



Neutral Citation: [2022] UKFTT 00312 (TC)

Case Numbers: TC08581

**FIRST-TIER TRIBUNAL
TAX CHAMBER**

By remote video

Appeal reference: TC/2020/03762
TC/2020/03760

*Remittance basis – s 809L ITA 2007 – debts waived subject to payment by non-UK third party
– property – services – derived from the gain*

Heard on: 20 to 21 June 2022
Judgment date: 31 August 2022

Before

**TRIBUNAL JUDGE RACHEL SHORT
ANN CHRISTIAN (Member)**

Between

**RAJ SEHGAL (1)
SANJEEV MEHAN (2)**

Appellants

and

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

Representation:

For the Appellants: Mr Michael Firth of Gray’s Inn Tax Chambers

For the Respondents: Mr Christopher Stone and Mr Bayo Randle of counsel, instructed by
the General Counsel and Solicitor to HM Revenue and Customs

DECISION

INTRODUCTION

1. With the consent of the parties, the form of the hearing was video. A face-to-face hearing was not held because at the time when the appeal was listed for hearing the Covid 19 pandemic made face-to-face hearings impractical.
2. The documents to which we were referred were contained in an agreed joint bundle amounting to 1520 pages.
3. Prior notice of the hearing had been published on the gov.uk website, with information about how representatives of the media or members of the public could apply to join the hearing remotely in order to observe the proceedings. As such, the hearing was held in public.

THE APPEAL

4. This is a joint appeal by Raj Sehgal (“RS”) and Sanjeev Mehan (“SM”) against closure notices issued to them on 22 July 2020 for the 2010-11 tax year. Those closure notices increased the capital gains tax assessed on the Appellants by £606,480 each. In HMRC’s view additional capital gains tax is chargeable because s 809L Income Tax Act 2007 (“ITA 2007”) applies to the settlement of an indemnity agreement made between entities with which the Appellants were connected.
5. The quantum of the capital gains tax charge is not in dispute for either Appellant.
6. No penalties are under appeal.
7. RS and SM appealed to this Tribunal on 26 October 2020.
8. The appeals of RS and SM are joined in accordance with the Tribunal’s directions of 31 July 2021. At the Tribunal we heard only from RS but it was agreed that the issues arising in both cases were identical.

BACKGROUND FACTS

9. The facts surrounding this appeal are complex, but are not disputed by the parties.
10. The transactions giving rise to the disputed charge under s 809L ITA 2007 arose from the sale by the Appellants, two UK resident but non-domiciled individuals, of a company in which they were the major shareholders in 2010.
11. On 25 February 2010, the Appellants entered into an arm’s length agreement (the Share Purchase Agreement (“SPA”)) to sell their 31.5% (SM) and 41.5% (RS) shares of Visage Group Ltd (“VGL”) to Centennial (Luxembourg) Sarl (“Centennial”), a Luxembourg resident subsidiary of the Li & Fung Group. The consideration was a mix of cash and loan notes issued by the purchaser, some of which were to be issued on deferred and earn out terms.
12. At the time of the sale, Internacionale Retail Ltd (“IR”), another company indirectly beneficially owned by SM (38%) and RS (38%), owed Visage Ltd (a subsidiary of VGL, “Visage”) approximately £6 million. IR was a subsidiary of SKS1 Limited, a Jersey company. (“SKS”)
13. Clause 8.1(d)(i) of the SPA provided
“The Individual Sellers hereby covenant with and undertake to indemnify the Purchaser fully on demand and to keep it indemnified against any and all Losses incurred, suffered or sustained by them or asserted against it or any member of the Group or any member of the Purchaser’s Group, or any or all of them arising out of any of the following:

[...] (d) (i) any failure by Internacionale Retail Limited to pay any amounts owed by it to any member of the Group as at the Completion Date by the date that is 30 days after the normal 120-day payment period for such debt (limited to amounts so owed plus costs and expenses in bringing a claim) and

(ii) any waiver or forgiveness by any member of the Group in respect of any amounts owed by Internacionale Retail Limited to any member of the Group prior to Completion (limited to amounts so waived, less costs and expenses in bringing a claim);

14. Shortly after the sale was completed, it became clear that the debt due from IR to Visage could not be recovered. This triggered clause 8.1 of the SPA and the Appellants were under an obligation to indemnify the purchaser (Centennial). (“the Indemnity”)

15. Li & Fung, however, were concerned about the effect on its own financial reporting of a straightforward payment of the indemnity amount and therefore requested that the Appellants’ obligations be discharged in a less straightforward way that Li & Fung hoped would not create any charge to profits.

16. A First Supplemental Agreement was entered into on 3 August 2010 which amended clause 8.1(d) of the SPA to read as follows (see clause 2.2 of the Supplemental Agreement):

“(d) (i) any failure by Internacionale Retail limited to pay any amounts owed by it to any member of the Group as at the Completion Date (or by any other company to pay equivalent amounts which have been agreed in writing by the Individual Sellers’ Representative and the Purchaser to replace the relevant Internacionale Retail Limited debts) prior to 15 September 2010 (limited to amounts so owed plus costs and expenses in bringing a claim) and

(ii) any waiver or forgiveness by any member of the Group in respect of any amounts owed by Internacionale Retail Limited to any member of the Group prior to Completion (limited to amounts so waived, less costs and expenses in bringing a claim);”

17. In the event, what happened was that SKS bought clothing goods from Miles Fashion Ltd (“Miles”), a German resident subsidiary of Li & Fung (Trading) Limited for €6,783,000. Those goods were only worth approximately £200,000 and were ultimately gifted to a charity in Africa. (“the Compensatory Transaction”)

18. The money SKS used was contributed by the Appellants (and to a lesser extent two others) and was monies received by them in accordance with the original SPA (by redeeming loan notes.

19. With reference to these events, a side letter (the “Side Letter”) was entered into on 23 December 2010 between Centennial and the Appellants whereby it was agreed between Centennial and the Appellants that:

(1) The payment by SKS to Miles “shall reduce the amounts owed to any member of the Group by IR as at the Completion date by the sterling equivalent of €6,783,0000”.

(2) Following receipt of the payment the Appellants were released from all and any existing or potential claims pursuant to clause 8.1(d)(i) of the SPA.

(3) IR’s obligation to make payment to Visage in respect of the debt referred to above was to be reduced by an equivalent amount and the purchaser “shall procure that Visage Limited shall not pursue” IR for such debts.

20. Following the transactions, as referred to above, Visage issued a credit note to IR for £6m in respect of the £6m debt (“the Credit Note”).

THE LAW

21. The relevant legislation is set out at s 809L ITA 2007:

“(1) An individual's income is, or chargeable gains are, “remitted to the United Kingdom” if

- (a) conditions A and B are met,
- (b) condition C is met, or
- (c) condition D is met.

(2) Condition A is that—

- (a) money or other property is brought to, or received or used in, the United Kingdom by or for the benefit of a relevant person, or
- (b) a service is provided in the United Kingdom to or for the benefit of a relevant person.

(3) Condition B is that—

- (a) the property, service or consideration for the service is (wholly or in part) the income or chargeable gains,
- (b) the property, service or consideration (i) derives (wholly or in part, and directly or indirectly) from the income or chargeable gains, and (ii) in the case of property or consideration, is property of or consideration given by a relevant person,
- (c) the income or chargeable gains are used outside the United Kingdom (directly or indirectly) in respect of a relevant debt, or
- (d) anything deriving (wholly or in part, and directly or indirectly) from the income or chargeable gains is used as mentioned in paragraph (c). [...]

