A HIGH COURT OF JUSTICE
(CHANCERY DIVISION)—19, 20, 23 AND 24 JULY AND 8 NOVEMBER 1984

Zim Properties Ltd. *v.* Proctor (H.M. Inspector of Taxes)[1]

Capital gains tax—Sum on compromise of action for negligence—
B *Whether disposal of asset—Whether sum derived from claim or from land—Whether asset acquired and market value at date of acquisition deductible—Finance Act* 1965, *s* 22.

On 12 July 1973 Zim Properties Ltd. ("Zim") contracted to sell land, which it had held as an investment, to another company for completion in one year's time. In due course the purchaser treated the contract as repudiated
C because Zim was unable to produce the conveyance to it of part of the land and was therefore unable to show good title. On 24 October 1974 Zim sued its solicitors, alleging that they had drawn the contract of sale negligently. On 23 January 1976 agreement was reached for the compromise of that action by payment to Zim by the solicitor's insurers of £69,000 in instalments of £60,000 and £9,000: those payments were duly made on 1 February 1976 and 2 April
D 1976.

On appeal by Zim against an assessment to corporation tax for its accounting period ended 31 March 1976, the Special Commissioners held that the £69,000 was a capital sum derived from an asset within s 22(3) of the Finance Act 1965, the asset not being the land but being Zim's cause of action against the solicitors or, alternatively, Zim's right to be compensated by the
E solicitors. The Commissioners also held that that asset had been acquired on 12 July 1973 and the market value of the asset at that date was therefore deductible as Zim's deemed acquisition cost. Zim appealed and the Crown cross-appealed.

Held, in the Chancery Division, dismissing Zim's appeal and the Crown's cross appeal:-

F (1) that Zim did not have a right to compensation, but had a claim against the solicitors which might or might not have succeeded, and that claim was an asset;

O'Brien v. *Benson's Hosiery (Holdings) Ltd.* 53 TC 241; [1980] AC 562 applied;

(2) that a case cannot come within paras (a)—(d) of s 22(3) Finance Act
G 1965 unless it comes within the general words of s 22(3), but those paragraphs are aids as to the interpretation of the general words;

Marren v. *Ingles* 54 TC 76; [1980] 1 WLR 983 followed. *Davenport* v. *Chilver* 57 TC 661; [1983] STC 426, doubted that point;

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[1] Reported [1985] STC 90; 129 SJ 68.

(3) the correct test as to whether a capital sum has been derived from assets is to look for the real (rather than the immediate) source of the capital sum;

O'Brien v. *Benson's Hosiery (Holdings) Ltd.* 53 TC 241; [1979] 3 WLR 572, (decision of Fox J.) followed. *Commissioners of Inland Revenue* v. *Montgomery* 49 TC 679; [1975] 2 WLR 326 explained;

(4) applying that test the £69,000 was derived from the claim, not from the land;

(5) that the claim arose on 12 July 1973;

Forster v. *Outred & Co.* [1982] 1 WLR 86 applied;

(6) that the market value of the claim on 12 July 1973 was deductible because the asset was acquired by Zim on the date of the contract of sale; it was not an asset which did not come to be owned without being acquired;

Davenport v. *Chilver* 57 TC 661; [1983] STC 426; followed on that point.

CASE

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

1. At a meeting of the Commissioners for the Special Purposes of the Income Tax Acts held on 19, 20 and 21 May 1980 Zim Properties Ltd. (hereinafter called "the Company") appealed against an assessment to corporation tax for its accounting period ended 31 March 1976 in the estimated sum of £15,000 in respect of chargeable gains arising on the alleged disposal by the Company of a chose in action.

2. Shortly stated the question for our decision was whether a sum of money received by the Company from the compromise of its High Court action against a firm of solicitors for damages for the firm's negligence while acting as the Company's solicitors in connexion with the proposed sale by the Company of properties (which negligence caused the sale to be called off) was consideration for the disposal or part disposal of an asset of the Company thus giving rise to a chargeable gain and, if so, how the gain should be computed.

3. The following authorities were cited to us: *Lysaght* v. *Edwards* (1876) 2 Ch D 499; *Glegg* v. *Bromley* [1912] 3 KB 474; *Commissioners of Inland Revenue* v. *Montgomery* 49 TC 679; [1975] Ch 266; *Raja's Commercial College* v. *Gian Singh & Co. Ltd.* [1976] STC 282; [1977] AC 312; *O'Brien* v. *Benson's Hosiery (Holdings) Ltd.* 53 TC 241; [1980] AC 562; *Davis* v. *Powell* 51 TC 492; [1977] 1 All ER 471; *Aberdeen Construction Group Ltd.* v. *Commissioners of Inland Revenue* 52 TC 281; [1978] AC 885; *Marren* v. *Ingles* 54 TC 76; [1980] 1 WLR 983; *Midland Bank Trust Co. Ltd. And Anor* v. *Hett, Stubbs & Kemp (A Firm)* [1979] Ch 384; *Stoke-on-Trent City Council* v. *Wood*

Mitchell & Co. Ltd. [1979] 2 All ER 65; *Halsbury's Laws of England, 4th Edition* Vol 6 para 86–87.

4. We the Commissioners who heard the appeal took time to consider our decision and gave it in writing on 23 December 1980.

5. A copy of our decision is appended to this Case and forms part of it. In our decision we have set out:

(a) a list of the documents which were proved or admitted before us (para 4): copies of these are available for inspection by the Court if required;

(b) the facts as agreed between the parties (para 3);

(c) the contentions of the Company (para 6);

(d) the contentions of the Inspector of Taxes (paras 7 and 8);

(e) our conclusions (para 9).

6. On 5 August 1981 both parties made a joint application to us for a Case to be stated on the points of principle for the opinion of the High Court. A copy of this application is appended hereto as a Schedule(1). Since the decision of Browne-Wilkinson J. in *Hallamshire Industrial Finance Trust Ltd.* v. *Commissioners of Inland Revenue*(2) [1979] 1 WLR 620 we believe ourselves to be justified, having determined issues raised in the Company's appeal, in acceding to the request of the parties, and we have stated and do sign this Case accordingly.

7. The question of law for the opinion of the Court is whether our decision on how the sum received by the Company from the compromise of its action for damages should be treated for corporation tax purposes was correct.

J. G. Lewis
E. Wix
} Commissioners for the Special Purposes of the Income Tax Acts

Turnstile House
94–99 High Holborn
London WC1V 6LQ
18 January 1982

Decision

1. We have before us an appeal by Zim Properties Ltd. ("the Company") against an assessment to corporation tax for its accounting period ended 31 March 1976 in the estimated sum of £15,000 in respect of chargeable gains arising on the alleged disposal by the Company of a chose in action.

2. Put shortly, the question for our decision is whether a sum of money received by the Company from the compromise of its High Court action against a firm of solicitors ("the firm") for damages for the firm's negligence

(1) Not included in the present print. (2) 53 TC 631.

while acting as the Company's solicitors in connexion with the proposed sale by the Company of properties (which negligence caused the sale to be called off) was consideration for the disposal or part disposal of an asset of the Company thus giving rise to a chargeable gain and, if so, how the gain should be computed.

3. The following facts are agreed between the parties:

(1) The Company is incorporated in England with limited liability, having as its main object the holding of property by way of investments. Its accounting period in all relevant years ended on 31 March.

(2) By a contract dated 1 September 1960 the Company acquired the properties known as 49 and 49a Faulkner Street, Manchester. Such properties were acquired by the Company and held by it at all times as an investment.

(3) In 1973, the properties were damaged as a result of fire and the Company decided that it should sell the property 49 Faulkner Street. A prospective purchaser was found for the property together with two other properties held by the Company, 51 Faulkner Street and 17 Nicholas Street, Manchester, at an aggregate price, subject to contract, of £175,000. The 3 properties are hereinafter called "the properties".

(4) The same solicitors ("the firm") who acted for the purchase of 49 and 49a Faulkner Street, were instructed to act for the Company in connexion with the proposed sale. Contracts ("the contract") were exchanged on 12 July 1973. Completion was due to take place on 12 July 1974, time to be of the essence. The date was not inserted in the contract, but is established by correspondence passing between the solicitors for the vendor and purchaser.

(5) Completion did not take place on the said date. The Company failed to show a good title to 49 Faulkner Street as required by the contract because the conveyance of 1960 conveying this property and also 49a to the Company was missing. A statutory declaration as to this was made by Mr. John Ziment, a director of the Company. As a result of this defective title, the purchasers, as they were entitled to do, treated the contract as repudiated. The purchaser commenced an action against the Company to recover the deposit which had been paid on exchange of contracts.

