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UT-2020-000269
UT-2020-000092
UT-2020-000093

Upper Tribunal
(Tax and Chancery Chamber)

Hearing venue: **The Rolls Building, Fetter Lane, London EC4A 1NL**

Heard on: 24 June 2022
Judgment date: 20 September 2022.

Income Tax – deemed distribution s 1020 Corporation Tax Act 2010 – Interpretation 'market value' – Correct approach to determining market value of benefit received - What constitutes 'new consideration'. HMRC appeal allowed, taxpayers' cross appeals dismissed.

Before

MRS JUSTICE BACON (Chamber president)
JUDGE PHYLLIS RAMSHAW

Between

THE COMMISSIONERS FOR HER MAJESTY'S REVENUE AND CUSTOMS

Appellants (and Respondents in cross appeal)

and

MR NEIL PICKLES
MRS SHARON PICKLES

Respondents (and Appellants in cross appeal)

Representation:

For HMRC: Ms Laura Poots, of counsel

For the Taxpayers: Mr Conrad McDonnell, of counsel

DECISION

Introduction

1. The Commissioners for Her Majesty's Revenue and Customs (**HMRC**) are the appellants and also the respondents in the cross appeal. Mr and Mrs Pickles (together **the taxpayers**) are the appellants in the cross appeal and respondents to HMRC's appeal.

2. The main issue in the appeal and cross appeals is the interpretation of the term "market value" in s. 1020 of the Corporation Tax Act 2010 (**CTA 2010**) and the correct approach to determining the market value of the benefit received by the taxpayers. The identification of what constitutes "new consideration" for the purpose of s. 1020 is also in issue.

Background

3. Prior to 2011 the taxpayers carried on a business in partnership, known as Holme Farm Produce. The business graded and processed potatoes. It had machinery, vehicles and other capital assets, some intangible fixed assets, trading stock and debtors. In 2011, the taxpayers set up a company for the purpose of incorporating the partnership, Holme Farm Produce Limited (**HFPL**), and subscribed for £95,000 worth of shares.

4. By agreement dated 27 March 2011 (**the sale agreement**) HFPL agreed to purchase the assets of the Holme Farm Produce business (not including the land, which was retained by the taxpayers) as a going concern, completion to take effect on 1 May 2011. The sale was for an agreed sum plus the assumption by HFPL of the trading liabilities of the business at the time.

5. It is common ground that the value attributed to goodwill on the sale was £1,199,043, based on a calculation carried out by Forrest Burlinson, the former agent of the taxpayers. The calculation was based on two years of actual sales, gross profits and two years of projections. The amount of £1,199,043 was credited by HFPL to the directors' loan account. Following the sale Mr Pickles acted as the managing director of HFPL and Mrs Pickles oversaw the accounting function.

6. On 30 January 2013 the taxpayers filed their returns for the tax year 2011/2012. They omitted to declare their share of the capital gain on the sale of the goodwill. HMRC opened enquiries into their returns on 13 December 2013 and, pursuant to s. 28A of the Taxes Management Act 1970, on 16 and 20 September 2016 it issued closure notices amending the taxpayers' self-assessment returns for the year 2011/12. The adjustments to the tax returns resulted in:

> (1) for Mr Pickles' tax return: £123,660.02 additional Income Tax (after dividend tax credits) and £21,440.00 Capital gains tax (**CGT**); and
>
> (2) for Mrs Pickles' tax return: £123,659.40 additional Income Tax (after dividend tax credits) and £21,440.00 CGT.

7. The closure notices were issued on the basis of agreement having been reached between HMRC and Forrest Burlinson that, as at 1 May 2011, the goodwill transferred (giving rise to the CGT charge) should be valued at £450,000. The income tax charges arose under s. 1020 of CTA 2010 as a distribution, and the amount assessed was based on the difference between the £1,199,043 and the agreed value of goodwill of £450,000, giving a total figure (across both taxpayers) of £749,043.

8. Meanwhile on 21 July 2014 HFPL was placed into administration, and the company was ultimately dissolved on 23 October 2015. By the time HFPL went into administration, the taxpayers had withdrawn £771,863 from the directors' loan account. The balance of the directors' loan account (£427,180) as at the date of administration was not repaid.