(5) Condition D is that property of a person other than a relevant person (apart from qualifying property of a gift recipient)—

- (a) is brought to, or received or used in, the United Kingdom, and is enjoyed by a relevant person,
- (b) is consideration for a service that is enjoyed in the United Kingdom by a relevant person, or
- (c) is used outside the United Kingdom (directly or indirectly) in respect of a relevant debt, in circumstances where there is a connected operation.”

Relevant debt is defined in s 809L(7):

“(7) In this section “relevant debt” means a debt that relates (wholly or in part, and directly or indirectly) to—

- (a) property falling within subsection (2)(a),
- (b) a service falling within subsection (2)(b),
- (c) qualifying property dealt with as mentioned in subsection (4)(a),
- (d) a service falling within subsection (4)(b),
- (e) qualifying property dealt with as mentioned in subsection (5)(a), or
- (f) a service falling within subsection (5)(b).”

Relevant person includes a close company (or company that would be a close company if UK resident) in which the individual is a participator or a 51% subsidiary of such a company (s.809M).

Section 809L expands upon Condition D:

“(2) For the purposes of section 809L(5), the question of whether or not the person whose property is dealt with as mentioned in paragraph (a), (b) or (c) of section 809L(5) is a relevant person is to be determined by reference to the time when the property is so dealt with.

(3) A “connected operation”, in relation to property dealt with as mentioned in section 809L(5)(a), (b) or (c), means an operation which is effected—

- (a) with reference to a qualifying disposition, or
- (b) with a view to enabling or facilitating a qualifying disposition.

(4) A “qualifying disposition” is a disposition that—

- (a) is made by a relevant person,
- (b) is made to, or for the benefit of, the person whose property is dealt with as mentioned in section 809L(5)(a), (b) or (c), and
- (c) is a disposition of money or other property that is, or derives (wholly or in part, and directly or indirectly) from, income or chargeable gains of the individual.

(5) But a disposition of property is not a qualifying disposition if the disposition is, or is part of, the giving of full consideration in money or money's worth for the dealing that falls within section 809L(5)(a), (b) or (c).

(6) Enjoyment by a relevant person of property or a service is to be disregarded in any of these cases—

- (a) if the property or service is enjoyed virtually to the entire exclusion of all relevant persons,
- (b) if full consideration in money or money's worth is given by a relevant person for the enjoyment, or
- (c) the property or service is enjoyed by relevant persons in the same way, and on the same terms, as it may be enjoyed by the general public or by a section of the general public.”

22. We were also referred to these authorities:

- (1) *O'Brien v Benson's Hosiery (Holdings) Ltd* [1980] AC 562
- (2) *Kirby v Thorn EMI plc* [1988] 1WLR 445
- (3) *Melville v IRC* [2000] STC 628
- (4) *DMWSHZ Its v HMRC* [2015] EWCA Civ 1036
- (5) *Nokes v Doncaster Amalgamated Collieries Limited* [1940] AC 1014
- (6) *Zim Properties v Proctor* [1985] STC 90
- (7) *Hardy v HMRC* [2016] UKUT 332
- (8) *WT Ramsay v IRC* [1981] STC 174
- (9) *Jones Bros Ruth (Civil Engineering Co Ltd) v HMRC* [2022] UKFTT 26 (TC)
- (10) *Root 2 Tax Ltd v HMRC* [2019] UKFTT 744 (TC)

(11) *R (oao Gaskin) v Richmond Upon Thames London BC* [2018] EWHC 1996 (Admin)

(12) *UBS AG v HMRC* [2016] 1 WLR 1005

23. Other sources:

(1) Letter from CIOT to HMRC dated 15 June 2012 and HMRC response of 19 September 2012 concerning the tax treatment of court orders made on divorce when assets used are outside the UK to settle divorce orders in the UK: “Condition A (of s 809L) requires property to be brought into the UK by H [the husband] (ie the capital sum is not brought to or used or received in the UK by him). Condition A is not fulfilled by the payment”

HMRC’s response “HMRC agree your conclusion that no taxable remittance will arise for the reasons given in your letter”.

(2) Chitty on Contracts 34th Edition.

(3) 2007 Pre-Budget Report and Comprehensive Spending Review.

(4) Finance Bill 2008 explanatory notes, including at paragraph 21 with reference to s 809L

“The general aim is to ensure that income or gains to which the remittance basis applies are only excluded from charge to UK tax where they are genuinely kept offshore and not brought into the UK. But where they are in effect remitted to the UK in such a manner that the individual has the use or enjoyment of them in the UK, the individual should be liable to tax on them”.

(5) HMRC Manuals RDRM 33130, 33410 & 33430: the remittance basis referring to:

“A service provided in the UK could be anything from child minding or house cleaning, accountancy or legal advisory services.... The person to whom the service is provided in the UK might not be the taxpayer themselves...” and in respect of an air ticket purchased abroad for travel to the UK “because part of the travel service was provided in the UK, there is a remittance to the UK.....”

EVIDENCE

Oral evidence

24. We were provided with a witness statement from Raj Sehgal dated 26 November 2021. Mr Sehgal (RS) gave evidence to the Tribunal and was cross examined by Mr Stone.

25. Mr Sehgal was a clear and convincing witness who stressed that he had been heavily involved with the relevant transactions at the time when they were carried out. He maintained throughout cross-questioning from Mr Stone that the main purpose of all of the structuring had been to ensure that what he referred to as Li & Fung’s “financial engineering” would be successful. Li & Fung wanted to ensure that payment under the indemnity was treated for accounting purposes as the repayment of a debt made in the ordinary course of business, and not as a reduction in the purchase price which had been paid for Visage.

26. RS accepted that the money which had been obtained on the sale of Visage from the loan note redemptions by himself and SM had been put into SKS.

27. From his perspective, had it not been for the “rosy relationship” with Li & Fung and their on-going need to co-operate (due to the three year earn-out rights) he would have walked away from IR and not paid out under the £6 million which was payable under the Indemnity.

28. From the Appellants’ perspective by far the most straightforward approach would have been to make the payment under the Indemnity, and this would not have given rise to any remittance tax issues.

29. He was aware of the risk of paying tax in the UK on gains kept outside of the UK and wanted to avoid an additional tax charge, since no tax charge would have arisen if the indemnity had been paid as originally planned. RS was candid about his desire not to repatriate any profits to the UK and that this had driven the Appellants’ decision about how the indemnity payment should be made, while stressing that from his perspective he wanted to end up in the same position as if the Indemnity had been paid.

30. He viewed the payments which were made between Miles and SKS as “the equivalent of settling the indemnity claim”. All that the Appellants obtained through the Compensatory Transaction was being put back in the position they would have been in if the Indemnity had been paid.

31. He consistently suggested that the IR debt had never be settled or repaid; it had been waived as a result of the arrangements with Miles and SKS.

32. RS did not confirm that it was the Appellants and their advisers who had suggested the Compensatory Transaction (the sale of the jackets from Miles to SKS), he suggested that the idea had arisen from conversations between all the parties during the period from September 2010 until January 2011 to come up with a solution which worked for both Li & Fung and the Appellants.