(6) The Company contended that this situation had arisen because of the negligence of the firm, in that the firm knew that the conveyance was missing when the draft contract was drawn and had, therefore, failed to advise the Company properly and protect the Company's position with regard to the contract. The Company sought advice as to its rights and in the result, a writ was issued against the firm on 24 October 1974. On 20 December 1974 the firm served a defence to the action.

(7) Subsequently, negotiations were entered into between the Company's solicitors (Berwin Leighton) and the solicitors (Davis, Campbell & Co.) for the insurers of the firm to explore the possibility of compromising the action.

(8) In January 1976, agreement for compromising the action was reached on the basis of a payment by the firm of a sum of £69,000 ("the sum"), including costs, payable by two instalments of £60,000 and £9,000. These payments were duly made (by cheques despatched on 4 February 1976 and 23 April 1976 respectively) and the action was withdrawn.

4. Copies of the following documents were produced before us:

(1) Contract dated 1 September 1960.

(2) The contract.

(3) Mr Ziment's statutory declaration with copy of draft conveyance bearing date 18 December 1960 exhibited thereto.

(4) Writ issued against the firm, with statement of claim.

(5) The firm's defence.

(6) Letter dated 24 November 1975 from Berwin Leighton to Davis, Campbell & Co. setting out the financial basis of the Company's claim against the firm.

(7) Bundle of telexes and letters relating to the agreement for compromising the action.

5. It was common ground between the parties that the negligence of the firm which gave rise to the damage suffered by the Company as claimed in the statement of claim was in the preparation of the contract. Nothing, apart from finding the missing conveyance, could subsequently have been done by the company to prove title. The contract was in such terms that the purchaser could not have been obliged to complete it even if a statutory declaration had been produced which evidenced that the missing conveyance had been duly executed. It also became common ground during the hearing before us that if the receipt of the sum gave rise to a chargeable gain by the Company, part of it fell to be assessed to corporation tax for the Company's accounting period ended 31 March 1976 and part of the period ended 31 March 1977.

The Company's contentions

6. Mr. A. Thornhill of Counsel appeared for the Company. He accepted that in fairness and according to common sense the source of the sum was a part disposal of the properties. The Company had been willing to accept liability on that basis—with the consequent benefit, in computing the liability, of apportionment on a time basis of the gain accruing from such of the properties as were owned by the Company before 6 April 1965. The Crown, however, was contending that there was a disposal of a chose in action (namely, the Company's cause of action against the firm for negligence or, alternatively, the Company's right to be compensated by the firm for their negligence), hereinafter called, in either alternative, "the right" for which no consideration had been given; and was not relying on any alternative derivation of the compensation. Mr Thornhill's contentions may be summarised as follows:—

(1) The right was not an asset for the purposes of s 22(1)(*). The payment received by the Company was analogous to the compensation received by an outgoing agricultural tenant of which Templeman J. had said in *Davis* v. *Powell*[1] [1977] 1 All ER 471 at page 474, "It is not derived from an asset at

(*) Unless otherwise stated, sections and schedules referred in this decision are those of the Finance Act 1965.

[1] 51 TC 492, at p 495.

all: it is simply a sum which Parliament says shall be paid for expense and loss which are unavoidably incurred after the lease has gone". In the present case the Company had a right to have its loss replaced by a sum of money. The same principle applied whether such a right was statutory or non-statutory. The Court of Appeal decision in *Marren* v. *Ingles*(1) [1979] 1 WLR 1145 was not authority to the contrary; it had not been argued in that case whether a right to a simple payment was an asset. Accordingly, the right in the present case was not an asset. If the right was an asset, the consequences would be far-reaching. Any right to recover a sum of money by way of compensation for loss or expense would give rise to a chargeable gain when the money was received. The tax recovered by a taxpayer on a repayment claim would be a capital sum derived from an asset, namely, the right to repayment. The repayment would give rise to a chargeable gain.

(2) If the right was an asset, it was not disposed of. Where the very nature of an asset is simply to yield a sum of money and no more, then when it yields the money the asset is not disposed of. If it were otherwise, it would have been unnecessary to provide by para 11(2), Sch 7 that the satisfaction of a debt should be treated as a disposal. Although the Court of Appeal appears to have assumed in *Ingles* case that the right was disposed of when payment was made, the point was not actually argued before it. Mr. Thornhill also claimed some support from the provisions of para 11, Sch 19, Finance Act 1969. These were clearly intended to enable the components of compensation for the compulsory acquisition of land to be attributed to their proper sources instead of all being treated as consideration for the disposal of the land itself. If the Crown's arguments were well founded, that part of the compensation which was attributable to removal expenses would clearly be brought into charge under s. 22(3) instead of being treated as exempt as the provisions seemed to intend.

(3) Whether or not the right was an asset and whether or not it was disposed of, it was itself a capital sum derived either from the properties or from the contract between the company and the firm. While the right could not be assigned, it was possible to assign its proceeds or otherwise turn it to account. Section 23(9) defined "capital sum" as "any money or money's worth...". The right was money's worth and was thus a capital sum. As such, it derived from the properties or, if not from them, from the contract (the company's rights under which were, by analogy with *O'Brien* v. *Benson's Hosiery (Holdings) Ltd.*(2), assets). The right had accrued on 12 July 1973 when the firm had negligently allowed the company to sign the contract and the damages, on a once for all basis, had to be related back to that date. Section 45(5), which provides that in the case of a disposal within (*a*), (*b*), (*c*) or (*d*) of s 22(3) the time of the disposal shall be the time when the capital sum is received, does not apply to disposals within the general wording of that subsection. Accordingly any chargeable gain to the company fell to be taken into account in the year 1973–74 and the assessment under appeal should be discharged.

(4) If the right was an asset and was disposed of, it had been acquired within the meaning of s 22(4) (*a*), "otherwise than by way of a bargain made at arm's length", with the result that it must be deemed to have been acquired (for the purposes of computation under para 4(1) (*a*), Sch 6) for a consideration equal to its market value on the day on which it was acquired. For this purpose but not for any other purpose the Crown's contention that

(1) 54 TC 76. (2) 53 TC 241.

the right arose on 12 July 1974 (the date fixed by the contract for completion of the sale of the properties) was accepted. By that date the value of the properties had greatly depreciated and the value of the right was high—possibly almost equal to the sum.(*) Where a right came into existence, whether by operation of law or otherwise, on a specific date it was no misuse of words to say that it had been "acquired" on that date. The reference in s 22(1) (*c*) to "property... coming to be owned without being acquired" must, it was true, be given some meaning but the wording of s 22(1) (*c*) as a whole suggested that it meant an asset which did not come to be owned at any particular point of time. Here the right must have accrued to the company at a particular point of time. The right had not come into existence by way of a bargain made at arm's length because what the company acquired at arm's length were the services of the firm, not the right to sue them for negligence. The relevant wording of s 22(4) (*a*) was apt to cover any means of acquisition whatsoever except a bargain at arm's length. Also, the Crown's argument that the section could not apply to circumstances in which consideration could not pass (as on the purported assignment of a right of action) involved reading words into the section that were not there and was misconceived. If a case fell within the description in (*a*) of subs (4) then there was deemed to be consideration. But in any case it was wrong to give the word "consideration" as it was used in the subsection the meaning that it had in law of contract. It was used in a much wider sense. It could include a loss or detriment. Here, the company had suffered a loss as a consequence of which it acquired the right. So this was a case where consideration could have passed.

(5) The right was an asset but the sum was properly derived from the properties thus giving rise to a part disposal of them. The contention was put in two ways to allow for the two possibilities either (a) that a valid contract for the sale of land gave rise to a disposal of the land or alternatively (b) that the disposal of the land only occurred on completion of the contract but was then related back to the date of a contract by virtue of para 10 of Sch 10 to the Finance Act 1971. By valid contract of sale was meant a contract under which *inter alia* the vendor could compel the purchaser to accept title: see *Lysaght* v. *Edwards* (1876) 2 Ch D 499 at the top of page 507. It was common ground that the company could not have compelled the purchaser to accept its title (although the purchaser could have accepted the title the company could offer and have compelled the company to complete) and that for this reason the contract was not a valid contract in the sense used by Jessel M. R. in the passage referred to in *Lysaght* v. *Edwards*. If a contract for the sale of land did give rise to a disposal of the land, then on the making of the contract the owner disposed of the land and acquired a right to payment of the purchase price conditional upon his being able to make title on completion. The right to the purchase price was a debt the cost of which was the value of the land which the owner had disposed of in return. The company did not dispose of the properties under the contract it made and did not acquire a fully enforceable right to a purchase price. The sum compensated the company for this failure to acquire a fully enforceable right to the purchase price. It derived from the properties just as much as the purchase price would have derived from the properties had the company ever been entitled to receive it or just as much as a sum received by the company for an assignment of its right to receive the

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([1]) 53 TC 241.

