TC03073

Appeal numbers: TC/2012/10201 & 10360

Capital gains tax – share valuation – negligible value claim – whether shares originally had value – whether intention to create legal relations – valuation criteria – TCGA 1992 s24 – appeal dismissed

FIRST-TIER TRIBUNAL
TAX CHAMBER

ROGER DYER and JEAN DYER **Appellants**

- and -

COMMISSIONERS FOR HER MAJESTY'S REVENUE & CUSTOMS **Respondents**

TRIBUNAL: JUDGE MALACHY CORNWELL-KELLY
MARK BUFFERY FCA AIIT

Sitting in public at 45 Bedford Square, London, on 11 November 2013

Mr Roger Dyer represented himself and Mrs Jean Dyer

Ms Lynne Gray, of HM Revenue and Customs, for the Crown

DECISION

1 This appeal is against the decisions of the commissioners contained in closure notices issued on 6 September 2012 denying relief under the provisions of section 24(2) the Taxation of Chargeable Gains Act 1992 and section 132 of the Income Taxes Act 2007.

2 This followed a claim by the taxpayers under section 24 of the Taxation of Chargeable Gains Act 1992 that their shareholdings in JD Designs Limited had become of negligible value, and under section 132 of the Income Taxes Act 2007 for the capital loss arising to be set against their net income for the tax years ending 5 April 2008 and 5 April 2009, with the balance of any loss carried forward as a capital loss. The commissioners had accepted that the shares were of negligible value as at 26 January 2009, the date of the claim, but concluded that they were of negligible value as at 31 October 2007, the date of their acquisition by the taxpayers, and had not therefore "become" of negligible value.

Facts

3 We received a substantial volume of documentary evidence, which included a statement of agreed facts, and oral evidence from both Mr Roger Dyer for the taxpayers and Mr Gordon Wheeler for the commissioners. We regarded both witnesses as honest and straightforward. From the evidence given, we find the following facts.

Introduction

4 Beautiful Design Limited was incorporated on 24 September 2004 with one £1 ordinary share issued to Miss Jenny Dyer, the daughter of the taxpayers, who then changed the name to JD Designs Limited which we will refer to as 'the company'. A further 99 £1 ordinary shares were subscribed for, issued and were fully paid up by Miss Dyer on 14 December 2004, bringing her holding to 100 £1 ordinary shares, that is 100% of the company's then issued share capital. The company commenced trading on or about 1 April 2005, though there was some pre-trading activity noted in minutes of a meeting on 15 December 2004. Until late 2008 the company traded under the name 'Jenny Dyer London' with a total input in loans by the taxpayers and their family trusts of £800,000. But by 2009 it was being wound down and dissolved, and it was finally struck off the register on 31 August 2010.

The registered marks

5 The activities of the company were boutique fashion design and manufacturing of women's clothes, sometimes with associated jewellery, marketed under the registered marks of 'Jenny Dyer London', 'Jenny Dyer' and a stylised depiction of the letters 'JD'. The registered marks were, and still are, all held in Miss Dyer's name alone, following advice that she would thus best avoid a situation where she could lose control of her brand names. The first two marks were registered in respect of:-

> Class 14
> Jewellery; costume jewellery; precious metals and their alloys; precious and semi-precious stones; pins, badges, lapel pins, earrings, bracelets, cufflinks, tie racks, rings, watches, clocks and dials and stopwatches and other horological and chronometric instruments; watch straps, watch bracelets; wrist watches; smokers' articles and articles of precious metal or coated therewith.
>
> Class 25
> Articles of clothing, headwear and footwear, all included in Class 25
>
> Class 40
> Tailoring; dress making; custom manufacture of jewellery.
>
> Class 42
> Design of clothing, furnishings; design of jewellery.

6 The third mark was registered in respect of Class 14 in the same terms, and for classes 40 and 42:-

> Class 40
> Custom manufacture of jewellery.
>
> Class 42
> Design of jewellery.

7 We refer collectively to these registered marks, and to the brand recognition which was built up in connection with them, as 'the Intellectual Property'.

8 During the company's years of trading, Miss Dyer acquired a significant reputation in the fashion world and the evidence from various published sources is that 'Jenny Dyer London' in particular became a valuable mark and that Miss Dyer herself became well known and prominent in the fashion business. While we are not required to put a figure on it, we are satisfied that the Intellectual Property had achieved significant value by the time the shares the subject of this appeal were acquired by the taxpayers on 31 October 2007.