33. He would have taken his own tax advice on any suggestions made by Li & Fung. By the time the final structure had been agreed in September 2010 he had received his own tax advice. The suggestion that more substance was required to support the Compensatory Transaction came from Li & Fung’s advisers.

34. He did accept that as a result of the transactions IR was better off because it no longer had a debt of £6 million outstanding and that the Appellants had been released from their obligations under the Indemnity. However, he did not view this as a benefit to the Appellants; they had merely extinguished a debt which they were always going to have to pay.

35. He also accepted that the price paid for the jackets provided from Miles was not and was not intended to be a commercial price. If the transaction had been done as a commercial deal, the Compensatory Transaction would not have worked.

Documentary evidence

36. We saw the following documentary evidence:

(1) Share Sale Agreement dated 25 February 2010 including:

- (a) Clause 3 – Consideration
- (b) Clause 8 – Indemnity
- (c) Clause 9 – Process for claims

(2) First Supplemental Agreement dated 3 August 2010 – changing clause 2.2 of the SPA.

(3) Side Letter dated 23 December 2010, between Centennial and the Appellants stating:

“In consideration of the payment of £1.00 by each party to the other.... the individual sellers’ representative and Centennial.....hereby agrees that for the purposes of clause 8.1(d) of the Initial Agreement (as amended.....) the payment by SKS1.....to Miles.....of an amount of Euro 6,783,000 in payment of invoices issued by Miles prior to or after the date of this letter in respect of the sale of stock to SKS1, shall reduce the amounts owed to any member of the Group by [IR]..... by the sterling equivalent of Euro 6,783,000 and.....

The individual Sellers shall have no liability pursuant to clause 8.1(d)(I) of the Initial Agreement....; and

[IR’s] obligation to make payment to Visage Limited to [IR] in respect of any unpaid invoices issued by Visage Limited on or before 28 February 2010 shall be reduced by the sterling equivalent of Euro 6,783,000 and the Purchaser shall procure that Visage shall not pursue [IR] for such debts to the extent that they are not in excess of the sterling equivalent of Euro 6,783,000”

(4) Tax indemnity dated 23 December 2010.

(5) Jacket purchase order and related invoices dated 1, 6, 9 13, 21 December 2010.

(6) Credit Note dated 17 December 2010.

(7) Correspondence between the Appellants and their advisers from 10 May 2010 to 14 February 2011 concerning the changes to the SPA and how payment of the IR debts would be settled and the terms of the Side Letter including:

(a) 28 May 2010 email from legal advisers Muckle concerning the amendment of the SPA.

(b) 10 September 2010 email Nick Cotterell to Robert Bacon:

“I have taken some independent advice on the above subject.... I am concerned that the proposed solution is somewhat contrived.... that there is a good chance that either the tax authorities or the auditors will pick it up” with the suggested solution as: “I think we can accept the cash being received from someone other than [IR] but I would ask that cash is paid by a method that doesn’t make it obvious on the bank statement which party sent the cash”

(8) Correspondence between the Appellants and Centennial and its representatives including:

(a) 2 June 2010 – Agreement to repay loan

(b) 20 July 2010 – Email from Muckles referring to meeting on 19 July 2010 and suggestion that the Indemnity would provide for another company to pay equivalent amounts to the Purchaser.

(c) 10 September 2010 – Email with suggestions for means of settling debt including payment by SKS.

(d) 11 September 2010 – email setting out concerns about remittance basis if SKS makes payment.

(e) 16 September 2010 – email suggesting SKS pays Miles.

- (f) 20 September 2010 – suggested use of purchase of goods.
 - (g) Email of 14 January 2011 – concerning amounts of jackets to be sent, to add to plausibility of the transaction.
 - (h) 25 January 2011 email from Miles Fashion: “We have now received an instruction to deliver the pallets to 5 separate Charity Shops”
- (9) Correspondence between HMRC and the Appellants from June 2013 to January 2021.

APPELLANTS’ ARGUMENTS

37. Mr Firth pointed out that HMRC had changed its position on several occasions about why there had been a remittance to the UK on these facts, concentrating initially on the Credit Note, then moving on to analyse the rights under the Side Letter and suggesting that Condition D was in point; all of those positions had subsequently been abandoned by HMRC indicating that they were struggling to establish a proper basis for raising a charge under s 809L ITA 2007.

38. HMRC’s arguments in their skeleton argument concentrated on Conditions A & B s 809L and the suggestion that the Side Letter and resulting transactions gave rise to “property” in the UK.

39. In Mr Firth’s view s 809L should not be treated as an anti-avoidance provision, rather it was “a codified approach to identifying remittances”.

Property analysis s 809L(2)(a) Condition A

40. The Appellants assert that none of rights which HMRC identify as “property” should properly be treated as such. The contractual property rights created by the Side Letter identified by HMRC are:

- (1) The release of the indemnity claims between the Appellants and IR.
- (2) The reduction in IR’s obligation to pay its debt to Visage.
- (3) The procurement of non-pursuance for debt between Centennial and IR

41. If any of these are property, they were not property received in the UK.

42. If they were received in the UK, they did not derive from taxable chargeable gains.

43. The rights under the Side Letter should not be treated as “property” because to do so would:

- (1) Be outside the ordinary meaning of the term.
- (2) Be inconsistent with the purpose of the legislation.
- (3) Give rise to absurd results.

Ordinary meaning of the term

44. “Property” is not a term of art and takes its meaning from the context in which it is used. See *Nokes*; Rights under a contract for service were not treated as property. The courts have cautioned against finding property rights by reference to other than real world analysis See *DMWSHZ*:

“In the real world under the ordinary law of contract the payment of a debt by a debtor to a creditor does not entail the transfer of anything by the creditor to the debtor. Its legal effect is to discharge the obligation to pay, with the result that the obligation disappears at the moment of payment. As Lord Wilberforce famously observed in *WT Ramsay Ltd v IRC* [1982] AC 300, 326D CGT “was created to operate in the real world, not in the world of make-belief;” an observation repeated by the House of Lords in *Barclays Mercantile Business Finance Ltd v Mawson* at [31].

“Even after the debt was repaid the Loan Notes continued in existence, not least because the Issuer still had the obligation to cancel the Notes under condition 5. In addition, the creditor's rights were transferred to the Issuer even if only for a *scintilla temporis*. In the course of his reply Mr Aaronson characterised this argument as “angels dancing on pinheads”. I agree. I do not believe that the approach to interpretation of taxing statutes laid down by *Barclays Mercantile Business Finance Ltd v Mawson* with its insistence on a realistic view of the facts leaves any scope for angels, pinheads or *scintillae temporis*. Mr Aaronson said that this was the wrong approach since what was in issue was not the appreciation of the facts, but the legal analysis of the facts. As I have said, in the real world when the debt was repaid the obligation to pay was discharged; and there were no remaining creditor's rights that could have been transferred to the Issuer. I cannot see that the world of CGT compels any different conclusion” [50]

45. On the Appellants’ analysis of the Side Letter: there has been a release of an obligation under the Indemnity in consideration for a payment, but that right (to be released from the indemnity obligation) is conditional on the payment being made between SKS and Miles, no right arises until payment has been made. That conditional right does not derive from anything. Once payment is made, there is no continuing right to be released from the Indemnity, there is no ongoing right or “property”.