(*) The question of the value of the right was not argued before us but was left over, by arrangement between the parties, for argument if it should become material as a result of our decision in principle—both parties agreeing that it could, if necessary take place before a single Commissioner.

purchase price under a fully enforceable contract of sale. The company derived the sum from the properties within the meaning of the general introductory words to s 22(3). None of the particular instances in subs (3) were relied on. The company's right of action against the firm was not an intervening asset from which the sum had to be derived following *Commissioners of Inland Revenue* v. *Montgomery* 49 TC 679. Section 22(3) (*a*) was framed on the assumption that rights of action were ignored. They were simply the mechanism for providing compensation. Alternatively, a contract for the sale of land did not give rise to a disposal of the land. The disposal only occured on completion. Nevertheless, upon the making of a valid contract of sale, the owner's rights over the land changed. He became a trustee for the purchaser subject to the purchaser's obligation to pay the price on completion. The company never obtained a right to compel payment of the purchase price. The sum compensated it for its failure to receive those rights. The sum derived from the properties just as much as the purchase price would have had it ever been received. Referring to possible objections to this contention, Mr. Thornhill argued:—

(i) It did not confuse what damages were for with the measure of their calculation. Support for the view that one must look at compensation and see what it was received for could be found in the Privy Council decision (albeit on an income tax and not on a capital gains tax point) in *Raja's Commercial College* v. *Gian Singh & Co. Ltd.*(1) [1976] STC 282 and in the speech of Lord Wilberforce (with which Lord Fraser had agreed) in *Aberdeen Construction Group Ltd.* v. *Commissioners of Inland Revenue*(2) [1978] AC 885.

(ii) Properly understood *Montgomery's* case did not prevent damages from being regarded as sums derived from an asset. This appeared from the interpretation put on that decision by Lord Russell in *O'Brien* v. *Benson's Hosiery (Holdings)*(3) [1980] AC 562 also by Fox J. at first instance in the same case [1977] Ch 378 and by Slade J. in *Ingles'*(4) case.

(iii) It was immaterial that, if his arguments were correct, damages for breach of contract might be treated differently for capital gains tax purposes according to whether or not an asset had been specifically appropriated to a contract. The two cases were simply different.

Summary

Summarising the inter-relationship of his contentions Mr. Thornhill pointed out that the Crown had not relied in the alternative on any contention that the sum was properly derived from the properties thus giving rise to a part disposal of them. He argued therefore that:— (i) if we accepted any of contentions 1, 2 or 3, the assessment should be discharged but if we rejected all of them, then (ii) if we accepted contention 4, the appeal should be adjourned for agreement of figures on the appropriate basis but if we rejected that contention also, then (iii) if we accepted contention 5, the appeal should be adjourned for agreement of figures on the appropriate bases.

The Crown's contentions

7. The Crown was represented by Mr. P. Ridd of the Office of the Solicitor of Inland Revenue. His formal contentions were as follows:—

(1) [1977] AC 312. (2) 52 TC 281. (3) 53 TC 241. (4) 54 TC 76.

A (1) The company's cause of action against the firm for negligence was a chose in action. [In amplification, it was submitted that, as the claim was compromised, negligence was never admitted and the sum paid by the firm could not therefore properly be categorised as "compensation".] Alternatively, the company's right to be compensated by the firm for their negligence was a chose in action.

B (2) All choses in action (being incorporeal property) are forms of property and, therefore, assets within s 22(1). Alternatively, the language of the statutory provisions does not justify any restricted view of the word "asset" such as to exclude the particular chose in action.

(3) The sum paid in settlement of the action was a capital sum derived from the said chose in action, so that there was a disposal of an asset within the C general words of s 22(3).

(4) The chose in action came to be owned without being acquired within the meaning of s 22(1) (*c*): the question of consideration for the acquisition does not therefore arise. Alternatively, if the said chose in action was acquired, no consideration was given for the acquisition within para 4(1) (*a*), Sch 6: and s 22(4) (*a*) does not apply, in particular because it is not applicable to D circumstances in which consideration cannot pass, and, in the alternative, because the said chose in action was acquired under a bargain made at arm's length.

8. (1) As regards the company's first and second contentions, Mr. Ridd contended that *Davis* v. *Powell*[1] decided only that the statutory compensation did not arise from the tenancy. One factor which may have influenced the E decision was that the compensation was in the nature of reimbursement of expenditure—contrast the present case. It had not been argued that the statutory right was an asset or that the true asset was the tenancy and statutory right rolled into one. The judge suggested contractually agreed compensation would be taxable—he did not have in mind any general principle that compensation cannot be taxable. While it had not been argued in *Ingles'*[2] F case whether a claim to a sum of money was an asset, it appeared from the remarks of Slade J. (at page 1139) that he thought that it was. Similarly in *Marson* v. *Marriage* 54 TC 59 the point was not argued but Fox J. had had no difficulty in treating it as an asset. But, however that might be, Mr. Ridd relied mainly on the statute itself: s 22(1) (*a*) expressly defined assets as including "debts". When the action was compromised and the sum received there was a G disposition within s 22(3): that too followed from *Ingles'* case.

(2) As regards the company's third contention, Mr. Ridd contended:

(a) The right was not a capital sum. *Glegg* v. *Bromley* [1912] 3 KB 474 made it clear that what could be assigned were the fruits of an action, described as future property. The right was not existing property capable of being turned into money.

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(1) 51 TC 492. (2) 54 TC 76; [1979] 1 WLR 1131.

(b) The loss did not accrue on 12 July 1973; at that date it was not certain that any loss would accrue. A

(c) Whether or not claims had to be related back to the date when the loss accrued, it was clear from the words in s 22(3) "notwithstanding that no asset is acquired by the person paying the capital sum" that disposal takes place at the time when the sum is paid or the money's worth handed over.

(d) The firm's obligation to pay damages was a secondary obligation arising out of their contract with the company. Thus the right was not a capital sum derived from the contract but was the contractual obligation itself. The right is the asset and is not the capital sum derived from it. It would be unjust in many cases if the tax were exigible at a time when a right to damages had accrued but no funds to pay the tax had been received. B

(3) As regards the company's fourth contention Mr. Ridd elaborated his specific contentions in para 7(4) above. The chose in action was not "acquired", it was conferred by law. Copyright was another example of an asset which was conferred by law and therefore not "acquired". If, however, the chose was acquired the case still fell outside s 22(4) (*a*) because that provision could only apply in circumstances where consideration was capable of passing. That followed from reading s 22(4) (*a*) in conjunction with para 4(1) (*a*), Sch 6. If there cannot be actual consideration, then there is no slot in which to place market value. In the present case when the claim came into being it was not susceptible to passing for a consideration. There was no bargain between the parties at that date. Consideration could not pass, so that there was no room to substitute market value for actual consideration. The word "consideration" should be given its ordinary contractual meaning and there was no warrant for giving it an extended meaning that would include the damage suffered by the company. As regards the Crown's alternative argument that the chose in action was acquired under a bargain made at arm's length, Mr. Ridd maintained that this was because its source was the arm's length contract between the company and the firm, whether the firm's obligation was viewed in terms of the law of contract or in terms of the law of tort. C D E F

(4) As regards the company's fifth contention Mr. Ridd contended that the sum was not derived from the properties, which were a separate and distinct asset and which after payment of the sum were unchanged and were still owned by the company. The damages received were for loss of the contract and the fact that in measuring the damages depreciation in value of the properties might have been taken into account was irrelevant. *Montgomery's*[1] case was clear authority for prohibiting the company from tracing the derivation of the sum through, successively, other assets—the right of action, the rights which the action asserted, the contract between the company and the firm (the benefit of which was also a chose in action)—and at last to the properties. Section 27(8), which declared that "sums obtained by way of compensation or damages for any wrong or injury suffered by an individual in his person or in his profession or vocation are not chargeable gains", showed that Parliament considered that without that provision there would be a disposal of a right of action or a right to compensation—as there could be G H

(1) 49 TC 679.

A nothing else which could be disposed of from which capital sums could be derived. Damages for breach of contract of sale of an unappropriated asset were not different in principle from damages for breach of contract of sale of an appropriated asset. In either case it was compensation for the loss of the bargain and whether or not there was an underlying asset was irrelevant.

Summary

B The result for which the Crown contended was that £60,000 was a capital sum derived from assets within s 22(3) and that, subject to deductions for the incidental costs of the disposal, no deduction fell to be made in the computation by virtue of para 4(1) (*a*), Sch 6, and that the appeal should be adjourned for agreement of figures because another matter remained unresolved.