9 There was no written agreement between the company and Miss Dyer to use the Intellectual Property, nor any payment by the company for its use, and consequently no deduction claimed by the company in respect of it. It is not clear whether that situation was always contemplated because, in the minutes of a meeting on 15 December 2004 between Mr Roger Dyer, Miss Dyer and an accountant to discuss how the business would be run, it was envisaged that:-

> Basic structure is for ['Jenny Dyer London'] to become a trading division of a company e.g. JD Designs Ltd, which would then operate under licence from Jenny Dyer and to use her name. Eventually, a lawyer generated licence agreement would be required, in the meantime an internal letter would suffice setting out the conditions.

10 No agreement was ever made, and no letter of the kind suggested was ever written. In an email to her father written on 9 May 2013, Miss Dyer said with reference to the period 2007-08 that "during this period I made my name and designs freely available [to the company] as events before and after Oct 2007 show". A specimen sales invoice in evidence however contained printed conditions, among which was:-

> 13 Intellectual Property Rights
> The Company are the owners of and retain all and any intellectual property rights as may subsist in the Goods, accompanying literature, promotional material and printed matter, including but not limited to design rights, copyrights and rights in the nature of copyright whether or not registered or capable of registration, and all and any trademarks of the Company (Intellectual Property Rights). Any unauthorised use or representation of any of the Intellectual Property Rights or any part thereof will constitute an infringement of the rights of the Company which will seek all appropriate remedies and reliefs to which it may be entitled in respect thereof.

11 The expression "The Company" in these conditions was defined as "[name of supplier]"; the invoice itself did not give the company's name, showing the supplier as "Jenny Dyer London" – which leaves it unclear who the supplier actually was.

12 A specimen manufacturing contract was also in evidence and, making no mention of the company, was headed "Jenny Dyer London". Clause 1 provided:-

> 1 All JDL drawings, designs, patterns and other copyright works or intellectual property are the exclusive property of Jenny Dyer London and should be treated with the utmost confidentiality and not be passed onto any third party.

13 The contract was signed "For and on behalf of Jenny Dyer London", with no mention of the company. It was confirmed by Mr Dyer that the Intellectual Property in the form of the registered marks is still owned by Miss Dyer personally, had never been owned by the company and are due for renewal in the next year or so.

Employment position

14 At no stage did Miss Dyer have a written employment or service contract with the company and none was envisaged in the meeting of 15 December 2004. On 6 December 2010, Miss Dyer wrote in an email to Mr Roger Dyer:-

> You asked me to clarify the understanding I have of my relationship with JDL as you say the tax people are querying this in some way. I always saw myself as being irrevocably tied to JDL and indeed you might remember when you and mum converted some of your loan to shares we discussed whether to formalise my obligations to JDL – as I recall we decided there was no need as it was all within the family.
>
> Prior to this, when the Californians and also Simon made offers they made it clear that as part of any deal they would expect me to enter into a formal contract – this of course was not a problem. Subsequently, the same thing came up with KC [Ho] in early 2008 and I was happy to give this commitment which (sic) this was reflected in the draft agreement. However, we did not proceed with this after my move to [New York] later in the year . . .

15 Miss Dyer was a director of JD Designs Ltd and under the company's Articles of Association Miss Dyer was free to terminate that office in accordance with Article 26 by notice in writing. When Miss Dyer left the company, no written notice was given. A draft Business Plan dated January 2008 makes no mention of Miss Dyer's employment position beyond stating that she was the sole director and makes no mention of the company itself, referring throughout to as "Jenny Dyer London". Mr Roger Dyer's evidence was that at the date of the taxpayers' share acquisition:-

> Jenny and the family were at one in JDL at the key date and beyond. We also know that, as our daughter, Jenny could be relied upon to meet normal family obligations . . . Jenny also had a further reason to continue serving JDL. This was her position in one of the family trusts where she was legally obligated as one of the trustees to safeguard its loan to JDL.

Mr Dyer, giving evidence, said that Miss Dyer had had what he described as an oral *de facto* contract "on trust".

