[2022] UKFTT 25 (TC)

TC 08377/V

CAPITAL GAINS TAX – agreement for grant of lease on payment of premium – taxpayer paid deposit at time of contract as part payment of premium due on completion – taxpayer defaulted on next stage payment of premium and so contract rescinded – was the lost deposit an allowable loss? – Hardy *(Upper Tribunal),* Lloyd-Webber *(First-tier Tribunal) and* Underwood *(Court of Appeal) considered – Held: the Tribunal was bound by the decision of the Upper Tribunal in* Hardy *– appeal dismissed*

FIRST-TIER TRIBUNAL
TAX CHAMBER

Appeal number: TC/2019/004422 V

BETWEEN

CHRISTOPHER DRAKE **Appellant**

-and-

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

TRIBUNAL: JUDGE ZACHARY CITRON

The hearing took place on 22 November 2021. The form of the hearing was V (video) on the Tribunal's Video Hearing service platform (Mr Brooke joined by telephone). A face to face hearing was not held because of the pandemic. The documents to which I was referred were a hearing bundle of 86 pdf pages.

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.

Further written submissions from the parties were made on 29 November 2021.

Mr D Ware of Bayliss Ware, accountants, for the Appellant

Mr K Brooke, Litigator of HM Revenue and Customs' Solicitor's Office for the Respondents

DECISION

1. In July 2014 the appellant entered into an agreement for lease (the "**Contract**") under which, at completion, he was to be granted a lease of a property (still under construction at the time of the Contract) in return for payment of a premium of £2.2 million. A 20% deposit was payable by him on the date of the Contract and a 10% stage payment was payable one year later, both as advance payments of the premium. The appellant defaulted on payment of the stage payment; this was a repudiatory breach and the Contract never completed. The issue in the appeal was whether the appellant had an allowable loss for the purposes of capital gains tax equal to his lost deposit.

PROCEDURAL BACKGROUND

2. HMRC issued a closure notice on 27 November 2018 in respect of the appellant's 2015-16 tax return, disallowing an allowable loss of £220,000 in respect of the deposit paid under the Contract. This resulted in additional tax payable of £60,762.80.

3. The appellant wrote to HMRC on 19 December 2018 appealing their decision as per the closure notice. On 30 May 2019 HMRC upheld their decision upon statutory review.

4. On 26 June 2019 the appellant notified his appeal to the Tribunal

FINDINGS OF FACT

5. On 17 July 2014 the appellant entered into the Contract with City Road Limited (referred to as the "seller") relating to a plot (referred to as the "demised premises") at a property in London EC1. Under the Contract

(1) the seller was required, at completion, to grant the appellant a lease of the demised premises, and the appellant to accept that lease;

(2) completion was to take place shortly after building work had been completed (the demised premises were in the course of construction at the date of the Contract);

(3) a deposit was to be paid by the appellant on the date of the Contract, equal to 20% of the "premium" (being £2.2 million) less the "reservation fee" (£5,000) (payable under a "reservation agreement" between the appellant and the seller dated 23 May 2014). A "stage payment" (10% of the premium) was payable by him 12 months later; and the balance of the premium was payable on completion. In the event that the appellant failed to pay either the deposit or the stage payment, the seller could treat such conduct as repudiation of the Contract without prejudice to any other right or remedy available to the seller;

(4) the appellant was entitled to assign the benefit of the Contract, after payment of the deposit and stage payment;

(5) The "standard conditions of sale (fifth edition)" applied, with certain exceptions.

6. The appellant paid the deposit (£215,000) when due but did not pay the stage payment due in July 2015. As a result, the seller treated the appellant as having repudiated the Contract; the Contract was never completed; and the seller kept the deposit (and reservation fee).

7. The reason for the appellant's defaulting on the stage payment was that, due to a perceived decline in property values after the Contract was signed, the value of the lease to be granted at completion was thought to be less than the premium due – he therefore had difficulty raising finance to pay the stage payment and/or the rest of the premium.

8. The commercial reality was that the appellant took commercial risk in entering into the Contract without funding to complete it (and with an extended period between signing and

completion), yet agreed to pay a 20% upfront non-refundable deposit. This led to him suffering an economic loss, when he was unable to raise finance to pay the remainder of the premium, and so made a repudiatory breach of the Contract by failing to pay the stage payment when due.

