending to cast his net very wide indeed. Thus "All forms of property" are assets, including "options, debts and incorporeal property generally" and also "any form of property created by the person disposing of it, or otherwise coming to be owned without being acquired". Accordingly, I see no reason to suppose that Parliament was taking at all a restricted view of the sort of assets which were to be within the scope of Part III of the Act. Looking in detail at the language of the section, it seems to me that the crucial provision for present purposes is s 22(3). That provides that there is for the purposes of the Act:

- G "A disposal of assets by their owner where any capital sum is derived from assets notwithstanding that no asset is acquired by the person paying the capital sum, and this subsection applies in particular to", *inter alia*, "capital sums received in return for forfeiture or surrender of rights, or for refraining from exercising rights."

There are, I think, two possible constructions of that subsection, namely:

- H (1) It is the Crown's contention that s 22(3) defines certain events which are deemed to be a disposal of assets. If one of those events occurs, then there is a disposal of assets. It is not, on this construction, necessary to ask whether there is an asset within s 22(1) which has been disposed of; there is simply a deemed disposal. If that is correct, then s 22(3)(c) provides a short and conclusive answer to the main point in the case. The Company certainly had rights under the service agreement. By the supplemental agreement it seems to me that the

(1) 49 TC 679; [1975] Ch 266.

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Company surrendered those rights in return for what the Company admits was a capital sum. Accordingly, on this construction, the case falls completely within s 22(3)(c). A

(2) The other approach is this. It may be said that the subsection is, in terms, dealing only with cases where a capital sum is derived from "assets", and "assets" must be assets of the nature described in s 22(1). Certainly that must be so in relation to the word "assets" where it is used in s 22(3)(a), (b) and (d). It is quite true, however, that the word is not used in s 22(3)(c) at all. But assuming this more limited view of s 22(3) to be correct, it seems to me that the language of para (c) is nevertheless of much importance as an aid to the construction of s 22(1). Thus, on this construction it is clear that mere "rights" of some sort must be assets for the purposes of s 22(1), since on this construction s 22(3) is dealing only with what are assets for the purposes of s 22(1); and it seems to me that in para (c) the draftsman must, on this construction, be assuming that a wide class of rights in fact falls within the description of assets. Thus, the word is apparently used in a wholly unrestricted sense; the paragraph refers simply to "rights" without any description or limitation. B C

In my view, it is a fair construction of para (c) to read it as treating some class of beneficial contractual rights as within the scope of s 22. As I have indicated, it seems to me that the ambit of s 22 is certainly very wide. If it is correct that some class of contractual rights is intended to be included, I see no reason for excluding valuable rights held by an employer under a service contract. Accordingly, in my view, it makes no difference which construction of s 22(3) is correct. One reaches, on the facts of the present case, the same conclusion by either route. D E

It is said on behalf of the Company, however, that there is one decisive consideration against treating the Company's rights under the service agreement as a form of property for the purposes of s 22(1); namely, the fact that, being a contract of personal service, the Company's rights under the service agreement are not assignable. Thus, it is said that the Act is concerned with the disposal of property in such manner as to give rise to capital gains, and that non-assignable rights cannot, in that context, be regarded as "property". I do not accept that contention for two reasons. First, it seems to me that a non-assignable lease, for example, must be an asset for the purposes of s 22(1). Mr. Thornhill, for the Company, seeks to avoid that difficulty by formulating a distinction between property which is inherently capable of being transferred though it may in the particular case be subjected to restrictions which prevent it being transferred (such as a non-assignable lease) and rights (such as those of the employer under a contract of service) which are inherently incapable of transfer. It is said that, to constitute property, the right must be either (a) a right that is capable of being transferred or (b) a right affecting an asset which is itself capable of being transferred. That test, I think, involves writing a great deal into the Act which is not there. Further, while I can see logic in excluding all non-transferable rights, I find it difficult to see, in the context of this Statute, a reasonable basis for a general rule which excludes some non-transferable rights but admits others, and does so simply on the basis of analytical distinctions between the types of property over which the rights are exercisable. The Statute is concerned with capital gains arising from assets. I see no reason why Parliament should have intended refined differences of the sort suggested by the Company. Of course, in this as in any other Statute, particular cases may be expressly dealt with. Section 27(4) provides that "non-marketable securities issued under the National Loans Act 1939 . . . shall not be chargeable assets". By s 27(9), "non-marketable F G H I

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A securities" means, *inter alia*, "securities which are not transferable". This, however, does not help the Company. Thus, it was obviously thought necessary to provide expressly that a limited class of non-transferable assets should not be chargeable assets.

B Secondly, the Act is not dealing only with the disposal of property. That is evident from s 22(3), which (whatever its correct construction on the matter which I have discussed above) clearly deals with some cases, at any rate, where there is no "disposal" of an asset in the ordinary sense at all. Looking at the whole matter, there are three other considerations which seem to me to be consistent with the conclusion that, by whatever route, the £50,000 was derived from assets within s 22. These are as follows:

C (1) It is clear from s 22(1) that "options" are assets for the purposes of the Act. There is no limitation or restriction upon the word "options" in s 22(1). As a matter of language, it would include an option to enter into a contract of service. If that is correct, there seems to me no reason why a contract of service itself should not be an asset.

D (2) Section 22(3)(d) provides that there is a disposal of assets where a capital sum is "received as consideration for use or exploitation of assets". As a practical matter, this could apply without difficulty to many service contracts. Thus, the servant may agree not only to serve the employer but also to perform duties for other persons if the employer so requires. The service agreement in the present case is indeed an example of such a contract, since Mr. Behar could be required to render services to third parties (in this case the subsidiaries of the Company). If an employer who has the benefit of such an agreement obtains capital sums by hiring out the employee's services to third parties, there seems E no reason, in principle, why the sums should not be taxable under s 22(3).

F (3) In general, it seems to me that, in the context of this Statute, there is nothing unreasonable in treating the employer's rights under a service contract as assets. The circumstances of the present case are no doubt unusual, but it is easy to imagine cases, for example in the entertainment world, where a contract of service of a star would be the most valuable rights owned by the employer.

Mr. Thornhill contends that to treat the rights under the service agreement as assets gives rise to difficulties or anomalies in the administration of the Act. For example, he says that if a man is employed to repair a chattel and, by failing to use due skill, damages it and has to pay compensation, the result of treating rights to compensation as an asset would be that the compensation would be a pure gain. Also, it is said that in such circumstances difficulties arise as to chattels G exempted from capital gains tax, in that compensation for damage would attract tax although the chattel is exempt. As to these points, there are, I think, two answers. First, the present case is not dealing with damage at all. The only relevant rights which ever existed were those under the service agreement. Compensation for damage is expressly dealt with by s 22(3)(a) and Sch 6, H para 13. Secondly, s 22(3) is expressly "Subject . . . to the exceptions in this Part of this Act"; that is to say, the various exemptions from capital gains tax made by the Act. My conclusion in the circumstances is that the Company's rights under the service agreement were, having regard to the provisions of s 22(3), assets for the purposes of s 22, and that the £50,000 was derived from such assets. I will return to the question of derivation later.