46. S 809 does not have an extensive definition of property, unlike for example the provisions of the IHT legislation considered in *Melville*:

“At the first stage I must only decide whether the right as a matter of law is property or a right or interest 'of any description' within the meaning of s 272. The words 'of any description' give to the words 'right' and 'interest' the broadest connotation. In the context of s 272, plainly the words 'right' and 'interest' connote any form of proprietary right or interest which is of value to its holder and which may be turned to account” [15]

47. In some circumstances rights under a contract can be property, but not in all circumstances, see *Hardy* and *Zim* properties.

48. A relevant question is whether an asset can be turned to account? In *Hardy* rights under a contract, while treated as rights with a value, were nevertheless not considered to be an asset for CGT purpose.

“What Mr Hardy acquired was primarily the right, subject to compliance with his own obligations, to compel performance of the Seller's obligations under the Contract, and in particular to obtain specific performance of the Seller's obligation to convey legal title to the Property to him.....We have no difficulty in accepting that this was a valuable right, but it does not necessarily follow that it was an asset for the purposes of the legislation.” *Hardy* [33]

49. Mr Firth made a distinction between “a subsisting contractual right which is the economic purpose of the transaction”, such as a bank account, where the relevant contract does represent the economic substance of the transaction and so should properly be treated as an asset and the

type of contractual right referred to here, which he described as a conditional right to be released from an obligation, which is not something which can be bought, sold, received or used in a particular place.

50. A contractual right which is conditional on the performance by the holder of that right is not property, at least until the condition is satisfied; both the Appellants and IR had no right to be released from their obligations (under the Indemnity or the debt obligations to Visage) until payment had been made by SKS to Miles under the Side Letter.

51. Once the condition in the Side Letter had been triggered, the parties' rights were released and that right of release could not be treated as a separate property right (see *DMWSHZ*).

Purpose of the legislation

52. Mr Firth relied on the analysis provided by the CIOT in correspondence of June 2012 and confirmed by HMRC in respect of sums paid outside the UK under the terms of a divorce settlement between two UK resident individuals. In those circumstances HMRC agreed that there was no remittance if one party used property held outside the UK to settle obligations under a divorce settlement, despite the fact that the payment released the payor from any further liabilities in the UK.

53. That could be extrapolated to both the Appellants and IR who were released from obligations in the UK as a result of the payment made between SKS and Miles.

Absurdity

54. HMRC's analysis, that any contract governed by English law gave rise to a remittance would be absurd. It is not realistic to suggest that contractual rights arise in any particular location. To follow that logic would go far beyond the intention of the legislation and lead to an absurd result.

Money analysis – s 809L (2)(a) Condition A

55. Money was not used to settle a trade debt in the UK as HMRC claim. It is generally accepted that money is used where it is paid, which was not in the UK. The proceeds of the Visage sale were kept offshore and applied in specie outside the UK, as accepted by HMRC. The statutory question is not where the benefit from the money arose, as HMRC suggest, but where it was used or received.

56. As in the CIOT example, where money is used to release one person from obligations against another in the UK, the remittance rules do not apply.

57. There are specific provisions at s 809L (3)(c) which deal with relevant debts and they focus on where the debt is paid off.

Service analysis – s 809L(2)(b) Condition A

58. The Appellants say that if a service has been provided, it has not been provided in the UK, saying that:

- (1) The release of the IR debts is not a service
- (2) The release of potential liabilities is not a service

59. The Appellants say that on any ordinary interpretation of the term no service has been provided in the UK. In the context of s 809L it is clear that a service has to be provided and enjoyed in a specific place and for consideration. A person who is owed money under an

indemnity cannot be treated as providing a service by accepting a payment to discharge that liability. Equally, a person who pays a sum to discharge their liability under an agreement such as the SPA is not providing consideration for a service.

60. The full or partial satisfaction of a liability does not involve the provision of a service to the person satisfying the liability and this does not change if the liability is settled through a third party.

61. The Appellants suggest that HMRC's analysis would mean that if a customer bought damaged goods and accepted a payment to release the seller's liabilities, the customer is providing a service to the seller of the goods. The fact that payment was made by a third party to release the indemnity does not change this analysis.

62. The only entities who benefited from the release of the Indemnity were Centennial and Li & Fung, neither of which are in the UK.

63. The purpose of s 809L is to address what is referred to in the explanatory notes as a "cash loophole", analysing these transactions as HMRC have done does not fit within that purpose.

64. If there were services, they were not provided in the UK. HMRC's analysis makes it hard to determine where the services were actually provided and is inconsistent with the CIOT analysis (dealing with divorce settlements) which does not make any reference to the service analysis. The factors suggested by HMRC to determine that the services are provided in the UK are arbitrary.

Arising from the gain s 809L(3) Condition B

65. In any event, property, services or money payments from the seller to the buyer under the SPA cannot possibly be the "remittance of a gain" arising from the sale of Visage. The reversal of a gain cannot be said to derive from a gain, either directly or indirectly (s809L(3)(b)).

66. Even if the contractual rights can be treated as property for these purposes, they are not derived from the gain: from the Appellants' perspective the payment made has reduced the gain obtained from the sale of the Visage shares.

67. The fact that payment has been made via two other companies does not change this analysis; the legal mechanism for payment does not alter its character. See *Jones Bros*

"We also hold that the insertion of the elements which created the purported contracts for differences do not alter the nature of the payments as earnings and the grant of the contracts was no more than a process for delivery of the bonuses. In our view, the legal mechanism by which the payments were made did not alter the character of the payments. The Appellants entered into contracts with the employees in respect of which it expected and intended to pay the employees at the settlement date. Looking at the reasons and background to the payments, their purpose was to deliver bonus payments and the cause of the payments was employment. In reality, the payments were not calculated by reference to fluctuations but were instead the amounts the Appellants had decided to award the employees as bonuses." [432]

and *Root2Tax*:

"In summary, in my view, it is appropriate to apply the widely drawn term "earnings from an employment" by reference to the overall effect of the arrangements under consideration in this appeal on the basis that the elements involved were plainly intended to operate together as a composite whole with commercial unity. Taking an unblinkered realistic view according to their overall effects, the transactions were put

in place as nothing more than devices intended to extract from the appellant sums, which were intended to be a reward for the Individual's employment services for it, without attracting any substantial employment tax charges" [237]

68. Mr Firth says that the key error in HMRC's submissions is starting at the wrong point; the starting point must be the Appellants and their obligations under the Indemnity. The Appellants had no obligation to IR, their only obligation was under the Indemnity. HMRC accepted in their letter of 15 January 2015 that the focus of the Appellants was the indemnity, while HMRC focused on the issue of the Credit Note.

69. There was no tax avoidance motive on the Appellants' part and despite HMRC's suggestion, s 809L is not in essence a tax avoidance provision; it is a codification of the circumstances in which a remittance will be treated as made to the UK. In any event, had the Appellants undertaken the transaction which they wanted to undertake; payment under the Indemnity, there would have been no remittance and no tax charge in the UK.

70. A reduction in IR's liability for its debt is incidental to the main focus of the Appellants, which is the Indemnity, which is the only contract which has any value. In order to understand the transaction, it should be looked at from the Appellants' perspective; from their perspective the only significant issue was how to deal with their liability under the Indemnity.