C Conclusion

9. We found the issues in this appeal elusive and difficult. Having considered them as best we can, our conclusions are as follows:

(1) As regards Mr. Thornhill's first contention and Mr. Ridd's first and second contentions, we think that the right was a chose in action which falls within the wide definition of "assets" in s 22(1). We cannot accept that any D analogy between the payment received by the company and the compensation received by an outgoing agricultural tenant is sufficiently close to justify the contrary view. We are reinforced in our opinion by several cases in which the courts (although the point was not argued before them) have assumed that a claim to a sum of money was an asset. We recognise that a universal application of the principle we have adopted may in other cases have E consequences that might be thought surprising but we do not think that this should deter us from reaching a decision which we think that the wording of the Finance Act 1965 requires.

(2) On Mr. Thornhill's second contention and Mr. Ridd's third contention, we think that the sum was a capital sum derived from the right within the meaning of the general words of s 22(3) read in their ordinary sense and that F payment of the sum was a disposal of the right. We find support for this in the Court of Appeal's assumption in *Ingles'*[1] case that extinguishment of liability by means of payment was a disposal. On appeal to the House of Lords, whose decision was published after the date of our hearing of the company's appeal, a similar assumption was made by Lord Wilberforce (with whose speech Lord Dilhorne and Lord Salmon agreed) and by Lord Fraser of Tullybelton (with G whose speech Lord Russell of Killowen agreed).

(3) We take next Mr. Thornhill's fifth contention—that the sum was properly derived from the properties. As he presented the argument, it had intellectual attractions; moreover, if right, it would result in a basis of charge to tax that many might regard as just and reasonable. We have, however, to look at the question in the light of *Montgomery's*[2] case, where Walton J. H (page 686) held that the derivation of assets could not be traced back in the manner of an abstract of title and that the question to be asked was, "From what asset... was the capital sum...derived?".

We are bound to apply this principle which remains unaffected by the House of Lords' disapproval, in *Ingles'* case, of the alternative reason which

(1) 54 TC 76. (2) 49 TC 679.

Walton J. gave for his decision in *Montgomery's*[1] case—that s 22(3) did not apply where "an asset is acquired by the person paying the capital sum". In applying the principle, we must ask from what asset any capital sum is derived. In some cases this may be as difficult to discover as it was to find the source of the Nile—and as controversial; but we have no doubt, as we have already held in sub-para (2) above, that in the present case the sum flows directly from the right and that it would be wrong in the circumstances to seek a more remote derivation. Whether the right itself was derivative is another question which we consider in sub-para (4) below.

(4) On Mr. Thornhill's third contention and Mr. Ridd's rebuttal (see para 8(2) above), we note that for the purposes of s 22 "capital sum" is defined as "any money or money's worth". While we accept Mr. Ridd's contention that the right itself was not assignable, it seems to us that the opinions expressed in the Court of Appeal in *Glegg* v. *Bromley*[2] (in particular by Fletcher Moulton L. J. at page 489 and Parker J. at pages 489–90) give more support to Mr. Thornhill than to Mr. Ridd. In our view the chose in action which was the right was property in the sense that a valid assignment could be made of its fruits or it could otherwise be turned to account. We regard it as money's worth and therefore a capital sum within the meaning of that phrase in subs (9). Although this capital sum (the right) would not have arisen but for the company's abortive attempt to sell the properties and was in that sense derived from them, we think in view of *Montgomery's* case and *O'Brien* v. *Benson's Hosiery (Holdings) Ltd.*[3] that for the purposes of s 22(3) we must regard the asset from which it was derived, not as the properties, but as the company's rights under its contract for services with the firm and as having arisen on 12 July 1973 when the firm breached its obligations by allowing the company to enter into the contract which could not be completed unless the missing conveyance were to be found.

(5) Our reaching these conclusions does not, however, enable us to discharge the assessment as Mr. Thornhill asks. We confess that we do not entirely follow his argument as regards the relevance of s 45(5) and the relation back of damages. It seems to us that the position is as follows:—

(i) The payment of £60,000 of the sum on 4 February 1976 was a part disposal of the right in the company's accounting period ended 31 March 1976.

(ii) The right arose on 12 July 1973, was a capital sum received by the company on that day was derived from the company's rights under its contract with the firm.

(iii) That any chargeable gain which may have arisen on acquisition of the right may be out of date for assessment does not appear to affect the acquisition cost of the right for the purpose of the computation of any chargeable gain arising on the receipt of the £60,000.

(iv) For the purpose of computing the acquisition cost of the right we accept Mr. Thornhill's fourth contention (other than the argument that the right arose in 1974—we have already held that it arose in 1973). In other words we hold that the right was acquired "otherwise than by way of a bargain at arm's length" and must therefore be deemed to have been acquired for a

(1) 49 TC 679. (2) [1912] 3 KB 474. (3) 53 TC 241.

consideration equal to its market value on the day on which it was acquired. There was no argument before us on what that value was.

(v) In the light of the foregoing it is not necessary for us to deal further with Mr. Thornhill's fourth contention.

6. The appeal fails in principle and we adjourn proceedings for agreement of figures.

J. G. Lewis
E. Wix
} Commissioners for the Special Purposes of the Income Tax Acts

Turnstile House
94–99 High Holborn
London WC1V 6LQ
23 December 1980

The case was heard in the Chancery Division before Warner J. on 19, 20, 23 and 24 July 1984 when judgment was reserved. On 8 November 1984 judgment was given dismissing Zim's appeal and the Crown's Cross appeal.

A. Thornhill for the Company.

Robert Carnwath for the Crown.

The following cases were cited in argument in addition to the cases referred to in the judgment:—*W.T. Ramsay Ltd.* v. *Commissioners of Inland Revenue* 54 TC 101; [1982] AC 300; In Re *Callbran* [1956] Ch 250; *Curtis* v. *Wilcox* [1948] 2KB 474

Warner J:—This case has come before me by way of an appeal and a cross-appeal against the decision of the Special Commissioners on an appeal to them by Zim Properties Ltd. (which I shall call "Zim") against an assessment to corporation tax for its accounting period ended 31 March 1976. The case is actually about the proper treatment, under the legislation relating to capital gains tax, of a sum of £60,000 received by Zim on 4 February 1976, in the following circumstances.

In 1960 Zim bought, as investments, properties in Manchester known as Nos. 49 and 49A Faulkner Street. In 1973 those properties were damaged by fire and Zim decided to sell No. 49 together with two other properties in Manchester that it also held as investments. They were No. 51 Faulkner Street and No. 17 Nicholas Street. On 12 July 1973, Zim entered into a contract for the sale of those three properties to a company called Courtdeals Ltd. The price for the three properties was £175,000, and it was not apportioned between them. In correspondence between the solicitors acting for Zim, who were Austin & Co., of Leeds, and the solicitors acting for Courtdeals Ltd., whose identity does not matter, it was agreed that completion should take place on 12 July 1974, and that, in that respect, time should be of the essence

of the contract. Completion did not, however, take place on that date because Zim had lost the 1960 conveyance of No. 49 Faulkner Street to itself, and so was unable to show a good title to that property. Courtdeals Ltd., as it was entitled to do, refused to complete the purchase, and it successfully sued Zim for the return of the deposit that it had paid on the exchange of contracts.

On 24 October 1974, Zim issued in the Queen's Bench Division a writ against Austin & Co. claiming damages for negligence. On the following day a statement of claim was served on Zim's behalf particularising that claim. On 20 December 1974, a Defence was served on behalf of Austin & Co., or more exactly on behalf of their insurers.

On those pleadings it was, in substance, common ground that Austin & Co. knew, when they drafted the contract of 12 July 1973, that Zim had lost the conveyance of 1960. Essentially Zim's claim was based on an allegation that, that being so, Austin & Co. ought to have included in the contract a provision to take account of that fact. The crucial paragraph in the statement of claim was in these terms:

> "The Defendants failed to advise the Plaintiffs that the loss of the said conveyance would create difficulties in proving title to 49 Faulkner Street and that provision should be made in the said contract for: (i) acceptance by Courtdeals Limited of secondary evidence of the said conveyance; and/or (ii) provision for adequate indemnity to Courtdeals Limited by way of insurance or otherwise in respect of the inability to produce the said conveyance; and/or (iii) acceptance of a reconstituted title to 49 Faulkner Street by Courtdeals Limited."

