[2020] UKUT 162 (TCC)

Appeal No: UT/2019/0106

PAYE and NIC – s471 of ITEPA 2003- the grant of a share option – whether option "available by reason of an employment" – appeal allowed

UPPER TRIBUNAL
TAX AND CHANCERY CHAMBER

Between

THE COMMISSIONERS FOR HER MAJESTY'S REVENUE AND CUSTOMS

Appellant

and

VERMILION HOLDINGS LIMITED

Respondent

Tribunal: **The Honourable Lord Ericht**
Judge Dean

Sitting in public at George House, 126 George Street, Edinburgh on 20 February 2020

For the Appellant: **Mr Roderick MacLeod, Advocate, instructed by the Office of the Advocate General for Scotland, for the Appellant (HMRC)**

For the Respondent: **Philip Simpson QC and David Pett, Barrister, instructed by French Duncan LLP for the Respondent (Vermilion Holdings Limited)**

DECISION

Introduction

1. An adviser to a company took an option over shares in the company instead of fees. The company came to be in financial difficulty. A rescue package was agreed with investors. The package was conditional on the adviser becoming director and executive chairman of the company and cancellation or amendment of the option. The adviser became director and executive Chairman and the option was cancelled and a new share option granted.

2. The issue in this case is whether the new share option falls within the provisions of sec 471 of the *Income Tax (Earnings and Pensions) Act 2003* ("ITEPA") to be treated as an employment-related securities (ERS) option for tax purposes.

Statutory Provision

3. Section 471 of ITEPA provides as follows:

"471 Share options to which this Chapter applies

(1) This Chapter applies to a securities option acquired by a person where the right or opportunity to acquire the securities option is available by reason of an employment of that person or any other person.

(2) For the purposes of subsection (1) 'employment' includes a former or prospective employment.

(3) A right or opportunity to acquire a securities option made available by a person's employer, or a person connected with a person's employer, is to be regarded for the purposes of subsection (1) as available by reason of an employment of that person unless–

(a)the person by whom the right or opportunity is made available is an individual, and

(b)the right or opportunity is made available in the normal course of the domestic, family or personal relationships of that person.

…

(5) In this Chapter–

'the acquisition', in relation to an employment related securities option, means the acquisition of the employment-related securities option pursuant to the rights or opportunity available by reason of the employment.

'the employment' means the employment by reason of which the right or opportunity to acquire the employment-related securities option is available ('the employee' and 'the employer' being construed accordingly), and

'employment-related securities option' means a securities option to which this chapter applies."

The facts of the case

4. The facts are set out in detail in the Decision of the First Tier Tribunal and can be summarised as follows.

5. In 2006, an exercise to raise equity funding for Vermilion Software Limited took place. As part of that exercise Vermilion Holdings Limited ("Vermilion" or the "Taxpayer") was set up. Vermilion was advised on the equity funding by Mr Noble and Dickson Minto WS. Mr Noble is a corporate advisory merger and acquisition and technology business specialist. He often works alongside management as a director cum investor. Dickson Minto WS is a firm of solicitors. Vermilion granted an option (the "2006 Option") in favour of Mr Noble's nominee company Quest Advantage Limited ("Quest"). It also granted an option in favour of Dickson Minto's nominee company (the "Dickson Minto Option"). These options were effectively payment for services which were provided in the process of the fundraising exercise.

6. However, by January 2007 Vermilion was in financial difficulty. As Mr Noble put it, Vermilion was "going to go bust." It was apparent that a further injection of new capital, as well as changes in management leadership, were required to rescue the company. A "Summary Report of Principal Legal Terms Relating to Rescue Funding Proposal" dated 9 March 2007 was prepared by Dickson Minto. (the "Rescue Funding Legal Summary")

7. The Rescue Funding Legal Summary set out the legal terms under which a consortium of investors would provide rescue funding to Vermilion.

8. It was a precondition of the rescue funding that Mr Noble would be appointed as chairman of the company. This precondition was set out in Section 3(viii) of the Rescue Funding Legal Summary:

   "Marcus Noble is to be appointed to the board as an Executive Chairman (we understand that, also as a condition of the Investment, Scott Carnegie was recently appointed to the board as Finance Director). Each of Mr Noble and Mr Carnegie will enter into appointment agreements with the Company, which will require, among other things, for them each to commit to devoting not less than 1-2 days per week of their time for the Company for the 12 months immediately following the entry into the Subscription Agreement. Each of them are to be paid £4,167 per month for their services.'"