HMRC'S ARGUMENTS

71. Mr Stone started by pointing out that s 809L is new legislation on which no authorities exist and therefore it is not surprising that HMRC have changed their analysis of its application over time particularly given the unusual circumstances of this case.

72. The transactions under consideration are contrived, their true nature was recognised by Grant Thornton in their letter of 18 December 2013 in which they referred to the release of IR's debt. "The effect of all of the above was that the debt due to Li & Fung Trading Ltd was effectively repaid in full with no charge to the profit and loss account of Li & Fung Trading Ltd".

73. HMRC's starting position is that two benefits have been provided in the UK as a result of the Side Letter; the release of the Appellants from their indemnity obligations and the release of IR from its debt obligations to Visage.

Property analysis – s 809L(2)(a) Condition A

74. Mr Stone stressed that it was not HMRC's position that all UK law governed contracts gave rise to remittances and that in a straightforward bi-party settlement of a debt, no questions of rights or services arising arose. But this is not a straightforward situation.

75. The Tribunal was obliged to take a realistic view of the facts and not to focus only on why the transaction happened; there is no purpose test in s 809L. What actually happened is that funds were "effectively transferred to the UK". The transaction was artificial because the Appellants had agreed to follow the alternative to a straightforward payment of an indemnity. The mere fact that the transaction was contrived is not what gives rise to the remittance, but it does suggest a need to look behind the transactions to identify what was really being done.

76. Property should be widely defined for these purposes because this is anti-avoidance legislation. Property should be defined as "any other asset which can be converted to money" in this context. See *Nokes* "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 the Act or document is intended to deal" *p105* and *Chitty on contract*; contractual rights can be property.

77. Mr Stone relied on the decision in *O'Brien v Benson* in which a contract to provide personal services was treated as an asset for CGT purposes:

“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.” p 573 Lord Russell

78. Similarly, at least before SKS has transferred payment to Miles, the rights under the Side Letter were valuable contractual rights.

79. The contractual rights created under the Side Letter are property rights, being the conditional release of the Appellants from their indemnity; the removal of IR’s debt obligations and the undertaking from Centennial that Visage would not pursue IR for the debt.

80. The *DMWSHZ* case can be distinguished because it did not consider anything other than a bi-party contract. On these facts there are two separate elements to the transaction, the flow of money (from SKS to Miles) and the release of the debt obligation are separate.

81. In this case property rights had been used in the UK. There was a clear UK connection; two UK companies had made payments under a contractual obligation governed by UK law. Without having to rely on any particular factors, payments of this nature were within the mischief at which s 809L was directed. Both the Appellants and IR had obtained a benefit in the UK as a result of the Side Letter.

82. HMRC accepted that once SKS had made its payment to Miles under the Side Letter, any property rights held by the Appellants and IR could no longer be turned to account, because their obligations had been extinguished, but before the rights in the Side Letter were triggered, the parties had contractual rights in the UK which were used in the UK.

83. There is also a relevant debt for s 809L(3)(c). The chargeable gains were used outside the UK to settle the IR debt which is a “relevant debt” because it relates to the property (the rights under the Side Letter).

Money analysis – s 809L(2)(a) Condition A

84. The funds from the loan notes are money which was used and enjoyed in the UK. It does not matter for these purposes that the money was not brought into the UK. This is clear from the drafting of 809L(6) which deals with the “importation of property”, suggesting that it is possible to use funds without importing them. In effect the money was used in the UK to settle a trade debt between two UK companies; IR and Visage and release the Appellants and IR from their contractual obligations.

85. The money is derived from the chargeable gain. If the money was used by any of the Appellants or IR, Condition B (809L(3)(a)) is satisfied. The money was used to derive a benefit for both IR and the Appellants. It was used to settle a trade debt of IR, which was governed by UK law and relieve the Appellants from their obligations under the UK law governed SPA.

Service analysis – s 809L(2)(b) Condition A

86. Counter to the Appellants’ position, Mr Stone suggests that without a specific definition of a “service” under s 809L, there is no necessary assumption that a service must be provided for consideration. A wide definition should be applied by reference to the “common and well-established meaning” of service.

87. The service provided here is the release and/or the procurement of the release of the IR debt and the release of the Appellants from liability under the Indemnity. Those services were provided by Centennial, it agreed to the release of the debt and the release of the Appellants' liability under the Indemnity.

88. The analysis which has been done (and the examples given) which apply to bi-party cases are not relevant here; the situation is different in tri-party situations. Centennial has provided a service by agreeing to release the Appellants from their indemnity and IR from its debt obligations. Both IR and the Appellants have benefited because someone else has paid money on their behalf.

Arising from the gain – s 809L(3) Condition B

89. There is a direct link between the chargeable gain arising on the Visage sale and benefits obtained in the UK by IR and the Appellants. There is a causal connection between the redeemed loan notes and the Credit Note. It is accurate to say that the IR debt was re-paid from the gain on the Visage sale.

90. It is impossible to ignore the fact that the payment made arose from the chargeable gain; under the terms of the SPA no debt was owed by the Appellants, the Appellants had received the full amount of consideration under the SPA. That consideration was used to inject funds into SKS to be transferred on to Miles, that was not a "reversal of the gain".

91. S 809(3)(b)(i) states that gains are caught if they are derived either directly or indirectly from the chargeable gain. Here the payment is derived indirectly; the use of the funds from the Visage share sale were transferred to SKS and used under the Side Letter.

92. The services provided derive from the chargeable gain, because it was brought about by the use of the capital gain to pay the proceeds from SKS to Miles.

FINDINGS OF FACT

93. On the basis of the oral and written evidence we make the following findings of fact:

- (1) It was known by August 2010 that IR would not be able to pay off its trading debts to Visage.
- (2) As a result of (1) the Indemnity at Clause 8.1 of the SPA was triggered on or before August 2010, under which the Appellants were obliged to make payment to Centennial in respect of IR's debts.
- (3) Payment under the Indemnity was the Appellants' preferred route to deal with IR's debts.
- (4) Payment under the Indemnity would not have given rise to a remittance in the UK.
- (5) Li & Fung did not want to recover the debt under the Indemnity because that would have resulted in an adjustment of the purchase price for accounting purposes. Li & Fung's aim was to ensure that the IR debt was paid in the normal course of business.
- (6) The Appellants were willing to accede to Li & Fung's wishes and avoid using the indemnity route because of the "ongoing relationship" with Li & Fung.
- (7) The Indemnity did not wipe out the debts outstanding between IR and Visage.

- (8) In the event, Centennial never made a claim under the Indemnity.
- (9) The effect of the Side Letter was to waive IR's debt obligations to Visage. IR's debts to Visage were not paid off.
- (10) The proposal to use another company to settle the debt was intended to avoid paying money into IR, which the Appellants thought would have resulted in a remittance.
- (11) In respect of the Compensatory Transaction, SKS did not actually want to buy any goods from Miles; it was not a clothing retailer and just a nominee share company in Jersey.
- (12) It was always understood that the jackets would be worth substantially less than the £6 million paid in order to give Li & Fung some financial value for the transaction.
- (13) The only purpose of including jackets in the transaction was to make it look like a genuine trading transaction.
- (14) The funds which arose from the redemption of the loan notes (arising from the SPA) were put into SKS and SKS paid that money into Miles.