The statement of claim contained additional allegations of negligence in these terms:

> "(d) The Defendants failed to advise the Plaintiffs to obtain and/or the Defendants failed to obtain on behalf of the Plaintiffs confirmation from the original vendors to the Plaintiffs of the said conveyance in sufficient time to complete by the said agreed date or at all. (e) The Defendants advised the Plaintiffs to enter into a contract whereby the date of completion was expressly agreed to be of the essence of the contract notwithstanding the said difficulties concerning proof of title to 49 Faulkner Street. (f) The Defendants failed to produce or obtain any or any evidence satisfactory to Courtdeals Limited and/or their legal advisers and/or in law that the Plaintiffs had a good and marketable title to 49 Faulkner Street in sufficient time to enable completion to take place by the said agreed date or at all. (g) The Defendants failed to produce any or any sufficient Abstract of Title pursuant to the provisions of the said contract of sale to Courtdeals Limited and/or their legal advisers and/or in law in sufficient time to enable completion to take place by the said agreed date or at all. (h) The Defendants failed to answer requisitions made by or on behalf of Courtdeals Limited to their satisfaction or at all in sufficient time to enable completion to take place by the said agreed date or at all."

By the statement of claim Zim claimed damages amounting to £104,138.46, made up of: (a) A sum of £100,000, which, so it was alleged on behalf of Zim, represented the difference between the sale price of £175,000 and the value of the properties in October 1974; and (b) A sum of £4,138.46, which, so it was alleged on behalf of Zim, represented interest on a loan that Zim had to obtain from a bank in consequence of the unavailability of the proceeds of sale of the properties for use in its business.

A The Defence, essentially, was to the effect that, before the exchange of contracts, Mr. Hill, a partner in Austin & Co., and Mr. John Ziment, a director of Zim, had discussed orally the problem presented by the absence of the conveyance of 1960 and possible methods of dealing with it, including the insertion in the draft contract of one or more of the terms suggested in the statement of claim, but that Mr. Ziment—and I quote from the Defence—

B "orally (i) stated that he had found the intended purchasers to be 'very difficult from the outset' and feared that any further complications might cause them to withdraw altogether from the transaction; (ii) repeatedly stressed the importance which he, Mr. John Ziment, attached to an early exchange of contracts; and (iii) expressly instructed Mr. Hill to proceed to exchange of contracts without inserting into the draft contract any C reference to and without otherwise drawing the attention of the intended purchasers to the absence of the said deed . . . with which instructions the Defendants duly complied".

There followed in the Defence a paragraph saying:

"If and in so far as may be necessary the Defendants will contend that had any reference to the said deed. . . been inserted into the draft D contract or been otherwise drawn to the attention of Courtdeals Limited, Courtdeals Limited would not have entered into the said Contract."

There were then two paragraphs dealing with the reasons why the date for completion of the contract was expressly made of the essence of it, and a paragraph dealing shortly with the additional allegations of negligence in the statement of claim which I have read. This paragraph was so worded as E manifestly to invite a request for further and better particulars. No such request was, however, made, from which it may be inferred that the parties attached little importance to those additional allegations. Indeed, it was common ground before the Special Commissioners that the real claim in the statement of claim was for negligence in the preparation of the contract and that, once contracts had been exchanged, nothing, apart from finding the F missing conveyance, could have been done to enable Zim to make title to No. 49 in such a way as to be in a position to compel Courtdeals Ltd. to complete.

After the close of pleadings negotiations were entered into between the solicitors then acting for Zim and those acting for Austin & Co.'s insurers. On 24 November 1975, the former, in response to an offer of £35,000 made by the latter, wrote a "Without Prejudice" letter setting out a calculation of what G they described as "the full extent of the loss suffered by our client". That calculation started with the purchase price of £175,000. To that were added a sum of £10,481 in respect of interest (less tax) for the period from 12 July 1974, to 30 November 1975; a sum of £1,048 in respect of interest (less tax) on Courtdeals Ltd.'s deposit for the same period; a sum of £2,000 in respect of the costs of the action; and another sum of £2,000 in respect of the cost of H Courtdeals Ltd.'s action, making a total of £190,529. From that total were deducted a sum of £103,000, described as "Present Site Valuation"; and a sum of £3,900, described as "Approximate value of rents received from June Quarter 1974 to September Quarter 1975 (incl.)". The result was a figure of £83,629.

The letter went on:

I "You will appreciate that this total takes no account of the financial loss suffered by our client as a result of your clients' representations to Mr. Ziment and his Bank that the sale would be completed and that it

would be safe to borrow money to purchase another property in anticipation of a successful completion. In view of the estimated total loss of £83,629 suffered by our Client, we do not consider that we are able to recommend to our client acceptance of your offer in the sum of £35,000."

Following further negotiations, agreement was reached on 23 January 1976, for the compromise of the action by the payment to Zim by Austin & Co.'s insurers of the sum of £69,000, as to £60,000 within 14 days and as to the balance of £9,000 within three months. Those payments were duly made on 4 February 1976, and 2 April 1976, respectively. The action was then withdrawn.

It is common ground that the £60,000 was a "capital sum" within the meaning of that expression in the legislation relating to capital gains tax. The first and main question at issue in the present proceedings is whether that capital sum was "derived" from any and, if so, what "asset" of Zim within the meaning of those expressions in that legislation.

The Crown's primary contention (which found favour with the Special Commissioners) is that Zim's right of action against Austin & Co. for negligence and breach of contract was an "asset" of Zim within the meaning of that term in the legislation and that it was the asset from which the £60,000 was "derived". Alternatively the Crown contends that the £60,000 was "derived" from the "asset" consisting in Zim's rights under its contract with Austin & Co. On either view, subject to some subsidiary questions which I leave aside for the moment, tax is payable on the whole of the £60,000 as, in effect, pure capital gain.

Zim's primary contention (which the Special Commissioners rejected) is that the £60,000 was "derived" from the three properties comprised in the contract of sale. On that view Zim is entitled to a deduction, in the computation of its capital gain, for its expenditure on the acquisition of the properties, and is also, in respect of No. 49 Faulkner Street, entitled to the benefit of an apportionment under para 24 of Sch 6 to the Finance Act 1965, so as to render chargeable to tax only that part of the gain deemed to be attributable to the period after 5 April 1965. Zim's alternative contention is that there was no "asset" of Zim, within the meaning of that term in the legislation, from which the £60,000 can be said to have been "derived". On that view, no tax at all is payable.

The statutory provisions that are directly in point on that main question are subs (1) of s 19 and subs (1), (2) and (3) of s 22 of the Finance Act 1965. Subsection (1) of s 19 was the general charging provision in force at the material time. It was in these terms:

> "Tax shall be charged in accordance with this Act in respect of capital gains, that is to say chargeable gains computed in accordance with this Act and accruing to a person on the disposal of assets." The first three subsections of s 22 were in these terms: "(1) All forms of property shall be assets for the purposes of this Part of this Act, whether situated in the United Kingdom or not, including—(a) options, debts and incorporeal property generally, and (b) any currency other than sterling, and (c) any form of property created by the person disposing of it, or otherwise coming to be owned without being acquired. (2) For the purposes of this Part of this Act—(a) references to a disposal of an asset include, except where the context otherwise requires, references to a part disposal of an asset, and (b) there is a part disposal of an asset where an interest or right

A in or over the asset is created by the disposal, as well as where it subsists before the disposal, and generally, there is a part disposal of an asset where, on a person making a disposal, any description of property derived from the asset remains undisposed of. (3) Subject to subsection (6) of this section, and to the exceptions in this Part of this Act, there is for the purposes of this Part of this Act a disposal of assets by their owner where
B any capital sum is derived from assets notwithstanding that no asset is acquired by the person paying the capital sum, and this subsection applies in particular to—(a) capital sums received by way of compensation for any kind of damage or injury to assets or for the loss, destruction or dissipation of assets or for any depreciation or risk or depreciation of an asset, (b) capital sums received under a policy of insurance of the risk of
C any kind of damage or injury to, or the loss or depreciation of, assets, (c) capital sums received in return for forfeiture or surrender of rights, or for refraining from exercising rights, and (d) capital sums received as consideration for use or exploitation of assets."

Subsection (6) of s 22, which is mentioned in subs (3), is not in point.

One way in which Mr.Thornhill, on behalf of Zim, attacked the decision
D of the Special Commissioners to the effect that the £60,000 was "derived" from Zim's right of action against Austin & Co., was this. (He did not put it first, but I think that logically I should deal with it first.) He pointed out that, on the pleadings in the action between Zim and Austin & Co., the outcome of the trial might have depended on whether the Court preferred the evidence of Mr. John Ziment or that of Mr. Hill. Alternatively it might have depended on
E whether the Court found as a fact that, if Courtdeals Ltd. had been told that the 1960 conveyance was missing, Courtdeals Ltd. would nonetheless have entered into the contract or would have declined to do so. In other words, what the Crown referred to as Zim's "right of action" against Austin & Co. was in reality no more than a claim which might or might not succeed. Such a claim, unlike an undoubted right, was not a form of property and therefore,
F having regard to the terms of s 22(1) of the Finance Act 1965, was not an "asset" for capital gains tax purposes.