LAW

Taxation of Chargeable Gains Act 1992

9. References in what follows to "sections" or "s" are to sections of Taxation of Chargeable Gains Act 1992.

10. Sub-section 1(1) (*The charge to tax*) provides:

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

11. Sub-section 2(2) (*Persons and gains chargeable to capital gains tax, and allowable losses*) provides:

> "Capital gains tax shall be charged on the total amount of chargeable gains accruing to the person chargeable in the year of assessment, after deducting —
>
> (a) any allowable losses accruing to that person in that year of assessment, and
>
> (b) so far as they have not been allowed as a deduction from chargeable gains accruing in any previous year of assessment, any allowable losses accruing to that person in any previous year of assessment (not earlier than the year 1965-66)."

12. Section 16 (*Computation of losses*) provides, so far as relevant:

> "(1) Subject to sections 261B, 261D and 263ZA and except as otherwise expressly provided, the amount of a loss accruing on a disposal of an asset shall be computed in the same way as the amount of a gain accruing on a disposal is computed.
>
> (2) Except as otherwise expressly provided, all the provisions of this Act which distinguish gains which are chargeable gains from those which are not, or which make part of a gain a chargeable gain, and part not, shall apply also to distinguish losses which are allowable losses from those which are not, and to make part of a loss an allowable loss, and part not; and references in this Act to an allowable loss shall be construed accordingly.
>
> …"

13. Section 21 (*Assets and disposals*) provides:

> "(1) All forms of property shall be assets for the purposes of this Act, whether situated in the United Kingdom or not, including—
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> (a) options, debts and incorporeal property generally, and
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> (b) currency, with the exception (subject to express provision to the contrary) of 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 Act—

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

(b) there is a part disposal of an asset where an interest or right in or over the asset is created by the disposal, as well as where it subsists before the disposal, 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."

14. Sub-section 24(1) (*Disposals where assets lost or destroyed, or become of negligible value*) provides:

"Subject to the provisions of this Act and, in particular to sections 140A(1D), 140E(7) and 144, the occasion of the entire loss, destruction, dissipation or extinction of an asset shall, for the purposes of this Act, constitute a disposal of the asset whether or not any capital sum by way of compensation or otherwise is received in respect of the destruction, dissipation or extinction of the asset."

15. Section 28 (*Time of disposal and acquisition where asset disposed of under contract*) provides:

"(1) Subject to section 22(2), and subsection (2) below, where an asset is disposed of and acquired under a contract the time at which the disposal and acquisition is made is the time the contract is made (and not, if different, the time at which the asset is conveyed or transferred).

(2) If the contract is conditional (and in particular if it is conditional on the exercise of an option) the time at which the disposal and acquisition is made is the time when the condition is satisfied."

16. Section 38 (*Acquisition and disposal costs etc*) provides, so far as relevant:

"(1) Except as otherwise expressly provided, the sums allowable as a deduction from the consideration in the computation of the gain accruing to a person on the disposal of an asset shall be restricted to—

(a) the amount or value of the consideration, in money or money's worth, given by him or on his behalf wholly and exclusively for the acquisition of the asset, together with the incidental costs to him of the acquisition or, if the asset was not acquired by him, any expenditure wholly and exclusively incurred by him in providing the asset,

(b) the amount of any expenditure wholly and exclusively incurred on the asset by him or on his behalf for the purpose of enhancing the value of the asset, being expenditure reflected in the state or nature of the asset at the time of the disposal, and any expenditure wholly and exclusively incurred by him in establishing, preserving or defending his title to, or to a right over, the asset,

(c) the incidental costs to him of making the disposal.

(2) For the purposes of this section and for the purposes of all other provisions of this Act, the incidental costs to the person making the disposal of the acquisition of the asset or of its disposal shall consist of expenditure wholly and exclusively incurred by him for the purposes of the acquisition or, as the case may be, the disposal, being fees, commission or remuneration paid for the professional services of any surveyor or valuer, or auctioneer, or accountant, or agent or legal

adviser and costs of transfer or conveyance (including stamp duty or stamp duty land tax) together—

(a) in the case of the acquisition of an asset, with costs of advertising to find a seller, and

(b) in the case of a disposal, with costs of advertising to find a buyer and costs reasonably incurred in making any valuation or apportionment required for the purposes of the computation of the gain, including in particular expenses reasonably incurred in ascertaining market value where required by this Act.