DECISION AND DISCUSSION

The background to s 809L

94. S 809L was introduced in 2008 to close loopholes in the UK's remittance legislation and to ensure that, (as stated in the explanatory notes) all gains which are "in effect remitted to the UK", resulting in an individual using or enjoying the gains in the UK are subject to tax in the UK. The Appellants resisted describing the provision as an anti-avoidance provision, but in our view that is an accurate description of its purpose. The explanatory notes refer to "measure to address a range of existing loopholes, flaws and anomalies in the remittance basis".

95. On our facts, the potential tax charge arises on RS and SM who are non-domiciled UK tax resident individuals and /or through their entity IR in the UK, in connection with which RS and SM are "relevant persons" (s809M).

The reality of the transactions

96. Both parties suggested that the Tribunal should take a realistic view of the transactions, as was stressed in the *BMBF* decision (referred to in *Root2Tax*),

"Taxing statutes generally draw their life blood from real world transactions with real world economic effects" [208]

but they had very different views of what that reality should be; either the real transaction here is the payment of the Indemnity, which is the reason the transactions were undertaken, or the real transaction is the repayment of the trade debt held by IR.

97. Mr Stone spent a significant amount of time stressing the "contrived" nature of the Compensating Transaction, and we agree, as did the Appellants, that the sale of the jackets to Miles was not, and was not intended to be a commercial transaction, its purpose was a means of transferring funds intra-group in a way which both satisfied Li & Fung's accounting criteria and avoided the risk of a tax charge in the UK for the Appellants.

98. However, whether s 809L is an anti-avoidance provision or not, and in our view, it is, it does not contain a purpose test and neither did either party suggest that there was any basis on

which we should adopt a *Furniss v Dawson* approach to this transaction ignoring certain steps, or re-characterising the transaction.

99. Therefore, our starting point is to identify the transactions which were actually undertaken and to understand them by reference to the wider context including the intention of the parties.

100. The actual transactions/contracts carried out were:

- (1) Entering into the SPA and the payments made under the SPA.
- (2) The amendments to the SPA.
- (3) The Side Letter.
- (4) The payment by SKS to Miles for the jackets (the Compensatory Transaction).
- (5) The issue of the Credit Note.

101. The parties concentrated on the three contractual rights contained in the Side Letter which HMRC said gave rise to property, money or services derived from the gain and received and used in the UK by the Appellants and IR, releasing the Appellants from their indemnity obligation and IR from its debts to Visage:

- (1) The release of the Appellants from their obligations under the Indemnity.
- (2) The reduction of IR's obligation to pay its trade debts to Visage.
- (3) Centennial's undertaking that it would procure that Visage would not pursue IR for the trade debts.

Property analysis – s 809L(2)(a) Condition A

Wide or narrow definition of property?

102. We were taken to various case authorities by the parties, but none provided a definitive answer to what the definition of property should be in the context of this legislation. The authorities merely indicate that what can be treated as “property” depends on the statutory context in which that term is used.

103. We accept that this legislation is intended to close a loophole and therefore may be expected to have been widely drafted and there is nothing in the legislation to suggest that a narrow definition of property is intended to apply. The explanatory notes suggest that the drafting was intended to ensure that “Where [gains] are in effect remitted to the UK, in such a manner that the individual has the use or enjoyment of them in the UK, the individual should be liable to tax on them”. This also supports a wide interpretation of the legislation; it was intended to cover any guise in which offshore gains could be “enjoyed” in the UK.

104. This is supported by the commentary in *Melville*:

“In summary, whatever the technical meaning of the term 'property', it seems to me that the terms 'property', 'interest' and 'right' are capable of embracing a general power of appointment depending on the legislative context, for they are terms capable (as is such a general power) of embracing anything which is capable of producing value, being realised and turned into money, and a general power is capable of exactly this: it may be exercised to vest property in the appointor and it may be released for valuable

consideration. Whether the words do bear this meaning in s 3(1) of the 1984 Act must depend upon the legislative scheme and purpose of the 1984 Act”.[13]

105. We also take note of the general principle to which Mr Stone referred reflected in *Chitty* on contracts, that rights under a contract can generally be treated as property.

106. We also take these principles from the authorities to which we were referred:

(1) As suggested in *Melville*, “property, interest and right” are different legal concepts, but one can be a component of another.

(2) “Property” is represented by a bundle of rights. All property represents a “right”, but not all rights are property, as counsel put it in *O’Brien v Benson*:

“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.” p 42

(3) It is possible for a conditional contract to be an asset for CGT purposes, the obligation on the employee to pay his employer £50,000 for release from his employment contract in *O’Brien and Benson* was a payment in respect of a conditional contract (the employee’s services were provided on the condition of payment by the employer) but the contract was nevertheless treated as a capital asset of the employer.

(4) When looking at a bi-party contract relating to an underlying asset, the rights arising under the contract cannot be separated from the asset which is the subject of the contract:

“In short, when a seller and a buyer enter into a contract for the sale of land, the seller does not dispose of an asset and the buyer does not acquire an asset. The asset, which is the land, is disposed of by the seller and acquired by the buyer when completion takes place, albeit that section 28(1) will then deem the date of the transfer to be the date of the contract. It makes no difference to the analysis whether one considers the buyer’s contractual right to obtain specific performance of the Contract or the buyer’s beneficial ownership of the land. These are two sides of the same coin, and both are contingent upon the buyer’s compliance with the buyer’s own obligations. If the buyer fails to complete, there is no disposal or acquisition of the asset.[40]” *Hardy*

(5) That is not the same as the position in *Zim Properties*, in which the right to bring a claim was treated as an asset for CGT purposes, because in that case there was no underlying asset to which that right could attach.

107. We have taken these principles and applied them to the Appellants’ circumstances also bearing in mind that the intention of s 809L is to bring into the charge to tax in the UK (to use the widest and most neutral possible term) some “value” which has been brought to account in the UK.

108. It is undeniably the case that as a result of the Side Letter the legal position of three parties and their rights and obligations changed:

(1) RS and SM lost their obligation to make a payment under the Indemnity.

(2) IR obtained protection from having to make a payment of its debts to Visage.

(3) IR lost the risk of being pursued by Visage for its debts.

Do those changes of legal position give rise to property, money or services in the UK?

Conditional contractual rights; Release of the Indemnity

109. Mr Firth's resistance to treating the specific rights arising under the particular contracts in question as property was based on an analysis of the actual rights underlying the contracts which were entered into, in his view, merely being party to a contract does not necessarily give rise to rights or property; if the contract is conditional, rights do not arise until the condition is satisfied.

110. Mr Firth looked beneath the terms of the Side Letter to argue that any rights pertaining to the Appellants' release from the Indemnity under the Side Letter were conditional on payments being made by a third party. Once that payment had been made, those rights were extinguished, as were IR's debt obligations to Visage.

111. We agree with the Appellants that the most accurate analysis is to consider that at this stage the Appellants have a right to be released from the Indemnity and IR has a right to have its obligations settled by another member of the group, but that claim is conditional on their rights under the Side Letter being triggered by the proposed payment between SKS and Miles.

112. We think that the decision in *Benson v O'Brien* can be distinguished because on its facts it concerned a subsisting, on-going employment contract, which was "conditional" only in the sense that services were performed on condition of being paid, whereas in this case it is the bringing into existence of the contractual relationship itself which is conditional. We would also note that both the *Benson* and *Nokes* decisions deal with contracts for personal services which are by their nature of a different order than commercial contracts.