Relevant legislation

9. S. 1000 CTA 2010 sets out the meaning of a distribution for the purposes of the Corporation Tax Acts. At the relevant time it provided (so far as material):

> "1000 **Meaning of 'distribution'**
>
> (1) In the Corporation Tax Acts 'distribution', in relation to any company, means anything falling within any of the following paragraphs.
>
> ...
>
> B. Any other distribution out of assets of the company in respect of shares in the company, except however much (if any) of the distribution—
>
> (a) represents repayment of capital on the shares, or
>
> (b) is (when it is made) equal in amount or value to any new consideration received by the company for the distribution.
>
> For the purposes of this paragraph, it does not matter whether the distribution is in cash or not.
>
> …
>
> G. Any amount treated as a distribution by section 1020 (transfers of assets or liabilities)."

10. At the relevant time, s. 1020 CTA 2010 provided:

> "(1) This section applies if on a transfer of assets or liabilities—
>
> (a) by a company to its members, or
>
> (b) to a company by its members,
>
> the amount or value of the benefit received by a member exceeds the amount or value of any new consideration given by the member.
>
> (2) The company is treated for the purposes of the Corporation Tax Acts as making a distribution to the member of an amount equal to the excess. But this is subject to section 1021.
>
> (3) For the purposes of subsection (1) the amount or value of a benefit, or of any consideration, is determined in accordance with the market value."

11. The exceptions set out in s. 1021 are not relevant to the present appeal.

The appeals to the FTT

12. The taxpayers appealed to the First-tier Tribunal (**FTT**). After addressing a preliminary issue regarding the status of the taxpayers' accountant, who was acting as their representative before the FTT, two substantive issues required determination, namely (i) the value of the capital gain on the sale of the goodwill; and (ii) the amount of the distribution, if any, made by HFPL to the taxpayers for the purposes of s. 1020. There was no dispute as to the CGT consequences of the transaction.

13. The FTT determined, after hearing expert evidence on behalf of HMRC, that the value of the goodwill was £270,200. That finding is not challenged by the parties in this appeal.

14. In respect of the distribution issue, the FTT initially found in its decision of 22 April 2020 (**the original decision**) that there was no transfer of assets from HFPL to its members, the taxpayers, for the purposes of sections 1000(1)(a) and 1020 of the CTA 2010 by the creation of the directors' loan account. Nevertheless, to the extent that the debt was paid by HFPL in the amount of £771,863 and such sum exceeded the value of the goodwill (£270,200), the FTT held that that sum (£501,663) was a benefit and accordingly a distribution. The FTT was, however, unable to reach a unanimous view on that point; Judge Malek as presiding member therefore had a casting vote, and his decision was the decision of the Tribunal.

15. The dissenting view of Mrs Dean, financial member, was set out in an annex to the decision. She took the view that the only way in which a fixed amount and date for the distribution could be ascertained was to treat it as happening when the debt for £1,199,043 was established in exchange for the transfer of the goodwill. At that date the directors could have demanded repayment in full, and the fact that they chose not to do so did not, in her view, alter the value of the distribution. The non-payment of £427,180 gave rise to a capital loss under the provisions for irrecoverable loans in s. 243 TCGA 1992. Mrs Dean's conclusion appears to have been, therefore, that the taxable distribution should be calculated by reference to the entirety of the debt of £1,199,043, less the value of the goodwill.

16. HMRC applied for permission to appeal against that decision. The FTT undertook a review of the decision (in accordance with Rule 40 of the Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules 2009. On the basis of that review, it issued a supplementary decision setting aside §§44–46 of the original decision, which were the main points of the decision that addressed the distribution issue; in their place amended reasons were provided. The supplementary decision was released on 12 August 2020.

17. The conclusion in the supplementary decision remained the same: that the amount of the distribution was £501,663, being the amount of the cash "actually received" by the taxpayers less the value of the goodwill. The change in reasoning was to say that while no new consideration was given by the members, there was nevertheless a transfer of assets under s. 1020(1)(b), consisting of the goodwill and other assets transferred by the taxpayers on or around 1 May 2011, and that the benefit was the amount actually received (£771,863) on the basis either that the benefit of a debt is only received when payment is made or, in the absence of expert evidence, that the amounts actually received could be regarded as an approximation for the value of the debt. The supplementary decision found that the test in s. 1020 does not on a literal reading take into account the value of the assets transferred by the members, but that on a purposive approach that section does not intend to leave out of account the value of the assets transferred (£270,200) in determining the benefit. (With some

diffidence, the FTT also outlined a potential alternative analysis under s. 1020(1)(a), but said that this had conceptual difficulties.)