…"

17. Section 43 (*Assets derived from other assets*) provides:

"If and so far as, in a case where assets have been merged or divided or have changed their nature or rights or interests in or over assets have been created or extinguished, the value of an asset is derived from any other asset in the same ownership, an appropriate proportion of the sums allowable as a deduction in the computation of a gain in respect of the other asset under paragraphs (a) and (b) of section 38(1) shall, both for the purpose of the computation of a gain accruing on the disposal of the first-mentioned asset and, if the other asset remains in existence, on a disposal of that other asset, be attributed to the first-mentioned asset."

18. Section 144 (*Options and forfeited deposits*) provides:

(1) Without prejudice to section 21, the grant of an option, and in particular—

(a) the grant of an option in a case where the grantor binds himself to sell what he does not own, and because the option is abandoned, never has occasion to own, and

(b) the grant of an option in a case where the grantor binds himself to buy what, because the option is abandoned, he does not acquire,

is the disposal of an asset (namely of the option), but subject to the following provisions of this section as to treating the grant of an option as part of a larger transaction.

(2) If an option is exercised, the grant of the option and the transaction entered into by the grantor in fulfilment of his obligations under the option shall be treated as a single transaction and accordingly—

(a) if the option binds the grantor to sell, the consideration for the option is part of the consideration for the sale, and

(b) if the option binds the grantor to buy, the consideration for the option shall be deducted from the cost of acquisition incurred by the grantor in buying in pursuance of his obligations under the option.

(3) The exercise of an option by the person for the time being entitled to exercise it shall not constitute the disposal of an asset by that person, but, if an option is exercised then the acquisition of the option (whether directly from the grantor or not) and the transaction entered into by the person exercising the option in exercise of his rights under the option shall be treated as a single transaction and accordingly—

(a) if the option binds the grantor to sell, the cost of acquiring the option shall be part of the cost of acquiring what is sold, and

(b) if the option binds the grantor to buy, the cost of the option shall be treated as a cost incidental to the disposal of what is bought by the grantor of the option.

(4) The abandonment of—

(a) a quoted option to subscribe for shares in a company, or

(b) a traded option or financial option, or

(c) an option to acquire assets exercisable by a person intending to use them, if acquired, for the purpose of a trade carried on by him,

shall constitute the disposal of an asset (namely of the option); but the abandonment of any other option by the person for the time being entitled to exercise it shall not constitute the disposal of an asset by that person.

(5) This section shall apply in relation to an option binding the grantor both to sell and to buy as if it were 2 separate options with half the consideration attributed to each.

(6) In this section references to an option include references to an option binding the grantor to grant a lease for a premium, or enter into any other transaction which is not a sale, and references to buying and selling in pursuance of an option shall be construed accordingly.

(7) This section shall apply in relation to a forfeited deposit of purchase money or other consideration money for a prospective purchase or other transaction which is abandoned as it applies in relation to the consideration for an option which binds the grantor to sell and which is not exercised.

(8) In subsection (4) above and sections 146 and 147—

(a) "quoted option" means an option which, at the time of the abandonment or other disposal, is listed on a recognised stock exchange;

(b) "traded option" means an option which, at the time of the abandonment or other disposal, is listed on a recognised stock exchange or a recognised futures exchange; and

(c) "financial option" means an option which is not a traded option, as defined in paragraph (b) above, but which, subject to subsection (9) below—

(i) relates to currency, shares, securities or an interest rate and is granted (otherwise than as agent) by a member of a recognised stock exchange, by an authorised person within the meaning given by section 143(8); or

(ii) relates to shares or securities which are dealt in on a recognised stock exchange and is granted by a member of such an exchange, acting as agent; or

(iii) relates to currency, shares, securities or an interest rate and is granted to such an authorised person as is referred to in sub-paragraph (i) above and concurrently and in association with an option falling within that sub-paragraph which is granted by that authorised person to the grantor of the first-mentioned option; or

(iv) relates to shares or securities which are dealt in on a recognised stock exchange and is granted to a member of such an exchange, including such a member acting as agent.