The acquisition of the taxpayers' shares

16 The "key date" referred to was 31 October 2007, when Mr Dyer acquired 310 shares in the company for £310,000 and Mrs Dyer acquired 40 shares for £40,000 at a premium of £999 per share. The issue of these shares represented the capitalisation of part of the £800,000 debt owed by the company to Mr and Mrs Dyer and their trusts. Following the issue of these shares the spread of shareholdings was that Miss J Dyer held 100 £1 ordinary shares, or 22.22%, Mr R Dyer held 310 £1 ordinary shares, or 68.89% and Mrs J Dyer held 40 £1 ordinary shares, or 8.89%.

Possible investors

17 In 2007 and 2008 the company made losses of £470,291 and £306,617, while in 2006 it had made neither a profit nor a loss. The company was unable to generate

sufficient cash flow to allow it to grow and consequently it had to turn to a total of £800,000 of funding provided by Mr and Mrs Dyer and their associated family trusts. From mid 2007, however, a number of unsolicited approaches were received which might have provided external investment.

18 The first was in May 2007 from a Mr Zak Bakare, who turned out to be the UK representative of a Californian branding company and interested in offering its marketing services to the company in exchange for equity. The approach was based on regarding the business as a worthwhile candidate capable of entering the American market with Mr Bakare's firm's support and, having researched the UK market looking to invest in British fashion designers, the Californian company had chosen Miss Dyer's business out of the seven they had interviewed. Their offer was not accepted.

19 The second was in October 2007 from a Mrs Stephanie Dorrence, a wealthy American married to the heir to Campbell soup fortune. It was in connection with Mrs Dorrence's interest that the Business Plan already referred to was prepared, but it transpired later that personal problems experienced by Mrs Dorrence meant that she was unable to commit to the company.

20 A Mr Simon Bernstein, the son of the well-known fashion designer Joan Bernstein, who had been acquainted with Miss Dyer for some while, heard of Mrs Dorrence's interest and asked Miss Dyer not to sell any equity without giving him a chance to invest. A meeting took place in which Mr Bernstein said he was looking to take a major stake in JD Designs Ltd, but resources to the extent needed were unlikely to be available and Mr Bernstein offered only £150,000. It was not pursued.

21 In 2005, a Mr K C Ho, a wealthy individual based in Singapore who was a personal friend and former client of Mr Roger Dyer, was approached by Mr Dyer to assist in sourcing manufacturers in China. Mr Ho was thus familiar with Miss Dyer and her work from that, and in January 2008 he indicated that he could be interested in taking a 49% equity interest in the business in exchange for an investment of £433,000 with a loan of £367,000, making £800,000 in total.

22 The effect would be to relieve Mr and Mrs Dyer of their outstanding financial commitment and they would withdraw from the shareholding leaving Miss Dyer with 51% of the share capital and Mr Ho with 49%. Steps were taken to proceed with this

proposal but it was to be based on a new company registered in Singapore. Draft agreements were prepared, but there is little evidence of how far the drafts progressed.

23 A draft agreement produced in the UK was not found to be satisfactory and in the papers, there is one completely blank template attached to an email from Mr Ho to Mr Dyer dated 7 August 2008 based on Singapore law, with a request for comment by Mr Dyer on it. There is nothing of substance further to indicate how the deal was envisaged or how it was being progressed, except that it is agreed that as part of the deal Miss Dyer would have been expected to enter into a formal contract with the new company.

24 Mr Ho wrote in August 2012, in response to a request from Mr Dyer to confirm the former's intentions in 2008, that:-

> I was delayed, as I remember, from our first discussions at the beginning of 2008, because of urgent business in China. I was however happy with the way the agreement was proceeding with Jenny and yourself. The exact form of my investment was not finalised by the time Jenny decided that her future lay in America as I had a number of alternatives available.

25 During June 2008 Miss Dyer met a Mr Andrew Rosen who had considerable interests in the fashion business in the United States. At first, Miss Dyer thought that Mr Rosen was a prospective investor in her business, but a personal relationship quickly developed between the two resulting in Miss Dyer leaving the UK to go to New York with Mr Rosen sometime in the autumn of 2008. The deal with Mr Ho was abandoned and the effect was to leave the company and its business rudderless. There was subsequently a report in the Wall Street Journal that Mr Rosen had persuaded Miss Dyer to close the business. The company was, as we have seen, wound down and eventually liquidated in 2009 and 2010.

Transfer of the company's shares

26 Article 11 of the company's Articles of Association provided for transfer of the shares outside the family circle or other existing shareholders and imposed very restrictive procedures, effectively giving the other shareholders rights of pre-emption to buy the shares at a value fixed by the company's auditors and giving the directors an absolute discretion to refuse to register any other transfer.