18. We note in passing that it is not clear whether the supplementary decision represents the views of both FTT members or only Mr Malek, and counsel were unable to cast light on the issue at the oral hearing. Since nothing turns on this, however, we have not sought further clarification.

19. The FTT granted HMRC's application for permission to appeal. The taxpayers in turn filed Rule 24 responses and subsequently applied for permission to cross-appeal, which was also granted by the FTT.

The grounds of appeal before the Upper Tribunal

20. Neither party disputes the FTT's conclusion that the value of the goodwill was £270,200. Both parties dispute the assessment of the value of the benefit received by the taxpayers for the purposes of s. 1020.

21. HMRC raises three grounds of appeal, namely that:

(1) The FTT erred by failing to identify the transfer of goodwill as the "new consideration" for the purposes of s. 1020.

(2) The FTT was wrong to conclude that the taxpayers only "received" a benefit when payments were made to them in satisfaction of the debt.

(3) The FTT erred in its approach to the valuation of the benefit received by reference to amounts drawn down by the taxpayers. Rather, HMRC contends, the value of the benefit is simply equal to the monetary amount of the debt agreed by the parties.

22. In their cross-appeal, the taxpayers contend that the FTT erred in its approach to determining the market value of the benefit received by them. They contend that this should have been assessed as the price a reasonably prudent purchaser would have paid for the debt, which they say cannot be more than the net value of the assets of the company (excluding the debt itself). Alternatively, they say that the value of a benefit given by a newly formed company cannot exceed the value of any new consideration given by the members by more than the company's called up share capital. On either argument the taxpayers say that they should pay tax on a distribution of £95,000 and no more.

23. Both parties therefore contend that the FTT's approach to valuation erred in law, but for different reasons and with different asserted outcomes. This is the central issue in this appeal before us.

24. Before we consider that issue, however, we will deal briefly with Grounds 1 and 2 of HMRC's grounds of appeal. Mr McDonnell, for the taxpayers, confirmed at the oral hearing that the taxpayers did not contest those grounds, albeit that they did not necessarily agree with HMRC's precise analysis of how the FTT had erred.

Ground 1: whether the goodwill should have been identified as the new consideration

25. The FTT's primary and preferred analysis set out in the supplementary decision was that the relevant transfer of assets took place under s. 1020(1)(b), and consisted of goodwill and other assets transferred by the appellants to HFPL. The FTT found at §14 that "there was no new consideration given by the members. They only ever transferred the assets." It nevertheless held at §15 that on a purposive approach the assessment of a distribution under s. 1020 should not leave out of account the market value of the assets transferred by members to the company under s. 1020(1)(b); accordingly,

the amount of the distribution was to be calculated as the sum received by the taxpayers less the market value of the assets transferred.

26. HMRC argues (and the taxpayers concur) that the "new consideration" referred to in s. 1020 is, in this case, the goodwill. We agree that the FTT erred in its analysis and in the conclusion it reached on this issue.

27. S. 1020(1) treats as a distribution the difference (in excess) between the amount or value of the benefit received by the member and the amount or value of any new consideration given by the member in connection with the transfer of assets between a member and the company. S. 1115(1)(a) defines new consideration as "consideration not provided (directly or indirectly) out of the assets of the company".

28. The consideration provided in this case was the value of the transfer of the goodwill given in return for the benefit received, which was the promise to pay £1,199,043. While the "purposive approach" adopted by the FTT gave the result that the value of the goodwill was taken into consideration, we consider that the FTT did not need to read this into s. 1020, since it was already there. S. 1020(1)(b) is clear: its purpose is to treat as a distribution any difference in value between the value of the asset transferred and the value of the benefit received by the member. The value of the asset transferred must therefore be the new consideration or form part of the new consideration.