9. In implementation of the pre-condition in clause 3(vii), Mr Noble was appointed as executive chairman of Vermilion from 16 March 2007.

10. Another pre-condition of the rescue funding was that the 2006 Option was cancelled or amended.

11. The 2006 Option and the Dickson Minto Option were dilution proof as they referred to a percentage of equity not a fixed number of shares. The other investors considered it unfair that Mr Noble and Dickson Minto would be getting a "free ride" if their options were not diluted along with the rest of the shareholders. Mr Noble and Dickson Minto conceded to this otherwise their options would have become worthless.

12. Section 3(ix) of the Rescue Funding Legal Summary states:

"(ix) the existing share option arrangements in respect of the Company [which is defined as Vermilion] are to be amended/cancelled as set out in Section 5 below of this Summary Report"

13. Section 5 states:

"At present, the Company is party to option agreements with 3 option holders which, conditional upon the Company achieving the First Equity Milestone, it is proposed are to be treated as follows:

(i) The Company has outstanding options granted to each of 22 Nominees Limited [ie the Dickson Minto Option] and Quest Advantage Limited [ie the 2006 Option] under 2 separate option agreements, each in respect of up to 2.5% of the issued equity share capital of [Vermilion] on the occurrence of an "Exit" (as defined therein). It is proposed that these option agreements are to be amended with the effect that each of these optionholders' entitlements will be diluted in line with the dilution of these option holders equity holdings in Vermilion following completion by the Consortium of the Investment, Such amended options will therefore be in respect of up to 1.5% of the issued equity share capital of the Company on an Exit. The diluted options will be in respect of F shares.

(ii) [deals with the third option holder and is not relevant to this appeal]"

14. Section 3(ix) provided that the 2006 Option was either to be cancelled or amended. Vermilion and Mr Noble chose to cancel the 2006 Option rather than amend it.

15. On 2 July 2007 Vermilion and Quest entered into an Option Agreement (the "2007 Option Agreement") granting the 2007 Option.

16. The 2007 Option Agreement provided that:
"2.2 No consideration shall be payable for the grant of the Option."

17. It further provided that:

"2.3 The existing option granted to the Optionholder by the Company and dated 1st February 2006 shall lapse with effect from the time that both parties have executed this Agreement."

18. It contained an "Entire Agreement" clause as follows:

"11.1 This Agreement contains the entire agreement between the parties or any of them with respect to the matters contemplated herein and shall supersede all prior offers, proposals, representations, agreements and negotiations relating thereto , whether written, oral or implied, between the parties or any of them or their respective advisers….."

19. At para 49 of the Decision, the FTT records an explanation as to why Vermilion and Mr Noble chose to cancel rather than amend. The explanation is given by Mr McDonald, the partner in Dickson Minto WS acting for Vermilion. The FTT states:

> "Mr McDonald's explanation was:
>
> '… variation agreements were not entered into at the time … as there was considerable time and financial pressure to complete the 2007 refinancing (as wages etc required to be funded) and having two documents rather than four was seen as simpler. There were already a very considerable number of documents given the significant amendments… The transaction bible for the 2007 refinance is bulky and again there was considerable pressure on fees….'"

20. The quotation from Mr McDonald at para 49 goes on to state:
"The consideration for the 2007 option was effectively the cancellation of the prior options which had been granted in 2006."

21. If Mr McDonald is expressing a view that as a matter of law the consideration for the 2007 Option was the cancellation of the 2006 Option, we do not agree. Clause 2.2 must be construed in accordance with its terms and the Entire Agreement clause. Clause 2.2 states in clear and unambiguous terms that no consideration is payable for the grant of the option. If the parties intention was that there was consideration and that the consideration was the cancellation of the 2006 Option they could easily have said so. We find as a matter of law that no consideration was payable for the grant of the 2007 Option.

22. In June 2016 Mr Noble's nominee company Quest novated the 2007 Option to Mr Noble. Mr Noble then exercised the 2007 Option in anticipation of the sale of the entire issued share capital of Vermilion to a subsidiary of a major listed US corporation on 8 November 2016.