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I turn to the Company's alternative contention that its rights were acquired for a consideration which cannot be valued, and that therefore the chargeable gain falls to be computed under the provisions of s 22(4)(b) of the Finance Act 1965. That, in my opinion, is a matter which can be determined only after hearing evidence as to valuation. No such evidence was before the Special Commissioners, though they did express a view as to the principle. It is I think, agreed that the point should, in some form, be remitted. In my judgment the case should simply be remitted to the Commissioners for determination of the question whether the right can be valued and, if so, what the value is.

The Company contends, in the further alternative, that the capital sum of £50,000 was derived from the Company's shares in Hosiery and South Coast and not from the service agreement. As to that contention, the Special Commissioners, in their decision, make the following statement:

"It was also contended, in the further alternative, by the Company that the £50,000 was paid in part to compensate the Company for a possible diminution as a result of Mr. Behar's departure in the value of its shares in . . . Hosiery and South Coast and that the Company's shares in these subsidiaries were, therefore, the assets from which, for the purposes of s 22(3) of the Act, the £50,000 was derived. While we would be prepared to infer from the evidence that this was the main factor which influenced the Company to exact such a large sum from Mr. Behar to release him from the service contract, we feel prohibited by the decision in *Commissioners of Inland Revenue v. Montgomery*(<sup>1</sup>) [1975] 2 WLR 326 from tracing the derivation of the £50,000 beyond the rights which the Company acquired under the service contract."

In my judgment, the £50,000 was derived from the service agreement and nothing else. Clause 1 of the supplemental agreement states, in terms, that the £50,000 is to be paid in consideration of the Company releasing Mr. Behar from the service agreement; and, in my view, that represents the reality of the matter. The only reason why the Company was in a position to bargain for the £50,000 was because of the service agreement. The shareholdings in Hosiery and South Coast gave it no rights at all to require anything from Mr. Behar. The fact (which, as I understand it, the Commissioners were prepared to infer) that the main reason why the Company demanded so much as £50,000 was because it was concerned as to the effect which the departure of Mr. Behar might have on the value of its shares in Hosiery and South Coast does not seem to me to indicate the source of the £50,000 at all. The reason why the Company wanted so much as £50,000 may have been the shareholdings. The reason why the Company was able to obtain the £50,000 was the existence of the service agreement. I do not think there is any more justification for going behind the service agreement as to the source of the £50,000 in this case than there was for going behind the policies of insurance in the *Montgomery* case. I therefore think that the Commissioners' conclusion on this point was correct.

The result is that I allow the appeal and remit the matter to the Commissioners for the purpose which I have indicated.

*Appeal allowed, with costs. Case remitted to Special Commissioners to determine whether, and if so at how much, the rights under the service agreement were to be valued.*

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(<sup>1</sup>) 49 TC 679.



A The Company's appeal came before the Court of Appeal (Bridge and Buckley L.JJ. and Sir David Cairns) on 17, 18 and 19 April 1978 when judgment was reserved. On 12 May 1978 judgment was given against the Crown, with costs.

*A. R. Thornhill* for the Company.

*Brian Davenport* for the Crown.

B The following cases were cited in argument in addition to those referred to in the judgment:—*Davis v. Powell* 51 TC 492; [1977] 1 WLR 258; *Pritchard v. Arundale* 47 TC 680; [1972] Ch 229; *Aberdeen Construction Group Ltd. v. Commissioners of Inland Revenue* 52 TC 281; [1978] 2 WLR 648; *London & Thames Haven Oil Wharves Ltd. v. Attwooll* 43 TC 491; [1967] Ch 772; *Mangin v. Inland Revenue Commissioner* [1971] AC 739.

C

**Buckley L.J.**—The judgment I am about to read is the judgment of the Court [Buckley and Bridge L.JJ. and Sir David Cairns].

The Respondent Company, Benson's Hosiery (Holdings) Ltd., ("the Company") appealed to the Special Commissioners for the purposes of the Income Tax Acts against an assessment to corporation tax in a sum of £50,000.

D The Commissioners allowed the appeal. The Inspector of Taxes appealed by way of Case Stated to the High Court and Fox J. on 17 March 1977 allowed that appeal. The Company now appeals from the decision of the learned Judge. The facts are fully set out in the Case Stated and we need not recapitulate them in this judgment. We shall use the same names and descriptions as are used in the Case. The question which arose for the decision of the Commissioners was whether for the purposes of the Finance Act 1965, Part III, a chargeable gain

E arose on the receipt by the Company in the year ended 31 July 1970 of £50,000 paid by Mr. Behar, an employee and director of the Company, to secure his release from his service contract with the Company. The Commissioners answered that question in the negative and discharged the assessment appealed against, holding that an employer's rights under a contract of service are not

F "property" for the relevant purposes. The learned Judge, allowing the appeal before him, held that the Company's rights under the service agreement were assets for the purposes of s 22 of the Act and that the £50,000 was derived from such assets.

In sub-para (6) of their decision (Case Stated, para 9) the Commissioners had held that under the service agreement the Company was obliged to provide

G Mr. Behar with employment during the term of the service agreement and that that obligation formed part of the consideration for the rights acquired by the Company thereunder. They did not accept the Company's submission that that obligation could not be valued and that accordingly the Company's rights were acquired "partly for a consideration that cannot be valued" within the meaning of s 22(4)(b) of the Act. The learned Judge, having decided that the £50,000

H was derived from assets of the Company, remitted the case to the Commissioners for the determination of the question whether the obligation to provide Mr. Behar with employment can be valued and, if so, what the value is. In sub-para (7) of their decision (Case Stated, para 9) the Commissioners rejected an alternative argument presented by the Company that the £50,000 was paid in

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part to compensate for a possible reduction in the value of the shares in Hosiery and South Coast due to Mr. Behar's departure, holding that they were prohibited from so doing by *Commissioners of Inland Revenue v. Montgomery*<sup>(1)</sup> [1975] 2 WLR 326. Fox J. agreed with this view. A

In this Court the Company has contended that its rights under the service agreement are not assets for the purposes of the relevant sections. They have also contended that upon the facts of the case the Company's receipt of the £50,000 must be treated as derived not merely from the supplemental agreement by which Mr. Behar was discharged from his obligations under the service agreement but rather from the shares held by the Company in the two subsidiaries. B

The tax to which the Company is liable, if at all, is corporation tax under the Income and Corporation Taxes Act 1970, s 238, but under s 265 of that Act chargeable gains to be included in the Company's profits for the purposes of corporation tax are to be computed in accordance with the principles applying to capital gains tax; so we have to apply the provisions of the Finance Act 1965, Part III, as though this were a capital gains tax case. The Finance Act 1965, s 19 (1), provides: "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." So there must be a chargeable gain which has accrued on a disposal of assets. Sections 22-26 of that Act deal with chargeable gains. Section 22(1) provides: C

"All forms of property shall be assets for the purposes of this Part of this Act, whether situated in the United Kingdom or not, including (a) options, debts and incorporeal property generally, and (b) any currency other than sterling and (c) any form of property created by the person disposing of it, or otherwise coming to be owned without being acquired." E

The Act contains no other provision in the nature of a definition of "assets". It contains no definition of "disposal". Section 22(2), (3) and (4), so far as relevant to the present case provides as follows:

"(2) For the purposes of this Part of this Act—(a) references to a disposal of an asset include, except where the context otherwise requires, references to a part disposal of an asset, and (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 . . . (3) Subject to subsection (6) of this section, and to the exceptions in this Part of this Act, there is for the purposes of this Part of this Act a disposal of assets by their owner where any capital sum is derived from assets notwithstanding that no asset is acquired by the person paying the capital sum, and this subsection applies in particular to— . . . (c) capital sums received in return for forfeiture or surrender of rights, or for refraining from exercising rights . . . (4) Subject to the provisions of this Part of this Act, a person's acquisition of an asset and the disposal of it to him shall for the purposes of this Part of this Act be deemed to be for a consideration equal to the market value of the asset—(a) where he acquires the asset otherwise than by way of a bargain made at arm's length and in particular where he acquires it by way of gift or by way of distribution from a company in respect of shares in the company, or (b) where he acquires the asset wholly or partly for a consideration that cannot be valued, or in connection with his own or another's loss of F

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(1) 49 TC 679; [1975] Ch 266.