27 The Taxation of Chargeable Gains Act 1992 provides:-

> *24 Disposals where assets lost or destroyed, or become of negligible value*
>
> (1) 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.
(1A) A negligible value claim may be made by the owner of an asset ("P") if condition A or B is met.
(1B) Condition A is that the asset has become of negligible value while owned by P.
. . .
(2) Where a negligible value claim is made:
(a) This Act shall apply as if the claimant had sold, and immediately reacquired, the asset at the time of the claim or (subject to paragraphs (b) and (c) below) at any earlier time specified in the claim, for a consideration of an amount equal to the value specified in the claim.
(b) An earlier time may be specified in the claim if:
(i) the claimant owned the asset at the earlier time; and
(ii) the asset had become of negligible value at the earlier time; and either
(iii) for capital gains tax purposes the earlier time is not more than two years before the beginning of the year of assessment in which the claim is made; or
(iv) for corporation tax purposes the earlier time is on or after the first day of the earliest accounting period ending not more than two years before the time of the claim.
(c) Section 93 of and Schedule 12 to the Finance Act 1994 (indexation losses and transitional relief) shall have effect in relation to an asset to which this section applies as if the sale and reacquisition occurred at the time of the claim and not at any earlier time.

251 General provisions
(1) Where a person incurs a debt to another, whether in sterling or in some other currency, no chargeable gain shall accrue to that (that is the original) creditor or his personal representative or legatee on a disposal of the debt, except in the case of the debt on a security (as defined in section 132).
(2) Subject to the provisions of sections [132, 135 and 136] and subject to subsection (1) above, the satisfaction of a debt or part of it (including a debt on a security as defined in section 132) shall be treated as a disposal of the debt or of that part by the creditor made at the time when the debt or that part is satisfied.

(3) Where property is acquired by a creditor in satisfaction of his debt or part of it, then subject to the provisions of sections 132, 135 and 136 the property shall not be treated as disposed of by the debtor or acquired by the creditor for a consideration greater than its market value at the time of the creditor's acquisition of it; but if under subsection (1) above (and in a case not falling within section 132, 135 or 136) no chargeable gain is to accrue on a disposal of the debt by the creditor (that is the original creditor), and a chargeable gain accrues to him on a disposal by him of the property, the amount of the chargeable gain shall (where necessary) be reduced so as not to exceed the chargeable gain which would have accrued if he had acquired the property for a consideration equal to the amount of the debt or that part of it.
. . .

272 Valuation: General
(1) In this Act "market value" in relation to any assets means the price which those assets might reasonably be expected to fetch on a sale in the open market.
(2) In estimating the market value of any assets no reduction shall be made in the estimate on account of the estimate being made on the assumption that the whole of the assets is to be placed on the market at one and the same time.

. . .

273 Unquoted shares and securities

(1) The provisions of subsection (3) below shall have effect in any case where, in relation to an asset to which this section applies, there falls to be determined by virtue of section 272(1) the price which the asset might reasonably be expected to fetch on a sale in the open market.
(2) The assets to which this section applies are shares and securities which are not listed on a recognised stock exchange at the time as at which their market value for the purposes of tax on chargeable gains falls to be determined.
(3) For the purposes of a determination falling within subsection (1) above, it shall be assumed that, in the open market which is postulated for the purposes of that determination, there is available to any prospective purchaser of the asset in question all the information which a prudent prospective purchaser of the asset might reasonably require if he were proposing to purchase it from a willing vendor by private treaty and at arm's length.

28 The Income Tax Act 2007 provides:-

131 Share loss relief

(1) An individual is eligible for relief under this Chapter ("share loss relief") if—
(a) the individual incurs an allowable loss for capital gains tax purposes on the disposal of any shares in any tax year ("the year of the loss"), and
(b) the shares are qualifying shares.
This is subject to subsections (3) and (4) and section 136(2).
(2) Shares are qualifying shares for the purposes of this Chapter if—
(a) EIS relief is attributable to them, or
(b) if EIS relief is not attributable to them, they are shares in a qualifying trading company which have been subscribed for by the individual.
(3) Subsection (1) applies only if the disposal of the shares is—
(a) by way of a bargain made at arm's length,
(b) by way of a distribution in the course of dissolving or winding up the company,
(c) a disposal within section 24(1) of TCGA 1992 (entire loss, destruction dissipation or extinction of asset), or
(d) a deemed disposal under section 24(2) of that Act (claim that value of the asset has become negligible).
(4) Subsection (1) does not apply to any allowable loss incurred on the disposal if—
(a) the shares are the subject of an exchange or arrangement of the kind mentioned in section 135 or 136 of TCGA 1992 (company reconstructions etc), and
(b) because of section 137 of that Act, the exchange or arrangement involves a disposal of the shares.