113. The best analogy we think for what IR has obtained is something akin to a group wide guarantee, or rights under a credit default swap written on the Appellants. Those undoubtedly represent a new set of rights, but in our view they cannot, in any "real world" sense be described as property before they are exercised, any more than a right to claim under an insurance contract is a property right before a claim is actually made.

114. For these reasons we agree with the Appellants that their rights to have their Indemnity obligations settled by a third party under the Side Letter, and IR's rights to have its debts settled by a third party, should not be treated as "property" for these purposes because of the conditional nature of those rights.

Contractual right to waiver of debt by third party

115. The next question must be whether, once the condition is satisfied and the parties' rights under the Side Letter are crystallised by the payment between SKS and Miles, either the Appellants or IR obtain something which is property rather than merely a right.

116. The rights represented by the Side Letter have now been vested as a result of the payment made between SKS and Miles. The Appellants have been relieved of their obligation to pay under the Indemnity and simultaneously, IR has a different party as its group "guarantor".

117. Mr Stone accepted that in a normal, bi-party case, no rights are created as between a debtor and creditor when a debt is paid off. However, in situations where the debt was extinguished by another means, through a third party, the analysis is different.

118. Should the bifurcation of a debt obligation in this way create a different result for tax purposes? Mr Firth was clear that it should not, but given that this is anti-avoidance legislation (despite what Mr Firth said) and that we are not taking a re-characterisation approach, in our

view we do need to consider what rights or property may or may not have been created by the actual transactions which were undertaken and cannot necessarily assume that the analysis is the same as had the proxy transaction (the Indemnity payment) been carried out.

119. On that analysis we agree with Mr Stone that the result of the addition of other third-party obligations as a means of waiving the IR debt means that some different analysis is required. The Compensatory Transaction may not have been commercial, but it was nevertheless a legally binding agreement between the parties which created rights and obligations.

120. As far as the Appellants are concerned, their obligations under the Indemnity are extinguished on payment being made through the Compensatory Transaction. By reference to the logic applied in *DMWSHZ*, our view is that this extinguishing of a debt should not be treated as giving rise to any property rights:

“As I have said, in the real world when the debt was repaid the obligation to pay was discharged; and there were no remaining creditor's rights that could have been transferred to the Issuer. I cannot see that the world of CGT compels any different conclusion” [50]

121. However, for IR we think the situation is less straightforward. It also has its debts waived as soon as the payment between SKS and Miles is made, but it also obtains an additional right; the undertaking from Centennial to procure that Visage will not enforce its debts against IR.

122. It is true that, from IR’s perspective, its commercial situation has not changed as a result of the Side Letter; it was always protected from having its debts to Visage enforced by Centennial because of the terms of the SPA and the Indemnity.

123. Looked at from that perspective, we agree with the Appellants that there should not be any different analysis whether IR’s debts were settled under the Indemnity or through the Side Letter.

124. This is the point made in the *Jones Bros* and *Root 2 Tax* FTT decisions relied on by the Appellant, with which we agree, that the form in which payments are made does not change their character:

“We also hold that the insertion of the elements which created the purported contracts for differences do not alter the nature of the payments as earnings and the grant of the contracts was no more than a process for delivery of the bonuses. In our view, the legal mechanism by which the payments were did not alter the character of the payments. The Appellants entered into contracts with the employees in respect of which it expected and intended to pay the employees at the settlement date”. [432]

125. IR has obtained no additional “value” as a result of the change in manner in which the Indemnity is to be satisfied. Its debts are merely being dealt with by a different third party.

126. However, in at least one way, IR’s legal rights have changed, because it has also obtained agreement from Centennial that it will not be pursued for its debts by Visage, what Mr Stone described as a “valuable promise”. We agree that this is at least a “right” and could potentially be “property” for the purpose of s 809L.

127. We do not consider that there can be any real dispute about these rights having been received or used in the UK by IR. IR is a UK resident, its debts were debts between two UK companies, they and the Side Letter were governed by UK law.

128. On the property question, we have come to the conclusion that IR’s rights under the Side Letter are not property because:

(1) Despite the fact that s 809L is in our view an anti - avoidance provision, the term “property” has not been given an extended meaning by the legislation and we can see no basis on which that meaning should be extended to include the kind of “rights” referred to for example in the IHT legislation. The other terms used in s 809L (“money or other property”) suggest that the focus is intended to be on tangible, realisable goods (or services) rather than intangible rights. It is worth noting that the legislation does not refer, for example, to any “benefit” or “value” which is received or used in the UK, although the explanatory notes do. In interpreting this legislation, we have relied on the suggestion in *Nokes* that we should consider the words of the statute and the mischief at which it is directed and have assumed that the explanatory notes should not be treated as significantly extending the clear words of the statute.

(2) Even if the extended interpretation of the legislation suggested by the explanatory notes is accepted, we do not think it is accurate to suggest that IR has obtained any additional value as a result of the triggering of its rights under the Side Letter; it was always protected from being pursued for its debts by the purchaser as a result of the Indemnity, it is only the manner in which that protection is provided which has changed from IR’s perspective.

(3) The capital gains legislation has recognised a wide variety of rights as assets, but that does not necessarily indicate that “property” should be equally widely defined, as made clear in the *DMWSHZ* decision. This also accords with the decision in *Hardy* that not all contractual rights should be treated as property.

(4) We accept the Appellants’ point that searching for “property” arising when the conditions of the Side Letter have been satisfied but before the IR debts have been waived is identifying “angels dancing on pinheads”. Any property rights exist only for a brief moment in time and cannot exist once the terms of the Side Letter have been activated by the payment between SKS and Miles. (See *Hardy* and *DMWSHZ* on this point)

(5) We have also taken some support from HMRC’s position in respect of the settlement of divorce agreements through payments made outside the UK. Those payments are made in a very different commercial context, but it is hard to escape the conclusion that the legal analysis underlying HMRC’s conclusions can be extrapolated to the facts in this case.

129. For these reasons we agree with the Appellants that the rights under the Side Letter are not property rights for the purposes of s 809L for either the Appellants or IR.

Service analysis – s 809L(2)(b) Condition B

Analysis of services provided

130. Mr Firth said that no service had been provided in the UK because on no basis could the release of a liability (under the Indemnity) be treated as the provision of a service. The beneficiaries in this instance were Centennial and Li & Fung; they obtained payment without triggering the Indemnity. It would give rise to a very odd analysis if a purchaser was treated as providing a service to a vendor when an indemnity was released. The fact that in this instance release from the Indemnity was procured through a third party does not create a service.

131. The Appellants’ have stuck to an analysis which suggests that the “real” transaction is a payment under the Indemnity. We do not understand there to be any disagreement between the parties that if this was in fact what had happened, no “service” would have been provided.

132. But the Appellants cannot escape the fact that this is not what actually happened; instead:
(i) SKS agreed with Miles to enter into a transaction with it for no commercial purpose to

settle the Appellants' obligations under the Indemnity and (ii) Centennial agreed to waive the debt due from IR.

133. There is no question of SKS and Miles providing any services in the UK, but in our view, we do need to decide whether Centennial's agreement to waive the debt due from IR and the Appellants' obligations under the Indemnity was the provision of a service. The Appellants' insistence that in normal circumstances a debtor does not provide a service to a creditor in paying off a debt are of no help here, because the release is not being effected by the debtor but a third party.