Ground 2: the time at which the taxpayers received a benefit

29. The FTT found at §9 of the supplementary decision that there were two forms to the benefit received by the taxpayers: the cash received and the benefit of a debt owing to them. In the case of the cash benefit, the FTT said that there was no issue as to when that was received. Regarding the debt, it found that the benefit was not received until payment was made.

30. The parties are agreed that this analysis was incorrect. It is common ground that the taxpayers received a benefit, for the purposes of s. 1020, at the point when they became entitled to the debt, i.e. when their contractually enforceable rights came into existence. On that basis the parties agree that the benefit should be valued as at (or around) 1 May 2011 when the contract took effect.

31. We agree. The approach adopted by the FTT entails the use of hindsight, in this case over a period of years, to determine the value of the benefit received. The amount that would ultimately be paid out would have been outside the knowledge of HFPL and the taxpayers in 2011 when the sale agreement took effect, and would have remained outside their knowledge when the taxpayers completed their 2011/12 tax returns in 2013. The FTT's analysis also separates the benefit into two distinct elements, before merging those benefits on each occasion that cash was received. The FTT erred in both identifying the nature of the benefit in this way and in its conclusions on the timing of the receipt of the benefit.

32. We consider (in agreement with the parties) that the benefit for the purpose of s. 1020(1)(b) in this case is the benefit of the contractually enforceable right to the agreed sum of £1,199,043. That right had crystallised on 1 May 2011; the taxpayers had therefore received the benefit of that right, and the valuation of that benefit must be assessed as at, or around, the date on which it came into existence.

33. For completeness on this point, we note that Mr McDonnell suggested in oral submissions that the credit to the directors' loan account might have been an overstatement of what was agreed between the parties, observing that the contract did not identify a fixed cash sum representing the goodwill in

the business. This point was not raised in the grounds of appeal or the taxpayers' skeleton argument, and it is difficult to reconcile with Mr McDonnell's acceptance, in his skeleton argument, that "it is common ground that the contractual sum of £1,199,043 was attributed to goodwill". In any event the FTT considered this argument and rejected it at §§37–39 of the original decision. Further, in its supplementary decision at §8, the FTT found that HFPL agreed to pay £1,199,043 in consideration of the transfer of the goodwill and as of 1 May 2011 the taxpayers became entitled to receive this sum on demand. The taxpayers have not sought to dispute those findings. We proceed on the basis that the enforceable right was to the sum of £1,199,043.

Ground 3: the FTT's approach to the valuation of the benefit received

HMRC's submissions

34. HMRC's position is the amount of the benefit for the purposes of s. 1020 is the face value of the debt, and no valuation is required. Alternatively, if a valuation is required, no relevant valuation evidence was put before the FTT; the Upper Tribunal should therefore uphold the closure notices on the basis that the taxpayers have not met their burden of proof on this point.

35. Ms Poots, for HMRC, argued as her starting point that the s. 1020(3) reference to "market value" is not engaged where the benefit is a promise to pay a sum of money, because no further steps are needed to determine the amount of the benefit. She contended that subsection (3) is only relevant where one cannot otherwise ascertain the amount or value of the benefit. By contrast, where the intention is that the shareholder will receive a sum of money, then the amount of the benefit is the monetary amount agreed by the parties. This interpretation, she said, fits with the purpose of s. 1020 which is to treat any "excess" in the hands of the members as a distribution. In this case clause 3 of the sale agreement provided that the sum of £1,199,043 was to be paid in cash or owing as a debt liable to be paid on demand. Further evidence of the intention to pay the full amount is the credit of £1,199,043 to the director's loan account. There is nothing to suggest the parties did not intend the full amount to be paid.

36. Ms Poots was asked if her submission reflected an intermediate position that market value should be interpreted as being the face value of the debt in the circumstances of this case. She indicated that this was an alternative to her primary position that subsection (3) was not engaged and noted that this would achieve the same result as her primary case.

37. Either way, she submitted that an approach which seeks to attribute a theoretical value to any promise to pay would lead to impractical and unlikely results. For example, where a shareholder purchases a company asset at market value, but the payment is deferred, s. 1020 would not be expected to apply. If, however, it is necessary to value the amount of the purchase price to reflect the deferred payment terms, that would result in the benefit received by the shareholder (the asset) exceeding the consideration paid by the shareholder (the purchase price). A distribution would therefore arise under section 1020. As a matter of practicality, this approach would also mean that a valuation would be required in every situation where the purchase price (or any part of it) was left outstanding.