Mr. Carnwath, for the Crown, submitted that such a claim was a form of property. Alternatively he submitted that, if it was not a form of property, it was nonetheless an "asset" for capital gains tax purposes. He urged on me the undesirability of reaching a conclusion in this case that would make it
G necessary, in any future like case, for the appellate Commissioners to decide, albeit on a balance of probabilities, whether a civil action that had in fact been compromised would or would not, if fought out, have succeeded.

I have, after considerable hesitation, come to the conclusion that Mr. Carnwath is entitled to succeed on that point. He is entitled to do so, I think, not on the strength of the various authorities to which he referred me on the
H scope of the concept of a "chose in action" in English law, or on the strength of what it is desirable or undesirable that appellate Commissioners should have to decide, but on the strength of the decision of the House of Lords in *O'Brien* v. *Benson's Hosiery (Holdings) Ltd.*(1) 53 TC 241. True the contractual rights that were there held to constitute an asset for capital gains

(1) [1980] AC 562.

tax purposes were undisputed. They were not a mere claim. But that formed no part of the *ratio decidendi* of the case. The *ratio decidendi* was that those rights were an asset for capital gains tax purposes because they were something that could be turned to account. That is apparent if one contrasts the reasoning of the Court of Appeal in that case with the reasoning of the House of Lords.

The essence of the reasoning of the Court of Appeal is to be found in a passage in its judgment, delivered by Buckley L.J., that begins at page 257 of the report, where he said this(1):

> "The question to which we have to address our minds is whether a chargeable gain has in the circumstances accrued to the Company on the disposal, actual or notional, of any asset. So the case turns primarily upon the question whether the Company has, or must be treated as having, disposed of an asset. The Company says that their rights under the service agreement were not an asset or assets for the relevant purposes. The Crown contends that those rights fall within the term 'incorporeal property generally' in s 22(1)(a) and that they are assets for the relevant purposes. At first impression one would not, we think, consider that an employer's rights to personal services under a contract of employment were appropriately descibed as 'property'."

Buckley L.J. then referred to *Nokes* v. *Doncaster Amalgamated Collieries, Ltd.* [1940] AC 1014, and cited some passages from the speeches in that case. He continued (at page 258):

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

Thus the essence of the reasoning of the Court of Appeal was that, having regard to the words of s 22(1) of the Finance Act 1965, an "asset" for the purposes of capital gains tax must consist of some form of property, and that, since the rights of an employer under a contract of employment were not assignable, they were not "property".

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(1) 53 TC 241.

In the House of Lords that reasoning was rejected in a speech by Lord Russell of Killowen with which the other Law Lords expressed their agreement. The key passage in Lord Russell's speech starts at the foot of page 269 of the report, and is as follows(1):

> "The battle ground lies in s 22(3)(c) of the 1965 Act. The question is whether (notwithstanding that as a result of the 1970 agreement Behar acquired no asset by paying £50,000) the capital sum was received by the taxpayer in return for surrender of its rights under the service agreement or for refraining from exercising its rights under the service agreement. My Lords, at first glance I find it difficult to see why the rights of the taxpayer under the contract of service was not an 'asset' of the taxpayer within the unrestricted language of ss 19 and 22 of the Statute. The Court of Appeal... in deciding this case in favour of the taxpayer (reversing Fox J.)... relied greatly on the reasons for the decision of this House in *Nokes* v. *Doncaster Amalgamated Collieries Ltd.*(2)... The question there was whether on the occasion of the approval by the court under the Companies Act of a scheme for the amalgamation of companies an employee's contract of service was automatically transferred to the new entity, the statutory language stating the relevant effect, on existing contracts and rights, of the order approving the amalgamation being of a width amply sufficient, *prima facie*, to embrace contracts of employment. This House however declined, despite the width of that language, to include within it contracts of employment: the reason was that to do so would breach a fundamental principle of the law that such contracts were not *assignable*, and that something more particular was needed than mere generality of language (however widely expressed) if such a breach of principle was to be accepted as being intended by Parliament. My Lords, I do not accept that that decision affords guidance to a decision under the capital gains tax legislation which deals not merely with assignments but with disposals. To treat the events which took place in the instant case as coming within the wide generality of the language of ss 19 and 22—and in particular of s 22(3)(c)—cannot be regarded as breaching any fundamental principle of the law that a contract of personal service is not assignable. Similarly I derive no guidance from the cases in bankruptcy law of *Bailey* v. *Thurston & Co., Ltd.*(3)... which decided that rights under a contract of personal service did not vest in the trustee in bankruptcy: and *Sutton* v. *Dorf*(4)... which similarly decided in the case of a statutory tenancy. It was contended for the taxpayer that the rights of an employer under a contract of service were not 'property' nor an 'asset' of the employer, because they cannot be turned to account by transfer or assignment to another. But in my opinion this contention supposes a restricted view of the scheme of the imposition of the capital gains tax which the statutory language does not permit. If, as here, the employer is able to exact from the employee a substantial sum as a term of releasing him from his obligations to serve, the rights of the employer appear to me to bear quite sufficiently the mark of an asset of the employer, something which he can turn to account, notwithstanding that his ability to turn it to account is by a type of disposal limited by the nature of the asset. In this connection I would also refer to the provisions of s 22(3)(a) which appear to me apt to cover a case where damages are recovered by an employer from a third party for wrongful procurement of breach by the employee of his contract of service."

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(1) 53 TC 241. (2) [1940] AC 1014. (3) [1903] 1 KB 137.
(4) [1932] 2 KB 304.

Thus the House of Lords treated as virtually irrelevant the use by s 22(1) of the word "property". It held to be dominant in ss 19 and 22 the words "asset" and "disposal". There are, it seems to me, two possible ways in which their Lordships may have reached that result. One was to take the view that s 22(1) was not intended to provide an exhaustive definition of "assets" but merely to enact that, whatever else might be comprised in that concept, it included "all forms of property". On that view "assets" was a wider concept than "property" and included any right that could be turned to account, even though a lawyer might not regard it as "property". The other possibility is that their Lordships agreed with the approach of Fox J. whose decision at first instance they were restoring. His view was that the word "property" was not a precise term but one of which the meaning might vary with the context (see page 251 of the report). That of course is true of almost any word, and it is interesting that, as was pointed out to me, there are passages in the judgment of Oliver L.J. (with which Bridge L.J. agreed) in *Trendtex Trading Corporation* v. *Credit Suisse* [1980] 3 All ER 721, in which he used the phrases "right of property" and "property right" in relation to a right to litigate in a context such that he clearly regarded it as irrelevant whether litigation embarked upon in exercise of that right would succeed.

Either way it would in my view be inconsistent with the decision in *O'Brien* v. *Benson's Hosiery (Holdings) Ltd.*(1) to hold that a right to bring an action to seek to enforce a claim that was not frivolous or vexatious, which right could be turned to account by negotiating a compromise yielding a substantial capital sum, could not be an "asset" within the meaning of that term in the capital gains tax legislation. I propose, for the sake of convenience, to refer to the right that Zim had, in that sense, to bring an action against Austin & Co. as its "right to sue" Austin & Co.

So I come to the contention that Mr. Thornhill put in the forefront of his case, which was that, in the correct analysis, the assets from which Zim derived the £69,000 were the properties comprised in the contract of sale. Mr. Thornhill based that contention on the provisions of subs s (2) and (3) of s 22 of the Finance Act 1965. He submitted that the receipt of the £69,000 should be treated as a part disposal of those properties, either by virtue of the general words of s 22(3)—that is to say, the words "there is for the purposes of this Part of this Act a disposal of assets by their owner where any capital sum is derived from assets"—or by virtue of s 22(3)(a) or by virtue of s 22(3)(c).

Mr. Thornhill's argument based on the general words rested on a premise which seems to me correct and which is this. The words "and this subsection applies in particular to" that introduce the lettered paragraphs in the subsection connote that those paragraphs describe particular instances of the application of the principle enacted by the general words. From that two consequences follow. The first is that a case cannot come within any of the lettered paragraphs if it cannot come within the general words. The other is that the lettered paragraphs may properly be looked at as aids to the interpretation of the general words. That indeed is what, in effect, Lord Wilberforce and Lord Fraser both said in *Marren* v. *Ingles*(2) 54 TC 76, at pages 96 and 99 respectively. Of the other three Law Lords, two expressed their agreement with the speech of Lord Wilberforce and one expressed his agreement with the speech of Lord Fraser. The contrary view expressed by Nourse J. in *Davenport* v. *Chilver*(3) [1983] STC 426 at page 439, must therefore be mistaken—nor did Mr. Carnwath seek to uphold it.

(1) 53 TC 241. (2) [1980] 1 WLR 983. (3) 57 TC 661.