> (9) If the Treasury by order so provide, an option of a description specified in the order shall be taken to be within the definition of "financial option" in subsection (8)(c) above.

Hardy

19. In *Hardy v HMRC* [2016] UKUT 0332 (TCC), the taxpayer entered into an agreement for purchase off-plan of a leasehold property; a deposit of 10% of the purchase price was payable on entering into the contract. The benefit of the contract was not assignable. The taxpayer was unable to complete and the seller exercised its right to rescind the contract and keep the deposit.

20. 'Issue 1' in *Hardy* was whether the taxpayer had acquired an asset.

21. The Upper Tribunal ("**UT**") noted that it is well established that contractual rights are capable of being an asset for capital gains tax purposes, and will be if they can be turned to account even if they cannot be transferred or assigned to another: see *O'Brien (Inspector of Taxes) v Benson's Hosiery (Holdings) Ltd* [1980] AC 562 at 572- 573

22. The UT said it was necessary carefully to analyse the contractual rights which the taxpayer acquired when he entered into the contract: this 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. The UT had no difficulty in accepting that this was a valuable right – but said it does not necessarily follow that it was an asset for the purposes of the legislation.

23. After citing case law indicating that beneficial interests in land do not transfer prior to completion of the contract, the UT concluded as follows:

> "40. 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.
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> 41. It follows that the First-tier Tribunal was correct to conclude that Mr Hardy did not acquire an asset for capital gains tax purposes when he entered into the Contract. He therefore had no asset to dispose of when the Contract was rescinded.
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> 42. We would add that counsel for HMRC submitted that, because the Contract was not assignable by Mr Hardy, he could not have turned it to account. As counsel for Mr Hardy submitted, this does not necessarily mean that it was not an asset, because Mr Hardy could have unilaterally declared himself a trustee of the benefit of the Contract for a third party and turned it to account in that way. But this does not affect the fundamental point considered above.
>
> 43. It follows from our conclusion on the first issue that the second and third issues do not arise. In deference to the arguments we received, we will nevertheless deal briefly with them."

24. 'Issue 2' in *Hardy* – whether the taxpayer had disposed of an asset – was considered by the UT on the assumption that the taxpayer's rights under the contract constituted an asset.

25. The UT concluded that the combined effect of s144(7) and s144(4) in a case such as the taxpayer's was that the taxpayer's loss of the right to enforce performance of the contract of sale, resulting in forfeiture of the deposit, did not amount to a disposal. The aspect of the taxpayer's circumstances discussed immediately before reaching this conclusion was that he had tried to avoid the deposit being forfeited – the UT decided that *even* in these circumstances, this fell within the statutory language of "abandonment" of a purchase.

26. 'Issue 3' in *Hardy* – whether the taxpayer incurred an allowable loss – was considered by the UT on the assumption that the taxpayer's rights under the contract constituted an asset which was disposed of when the contract was rescinded.

27. The UT found that that the deposit had not been paid wholly or even mainly by the taxpayer for the acquisition of contractual rights under the contract, but as a part-payment of the purchase price of the property. The acquisition of the right to enforce performance of the contract was incidental. So the forfeited deposit was not in any event an allowable loss.

Lloyd-Webber

28. In *Lloyd-Webber & Anor v HMRC* [2019] UKFTT 717 (TC), the taxpayers entered into contracts to purchase two plots of land in Barbados together with the villas to be constructed on them. They paid a deposit on the purchase price. Under the contracts, further amounts became due as progress was made on constructing the villas. Over time, the taxpayers made payments under the contracts of over $11m to the vendors. However, serious problems emerged over the next few years in the construction of the villas. About four years after the original contracts were entered into, the taxpayers entered into further contracts with the sellers, terminating the original contracts; the taxpayers acquired certain rights under the further contracts, but these rights ended up as being of negligible value. The taxpayers claimed allowable losses equal to their payments under the original contracts.