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A 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, or (c) where he acquires the asset as trustee for creditors of the person making the disposal."

B There is no suggestion in this case that the supplemental agreement was not negotiated at arm's length.

C The question to which we have to address our minds is whether a chargeable gain has in the circumstances accrued to the Company on the disposal, actual or notional, of any asset. So the case turns primarily upon the question whether the Company has, or must be treated as having, disposed of an asset. The Company says that their rights under the service agreement were not an asset or assets for the relevant purposes. The Crown contends that those rights fall within the term "incorporeal property generally" in s 22(1)(a) and that they are assets for the relevant purposes. At first impression one would not, we think, consider that an employer's rights to personal services under a contract of employment were appropriately described as "property". Counsel drew our attention to *Nokes v. Doncaster Amalgamated Collieries Ltd.* [1940] AC 1014 in which it was held in D the House of Lords that, where an order was made by the court under the Companies Act 1929, s 154, for the amalgamation of two companies, a contract of service existing at the date of the amalgamation between a workman and the transferor company did not automatically become a contract of service between the workman and the transferee company. Under that section of the Companies Act 1929, when sanctioning a scheme for reconstruction or amalgamation, the court had power to provide by order for the transfer to a transferee company of the whole or any part of the undertaking and of the property or liabilities of the transferor company. Subsection (4) of the section provided: "In this section the expression 'property' includes property, rights and powers of every description, and the expression 'liabilities' includes duties." The question in that case was whether, where such an order was made transferring all the property of a transferor company to a transferee company, the effect was that a contract of service previously existing between an individual and the transferor company became a contract between that individual and the transferee company. Viscount Simon L.C. after considering the practical results which might follow from holding otherwise, reached the conclusion that contracts of service were not so affected. At the foot of page 1023 the Lord Chancellor said:

G "At any rate, after examining s. 154 with close attention and considering the consequences of its application in different cases, I can come to no other conclusion than that an order made under it does not automatically transfer contracts of personal service. The word 'contract' does not appear in the section at all, and I do not agree with the view expressed in the Court of Appeal that a right to the service of an employee is the property of the transferor company. Such a right cannot be the subject of gift or bequest; H it cannot be bought or sold; it forms no part of the assets of the employer for the purpose of administering his estate. In short, s. 154 when it provides for 'transfer' is providing in my opinion for the transfer of those rights which are not incapable of transfer and is not contemplating the transfer of rights which are in their nature incapable of being transferred. I must make I it plain that my judgment is limited to contracts of personal service with which the present appeal is concerned."

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Lord Atkin, at page 1033, said:

“My Lords, I should have thought that the principle that a man is not to be compelled to serve a master against his will is just as deep-seated in the common law of this country as that which was under discussion in the case cited”—he is there referring to *Leach v. Rex* [1912] AC 305 which he had cited on the previous page—“and that here there is no clear, definite or positive enactment overturning it. But in truth the general words in this section describing ‘property’ seem to me to add nothing to the word ‘property’ standing by itself which would be taken by any lawyer to include property, rights and powers of any description.” At page 1034 he said: “I am satisfied that this in the main procedural section should not be construed so as to transfer rights which in their nature are by law not transferable.”

Lord Porter, at page 1051, said:

“Having regard to these considerations I find myself thrown back upon a consideration of the meaning to be placed on the word ‘property’ in sub-s. 1(a). Prima facie I should not expect it to include non-transferable contracts. In truth the word ‘property’ is not a term of art but takes its meaning from its context and from its connotation in the document or Act of Parliament in which it is found and from the mischief with which that Act or document is intended to deal.” At page 1053 he said: “I may sum up my view by saying that the word ‘property’ in s. 154, whether considered alone or in conjunction with the words ‘rights and powers of every description’ means property with which the original company has the right to deal without having to obtain the consent of some third party, and I cannot think that the addition of s. 154 sub-s (1)(f) empowering the Court to make provision for incidental consequential and supplementary matters is sufficient to widen the content of the section so as to include non-transferable contracts.”

In the light of those observations we ask ourselves whether there is here any ground for interpreting the word “property” as extending to non-assignable contractual rights such as arise under a contract of personal service. The answer depends upon the proper construction of s 22. The opening words of s 22(1) clearly indicate that an “asset” for the purposes of the charge to tax must consist of some form of property. The only word in the three following sub-paragraphs of that subsection which might possibly conflict with this view is the word “options”, for incorporeal property is obviously a form of property, as also are debts and currency, and sub-para (c) merely refers to “any form of property”. We are not in this case concerned with any kind of option, but we would construe “options” in this context as limited to options which are recognisable as having the character of property. We regard the sub-paragraphs as having been inserted in the subsection *ex majori cautela* in case anyone might possibly suggest that such things as are mentioned in them might not have been intended to be caught by the opening general words of the subsection. As was said by Lord Atkin in the definition of the word “property” in *Nokes*<sup>(1)</sup> sub-paras(a), (b) and (c) in the present case in our opinion add nothing to the effect of those general words.

Mr. Davenport has contended that incorporeal property here embraces all contractual rights. We think that s 22(2)(b) may throw some light, although not very brilliant, upon whether this view is correct. If incorporeal property

(1) [1940] AC 1014.