From that it follows that a capital sum may be derived from assets within the meaning of the general words in s 22(3) even though those assets may not be the immediate source of that sum. That is not to say that Walton J. was wrong in holding in *Commissioners of Inland Revenue* v. *Montgomery*[1] 49 TC 679, that the sum received by the trustees from Mr. Greene was derived from their rights under the policies. It means no more than that it would be a mistake to interpret Walton J.'s decision in that case as authority for the proposition that the asset from which a capital sum is derived must always be the asset that constitutes its immediate source. The true view was hinted at by Fox J. in *O'Brien* v. *Benson's Hosiery (Holdings) Ltd.* when he referred (at page 254 of the report) to "the reality of the matter". One has to look in each case for the real (rather than the immediate) source of the capital sum.

On that premise, with which, as I have already indicated, I agree, Mr. Thornhill's argument proceeded as follows. If the properties had been sold, the sale price would have been derived from them. Because the properties were not sold, compensation was received from Austin & Co.'s insurers for the loss that Zim suffered by reason of there having been no sale of the properties. Thus the compensation was derived from the properties as much as the sale price would have been if the properties had been sold. To hold otherwise would be to transgress the basic rule that capital gains tax is a tax on real gains, not on "arithmetical differences". It would also be inconsistent with authorities showing that a right to compensation for loss is not an "asset" for capital gains tax purposes.

Mr. Thornhill's reference to the basic rule that capital gains tax is a tax on real gains, not on "arithmetical differences" was of course a reference to the words of Lord Wilberforce in *Aberdeen Construction Group Ltd.* v. *Commissioners of Inland Revenue*[2] 52 TC 281, where he said (at page 296):

> "The capital gains tax is of comparatively recent origin. The legislation imposing it, mainly the Finance Act 1965, is necessarily complicated, and the detailed provisions, as they affect this or any other case, must of course be looked at with care. But a guiding principle must underlie any interpretation of the Act, namely, that its purpose is to tax capital gains and to make allowance for capital losses, each of which ought to be arrived at upon normal business principles. No doubt anomalies may occur, but in straightforward situations, such as this, the courts should hesitate before accepting results which are paradoxical and contrary to business sense. To paraphrase a famous cliche, the capital gains tax is a tax upon gains: it is not a tax upon arithmetical differences."

It does not, however, seem to me "contrary to business sense" to treat the £69,000 received by Zim in this case as a gain. The fact is that, after its receipt of that sum, Zim still owned the properties, unaffected and unimpaired by the fate of its contract with Courtdeals Ltd. Mr. Thornhill invited me to approach the case on the footing that there had been a fall in property values in Manchester between July 1973 and July 1974, followed, in the period between July 1974 and the winter of 1975–76, by a rise in such values which did not quite compensate for the earlier fall; that it was because of that fall that Zim

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(1) [1975] 2 WLR 326. (2) [1978] AC 885.

had suffered damage from the loss of its sale to Courtdeals Ltd.; and that it was for that damage (or for part of it) that Zim had been compensated by Austin & Co.'s insurers. There are no findings of fact by the Special Commissioners to support that approach, but Mr. Thornhill suggested that I could infer the necessary facts from (i) the allegation in the statement of claim in Zim's action against Austin & Co. that the value of the properties in October 1974 was £75,000, (ii) the statement in the letter of 24 November 1975, that the then "site valuation" was £103,000 and (iii) the circumstance that Austin & Co.'s insurers had been prepared to settle for £69,000. I very much doubt if it is open to me to go that far in drawing inferences of fact, but, if it is, it remains true that, since Zim retained the properties, whether it would or would not in the end turn out to have suffered a loss on them would depend on what happened to property values in Manchester thereafter. As to that there is no evidence at all.

In support of his submission that a right to compensation for loss is not an "asset" for capital gains tax purposes, Mr. Thornhill cited *Davis* v. *Powell*[1] [1977] 1 WLR 258, *Davenport* v. *Chilver*[2] [1983] STC 426, and *Drummond* v. *Austin Brown*[3], [1984] STC 321. He also pointed out that, as a matter of common sense, it must be accepted that not every right to a payment is an asset for capital gains tax purposes. He gave as examples of rights that it would manifestly be ridiculous to treat as capable of generating capital gains a right to a repayment of tax and a right to the payment of costs at the end of successful litigation. Yet, he said, unless some such general rule as he was contending for existed, there would be, at all events since the enactment of s 90 of the Finance Act 1981, no escape from the conclusion that a repayment of tax, or a payment under an award of costs, should be treated as pure capital gain.

I have no difficulty in accepting that not every right to a payment is an "asset" within the meaning of that term in the capital gains tax legislation. Perhaps the most obvious example of one that is not is the right of a seller of property to payment of its price. The relevant asset, then, is the property itself. What that shows, however, to my mind, is no more than that the interpretation of the capital gains tax legislation requires, as does the interpretation of any legislation, the exercise of common sense, rather than just the brute application of verbal formulae. In saying that I am, I think, expressing much the same thought as was expressed by Lord Wilberforce in *Aberdeen Construction Group Ltd.* v. *Commissioners of Inland Revenue*[4].

I return to the three authorities that Mr. Thornhill cited on this part of the case. I found it astonishing that he should cite them in support, not of his contention that there was no relevant asset from which Zim derived the £69,000, but in support of his contention that the relevant assets were the properties. For *Davis* v. *Powell* and *Drummond* v. *Austin Brown* to support the latter contention it would have been necessary for Templeman J. to hold in *Davis* v. *Powell* that the £591 was derived from the lease, which is the very opposite of what he did hold, and for the Court of Appeal to hold in *Drummond* v. *Austin Brown* that the £31,384 was derived from the lease there in question, which again is the very opposite of what it did hold. Those two

(1) 51 TC 492. (2) 57 TC 661. (3) 58 TC 67. (4) 52 TC 281.

A authorities would, so it seems to me, lend support to Mr. Thornhill's alternative contention (that there was here no relevant asset) were it not for the decision of the House of Lords in *O'Brien* v. *Benson's Hosiery (Holdings) Ltd*[1]. In the light of that decision I must, I think, conclude that *Davis* v. *Powell*[2] and *Drummond* v. *Austin Brown*[3] are merely instances of the application of the legislation to particular facts and that they do not evince any
B principle beyond the general principle, the existence of which I have already acknowledged, that not every right to a payment is an "asset" for capital gains tax purposes.

The judgment of Nourse J. in *Davenport* v. *Chilver*[4] fell into two parts. The first part, on which I have already had occasion to comment, related to Miss Chilver's rights in respect of her own and her father's Latvian property.
C The second part related to her rights in respect of her mother's Latvian property. It was on this second part of the judgment that Mr. Thornhill relied in the present connection. Having read and reread it, I do not think that it helps Mr. Thornhill. I observe, incidentally, that in that part of his judgment Nourse J. expressly rejected a submission that a statutory right to compensation for irretrievable loss could not be an asset for capital gains tax purposes.

D For those reasons, I reject Mr. Thornhill's submission based on the general words of s 22(3). It seems to me that, if one is to search for "the reality of the matter", the reality is that Zim derived the £69,000 from its right to sue Austin & Co.

I turn to Mr. Thornhill's submissions based on s 22(3)(a). He formulated them in two different ways. First he submitted that that paragraph applied
E because Zim, upon entering into the contract for the sale of the properties, acquired contractual rights which were, within the meaning of para 8 of Sch 6 to the Finance Act 1965, derived from the properties and, in the event, those rights were lost or depreciated to nil. There are two flaws in that argument, as Mr. Carnwath pointed out. The first is that para 8 of Sch 6 does not apply in this case because there was never any disposal of Zim's rights under the
F contract of sale. The second is that Zim never lost (or had depreciated to nil) any right that it had against Courtdeals Ltd. From the outset Zim's title to No. 49 Faulkner Street was defective and from the outset Zim had no right to foist that defective title on Courtdeals Ltd.

The other way in which Mr. Thornhill put his case under s 22(3)(a) was this. He said that the £69,000 was a capital sum received by Zim by way of
G compensation for depreciation of the properties, in that, in the events that had happened, Zim was entitled to receive from Austin & Co. compensation for any depreciation in the value of the properties. Mr.Carnwath described this formulation as the most attractive of Mr. Thornhill's ways of putting his case. Of course, I could accept it only if I accepted that it was open to me to draw the inferences of fact, as to the changes in property values in Manchester and
H so forth, that I mentioned earlier. Assuming, however, that it is open to me to draw those inferences, and assuming further that it is proper to describe the £69,000 as "compensation" for something, it seems to me that it can only be described as compensation for the consequences of Austin & Co.'s alleged negligence. The depreciation in the value of the properties was not a

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(1) 53 TC 241. (2) 51 TC 492. (3) 58 TC 67. (4) 57 TC 661.

consequence of that negligence. It was something which, if it happened, happened as a result of forces affecting the property market in Manchester, independently of that negligence. Its relevance for present purposes was merely as a factor entering into the computation of the amount of the so-called compensation, other material factors being the notional interest, the costs of the two actions and, no doubt, people's estimates of Zim's chances of success in the action.