29. The First-tier Tribunal ("**FTT**") set out the issues thus:

> "11. HMRC had initially argued, relying on the decision of the Upper Tribunal in [*Hardy*], that the rights under the [original] Contracts were not assets for CGT purposes. However, it is now common ground, on the basis of the decision of the Court of Appeal in *Underwood v HMRC* [2009] STC 239 (which was not cited to the Upper Tribunal in *Hardy*), that the decision in *Hardy* is per incuriam and not binding on the Tribunal.
>
> 12. Accordingly, it is not disputed that [the taxpayers] acquired assets, namely the rights under the [original] Contracts, and that there was a disposal of those rights when they were released in accordance with the [subsequent] Contracts. It is also not disputed that [the taxpayers] suffered a commercial loss in that they have spent considerable sums and it seems unlikely that the villas will in fact be built. The issue between the parties is whether the amounts paid under the [original] Contracts were, as [the taxpayers] contend, paid to acquire/enhance their contractual rights and allowable as a deduction under s38 or, as HMRC argue, the payments were made to acquire/enhance the estates in land which were the ultimate subject matter of the [original] Contracts."

30. The FTT reviewed the case law and decided that for the purposes of s38 it was necessary, taking an objective approach, to consider what the payments made by the taxpayers under the original Contracts were, in reality, for.

31. The FTT concluded that although they entered into the original contracts with the intention of ultimately acquiring completed villas, the payments made by the taxpayers under those

contracts were for the acquisition of contractual rights, the only asset they actually acquired. The FTT reached that conclusion via the following analysis:

(1) the UT's decision on 'issue 3' in *Hardy* was obiter and so not binding;

(2) given the "very limited reasoning" by the UT in *Hardy* on this issue – in particular the "absence of any consideration of" s43 or s144 – the FTT was unable to derive any assistance from *Hardy*;

(3) on the completion of a contract, s43 allows expenditure initially incurred on obtaining contractual rights to be treated as expenditure on land as, in such circumstances there has been either a "merger" or "change in nature" of those contractual rights and, as it is the payment for those contractual rights that entitle a person to have the land conveyed to him on completion (and therefore be in the same ownership) the value of the land, "an asset", is "derived from" another "asset in the same ownership", namely, the contractual rights.

(4) by contrast, because the grant of an option is treated under s144(1) as a separate disposal, s 144(2) is required, if the option is exercised, to treat the grant and the transaction entered into under the option as a "single transaction" and accordingly, if the option binds the grantor to sell, provides for the consideration for the option to be part of the consideration for the sale and, if the option binds the grantor to buy, provides for the consideration to be deducted from the cost of the acquisition;

(5) because of the effect of s43 an equivalent provision is not necessary in circumstances where there has not been completion of a contract;

(6) additionally, if Parliament considered that a loss in circumstances such as in *Lloyd-Webber* should be excluded from relief, provision could have been made, as it was by s144(7) in the case of losses resulting from a forfeited deposit.

Underwood

32. In *Underwood v HMRC* [2009] STC 239, the taxpayer contracted to sell land to a third party (B) and would have realised an allowable loss if he disposed of the land. However, before completion of that sale contract, the taxpayer contracted to re-purchase the land from B, and also to sell it to C. At completion, the land was never transferred to (and from) B – instead, on the completion date, it was transferred from the taxpayer to C, and the taxpayer paid B the excess of the repurchase price over the sale price.

33. The question was whether the taxpayer had realised an allowable loss on disposal of the land to B.

34. The Court of Appeal held that there was no event that resulted in the disposal of the property by the taxpayer to B under the sale contract or an acquisition by B of the property under that contract. There could have been a disposition only if the beneficial interest in the property had been transferred to B. It was common ground that the sale contract itself did not transfer the beneficial interest. There was no event which could have constituted the disposal to B. All that actually happened was that the position as between the taxpayer and B was treated as settled by treating the taxpayer as a debtor of B. As between the taxpayer and B there was a single event, namely the netting off of the price stipulated by the sale contract against the price stipulated in the re-purchase contract.