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- A for the present purpose embraces all contractual rights, it would seem that every distinct right under a contract must constitute a separate asset, notwithstanding that all the rights under a contract may also together constitute what one might call a composite asset. If this were so, the creation of an interest or right in or over that composite asset or any of the constituent rights would, as it seems to us, itself constitute the disposal of an asset rather than a part disposal
- B of a pre-existing asset as provided by s 22(2)(b). Take for example a lease of property, which may comprise a bundle of rights and liabilities. Any adjustment of those rights and liabilities which is as a whole favourable to the lessor will result under Sch 7, para 15(3), of the Act in a disposal by the lessee of an interest in the property, that is to say, as we see it, a part disposal under s 22(2)(b) of the asset consisting of the leasehold interest which belongs to the lessee; not a
- C disposal of an entire asset consisting of any particular right previously belonging to the lessee under the lease. This causes us to approach this submission of Mr. Davenport with caution. Section 22(3) deals with what may be called notional disposals. Mr. Davenport relies on s 22(3)(c) for saying that such a notional disposal must be supposed to have occurred in this case because the £50,000 was received by the Company in return for the surrender by Mr. Behar of his
- D rights under the service agreement. Mr. Davenport says that such a disposal must be taken to have occurred even if one cannot identify an asset which has been wholly or partly disposed of either actually or notionally. In our opinion, however, when sub-para (c) is read with the opening words of s 22(3), it is clear that it can only operate when it can be said that the capital sum is derived from an asset or assets, for the sub-paragraphs are particularisations of the
- E general words in the opening part of the subsection. So the rights surrendered, or which the recipient of the capital sum refrains from exercising, must be rights forming part of or appertaining to an asset and s 22(3)(c) cannot operate unless such an asset within the meaning of s 22(1) can be identified. Section 22(4) introduces the important concept of a notional consideration for the disposal of an asset in certain cases, including where the transaction is not a bargain at
- F arm's length or the actual consideration cannot be valued. This takes one to s 44(1) which provides: "Subject to the following subsections, in this Part of this Act 'market value' in relation to any assets means the price which those assets might reasonably be expected to fetch on a sale in the open market." So, to make these provisions workable, any asset to which they are capable of applying must be one for which a market value can be ascertained in accordance with s
- G 44(1). A right to personal services under a contract of service is, of course, unassignable. It cannot be bought or sold. Moreover it cannot survive the demise of either of the parties. It can have no actual marketable value, for there can be no market for what is unsaleable. It would not, we think, be practicable to suppose a notional market upon which the market value for the right could be estimated such as was invoked in *Inland Revenue Commissioners v. Crossman* [1937] AC
- H 26 for in the case of a contract of personal service the subject matter, which for the present purpose consists of the employer's rights under the contract, is inherently unsaleable; it is not merely subject to restrictions which can be taken into account in estimating a price on a hypothetical market. The rights of an employer under a contract of service could not even be sold and transferred with the consent and co-operation of the employee. All the employer could do would
- I be to agree to discharge the employee from the existing contract so as to free him to enter into a new contract with a new employer. This could, no doubt, be achieved by a tripartite contract, but it would not be a contract of sale and there would, in our opinion, certainly be no actual disposal of any asset by the former employer to the new one. Moreover, we find it hard to see how a market value could be placed upon the right to services of an employee under a contract of



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personal service having regard to the fact that such a contract is always liable to be determined by the death of either party, that is, of either of the original parties to the contract. A

If Mr. Behar had repudiated the service agreement, the Company could have recovered damages from him. These would presumably have been quantified by estimating the cost of replacing Mr. Behar by another director with the same duties for the unexpired term of the service agreement and setting against that cost what it would have cost to continue to employ Mr. Behar under the service agreement for the same period. Loosely this might be said to involve making an estimate of the market value of Mr. Behar's services, but it would not, we think, in truth amount to this. In this type of employment no one man's skill can be reckoned to be the precise equivalent of another's. The Commissioners found as a fact that Mr. Behar had been particularly successful. His skill and experience may have been of exceptional value to the Company. They might not be equally valuable to anyone else; and, even if they would be, the cost to the Company of an adequate replacement would not necessarily be a measure of the value of Mr. Behar's services either to the Company or to any new employer. In the light of these considerations it seems to us that the concept of a market value is entirely inappropriate to a contract of personal service. B C D

Section 22(4) may not be applicable to this case, in which event market value may have no direct relevance, but this would not affect the validity of the preceding argument upon the construction of the section, for an asset must be something of a kind to which all the provisions of the section are capable of applying in suitable circumstances. It is, we think, worth nothing that pension rights and analogous benefits are specially dealt with in s 22(4)(b) where they are coupled with assets acquired for a consideration that cannot be valued. It is, of course, possible to put a market value on such a right or benefit, which is what the subsection requires to be done, but the significance of this sub-paragraph seems to us to be that it appears to assume that the services in consideration of which the right or benefit has been granted are incapable of valuation. These considerations lead us to the conclusion that an employer's rights under the contract of service do not constitute an asset or assets within s 22. E F

The learned Judge reached a contrary conclusion on this point. In so doing he was very much influenced by s 22(3)(c). He said, we think rightly, that the concept of what are "assets" for the purposes of s 22 is a very wide one. He considered two constructions of s 22(3)(c), viz., (1) that it defines certain events in which a disposal of assets is to be deemed to have been made without any necessity to identify an asset which has been disposed of or, we may add, from which a capital sum has been derived; and (2) using s 22(3)(c) as an aid to the construction of s 22(1) to include in the terms "assets" a wide class of rights, so as to give to the word "assets" a wholly unrestricted sense. He thus reached the conclusion that it made no difference which construction was adopted, since on the facts of the case one would reach the same conclusion by either route. With deference to the learned Judge, we do not think it legitimate to use or construe s 22(3)(c) in this way. In our opinion it is an overriding requirement of s 22(3) that for a chargeable gain to arise a capital sum must have been "derived from assets", if there has not been an actual disposal of an asset by the person paying the capital sum. The four sub-paragraphs of the subsection are introduced by the words "and this subsection applies in particular to". It is consequently, in our judgment, not admissible to use any of the sub-paragraphs to extend that overriding requirement, unless this is absolutely necessary to G H I

(Buckley L.J.)

- A give coherence to the provisions of the Act. The subsection must, of course, be read as a whole and in its context, but, in our judgment, the considerations to which we have drawn attention do not support an argument that to make sense of the Statute s 22(3)(c) must be read as controlling the interpretation of the overriding requirement of the subsection. This, in our opinion, negatives both the alternative constructions envisaged by the learned Judge.
- B Fox J. placed some reliance on the reference in s 22(1)(a) to "options", which he said would, as a matter of language, include an option to enter into a contract of service. If such an option were an asset, he said, there seemed to be no reason why a contract of service itself should not be an asset. We do not think, however, that upon the true construction of s 22(1) "options" can there be understood to extend to any form of option right which cannot be recognised as a form of property. An option to acquire property can, we think, appropriately be classified as itself a property right, but an option to acquire or exercise some right or benefit which is not property (e.g., the right to attend some public performance at a reduced price) cannot, we think, be appropriately classified as property. So, if we are right in thinking that the benefit of a contract of service is not property, neither is an option for such a contract; and, if we are right in our construction of "options" in s 22(1), such an option would not fall within the subsection.
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- Mr. Davenport has urged that nowadays it is not unknown for anyone who can earn very large sums by the exploitation of his personal talents to enter into a contract of service at a relatively low salary with a company formed for the purpose of exploiting that person's talents for profit. He contends that in such a case the right of exploitation would be an asset of the company, and that, if a capital sum arising from the exploitation of that asset were to be received by the company, it would constitute a chargeable gain for the purposes of the Act. Perhaps this may be correct (but we should not be taken so to decide), although it has not been made clear how any receipt arising from exploitation of the person's talents could have the character of a capital sum. It would seem to us more likely to have the character of the profit of carrying on a business. But, in any event, this is not such a case. It is true that under clause 1 of the service agreement Mr. Behar could be required by the Company to render services to any subsidiary of the Company and that in pursuance of the service agreement he acted as managing director of both Hosiery and South Coast. The £50,000, however, was not received as consideration for any exploitation of the Company's right to require Mr. Behar to work for the subsidiaries, nor was it paid for the surrender of any right of Mr. Behar to be so employed. The service agreement seems to us to be more analogous in this respect to a contract to act as a farm bailiff or a business manager. It is in terms a contract to act as the sales and merchandise director of the Company: any services to subsidiary companies are treated as part of his duties as such a director of the Company. Mr. Behar has no right under the agreement to insist upon his skills being employed in any business other than the Company's. The £50,000 was paid for Mr. Behar's release from the service agreement, that is, from his obligation to serve as sales and merchandise director of the Company not as consideration for any exploitation of his talents.
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- This brings us to the last point with which we need to deal. Mr. Thornhill has contended as an alternative argument that on a true view of the facts the £50,000 was not paid for Mr. Behar's release but as compensation for the loss in value of the Company's shares in the two subsidiaries resulting from Mr. Behar's ceasing to act as marketing director of each of those companies. The
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shares in the subsidiary companies were undoubtedly assets of the Company. The argument is that the sum paid "derived" from those assets, but in our judgment, it cannot be correct to say that the sum derived from those assets within the meaning of the section. Such an anticipated loss in value may have had an important bearing on the negotiation of the amount of the sum paid. It was paid, however, as consideration for the Company's entering into the supplemental agreement whereby they released Mr. Behar from his obligations under the service agreement. The Commissioners felt themselves to be prohibited by the decision of Walton J. in *Commissioners of Inland Revenue v. Montgomery*(1) [1975] 2 WLR 326 from accepting this alternative argument, and Fox J. said that there was no more justification for going behind the service agreement than there was for going behind the policies of insurance in *Montgomery*. We agree with this view and would not have accepted the alternative argument, but, if we are right on construction, the point does not arise. Nor does the question which the learned Judge remitted to the Commissioners arise.