The taxpayers' submissions

38. The taxpayers' case is that when determining the "amount" or value of the benefit received by a member, the "open market value" of that benefit must be determined, taking as the reference point the position of a purchaser of reasonable prudence: *Findlay's Trustees v Inland Revenue Commissioners* [1938] SVC 155.

39. Mr McDonnell submitted that the market value of the benefit received by the taxpayers could not exceed the company's ability to pay at the relevant time, which had to be determined by reference to its net asset value. In this case HFPL was a newly formed company, and the only assets held by it were the assets of the partnership business it had acquired, plus the initial £95,000 share capital. The net assets of the company immediately following the sale agreement were therefore the goodwill of £270,200 plus £95,000, a total of £365,200. Both sides of the transaction were the same: HFPL purchased a business and any promise to pay was a liability to be paid out of the assets HFPL had just purchased. Mr McDonnell said that this outcome had the advantages of being straightforward, logical, and consistent with the general principles applying to company distributions.

40. The alternative way of putting essentially the same point was to say that the open market value of a promise to pay must be less than face value if the company is in fact unable to pay the full amount in question. The market value of the HPFL's promise to pay must therefore be discounted by reference to the company's inability to pay the full amount. The only evidence for that market value had to be the evidence of HPFL's net asset value at the time of the transaction, since no prudent third-party purchaser would have paid more than that. The determination of the market value of the company's promise to pay should therefore have been a simple matter: on the same basis as above, a prudent purchaser would not have paid more than £365,200.

Interpretation of "market value"

41. We reject HMRC's submission that s. 1020(3) is not engaged where the benefit is a promise to pay a sum of money, and that it is only relevant if you cannot otherwise ascertain the amount or value of the benefit. Subsection (3) has no caveats – it applies to all cases falling within subsection (1). The amount or value of both the new consideration and the benefit are to be determined in accordance with market value. It appears to be uncontroversial that the market value of cash is its face value (subject to currency exchange rates if not sterling). But subsection (3) is still engaged, even though no further steps may be necessary to determine the market value in that scenario.

42. Equally, however, we reject the taxpayer's argument that the market referred to in subsection (3) is the "open market" as defined in relation to other taxes and as considered in case law, i.e. a hypothetical willing vendor and purchaser both assumed to be prudent and assuming an arm's length transaction. There is no definition of "market value" for the purpose of Part 23 of the CTA 2010 or specifically s. 1020. This is in contrast to Part 12 where s. 609 defines "market value" as having the same meaning as in s. 272–273 of, and Schedule 11 to, the Taxation of Chargeable Gains Act 1992 (**TCGA**) and Part 6 of the CTA 2010 where s. 210 provides that the market value of a qualifying investment is determined in accordance with sections 272–274 of TGCA. Those provisions in TCGA define market value of assets as the price which those assets might reasonably be expected to fetch on a sale in the open market subject to certain caveats. (We also note that s. 381 of the CTA 2010 defines "market value" for the purposes of Chapter 2 of Part 9 of the CTA 2010 by reference to the Capital Allowances Act s. 70YI(2), which provides for market value to be determined on the assumption of a disposal by an absolute owner free from all leases and other encumbrances.)

43. We conclude that "market value" for the purpose of s. 1020 is not to be interpreted as the "open market" value as defined in s. 272 of TCGA or any other similar provisions. Had the drafter intended that to be the case then a definition to that effect would, in our view, have been included as in s. 609 and s. 210. We agree with HMRC that we cannot directly import definitions used for the purposes of other taxes, as the statutory provisions are different.

44. We are fortified in that conclusion by a purposive construction of the provision (as endorsed by Lord Nicholls in *Barclays Mercantile Business Finance v Mawson* [2005] STC 1, §28). The purpose of s. 1020 is to prevent shareholders extracting value from a company untaxed. That is achieved by

treating as a distribution any difference between the value of the asset transferred and the value of the benefit received by the member, where there has been an over- or undervalue of an asset transferred from one to the other. The "market value" should accordingly, in our view, be determined by reference to the value attributed to the benefit by a member of a company (sharing the attributes and knowledge of the taxpayers), rather than the value which might be placed on the relevant asset by an arm's length third party trader.