The case law

29 A summary of the characteristics of the market to be hypothesised when valuing an asset was given by Hoffman LJ in the inheritance tax case of *IRC v Gray* [1994] STC 360 at 372:-

> The only express guidance which s 38 offers on the circumstances in which the hypothetical sale must be supposed to have taken place is that it was 'in the open market.' But this deficiency has been amply remedied by the courts during the century since the provision first made its appearance for the purposes of estate duty in the Finance Act 1894. Certain things are

> necessarily entailed by the statutory hypothesis. The property must be assumed to have been capable of sale in the open market, even if in fact it was inherently unassignable or held subject to restrictions on sale. The question is what a purchaser in the open market would have paid to enjoy whatever rights attached to the property at the relevant date (see *IRC v Crossman* [1937] AC 26). Furthermore, the hypothesis must be applied to the property as it actually existed and not to some other property, even if in real life a vendor would have been likely to make some changes or improvements before putting it on the market (see *Duke of Buccleuch v IRC* [1967] 1 AC 506 at 525). To this extent, but only to this extent, the express terms of the statute may introduce an element of artificiality into the hypothesis.
>
> [1994] STC 360 at 372In all other respects, the theme which runs through the authorities is that one assumes that the hypothetical vendor and purchaser did whatever reasonable people buying and selling such property would be likely to have done in real life. The hypothetical vendor is an anonymous but reasonable vendor, who goes about the sale as a prudent man of business, negotiating seriously without giving the impression of being either over-anxious or unduly reluctant. The hypothetical buyer is slightly less anonymous. He too is assumed to have behaved reasonably, making proper inquiries about the property and not appearing too eager to buy. But he also reflects reality in that he embodies whatever was actually the demand for that property at the relevant time.
>
> It cannot be too strongly emphasised that although the sale is hypothetical, there is nothing hypothetical about the open market in which it is supposed to have taken place. The concept of the open market involves assuming that the whole world was free to bid, and then forming a view about what in those circumstances would in real life have been the best price reasonably obtainable. The practical nature of this exercise will usually mean that although in principle no one is excluded from consideration, most of the world will usually play no part in the calculation.
>
> The inquiry will often focus on what a relatively small number of people would be likely to have paid. It may have to arrive at a figure within a range of prices which the evidence shows that various people would have been likely to pay, reflecting, for example, the fact that one person had a particular reason for paying a higher price than others, but taking into account, if appropriate, the possibility that through accident or whim he might not actually have bought. The valuation is thus a retrospective exercise in probabilities, wholly derived from the real world but rarely committed to the proposition that a sale to a particular purchaser would definitely have happened.

30 Further well established principles relevant emerge from the decided cases. First, that in case where there is a restriction on the transfer of shares in a company's articles the valuation is to proceed on the basis that the purchaser would be entitled to be registered as owner of the shares but would thereafter be subject to the restrictions on transfer: *CIR v Crossman* [1937] AC 26, and *Lynall v CIR* [1972] AC 680.

31 Second, that the open market hypothesis does not require the seller to be hypothetical but postulates a sale in the real world, and that it is an issue of fact whether the attributes of the actual seller would be taken into account in the market; it

is equally a question of fact whether there are any special purchasers and what, if any, premium they would be prepared to pay: *Walton v IRC* [1996] STC 68.

32 Third, that the valuation is at the valuation date looking forward into the future, and regard may be had to later events for the purpose only of deciding what forecasts could reasonably have been made: *Erdal v RCC* [2011] UKFTT 87 (TC), citing authority. And, lastly, that the relevant information reasonably required by the hypothetical purchaser is available to be supplied, the latter not being assumed to know more than the seller and to be taking the company in its actual state: *Marks v RCC* [2011] UKFTT 221 (TC).