35. The court said this at [52-53] (Lawrence Collins LJ) and [65] (Lord Neuberger) of the judgement:

> "[52] It is true that the [re-purchase contract) must have proceeded on the basis that [B] had an interest in the Property capable of constituting the subject

> matter of [that contract]. But there was at that time no disposal to [B] because [B] obtained nothing additional to the rights which it acquired on the making of the [sale and re-purchase contracts]. It is unrealistic and contrary to the facts to conclude that there were two events, one by which [the taxpayer] disposed of the Property to [B] and another by which [B] disposed of the Property to the taxpayer. The netting off was the only 'performance' of those contracts. There was no other performance at all, and the netting off was accepted by the parties in substitution for the performance required by the contracts. To the extent that [B] turned an asset to account, the asset was its contractual rights under the [sale contract] to acquire the Property, and not its beneficial interest in the Property.
>
> [53] [B] did not acquire the Property by becoming the beneficial owner of it, and [the taxpayer] did not dispose of it. [B] did not pay [the price under the sale contract] for a beneficial interest in the Property. [B] agreed that its obligation to pay [the price under the sale contract] could be set off against the taxpayer's obligation to pay [the price under the re-purchase contract] thereby extinguishing [B]'s interest in the Property, which was the right to require transfer of the beneficial interest, but subject to the Option.
>
> …
>
> [65] The authorities have been fully considered by Lawrence Collins LJ and there is nothing that I wish to add about them, save in relation to Lord Russell of Killowen's statement in *O'Brien* (*Inspector of Taxes*) *v Benson's Hosiery* (*Holdings*) *Ltd* [1979] STC 735 at 738–739, [1980] AC 562 at 573 that 'the mark of an asset' is 'something which can be turned to account'. Mr Soares, who appears for [the taxpayer], says his client disposed of the property to [B] by turning it to account on [the completion date]. In my view, that is not correct: if he turned anything to account, as against [B] on [the completion date], it was the [sale] contract.

APPELLANT'S ARGUMENTS

36. The appellant's arguments included the following:

(1) The appellant had rights (the benefit of the Contract) that he could turn to account as soon as he paid certain sums under the Contract. These rights were fully marketable. Under s21(1), such rights are an asset for the purposes of capital gains tax.

(2) Those rights were extinguished on rescission of the Contract, and the appellant suffered a real monetary loss of £220,000. Section 24 provides that the extinction of an asset is treated as a disposal for capital gains tax purposes

(3) Had he sold his contractual rights at a profit, the gain would have been chargeable. Section 16 directs that capital losses will be calculated and allowed in the same way gains are calculated and taxed.

(4) A fundamental difference between *Hardy* and this case, is that the contract in *Hardy* was not assignable; the taxpayer in *Hardy* did not own an asset that he could market and sell and therefore turn to account.

(5) The facts of this case were analogous to those in *Lloyd-Webber*; and so this Tribunal should follow the decision of the FTT in *Lloyd-Webber*.

(6) *Hardy* failed to take [52-53] of *Underwood* into account, by determining that the contractual rights and the beneficial interest in the property were two sides of the same coin. *Underwood* confirmed the existence of separate rights, as the taxpayer argued in *Hardy*.

(7) *Hardy* ignored the binding conclusion in *Underwood* that B had made a gain based on the disposal of its contractual rights without the transfer of beneficial interest in the property. The taxpayer in *Hardy* acquired an asset, contrary to the UT's decision on 'issue 1'.

(8) Because the appellant was entitled to assign the benefit of the Contract, the "two sides of the same coin" argument made in *Hardy* at [40] did not apply, such that, in this case, the Contract comprised a capital gains asset in the appellant's hands.

HMRC'S ARGUMENTS

37. HMRC essentially relied on the authority of *Hardy*: although they had in *Lloyd-Webber* conceded that the decision on 'issue 1' was *per incuriam*, this was only in respect of 'issue 1': the decision in *Hardy* on 'issue 2' was good law and meant there was no disposal of a capital gains asset on the facts of this case.

DISCUSSION

38. The issue in this case is whether, upon rescission of the Contract by reason of the appellant's repudiatory breach (i.e. non-payment of the stage payment due under the Contract), a loss accrued to the appellant on the disposal of an asset (the loss being equal to his "acquisition cost" in that asset).