For these reasons we allow this appeal.

*Appeal allowed, with costs. Leave to appeal to the House of Lords granted.*

The Crown's appeal against the above decision came before the House of Lords (Lord Diplock, Viscount Dilhorne, Lords Simon of Glaisdale, Fraser of Tullybelton and Russell of Killowen) on 2 and 3 July 1979 when judgment was reserved. On 25 October 1979, judgment was given unanimously in favour of the Crown who did not seek costs.

(2) *Michael Nolan Q.C.* and *Brian Davenport* for the Crown. The Finance Act 1965 applies to all forms of rights upon whose disposal a capital sum may be received. "Disposal" need not involve a transfer: a surrender of rights is equally a disposal. [Reference was made to the Act of 1965, ss 19, 22, 27, 44, Sch 6, paras. 1, 2, 4 (1)(a)(b), Sch 7, paras 11(1)(2), 14.] The existence and nature of the reliefs given by s 27 supports the concept, expressed in s 22, of "assets" comprehending as wide a variety of rights as can be imagined. The scheme of Sch 6 is to bring in everything that is not covered by the income tax provisions (while avoiding double taxation).

The taxpayer Company says that the question is whether capital gains tax should apply to property that is of an inherently transferable nature. That is not the test. The taxation Acts are concerned with the derivation of profit, either by services, which is generally covered by the income tax provisions, or from goods in the course of trade, or by the accrual of gains by the ownership of rights, particularly rights of property. If one has something for which one can get £50,000, that is an asset, and the sort of wealth with which one would expect the Act of 1965 to be concerned. There is no decided case that deals very clearly with the case of, for example, the actor or footballer whose services change hands for a large sum, but in those cases there must be a gain or loss on the transaction coming within the scope of the taxing system. If one is to look at another line of authority, the estate duty line is more helpful than the Companies Act or

(1) 49 TC 679.

(2) Argument reported by Michael Gardner Esq., Barrister-at-law.

- A Bankruptcy Act lines. [Reference was made to Finance Act 1894, ss 1, 2, 7(5), 22(1)(8).] There are two estate duty cases that show that non-assignability is no barrier to the ascertainment of a market value: *In re Cassel* [1927] 2 Ch 275; *Inland Revenue Commissioners v. Crossman* [1937] AC 26: see per Viscount Hailsham L.C. at page 40. *Nokes v. Doncaster Amalgamated Collieries Ltd.* [1940] AC 1014 and the bankruptcy cases were essentially cases where the law depended for its operation on a transfer, so that it only operated on rights that were transferable. Those cases have no application to a case where tax becomes due without any transfer.
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- Even in the case of a purely personal right, as in *In re Cassel* [1927] 2 Ch 275, inherently inalienable, there is no reason in principle why such a right should not be made the subject of taxation, nor any insuperable reason why it cannot be the subject of market valuation. The words of s 22(4) do presuppose that the asset can be the subject of such a valuation, but this means a valuation within the meaning of the Act: see s 44. The difficulty for the Crown lies in the word "sale" in s 44(1): in bringing within provisions expressed in relation to sale an asset that is not subject to sale. In view of the estate duty cases, however, the words mean "on a sale, if they were saleable, in the open market". One has to assume a notional, hypothetical sale. [Reference was made to the Act of 1965, Sch 6, para 5.] It may be that the draftsman has simply followed precedent in putting in the valuation section.
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- The right of a protected tenant is a purely personal right, but, if a consideration is paid by the landlord for a tenant giving up his right, that is regarded as a taxable capital gain. The fact that the right is not assignable is no bar to that. Or one might postulate a transfer of shares in exchange for a promise to educate the transferor's son. The promise could not, perhaps, be valued, but the shares can be. No difficulty was found in practice in the present case, nor in practice would there be in other fields. The Crown is reluctant to accept that in all cases an asset, to be taxable, needs to be a form of property, but the right here is certainly incorporeal property within these provisions. The Crown adopts what Lord Simon of Glaisdale said in *Fleming v. Associated Newspapers Ltd.* 48 TC 382, 410-11; [1973] AC 628, 646-7. When one looks at ss 22 and 27 of the Act of 1965, one sees how very widely s 22 is drafted, and how things accordingly have to be left out in s 27.
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- D. C. Potter Q.C.* and *Andrew Thornhill* for the taxpayer Company. As to the meaning of the phrase "all forms of property", the first task must be to identify the property. There could be doubt as to whether it was the right to Mr. Behar's services under the agreement or the right to his services conditional on being paid remuneration and otherwise performing his obligations to the employer. The only right to Mr. Behar's services that the taxpayer Company had was a conditional right: conditional on paying him his money. Thus, the form of property that is said by the Crown to be within s 22 is that conditional right. The £50,000 came into the taxpayer Company simply for the giving up of that conditional right, the release of that contractual right. As regards "all forms of property", therefore, the taxpayer Company's first submission is that, on the true construction of that conditional right, it is not a form of property. More exactly, it was not intended by Parliament to be a form of property for the purposes of the capital gains tax legislation.
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- The following propositions are made: (1) The reference in s 22(3)(c) to "rights" does not extend the meaning of "assets" beyond s 22(1), or of the word "property" for the purposes of taxation. A number of indications support this proposition. Everywhere that one finds "assets" in ss 22 and 23 it could
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equally well read “form of property”. Which is the same as “on a disposal of rights”, not being themselves forms of property. Assets are likely to be a bundle of rights, some conditional, some not. Parliament does not intend that one should dissect them and say that each is an asset. In themselves they are not recognisable as property, but as a bundle they are. One is looking for property, not simply rights. When not a form of property “right” has a very wide meaning. Paragraph 4 of Sch 6 concentrates on the gain accruing on disposal of an asset, not rights, and one then looks at the consideration given for the acquisition. Parliament in s 22(3)(c) did not intend to do more than to extend the tax to disposals, including part disposals, of property. The Court of Appeal rightly based their decision on the interpretation of “right” in s 22(3)(c) as meaning property. The phraseology is intended to remove doubt. There is no genus or restriction, simply a plotting of a boundary.