Submissions

33 We include under this heading the 'expert' valuation opinions cited by each party. The taxpayers contended themselves with reference to existing commentaries, and the Revenue adduced the evidence of Mr Gordon Wheeler. Mr Wheeler is an officer of the commissioners' Share and Assets Valuation Office and a member of the Business Valuation Faculty of the Royal Institution of Chartered Surveyors. As such, Mr Wheeler is not an independent expert witness and indeed he had a minor involvement in the handling of this case; although Mr Wheeler is clearly well versed in valuation matters, his views are put forward on behalf of the commissioners and his opinions must be seen as those of an officer whose primary duty is to his employers.

For the taxpayers

34 The essential question addressed in Mr Dyer's argument was - what was the value of those shares at the date of their acquisition? He submitted that before the value could be ascertained, the position of Miss Dyer, as the creative driving force behind the company, together with the intangible assets - the copyright and trademarks in her name - had to be established.

35 The evidence from the various publication and news sources shown to the tribunal proves that 'Jenny Dyer London' was a well established and recognised brand throughout the fashion industry by October 2007 and that the business therefore had substantial value, which was certainly a great deal more than negligible, or nil. Any prospective purchaser of the company's shares would take account of the position that Miss Dyer had achieved and the extent to which her designs and products were admired and sought after.

36 In terms of Miss Dyer's relationship to the company, there was plainly a total commitment to it and its business; it was inconceivable that the business could have

been carried on between 2005 and 2008 without there being some kind of contract and the tribunal had sufficient evidence to infer from the circumstances the existence of a *de facto* oral contract between Miss Dyer and the company. The same went for the Intellectual Property owned by Miss Dyer which had always been made freely available to the company throughout its trading life; in the light of the commercial documents produced, it was proper to infer the existence of an informal licensing of the Intellectual Property to the company.

37 The hypothetical purchaser of the shares would therefore know that this was the case and that the brand name was of significant value. This was recognised by the three offers to invest before the relevant date, culminating in an accepted offer some three months after this date to purchase minority interest of 49% of Jenny Dyer London for a share and loan sum totalling £800000, leaving Jenny Dyer with 51%.

38 The hypothetical purchaser would thus be buying the benefit of the Intellectual Property and Miss Dyer's services as a result of acquiring the shares. In addition, the January 2008 Business Plan gives an overview of the company at the relevant date, its future prospects and therefore the existence of substantial value in Jenny Dyer London at 31 October 2007. Having regard to this, our contention is that the shares into which the loans were converted had a minimum market value of £350000, bearing in mind the accepted offer some three months after 31 October 2007 of £433000 plus £367000 of loans for a 49% minority holding.

For the Crown

39 Except for a small non-trading profit of £2,438 in 2006 (when the company did not make any sales and this figure represents net closing stock and work in progress), throughout its life the company suffered trading losses and struggled to generate sufficient cash flow to allow it to grow. The company therefore had to rely to a large extent on funding provided by the taxpayers and their family trusts.

40 From early 2007, a number of attempts were made to secure external investment, but none came to fruition. In January 2008, Mr K C Ho, a wealthy individual operating out of Singapore, was looking to take a 49% equity interest in exchange for an investment of £800,000 and as part of the deal Miss Dyer would have been expected to enter into a formal contract; his interest would have been through a new

company registered in Singapore. However, this was not completed by the time Miss Dyer decided that her future lay in America.

41 Mr Ho's first interest was expressed after the valuation date and as such represents inadmissible hindsight. Fiscal valuations refer to a specific point in time and the information which can be taken into account in the valuation process should be limited to what is known at that point in time. The benefit which can be gained through the knowledge of subsequent events must therefore be left out. Judicial authority for this comes from *Holt v IRC* [1953] where Dankwerts J said "It is necessary to assume the prophetic wisdom of a prospective purchaser at the moment of the death of the deceased and firmly to reject the wisdom which might be provided by the knowledge of subsequent events".

42 The three registered trademarks were all held in the name of Miss Dyer, purposely to avoid the situation where she could lose control of her name. It is acknowledged that there were no formal licensing agreements in relation to them, or any payment by the company for their use. At no stage did Miss Dyer have a formal employment or service contract with the company and the absence of a formal employment or service contract in relation to the services of Miss Dyer is significant. Miss Dyer did hold an office within the company, as the sole director and under the terms of the company's Articles Miss Dyer was free to terminate that office in accordance with Article 26 and by notice in writing, but no notice period was specified. No evidence has been supplied to suggest that Miss Dyer occupied any other specific role within the company.