45. The circumstances which inform what, from that perspective, is the "market value" of the relevant asset or benefit will vary depending on the transaction and the nature of the asset or benefit. For example, a tangible asset that constitutes the benefit received such as a car will require an evaluation of the condition and attributes of the asset itself, and its market value can usually be readily ascertained based on objective evidence; in such a case the surrounding circumstance of the agreement may have little bearing on determining the market value. In other cases, it may be necessary to consider the circumstances of the transaction and the intentions and knowledge of the parties. Ultimately, however, while (as just explained) the market value should be assessed by reference to the value to a member sharing the taxpayers' attributes and knowledge, the valuation must remain grounded in objective considerations: a purely subjective valuation (particularly one motivated by an intent to under- or overvalue an asset) would defeat the purpose of s. 1020.

46. That last point provides the answer to the example posited by Mr McDonnell of a small company agreeing to pay £1 billion for an asset that was only worth £1000. HMRC's case, he said, would result in a s. 1020 deemed distribution of £999,999,000, which must be incorrect. The short answer is that in such a case there could be no genuine intention to repay the sum agreed, and the market value of the promise could not in those circumstances be assessed by reference to the face value of the debt.

Application to the facts of this case

47. Having regard to the considerations set out above, we are of the view that the market value of the benefit to the taxpayers should be determined from the perspective of the value to be attributed to that benefit by a member of a company, with the attributes of the taxpayers, and with knowledge of the full facts surrounding the transaction.

48. Our starting point is to consider the nature of the benefit. The relevant clauses in the sale agreement provide:

> "2.1 The Vendors agree to sell with full title guarantee and the Purchaser agrees to purchase as a going concern with effect from the Transfer Date the Business and the Assets including without limitation:
>
> 2.1.1 the goodwill of the Vendors in relation to the Business …
>
> …
>
> 3.1 The purchase price for the Assets ('the Consideration') shall be:
>
> 3.1.1 the sum equal to the aggregate value of the Assets less the aggregate value of the Liabilities determined in each case by reference to the books of accounts of the Vendors at the Transfer Date; and
>
> 3.1.2 the assumption by the Purchaser of the Liabilities in accordance with this Agreement.

> 3.2 The amount of the Consideration determined in accordance with clause 3.1.1 shall be satisfied in cash at such time as the Purchaser may decide and, in the meantime, shall remain owing as a debt payable on demand."

49. Since (as discussed above) it is common ground that the sum of £1,199,043 was attributed to goodwill, the effect of the clauses above was that the benefit to the taxpayers was the promise made by HFPL to pay to them the amount of £1,199,043 either in the form of cash (at such time as HFPL decided) or as a debt payable on demand.

50. There is no evidence suggesting that the parties did not consider and intend £1,199,043 to be the value of the promise. The promise arose as a result of the agreement by the taxpayers to transfer the goodwill to HFPL. The amount agreed to be paid was arrived at as a result of a third-party valuation of the goodwill. The promise was objectively recorded in the agreement for sale as being payable in cash or payable on demand as a debt. Additionally, HFPL credited the amount of £1,199,043 to the directors' loan account. There was no evidence to suggest that the promise was not genuine or that the parties did not intend for the amount to be paid.

51. We disagree with Mr McDonnell's submission that the face value of such a promise is to be valued in light of how much the company could pay if the demand was made immediately at the date on which the agreement came into effect. In our judgment, the market value is the value to the member (who in this case does not require immediate payment) of a genuine promise to pay, objectively evidenced, in circumstances where the member has every expectation that the promise would be honoured. We accept HMRC's argument that there is no general principle that a debt is to be valued on what can be obtained now. The member can look forward to future profits and is assumed to have the knowledge that the taxpayers had. Indeed, in this case, notwithstanding the later revaluation of the goodwill at £270,2000, the taxpayers did in fact receive £771,863 (of which around £434,230 was withdrawn in the first year).