(2) Applying the test of the man on the Clapham omnibus, what businessman would say, in talking of “any property”, that personal services are property? They simply are not, in the business connotation. The approach of Lord Wilberforce in *Aberdeen Construction Group Ltd. v. Inland Revenue Commissioners* 52 TC 281; [1978] AC 885 is the right one. Personal rights are simply not within the minds of businessmen.

[Lord Diplock—It is not a tax on businessmen; it is a tax on assets of all kinds.]

(3) In s 22 itself, subs (3) refers to “capital sum” (subs (2) refers to “an asset”; presumably these have different meanings). “Capital sum” is defined in s 22(9) in the widest terms; see also Sch 6. It is thus a compendious way of referring to money or money’s worth. One thus has two concepts: assets, and money or money’s worth. This indicates that they are not exactly the same: “money or money’s worth” is a wider concept than property.

(4) These rights are non-assignable; they do not pass to executors, nor to a trustee in bankruptcy. The idea of non-assignable property is anomalous. [Reference was made to *Bailey v. Thurston & Co. Ltd.* [1903] 1 KB 137, 138, 139.] A right to personal services does not vest in a trustee in bankruptcy. It is within the power of Parliament to transfer the untransferable, but *Bailey v. Thurston & Co. Ltd.* shows that, when it intends to do so, it says so specifically. *Sutton v. Dorf* [1932] 2 KB 304 is not just saying that a statutory tenancy under the Rent Restriction Acts is not assignable: “no estate or property . . . at all” (page 307). The cases show that, notwithstanding the mandatory language of the bankruptcy legislation, all property vests in the trustee, it does not include a right to personal services, which simply is not “property” for that purpose. It is not just that it is not property that does not vest in the trustee; Parliament is sovereign and could vest any property it liked. Section 22(3)(c), the only paragraph that does not refer to assets as “assets”, cannot be taken as extending the fundamental charging provisions so that they apply to “rights” rather than “assets”. “Assets” is used as a term of art rather than in its historical meaning, i.e., what is available to pay off creditors. In the case of a surrender or variation of rights attached to shares, one would still have the shares. Section 22(3)(c) has a legitimate function in such a case. Having given it that function, one cannot say that it widens the tax to a tax on rights generally. One must itemise the pieces of property on which the tax is payable. It means all pieces, items, of property. If the tax is on the pieces, it cannot also be on rights. “Property” is usually no more than a bundle of rights.



A (5) As to *Nokes v. Doncaster Amalgamated Collieries Ltd.* [1940] AC 1014, in the second part of what Lord Atkin says, at page 1027, he is going back to transferability, but one must remember that a sovereign Parliament had provided that all property of the transferor company should be transferred to the transferee company. Viscount Simon L.C. is saying, at page 1024, that a right to personal services is not property. When Parliament refers to "property" that includes the services of a serf. Although it is open to Parliament to include the services of a free man, the concept of our law is that these are not *prima facie* property of the employer. There are thus two points in *Nokes*. One is this: Parliament in a free country, presumably not faced with the distinction between serfs and free men, must be taken, when using the word "property", not automatically, without specific language, to include the services of a free man. That general proposition, particularised in this case, is that Parliament in 1965, having the decision in *Nokes* and the earlier cases, must be presumed not to have extended the concept of "property" to a right to personal services.

D (6) Anomaly is produced by accepting that an agreement for services is an item of property. Take as an example an extension of a service agreement from two years to 20 years. The master has got money's worth. This is the point at which tax becomes payable. He has a capital sum. This does arise from the original contract in the sense of the bargaining power of the employee. There is also an anomaly in the case of a "golden handshake". A hardship arises that Parliament did not intend; it does now tax it to some extent; it intended that the rest should be tax-free. Schedule 7, para 12, to the Act of 1965 does not take in the case of the ordinary golden handshake. The personal obligation is not mentioned there because it simply is not in it. [Reference was made to Sch 6, para 2(1).]

F (7) As to s 22(4), the Crown's point about consideration that cannot be valued—a promise to educate a man's son, for example—the taxpayer company accepts that, but that is also a promise of personal services, which itself cannot be valued. If it has no market value, that is an indication that it is not "property". A contract for personal service is not the property of the promisee. It has no market value; and so it is no asset, because the concept of base cost simply does not fit an asset that has no market value. As to s 22(4)(b), Parliament has in mind considerations that cannot be valued, but it does not seem that it has in mind that there are assets that cannot be valued. "Market value" presupposes a notional transferor and transferee. A right to personal services is by its nature inherently not transferable. It therefore has no market value and is not an item of "property".

H As to *Inland Revenue Commissioners v. Crossman* [1937] AC 26, it does no more than determine the method of valuation of shares where the right to make a free disposal of them is limited by the memorandum or (in the present case) the articles of the company. Indeed, so far from the shares there having been inherently non-transferable, Viscount Hailsham L.C. sets out, at page 32, the relevant article, which shows that there could be a transfer in the family, and then an elaborate code showing how one could make a transfer: see at pages 32, 34. *In re Cassel* [1927] 2 Ch 275 was not a case of a purely personal right; it was a right *in rem* of a benefit under a trust. So, on the taxpayer company's main point, I it says that Parliament could not have intended to include a non-assignable right to inherently personal services as an asset.

The taxpayer Company's second submission is that if the right to Mr. Behar's services is property it was acquired at market value by virtue of s 22(4)(b) of the Finance Act 1965. At present, the tax is stated to be the rate of tax

on the receipt of £50,000. That is the Crown's claim. Part of the base cost of the right is to give the employee work to do to enable him to keep his hand in. That is an asset that cannot be valued. If, adopting the Crown's example, a promise to educate a friend's son cannot be valued, and that is a classic case, an undertaking to provide an employee with work is equally a classic case. How can the valuation possibly begin? How much would Mr. Behar have wanted if he had had to work? The Commissioners are wrong: this is an asset that one cannot begin to value.

So, the acquisition cost is, under s 22(4), not the consideration that the taxpayer Company gave for Mr. Behar's services when they first took him on, but the value of his services when they took him on. It was just the same when he left. He was worth £50,000. The base cost to the taxpayer Company was £50,000. So, no tax is payable.

That is the issue of law that the House has to decide. Alternatively, it is so patent a fact that the base cost cannot be valued that the House can take judicial notice of it. It should therefore send the case back to the Commissioners with the intimation that in law the obligation of the employer taxpayer Company to provide Mr. Behar with work is a consideration that cannot be valued, so that, in estimating the base cost, one must deduct what would have been paid if rescission of the contract had followed the very moment of its making. It offends common sense to say that valuers could be found who could value the cost of providing work for a particular employee of a particular company.