134. It is clear that Centennial has provided something of value to IR and the Appellants, even if in the round and looking at the transaction as a whole, the economic effect is the same as if the Indemnity had been paid by the Appellants.

135. Considering the definition of a "service" suggested by the Appellants from the *Richmond on Thames* decision "any self-employed economic activity, normally provided for remuneration" we do not think that it is stretching the meaning of "service" too far to suggest that this was some sort of financial service, in the same way as someone providing a third-party guarantee or credit protection insurance is providing a service.

136. From both the Appellants' and IR's perspective the "service" was commercial and for consideration, being the extinguishing of their obligations under the Indemnity (the Appellants) and the waiving of its debt obligations (IR). We think it is clear in this context that an agreement not to take an action or pursue a claim can be a "service".

Were services provided in the UK?

137. We then have to determine whether that service was provided in the UK; as far as IR is concerned, it is in the UK, the agreement is governed by UK law and the relevant debts are between two UK companies. It is hard to see how, if a service has been provided, it can have been provided anywhere other than in the UK; the effect of the service was certainly in the UK, it is IR's debt obligations in the UK which are waived.

138. We also note that the descriptions of services provided in the UK in HMRC's manual suggest that if a service is enjoyed in the UK, it is treated as made in the UK for these purposes (see RDRM 33130).

139. The situation for the Appellants is more complicated, they are not in the UK, but the Side Letter is governed by UK law and the SPA was governed by UK law.

140. Of the indicia suggested by HMRC to determine the place where services are provided for these purposes, in our view where the services relate to the release of a debt, the most important indicia is where the debt is located; by reference to the normal application of situs rules, the debts owed by the Appellants have a UK situs and therefore the service should be treated as made in the UK.

141. For these reasons we have concluded that the release of the obligations of both the Appellants and IR does entail providing a service in the UK under Condition B.

Does the property or service derive from the gain s 809L(3) Condition B

142. In order to give rise to a tax charge under s 809L the property or service must "derive from the income or chargeable gains". HMRC's position is that the property or services are derived from the chargeable gains generated from the Appellants' share sale.

143. For these purposes, a “chargeable gain” is defined at s 989 ITA 2007 and takes its meaning from the Taxation of Chargeable Gains Act 1992. (“TCGA 1992”)

144. A capital gain is specifically defined in the TCGA 1992, and is made up of specific elements: sale proceeds minus allowable deductions, s 15 TCGA 1992 and related sections:

“15(1) The amount of the gains accruing on the disposal of assets shall be computed in accordance with this Part.....

15(2) Every gain shall, except as otherwise expressly provided, be a chargeable gain”

145. On that premise, a chargeable gain is not the equivalent of the sale proceeds for a particular transaction, it is the result of an arithmetical application of the chargeable gains rules. The sale proceeds from a share sale are not the same thing as the chargeable gain which has been generated.

146. In the context of commercial transactions such as share sale agreements the legislation recognises that sale proceeds can alter over time, through earn out and pay back arrangements; s 48 TCGA 1992 (at least as regards ascertainable consideration) provides for claims to be made to reduce the chargeable gain. Similarly, ESCD33 allows payments made under indemnities which are part of a company sale agreement to be treated as reducing the gain on that sale.

147. The legislation at s 809L has as its starting point a “chargeable gain” and not any other sum or proceeds. In our view, the starting point must be that that gain is calculated in accordance with the CGT rules and takes account of deductions available, including in earn-out and indemnity situations such as this.

148. This is, we think, another way of expressing the Appellants’ argument that any remittance derived from the Indemnity in the UK cannot be derived from the gain arising on the Visage share sale, because a payment under the Indemnity would have reduced rather than increased this gain.

149. For this reason, we agree with the Appellants that the payments made under the Indemnity do not derive from the chargeable gain, rather they are one of the elements which produce that gain, in this instance reducing its level.

150. A mere tracing exercise of the proceeds of the Visage sale, represented by the loan notes, through SKS and on to Miles is not the same as identifying the “gain” which has been remitted to the UK. The tax charge in s 809L is not a charge on cash proceeds from a profitable transaction entering the UK; if it was, we would agree with HMRC’s analysis on this point, it is a charge on other things (property, money and services) entering the UK which derive, directly or indirectly from a gain.

151. If the test in s 809L was whether property, money or services had entered the UK which represented the proceeds of an offshore sale of assets, again, we would agree with HMRC’s analysis, but that is manifestly not the test in s 809L, which is predicated on something which is derived from a gain. The Indemnity is the opposite of that, it is a subtraction from the gain.

152. The Appellants suggested some numerical examples to prove their point; if the indemnity had been for the full value of the Visage shares, there would have been no gain at all and we accept the force of this argument.

153. The Appellants refer to the general principles of capital gains tax referred to in *Ramsay*:

“The capital gains tax was created to operate in the real world, not that of make-belief”
[182]

And we agree that adopting HMRC's approach and suggesting that funds paid in order to reduce the proceeds of a share sale should be treated as generating a taxable gain in the UK has something of Alice in Wonderland about it.

Has the form in which the Indemnity was settled changed the nature of the payment?

154. The situation is complicated here by the manner in which the payment is made. The parties agreed that had the payment been made under the Indemnity, no issue would have arisen under s809L. Can it be said that the Compensatory Agreement changed the character of the payment made?

155. The Appellants attempted to argue that the since the essence of the Compensatory Transaction was to settle the Indemnity in another form, the form in which the Indemnity was actually paid could not alter the analysis. From the Appellants' perspective, the transactions all stem from the Indemnity.

156. It is certainly the case that the Compensatory Agreement changed the legal form of the payment; from a payment under the Indemnity to a payment between two different parties and an agreement to release the debt.

157. However, in our view, in concentrating on whether property, money or services which are brought into the UK are, or are derived (directly or indirectly) from the gain, s 809L is asking us to consider not the manner of payment, but its source.

158. There was no dispute between the parties that the source of the payment was the profit generated on the Visage sale through the redemption of the loan notes. But, as we have already said, those proceeds are not the same as the "gain" on which the legislation is focused.

159. On this analysis, the process through which the proceeds passed through SKS to Miles and allowed Centennial to agree to the issue of the Credit Note by IR, does not alter the analysis of whether the property, money or services (being the release of the Indemnity) derives from the gain; it does not.

Money analysis – s 809L(2)(a)

160. Having come to this conclusion on whether the property or services are derived from the gain, we have not gone on to consider the money analysis; our conclusion would be the same, the money used in the UK (via the loan note redemption) does not derive from the gain.

CONCLUSION

161. For these reasons we have concluded that:

- (1) The rights under the Side Letter are not property used in the UK by IR and/or the Appellants.
- (2) A service has been provided in the UK to the Appellants and IR under the Side Letter through Centennial agreeing to settle the Indemnity by another means and waive IR's debts.
- (3) However, neither the property nor the service derives from the chargeable gain arising on the sale of the Visage shares under the SPA.
- (4) The Appellants' appeal is therefore allowed.

RIGHT TO APPLY FOR PERMISSION TO APPEAL

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

**RACHEL SHORT
TRIBUNAL JUDGE**

Release date: 31 AUGUST 2022