So I reject Mr. Thornhill's submissions based on s 22(3)(a) and turn to his submission based on s 22(3)(c). This was to the effect that the £69,000 was received by Zim "in return for" its "refraining from exercising" to the full its right to sue Austin & Co. No doubt that is correct. Mr. Thornhill then referred to para 13 of Sch 6 to the Finance Act 1965, and submitted that that provision demonstrated that the assets deemed to be disposed of under s 22(3)(c) were not necessarily the rights that the taxpayer refrained from exercising. He concluded that those assets must be, in the present case, the properties.

I agree with Mr. Carnwath that there is there a *non sequitur*. Assuming (without deciding) that Mr. Thornhill is right in saying that, where s 22(3)(c) applies, the relevant assets may be assets other than the rights referred to in that paragraph, it does not follow that, in the present case, those assets were the properties. It seems to me that, in deciding what the relevant assets were, one must have regard to the same considerations as in applying the general words at the beginning of s 22(3). The reality of the matter is still that the £69,000 was derived by Zim from its right to sue Austin & Co., rather than from the properties.

In the result I think that the Special Commissioners came to the right conclusion on what I have described as the first and main question in this case. I turn to the subsidiary questions. They arise from two contentions put forward by Mr. Thornhill in an endeavour to lessen Zim's liability to tax if I should hold that the relevant asset was its right to sue Austin & Co.

Of those contentions, the first rested on subs (4) of s 22 of the Finance Act 1965. That subsection was, so far as material, in these terms:

> "Subject to the provisions of this Part of this Act, a person's acquisition of an asset and the disposal of it to him shall for the purposes of this Part of this Act be deemed to be for a consideration equal to the market value of the asset—(a) where he acquires the asset otherwise than by way of a bargain made at arm's length and in particular where he acquires it by way of gift or by way of distribution from a company in respect of shares in the company, or (b) where he acquires the asset wholly or partly for a consideration that cannot be valued, or in connection with his own or another's loss of office or employment or diminution of emoluments, or otherwise in consideration for or recognition of his or another's services or past services in any office or employment or of any other services rendered or to be rendered by him or another."

Mr. Thornhill's contention was as follows. Zim, he said, acquired its right to sue Austin & Co. "otherwise than by way of a bargain made at arm's length". Zim must therefore be deemed to have acquired that right for a consideration equal to its market value. Zim acquired the right to sue Austin & Co. in July 1974, when Courtdeals Ltd. declined to complete the purchase of the properties. The market value of the right at that time was accordingly deductible in computing the capital gain.

That contention was accepted by the Special Commissioners except that they held that the right arose on 12 July 1973, when the allegedly defective contract for sale was entered into. There having been no argument before them on what the market value of the right on that day was, they adjourned the proceedings for, as they expressed it, "agreement of figures".

I should for my part have thought it doubtful if the right to sue here in question could have had a market value either in July 1973 or in July 1974. However, the arguments of Counsel before me proceeded on the footing that that right had a market value on each of those dates, and I will assume that that is correct. Two points were argued. The first arose out of a submission of Mr. Carnwath that there was never an "acquisition" by Zim of the right to sue within the meaning of that word in s 22. The second was whether, if there was such an acquisition, it occurred in July 1973 or in July 1974.

In support of his submission on the first point Mr. Carnwath relied on the reference in s 22(1)(c) to property "coming to be owned without being acquired". That showed, he said, that the word "acquire" and its derivatives were used in the Act in a narrower sense than their normal sense. Mr. Carnwath was, however, despite several attempts, unable to define that narrower sense in any satisfactory way. I observe that a similar argument was advanced by Mr. Carnwath in *Davenport* v. *Chilver*[1] and there rejected by Nourse J. (see [1983] STC 426 at page 441). I have no hesitation in rejecting it here too, and I turn to the more difficult question whether Zim acquired the right in question in July 1973, as Mr. Carnwath submits and the Special Commissioners held, or in July 1974, as Mr. Thornhill submits.

On that question I was referred to *Midland Bank Trust Co. Ltd.* v. *Hett, Stubbs & Kemp* [1979] Ch 384, to *Forster* v. *Outred & Co.*, [1982] 1 WLR 86, and to what Hodgson J. said about *Forster* v. *Outred & Co.* in *Dove* v. *Banhams Patent Locks Ltd.* [1983] 1 WLR 1436, at page 1445. I also took the opportunity of rereading the judgment that the Court of appeal delivered on 12 May 1982, in the unreported case of *Baker* v. *Ollard & Bentley.*[2] I mentioned that case to Counsel during the argument, but they were unable to find it. I found it myself only after the argument was concluded and I had reserved judgment. I did not invite further argument upon it because nothing in it leads me to take a view different from that which I would have taken in its absence.

Mr. Thornhill relied strongly on *Midland Bank Trust Co. Ltd.* v. *Hett, Stubbs & Kemp*. In my view, however, that case does not help him. The main question at issue there was whether the plaintiff could sue in tort as well as in contract. Oliver J. held that it could. It was not in dispute that the cause of action in contract arose at the date of the breach of contract. There was a dispute as to when that breach occurred, but Oliver J.'s decision as to that is of no relevance to the present case, where it is common ground that the breach of contract, if there was one, occurred in July 1973. In saying that I ignore, of course, what I have called the additional allegations of negligence in the statement of claim. There was no dispute in the *Midland Bank* case that the cause of action in tort, if there was one, arose when actual damage was suffered by the owner of the option, nor was there any dispute as to when that

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(1) 57 TC 661. (2) 126 SJ 593.

was. Here the whole dispute is as to when Austin & Co.'s alleged negligence resulted in actual damage to Zim so as to give rise to the latter's cause of action, if any, in tort. A

On that question Mr. Carnwath relied, naturally, on *Forster* v. *Outred & Co.*(1) Mr. Thornhill sought to distinguish that case on the ground that there the execution of the mortgage deed had an immediate depreciatory effect on the value of the plaintiff's land whereas here it was not until the contractual date for completion arrived that it could be ascertained whether the alleged flaw in the contract of sale would result in actual damage to Zim. Until then, he said, any attempt by Zim to assert a claim in tort against Austin & Co. could be met with the objection that the lost conveyance might be found and that, even if it were not, Courtdeals Ltd. might be prepared to accept the defective title. B

I admire Mr. Thornhill's ingenuity, but I think that that would be too fine a distinction to draw between the two cases. I have in mind in particular the passage in Stephenson L. J.'s judgment in *Forster* v. *Outred & Co.*(at page 98 of the report) where he said that the plaintiff had suffered actual damage through the negligence of her solicitors by entering into the mortgage deed in that she was thereby subjected to a liability which might "according to matters completely outside her control mature into financial loss", and the passage in Dunn L. J.'s judgment in that case where he said (at page 99): "I would hold that in cases of financial or economic loss the damage crystallizes and the cause of action is complete at the date when the plaintiff, in reliance on negligent advice, acts to his detriment." Sir David Cairns, the third member of the Court in that case, agreed with both judgments. It seems to me that in the present case, if one looks at Zim's claim against Austin & Co. as it was pleaded, it would be true to say that the essence of it was that Zim had, in reliance on the negligent advice of Austin & Co., acted to its detriment in entering into a contract in inappropriate terms and that Zim was thereby subjected to the risk of financial loss according to matters completely outside its control. C D E

I therefore agree with the Special Commissioners that the relevant date was 12 July 1973. I do not overlook the dictum of Hodgson J. in *Dove* v. *Banham's Patent Locks Ltd.*(2) to the effect that *Forster* v. *Outred & Co.* may not be reconcilable with more recent authority in the House of Lords. I apprehend, however, that it is not for me, as a Judge of first instance, to say that that authority is no longer good law. F

Mr. Thornhill's other subsidiary contention was of the kind that needs only to be stated to be rejected. It was to the effect that Zim's right to sue Austin & Co., being a right to submit its claim against its solicitors to the decision of the Court, was acquired only when the writ was issued on 24 October 1974, so that the market value of the relevant asset had to be ascertained as at that date. To be fair to Mr. Thornhill, he put that contention forward almost apologetically and did not press it. I therefore do not think that I need say any more about it. G H

I think that, in the result, I should dismiss both the appeal and the cross appeal.

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(1) [1982] 1 WLR 86. (2) [1983] 1 WLR 1436.

A *Appeal and cross-appeal dismissed.*

[Solicitors:—Messrs. Berwin Leighton; Solicitor of Inland Revenue.]