*Thornhill* following on *Commissioners of Inland Revenue v. Montgomery* 49 TC 679; [1975] Ch 266. The taxpayer Company's third submission is that the sum of £50,000 is to be treated, under s 22(3)(a), as derived at least in large measure from the shares of the taxpayer Company in its two subsidiary companies. It was paid to secure the release of Mr. Behar, but the question under s 22(3) is a different one: is a capital sum "derived from an asset"? A capital sum may be paid for one thing but be derived from a different thing. The £50,000 was derived from the shares in the two subsidiaries. The directors were seeking compensation for the diminution in the value of the shares. The taxpayer Company does not have to show that they were actually diminished in value. Section 22(3)(a) talks of "risk of depreciation of an asset".

Where compensation comes to someone because of damage or injury to property it usually comes through the intervention of some legal right. It may well be that all those intervening rights are themselves assets for the purpose of the capital gains legislation, but the intention of Parliament in enacting s 22(3)(a) was that the compensation should be treated as derived not from the intervening asset but from property damaged or destroyed. In *Commissioners of Inland Revenue v. Montgomery* 49 TC 679; [1975] Ch 266, what Walton J. says, at page 686F, appears to lay down a general proposition that, if the sum is immediately derived from asset A, it cannot be more remotely derived from asset B. If any such proposition was laid down, it goes too far and should be rejected. The result, if the taxpayer Company is right in this submission, is that the £50,000 is properly derived from the shares and that there is a part-disposal by the taxpayer Company of the shares in its two subsidiaries. The taxpayer Company can then set against it part of the cost of the acquisition of the shares. It is not just a question of identifying the legal right to the sum of money, but a question of what loss the legal right was intended to compensate.

The taxpayer Company's submission does not involve rewriting the agreement; the right that the compensation was paid for was the right to Mr. Behar's services, but it was not "derived from" that right. Mr. Behar's services would not have been worth £50,000 if he had not been a director of the two subsidiary companies.

- A The description of the payment in the contract does not necessarily serve to identify what the payment was being made for in commercial terms. So, in the present case, it is a superficial analysis to say that the £50,000 was paid for Mr. Behar to give up his rights. The Commissioners thought that they were precluded from tracing the derivation of the £50,000 back to the shares by *Commissioners of Inland Revenue v. Montgomery* 49 TC 679; [1975] Ch 266.
- B But for that they would have held that it did derive from them. It cannot be said that the Company would have got as much from Mr. Behar if it had not had the shares in its two subsidiaries. The case is on all fours with compensation received by a trader. The first task is to identify what the compensation is paid for. What loss is the trader seeking to recover?

- C *Nolan Q.C.* in reply (he was not required to reply on the *Commissioners of Inland Revenue v. Montgomery* 49 TC 679; [1975] Ch 266 point). As to whether s 22(1) of the Act of 1965 extends to rights *in rem* but not to rights *in personam*, one has only to read the subsection to see that it expressly includes debts, which commonly arise under a personal contract. Even an unsecured debt can give rise to a chargeable gain.

- D If it is not so limited, is it limited to rights that can be transferred? The taxpayer Company came down in the end to "rights that were inherently transferable". In the context of an Act designed to attack not transfers but disposals on which gains may arise—on forfeiture no less than on transfer—there is no ground for limiting the scope of "assets" to "transferable assets".

- E As to statutory tenancies, in *Commissioners of Inland Revenue v. Montgomery* 49 TC 679; [1975] Ch 266 the court referred to the surrender of a statutory tenancy as something to which s 22(3)(c) would apply: see at page 687. It need not, however, be so limited: many contracts of a personal character could not be assigned, but have a money value. To say that they are not within the Act is to read in words that are not there and that do not fall to be implied. So, here, there was a contractual right, which is a form of property, and from that property a chargeable gain was derived. To say that the services of a free man are not property is unrealistic: here, the taxpayer Company got £50,000 for such services. It would be surprising if an employer could part with an employee for a sum that escaped all taxation.

- G As to the bankruptcy cases, and market valuation, the taxpayer Company said that one must at least be able to find a transferee. It is clear, however, that there could be no transferee of the rights conferred on the two ladies in *In re Cassel*[1927] 2 Ch 275: they were personal rights that they had no right to sell or transfer. One must make such assumptions as are necessary to get at a valuation. The Crown does not accept that an asset of this kind cannot be valued within s 44(1).

- H As to "base cost", this was dealt with by Fox J., and there was no appeal to the Court of Appeal from that part of his order. The position of the Crown is clear: it is quite wrong to pick out one obligation of an executory nature—to provide work—and regard that as the cost of the acquisition by the employer of the benefit of the contract. That is not what is envisaged by Sch 6, para 4(1)(a). (It is a question of law.) There is no question here of a consideration in money or money's worth being given by the taxpayer company wholly for the acquisition of an asset represented by Mr. Behar's rights under the service contract.
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*Michael Nolan Q.C.* and *Brian Davenport* for the Crown. A

*D. C. Potter Q.C.* and *A. R. Thornhill* for the Company.

The following cases were cited in argument in addition to those referred to in Lord Russell of Killowen's speech:— *In re Cassel* [1927] 2 Ch 275; *Aberdeen Construction Group Ltd. v. Commissioners of Inland Revenue* 52 TC 281; [1978] AC 885; *Commissioners of Inland Revenue v. Montgomery* 49 TC 679; [1975] Ch 266. B

**Lord Diplock**—My Lords, I have had the advantage of reading in draft the speech of my noble and learned friend, Lord Russell of Killowen. I agree with it and, for the reasons stated by him, I think this appeal should be allowed.

**Viscount Dilhorne**—My Lords, I have had the advantage of reading in draft the speech of my noble and learned friend, Lord Russell of Killowen. I agree with it and have nothing to add. For the reasons stated by him, I think this appeal should be allowed. C

**Lord Simon of Glaisdale**—My Lords, I have had the privilege of reading in draft the speech about to be delivered by my noble and learned friend, Lord Russell of Killowen. I agree with it; and for the reasons which he gives I would allow the appeal and concur in the order which he proposes. D

**Lord Fraser of Tullybelton**—My Lords, I have had the advantage of reading in draft the speech prepared by my noble and learned friend, Lord Russell of Killowen. I agree with its reasoning and conclusions, and I also would allow this appeal.

**Lord Russell of Killowen**—My Lords, in September 1968 the Respondent Company ("the taxpayer") entered into a written agreement with a Mr. Behar ("Behar") under which Behar agreed to serve the taxpayer as sales and merchandise director in exchange for an annual remuneration for a period of seven years. In April 1970, by a further written agreement, the taxpayer released Behar from any obligation further to serve the taxpayer in consideration of payment by Behar to the taxpayer of £50,000. The question in this appeal is whether that sum (subject perhaps to some deduction) is to be brought into the computation of the taxpayer's profits for corporation tax: and that question in turn depends upon whether it was a capital gain accruing to the taxpayer on the disposal of an asset within that part of the Finance Act 1965 that introduced capital gains tax. Hereunder the primary question is whether the right of the taxpayer under the contract to require the personal services of Behar was an "asset" within the 1965 Act. Before turning to the language of the Statute I will summarize the facts and the two agreements involved. E F G

In 1968 a company called Benson's Hosiery Ltd. ("Hosiery") was carrying on a business of selling hosiery through thitherto unexploited outlets, such as shops not usually associated with such goods. Behar owned 25 per cent. of Hosiery's issued share capital, had been for some years its sales and merchandise director and had pioneered and exploited with conspicuous success their novel method of hosiery marketing. The taxpayer (a holding company) in 1968 acquired the issued share capital of Hosiery in exchange for shares in the taxpayer. At the same time it acquired the issued share capital of another company, South Coast Warehousemen Ltd. It was in those circumstances that H

(Lord Russell of Killowen)

- A the taxpayer entered into a service agreement with Behar, who, it will have been observed, became a shareholder in the taxpayer. By that service agreement Behar was appointed sales and merchandise director of the taxpayer for seven years at a salary of £4,000 per annum. There was no provision for commission or bonus, though it appears that some bonus was paid. Thereunder Behar was required to perform the duties assigned to him by the board of the taxpayer
- B including rendering services to any subsidiary of the taxpayer: these services would no doubt be within the scope of a sales and merchandise director. His major function was to find and maintain sales outlets, and this function he performed with "conspicuous success".