39. A number of questions arise in this case in relation to *Hardy*, a decision of the UT on similar facts which may, therefore, be binding on this Tribunal. The questions are as follows (with short explanations, taken from *Jowitt's Dictionary of English Law*, of legal terms used in the questions):

(1) What is the *ratio* of *Hardy*?

(*Ratio* (short for *ratio decidendi*) means the legal basis for a judicial decision. It includes only those statements of legal rules or principles that are the essential basis for reaching the decision, as opposed to other observations on the law (known as *obiter dicta*) which the judgment may contain. The *ratio* is important in the doctrine of precedent since it is only that part of the judgment of a superior court that constitutes a precedent.)

(2) What is the *ratio* of *Underwood*, a decision of the Court of Appeal that predates Hardy?

(3) Does *Underwood* render the decision in *Hardy per incuriam*?

(A decision or dictum of a judge which clearly is the result of some oversight is said to have been given *per incuriam*.)

(4) If *Underwood* does not render the decision in *Hardy per incuriam*, is *Hardy* binding in this case or is *Hardy* distinguishable?

(Even where a precedent is binding a court may seek to "distinguish" it if it considers that to follow it would bring about an unjust result in the instant case, i.e. it may point out differences between the two cases which may be said to render the earlier decision inapplicable to the instant case; but this is legitimate only where the differences are material to the point in question.)

The *ratio* of *Hardy*

40. *Hardy* decided that no allowable loss arises for capital gains purposes where a deposit for acquisition of a property is lost due to the taxpayer defaulting on his obligations to make the full payment at completion, so triggering rescission of the acquisition contract. The UT

primarily decided this on grounds that the taxpayer had no relevant asset (and an allowable loss for capital gains tax purposes can only arise on disposal of an asset).

The *ratio* of *Underwood*

41. *Underwood* decided that where a taxpayer has two contracts with the same person (B), one to sell and the other to re-purchase the same piece of land, and settles those contracts by payment of the net excess of the re-purchase price over the sale price, no allowable loss for capital gains purposes arises to the taxpayer on the sale to B, as there is no disposal of the land to B.

Does *Underwood* render the decision in *Hardy per incuriam*?

42. Both parties in this case pointed to the fact that, in *Lloyd-Webber*, it was common ground, on the basis of the decision of the Court of Appeal in *Underwood* (which, it appears, was not cited to the UT in *Hardy*), that the decision in *Hardy* was *per incuriam* and not binding on the Tribunal in that case.

43. This view of the non-binding nature of Hardy is itself a decision of the FTT and so not binding on this Tribunal (but is of persuasive authority).

44. I note that the decision in *Lloyd-Webber* does not explain what it was about *Underwood* that renders *Hardy per incuriam*.

45. As *Hardy* is a decision of the UT on similar facts to those in this case, and therefore potentially binding on this Tribunal, I do not think it is legally sound for me to assume it is *per incuriam*, simply because the parties to this case both appear to have assumed that. For this reason I invited post-hearing submissions from the parties on this issue.

46. It seems clear to me that the *ratio* of *Underwood* (see [41] above) has no bearing on the *ratio* of *Hardy* (see [40] above), and certainly does not render *Hardy per incuriam*. What may be relevant in *Underwood* are judicial statements quoted at [35] above as they indicate that the taxpayer and B may have disposed of contractual rights under the contracts between them (even though, as the case decides, the taxpayer did not make any disposal of the land itself). In particular it is the following statements (the "**Statements**") that may be relevant to the question of whether *Underwood* renders *Hardy per incuriam*:

> (1) "To the extent that [B] turned an asset to account, the asset was its contractual rights under the [sale contract] to acquire the Property, and not its beneficial interest in the Property."
>
> (2) "Mr Soares, who appears for [the taxpayer], says his client disposed of the property to [B] by turning it to account on [the completion date]. In my view, that is not correct: if he turned anything to account, as against [B] on [the completion date], it was the [sale] contract."