43 The taxpayers accept that formal employment or service contracts would have been put in place if investors outside of the immediate Dyer family had entered the company's share register, and Mr Ho was insistent upon Miss Dyer entering into a formal employment contract for his investment to come to fruition and was not content to rely on the implied or oral contract said to be in place.

44 If an oral contract had existed it would be necessary to look at the conduct of the parties to establish its terms and the most significant element of such a contract would be the right to termination: when Miss Dyer took the decision to leave the company and join Mr Rosen in the United States, no evidence has been provided to indicate that she was required to give, or indeed did give, any notice of her intention to terminate her employment with the company. There seems to have been little regard to the company's indebtedness to her parents and the family trusts, or to their equity interests, and she effectively walked away from the company leaving it to fail. No

evidence has been provided to suggest that the taxpayers sought any form of redress through the courts in respect of any failure by Miss Dyer to fulfil any obligations she had to the company.

45 The driving force behind the business was Miss Dyer. The company's own business plan implies that she was the sole creative force within the business, with a totally free hand day to day in carrying out responsibilities for creating the design concepts, formulating collections, selecting materials to be used etc. There are numerous press articles and comments regarding Miss Dyer, her designs and how talented she is; the income generating component of the business was Miss Dyer, as she was the sole creative talented designer within the company. It was Miss Dyer who had the potential to drive the company forward; she was the 'Key Person'. The future value of the company would then, to a very large extent, be reliant upon her continuing presence.

46 The position at the valuation date was that the company had failed to generate any profits and went on to incur substantial trading losses; that, notwithstanding the capitalisation of the taxpayer's loans, it continued to carry a deficiency of shareholders' funds in excess of £400,000; that the driving force of the company, Miss Dyer is not tied into it within terms of an enforceable contract and had only a minority interest in the company's equity; and that the registered trade marks were held outside the company without any entitlement to their continuing use.

47 Christopher Glover, a chartered accountant and an independent share valuation specialist of more than 30 years, in his publication "Valuation of Unquoted Companies" said that "no purchaser would evaluate such a business on a going concern basis. He would pay no more than the shares would be worth on a liquidation". The new holder of the parcel of shares would not be in a position to ensure the retention of services of Miss Dyer nor would they be able to ensure the continuing use of various registered business marks.

48 The hypothetical purchaser would then hold shares in a company with little or no cash reserves, with a deficiency on the balance sheet in excess of £400,000, with no power to ensure the continuing services of Miss Dyer, the company's key employee, and with no power to ensure the continuing use of the businesses registered marks. It would be an equity interest that, to use the published words of Mr Glover, one would value at "no more than the shares would be worth on a liquidation". On a liquidation of J D Designs Ltd, there would be no distribution to its members, given the £400,000

deficiency on the company balance sheet. Therefore, the value of the 310 £1 ordinary shares and 40 £1 ordinary shares at 31 October 2007 is nil.

49 Mr Wheeler's submission was to the same effect. Firstly, postulating the sale of a 68.89% holding in the company, and treating the restrictions on transfer as being lifted for the purpose of the hypothetical sale but returning for the purchaser, secondly taking account of the position with regard to Miss Dyer, namely that in his view she had no obligation to the company either with regard to the Intellectual Property or her employment, and thirdly taking the situation as it existed at the valuation date, Mr Wheeler was also of the view that no buyer would pay more than the company was worth in a liquidation. Any hypothetical purchaser would insist upon legally enforceable rights both to the Intellectual Property and to Miss Dyer's services being established, which was not the case at the valuation date.

50 Mr Wheeler was in agreement with the advice given to Mr Dyer by his solicitors that a buyer would require: (i) an assignment of the rights to the Intellectual Property to the company with supporting warranties, or (ii) a perpetual exclusive royalty-free licence to the company of the Intellectual Property rights, and (iii) a service contract between Miss Dyer and the company tying her to it.

Conclusions

51 Part of Mr Dyer's representation was devoted to demonstrating how, in his submission, the commissioners had behaved unreasonably or failed to take relevant matters into account. It must therefore be emphasised that it is the not the function of the tribunal to pass upon the adequacy or otherwise of the commissioners' handling of a case prior to the appeal. The tribunal's jurisdiction is laid down by statute and does not extend, unless it is specifically so provided, to reviewing matters of administration leading to decisions under appeal. In a case such as this, the tribunal's only function is to resolve the issue between the parties as it has emerged in the appeal.