- In March 1970 Behar sought release from his service contract. I suppose, my Lords, that he considered that his services were undervalued in the service contract, even with bonuses, and wished to be at liberty to earn more elsewhere. Of course, if he simply walked out he might have been liable for considerable damages for breach of contract. It is perhaps for question whether, in the circumstance that the taxpayer was only a holding company and could not assert direct damages in trade from his possible defection, such damages could embrace decline in profitability of its shares in the subsidiaries. In the result the agreement of 1970 in express terms required the payment by Behar of £50,000 in consideration of his release from the service contract. It also imposed limitations upon Behar's ability to sell his shareholding in the taxpayer, which I do not consider relevant to detail. The £50,000 in the taxpayer's accounts was deducted from the figure of goodwill, which had been built up from the excess cost to the taxpayer of the acquisition of the shares in subsidiaries over their book value net assets: I do not think that point assists in solution of the present appeal.
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- With that display of the essential facts I turn now to the relevant statutory provisions in order to examine whether there has been here a capital gain on the disposal of an asset. Section 19 of the 1965 Act is the charging section. It imposes a charge to the tax in respect of "chargeable gains computed in accordance with this Act and accruing to a person on the disposal of assets". Section 22(1) provides that "all forms of property" shall be relevantly "assets" including—(a) options, debts and incorporeal property generally, and (b) . . . (c) any form of property created by the person disposing of it, or otherwise coming to be owned without being acquired". Section 22(3) is of importance. That relevantly provides as follows:
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- G "(3) . . . there is . . . a disposal of assets by their owner where any capital sum is derived from assets notwithstanding that no asset is acquired by the person paying the capital sum, and this subsection applies in particular to—(a) capital sums received by way of compensation for any kind of damage or injury to assets or for the loss, destruction or dissipation of assets or for any depreciation or risk of depreciation of an asset, (b) . . . (c) capital sums received in return for forfeiture or surrender of rights, or for refraining from exercising rights . . ."
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- I should make it clear at this stage that it is not disputed by the taxpayer that the receipt of £50,000 involves a capital sum. The battle ground lies in s 22(3)(c) of the 1965 Act. The question is whether (notwithstanding that as a result of the 1970 agreement Behar acquired no asset by paying £50,000) the capital sum was received by the taxpayer in return for surrender of its rights under the service agreement or for refraining from exercising its rights under the service agreement. My Lords, at first glance I find it difficult to see why the rights of the taxpayer under the contract of service was not an "asset" of the taxpayer within



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the unrestricted language of ss 19 and 22 of the Statute. The Court of Appeal ([1979] Ch 152(1)) in deciding this case in favour of the taxpayer (reversing Fox J. [1977] Ch 348(2)) relied greatly on the reasons for the decision of this House in *Nokes v. Doncaster Amalgamated Collieries Ltd.* [1940] AC 1014. The question there was whether on the occasion of the approval by the court under the Companies Act of a scheme for the amalgamation of companies an employee's contract of service was automatically transferred to the new entity, the statutory language stating the relevant effect, on existing contracts and rights, of the order approving the amalgamation being of a width amply sufficient, *prima facie*, to embrace contracts of employment. This House however declined, despite the width of that language, to include within it contracts of employment: the reason was that to do so would breach a fundamental principle of the law that such contracts were not *assignable*, and that something more particular was needed than mere generality of language (however widely expressed) if such a breach of principle was to be accepted as being intended by Parliament. My Lords, I do not accept that that decision affords guidance to a decision under the capital gains tax legislation which deals not merely with assignments but with disposals. To treat the events which took place in the instant case as coming within the wide generality of the language of ss 19 and 22—and in particular of s 22(3)(c)—cannot be regarded as breaching any fundamental principle of the law that a contract of personal service is not assignable. Similarly I derive no guidance from the cases in bankruptcy law of *Bailey v. Thurston & Co. Ltd.* [1903] 1 KB 137 which decided that rights under a contract of personal service did not vest in the trustee in bankruptcy: and *Sutton v. Dorf* [1932] 2 KB 304 which similarly decided in the case of a statutory tenancy.

It was contended for the taxpayer that the rights of an employer under a contract of service were not "property" nor an "asset" of the employer, because they cannot be turned to account by transfer or assignment to another. But in my opinion this contention supposes a restricted view of the scheme of the imposition of the capital gains tax which the statutory language does not permit. If, as here, the employer is able to exact from the employee a substantial sum as a term of releasing him from his obligations to serve, the rights of the employer appear to me to bear quite sufficiently the mark of an asset of the employer, something which he can turn to account, notwithstanding that his ability to turn it to account is by a type of disposal limited by the nature of the asset. In this connection I would also refer to the provisions of s 22(3)(a) which appear to me apt to cover a case where damages are recovered by an employer from a third party for wrongful procurement of breach by the employee of his contract of service. Reliance was placed by the taxpayer and the Court of Appeal upon the provisions of ss 22(4) and 44(1) of the Statute which in certain circumstances introduce the concept of a market value: the contention being that the rights of the employer under the contract of service being non-transferable they could have no market value. In my opinion it is erroneous to deduce from s 22(4), the language of which has no direct application to the present case, a principle of general application for the purposes of capital gains tax that an asset must have a market value. This appears to me to be a preferable answer to the alternative contention of the Crown of analogy with the estate duty cases such as *Inland Revenue Commissioners v. Crossman* [1937] AC 26 in which a market value could be found notwithstanding restrictions on transfer of shares in a private company. It appears to me that there is a distinction to be drawn between a case in which the asset has the essential character of transferability

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- A but subject to restrictions imposed by the contract contained in the articles of association, and the asset in the instant case which lacks that essential character. The Court of Appeal, I think, placed some reliance on the provisions of the Statute relating to part disposals. While I can envisage that problems may arise in the application of such provisions I can find nothing in them to lead me to conclude that the decision of Fox J. was erroneous. The final point taken for
- B the taxpayer was that in truth the £50,000 payment was derived from the taxpayer's shareholding in its subsidiary companies. This submission was rejected by both Fox J. and the Court of Appeal and I am content to say that I agree with them.

Accordingly, my Lords, I would allow this appeal and restore the order of Fox J. Having regard to the terms upon which leave to appeal was given by

C the Court of Appeal there will be no order for costs here and the order for the costs of the appeal to the Court of Appeal shall stand.

*Appeal allowed. The Crown did not seek costs.*

[Solicitors:—Solicitor of Inland Revenue; Howard, Kennedy & Rossi.]

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