52. Mr McDonnell suggested that although the sale agreement was a *bona fide* agreement, the business carried on by HFPL was a very risky business and that the parties must have understood that HFPL's promise was to pay out only "if it could". That was not borne out by the evidence before the FTT. Mr Pickles' evidence was quite the opposite: that he "felt very buoyant about the prospects of the business" and he "certainly wouldn't have wanted to sell it to a third party for less than this [circa £1.2m]". Whilst we accept that the personal motivations and subjective view of Mr Pickles are not determinative, they undermine Mr McDonnell's arguments as to what the agreement was understood by the parties to be. We can see no reason why the face value of the debt should be discounted on this basis.

53. There is, moreover, a fundamental problem at the core of Mr McDonnell's argument, which is that it involves valuing the promise on the basis of hindsight. The dispute has arisen in this case because the goodwill was subsequently revalued to be far less than that agreed at the time of the transaction. (If the value of the goodwill transferred had in fact remained assessed at £1.2m, it would presumably have been common ground that the promise to pay could be given a market value of £1.2m and that s. 1020 would not be engaged.) But to discount the value of the promise as a result of a subsequent revaluation of the goodwill requires the use of hindsight to determine what the company's net assets were worth when the promise was made – indeed a very considerable degree of hindsight, since it was not until the FTT decision that the value of the goodwill was set at £270,200.

54. As discussed under Ground 2 above, both parties accept that the benefit must be valued at or around the date on which it came into existence and cannot be valued on the basis of facts which were only known years later (such as the amount that would ultimately be paid out by HFPL). The market

value of the promise at the time that it was made cannot therefore, consistent with that approach, be discounted on the basis of a subsequent revaluation of the assets transferred by the taxpayers. Although it is now established that the value of the goodwill was £270,200 and not £1.2m, it is difficult to see any logical basis on which that knowledge, acquired only many years down the line, should change the market value of the promise, assessed at the time of the sale agreement.

55. Furthermore, the suggestion that, in every case where a shareholder transfers an asset to its company in return for a promise to pay, a valuation of the company's net asset base is required to assess liability under s. 1020, would in our judgment go far beyond the purpose of that provision. It would likewise (as Ms Poots noted) be absurd if a valuation of the shareholder's ability to pay were required on every occasion where a shareholder purchased a company asset on deferred payment terms.

56. We are of the view that Mr McDonnell's analysis could lead to absurd results which are not in accordance with the purpose of the provision. On Mr McDonnell's analysis a distribution in the amount of £95,000 arose in this case, being the difference between the value of the new consideration and the value of the promise. He accepts, however, that any amounts the taxpayers drew from the directors' loan account would be taxable, most probably under s. 1000(1) paragraph B. On that analysis, if the taxpayers had withdrawn £1.2m, they would have been liable to a tax charge on the whole amount, because there would be no new consideration to take into account under paragraph B of s. 1000(1). The taxpayers would therefore have been liable to tax on an amount that was in excess of the amount intended by the legislation to be taxed.

57. As a final point, we note that if the full value of a director's loan is not in fact received there is a relieving provision under s. 243 TCGA 1992, referred to by Mrs Dean in her dissenting opinion. Whether that provision can be used will, however, depend on the circumstances of the particular case, and it has not been relied on in this case so we do not make any specific findings on that here.

58. Having regard to all of these considerations, in our judgment the market value of a promise to pay must be assessed by reference to the facts as they are known at the time of the transaction. On that basis we conclude that the market value of the benefit, on the facts of this case, is to be taken to be its face value i.e. £1,199,043.

59. For the above reasons we find that the FTT materially erred in law. HMRC's appeal is allowed and the taxpayers' cross appeals are dismissed.

60. We therefore set aside the decision of the FTT.

61. Submissions as to disposal were made by the parties in the event that the Upper Tribunal decided that expert evidence was required in order to determine the market value of the benefit. As we have not found that expert evidence is required, we do not need to set out or address those arguments.

62. We remake the decision as follows. The market value of the benefit received by the taxpayers is £1,199,043. The closure notices in respect of the charge to income tax should be increased on the basis of the value of the distributions received as being (in total) £928,843.

Signed on Original
Mrs Justice Bacon
Judge Phyllis Ramshaw

RELEASE DATE: 20 September 2022