52 In doing so, we look first at the question of Miss Dyer's employment. It has been argued by the taxpayers that Miss Dyer was *de facto* an employee of the company on terms which must be inferred from the course of dealing over the years. In our view, this contention struggles to find any supporting evidence. The course of Miss Dyer's relations with the company was marked by the utmost informality which persisted right to the time of her leaving it in 2008, without notice of any sort and without so

much as a letter of resignation; so casual and informal was this final act, indeed, that we do not even have a date for it.

53 All the documentary references to Miss Dyer's dealings with the company are couched in the language of family relations: writing to her father in 2010 about the position when her parents became shareholders, Miss Dyer said "we discussed whether to formalise my obligations to JDL – as I recall we decided there was no need as it was all within the family", but that if the hoped-for outside investors had decided to invest she would have been happy to "enter into a formal contract". This understanding of matters was shared by Mr Dyer, whose evidence was that "Jenny and the family were at one in JDL at the key date and beyond. We also know that, as our daughter, Jenny could be relied upon to meet normal family obligations." Seeking to maintain that a contract existed, the most that Mr Dyer could say was that there was an oral *de facto* contract "on trust".

54 None of this evidence is consistent with an intention to create legal relations between Miss Dyer and the company. Testing the matter this way, if the company had wished to challenge Miss Dyer's departure, what terms or conditions could be pleaded in support? Or if Miss Dyer had been told by the company that her services were no longer needed, what case could she have mounted in response?

55 If a contract is to be implied from circumstances there must at least be an indication of what the employee's obligations are, how her remuneration is to be ascertained and in what circumstances the contract may be terminated. The position was left undefined and it was acknowledged that a contract tying Miss Dyer to the company would be needed if any outsider was to become a shareholder. In the absence of defined terms and conditions of any sort, we conclude that there was no contract between Miss Dyer and the company and that in its absence the hypothetical purchaser would not have proceeded with a purchase of the shares.

56 The position with regard to the Intellectual Property is just as clear. It is accepted that no assignment or licensing of the rights to the company took place and it is also accepted that it had to do so before an acquisition of the business could proceed; without that, the shares would not have been purchased by any buyer in the market who can be hypothesised. Such evidence as there is of the buying and selling documentation in fact used by 'Jenny Dyer London' leaves it unclear who it was who was the buyer or the seller, since no mention at all is made in the documentation of the company's existence.

57 A third party dealing with 'Jenny Dyer London' could not tell whether it was dealing direct with the owner of the registered mark; or whether the company was using the name as a trading style, since the normal reference in commercial documentation to that being the case was absent. There is nothing in the obscurity of the transaction documents, or in the company's accounting records, which entitles the tribunal to imply the existence of an oral licence or agreement to assign the rights, or to determine upon what terms they could be said to have been granted.

58 It is quite clear that any potential investor in the company would have required (either before investment or by way of a subscription agreement with the existing shareholders and directors) the company to have undisputed and unfettered rights to use the Intellectual Property, along with a firm contractual commitment from Miss Dyer to the company. Without these, the company was effectively worthless at the time of the investment by Mr and Mrs Dyer. The subsequent departure of Miss Dyer to the USA, leaving the company to founder and her parents to pick up the cost, clearly demonstrates why investors routinely require such safeguards.

59 In these conclusions we have considered the hypothetical possibility of a special purchaser who would not object to the twin defects we identify regarding the Intellectual Property and Miss Dyer's employment. The only such person or persons of which there is any possibility are Mr and Mrs Dyer themselves, and it is evident that they did not in fact object to these defects. The statutory hypothesis, as amplified by the authorities, however requires us to envisage a sale in the open market at arm's length to a buyer described by Hoffman LJ in *Gray* in these terms:-

> The hypothetical buyer is slightly less anonymous. He too is assumed to have behaved reasonably, making proper inquiries about the property and not appearing too eager to buy. But he also reflects reality in that he embodies whatever was actually the demand for that property at the relevant time.

60 There is no evidence that any buyer existed or might have existed whose attitude to the defects in the assets whose sale is hypothesised would resemble that of Mr and Mrs Dyer when acquiring the shares. Unhappily for Mr and Mrs Dyer, the appeals against the commissioners' determinations must therefore fail.

61 This document contains the full findings of fact and reasons for the decision. Any party dissatisfied with this decision has a right to apply in writing 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 the tribunal no 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.

MALACHY CORNWELL-KELLY
TRIBUNAL JUDGE

RELEASE DATE: 22 November 2013