47. The first of these Statements is clearly *obiter*, as it relates to the capital gains tax position of B (whereas the case was about the taxpayer's capital gains tax position). It is also tentative as to whether or not B did turn an asset to account – hence, the qualifying opening words, "*to the extent that* …"

48. The second of these Statements reflects the *ratio* of the decision in that it states that the taxpayer did not dispose of the property to B – but it is *obiter* as regards the taxpayer turning his sale contract to account, as the disposal of this contract was not part of the *ratio* of the decision. Also, like the first Statement, it is tentative as to whether or not the taxpayer did turn anything to account: hence the qualifying opening words, "*if he turned anything to account* …"

49. Subject to those reservations, I acknowledge that both Statements express the view that contracts to convey property, or the rights under those contracts, are capable of being turned to account in their own right (even where there is no disposal of the land that is the subject matter of the contracts).

50. Does this view clash with the decision on 'issue 1' in *Hardy*? *Hardy* acknowledged that contractual rights will be capital gains assets if they can be turned to account (see at [31]). *Hardy* then went on to say that the contractual rights acquired have to be analysed carefully – not every valuable right was necessarily an asset for the purposes of the capital gains tax legislation (see at [33]); and then said contracts for the sale of land do not create capital gains assets for the buyer distinct from the land itself, essentially because the right is contingent upon the buyer complying with his own contractual obligation to complete (i.e. pay) (see at [40]). I am not persuaded that the Statements clash with this analysis, essentially because the Statements do not address the specific question of whether contractual rights under land contracts are capital gains assets. (It is not surprising that *Hardy* probed further in its analysis of the capital gains status of land contracts than did *Underwood*: the point was mentioned in *obiter* and tentative terms in *Underwood*; whereas it was the heart of 'issue 1' in *Hardy)*.

51. Even if I am wrong about this – such that the view expressed in the Statements (see [49] above) does clash with the decision on 'issue 1' in *Hardy* – the Statements are in such tentative terms, and so clearly *obiter*, that I would be unable to conclude from this state of affairs that *Hardy* was decided *per incuriam* by reason of having overlooked *Underwood*.

52. I am therefore regrettably unable to follow the FTT in *Webber-Lloyd* in treating *Hardy* as having been decided *per incuriam*.

Is Hardy binding authority in this case?

53. The principal factual difference between this case and *Hardy* is that the benefit of the contract in *Hardy* was not assignable in any circumstances, whereas in this case the appellant was entitled to assign the benefit of the Contract, after payment of the deposit and stage payment.

54. However, this factual difference does not justify distinguishing *Hardy* from this case, as

(1) the decision on 'issue 1' in Hardy expressly considered the issue of assignability, and decided that it was not a significant factor i.e. the analysis applied equally to assignable, and unassignable, contracts (see at [42] of the decision); and

(2) in fact, the benefit of the Contract never became assignable, as the stage payment was never paid.

55. I conclude that *Hardy* is binding authority in this case – and so this appeal must be dismissed, as the rescission of the Contract, by reason of the appellant's repudiatory breach, did not constitute a disposal of an asset for capital gains purposes.

Alternative analysis

56. If I am wrong in the foregoing analysis – i.e. if the decision in *Hardy* <u>is</u> *per incuriam*, or if *Hardy* is <u>not</u> binding authority in this case – my decision would be as follows:

(1) I am not persuaded that *Hardy* was correct to say, as regards 'issue 1', that rights under a contract to acquire land are not assets for capital gains tax purposes;

(2) however, it is not necessary to reach a firm conclusion on this point because, even if they are, it is clear that a forfeited deposit of purchase money does not constitute the disposal of a capital gains asset: see s144(7) read together with s144(4). This was the analysis of 'issue 2' in *Hardy*, and I respectfully agree with it. Indeed, the FTT in *Lloyd-*

Webber was also in agreement that losses resulting from a forfeited deposit were excluded from relief as capital losses by these provisions (which did not apply on the facts before it, as *Lloyd-Webber* was not about a forfeited deposit) (see at [31] of *Lloyd-Webber*).

(3) I would thus have dismissed the appeal, even on this alternative basis.

CONCLUSION

57. The appeal is dismissed

RIGHT TO APPLY FOR PERMISSION TO APPEAL

58. 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.

ZACHARY CITRON
TRIBUNAL JUDGE

Release date: 17 JANUARY 2022