Procedural history

23. On 17 August 2017 HMRC decided to assess Vermilion for income tax under PAYE and Class 1 National Insurance Contributions in relation to the 2007 Option exercised by Mr Noble in the tax year 2016–17.

24. The PAYE in the sum of £285,148.76 was assessed under regulation 80 of the Income Tax (Pay as You Earn) Regulations 2003 ('Regulation 80 Determination"). The NIC in the sum of £100,709.98 was assessed under s 8 of the Social Security Contributions (Transfer of Function etc.) Act 1999; ('Section 8 Decision'). There is no dispute as to *quantum*.

25. The First Tier Tribunal allowed the appeal. It found that the 2007 option was not an employment-related securities option for the purposes of sec 471 of ITEPA 2003. HMRC appealed to the Upper Tribunal.

The decision of the First tier Tribunal

26. The FTT identified that the single issue for determination was whether the 2007 option granted on 2 July 2007 when Mr Noble was already appointed as the director of Vermilion was an appointment-related securities option within the meaning of section 471 ITEPA (para 5).

27. The First-tier Tribunal found that the 2007 Option was not an employment-related securities option for the purposes of sec 471(para 145).

28. It did so for two reasons. Both of these reasons were under sec 471(3).

29. In respect of the first reason, the First Tier Tribunal addressed itself to the meaning of the phrase "by reason of an employment" in sec 471(3), and stated:

    "105. As a matter of fact, I find Mr Noble's directorship was not the *causa* for the grant of the 2007 Option, but for the same reason as Dickson Minto being granted a 2007 Option. Without their respective Supplier Options granted in 2006, neither Mr Noble nor Dickson Minto would have been granted (via their nominees companies) the right to the 2007 Options. The right to acquire the 2007 Option in each case emanated from the right under the Supplier Option received in 2006.
    106. The respondents would not dispute that these are the facts in relation to the 2007 Option either. However, their contention is that the deeming effect of s 471(3) means that the grant of the 2007 Option 'is to be regarded' as having been made available by reason of Mr Noble's directorship, despite any fact-findings to the contrary."

30. The Tribunal went on to say:

    "115. In the present case, I have found that Mr Noble's directorship was not the *causa* for the grant of the 2007 Option. On the other hand, by virtue of subsection (3), the 2007 Option was deemed to be made available by reason of Mr Noble's employment. An anomaly therefore arises, between a statutory fiction as a result of the deeming provision under subsection (3), and my finding of fact that the 2007 Option was not granted by reason of Mr Noble's employment."

31. The FTT held that the effect of the deeming provision under section 471(3) should be limited as a matter of statutory construction by de-coupling sub-section (1) and (3) (paras 128-140).

32. The second, and alternative, reason was that the deeming effect of sec 471(3) could be limited by considering who had "made available" the right or opportunity for Mr Noble to acquire the 2007 Option. The analysis of the underlying causes that led to the grant of the 2007 Option, and the economic mechanism whereby the 2007 option came to be granted, meant that Mr Noble's right to acquire the 2007 option was not "made available" by Vermilion as his employers. (para 141)

Submissions for the HMRC

33. Counsel for HMRC submitted that the FTT erred in its interpretation and application of section 471 on two grounds:

(i) by failing to give effect to the ordinary meaning of the words of sec 471(1);

(ii) by the finding that there was an anomaly in the "deeming provision" under section 471 (3) which, in effect created a further exception to the general rule under section 471(1).

34. In relation to the first ground, Counsel submitted that the starting point was to identify the ordinary meaning of the language used in the overall context of the legislation (*R* v *Secretary of State for the Environment, Transport and the Regions, Ex Parte Spath Holme Limited* [2001] 2 AC 349 at page 396). The express scope of section 471 was to identify the type of option to which chapter 5 of ITEPA applied and that scope was intentionally broad. Where a person acquired an option and the right to acquire it was available by reason of that person's appointment, section 471(1) was engaged and the option comes within the scope of Chapter 5 ITEPA. Where the conditions for 471(1) were met, it was not necessary to consider the provisions of sub-sections 2, 3 or 4. As the FTT had found that Vermilion had made available the 2007 option and accepted that Mr Noble was an employee, the FTT was bound to hold that the 2007 option came within section 471(1).

35. Counsel further submitted that the provisions of section 471(3) only act as a restriction on the broad application of section 471(1) where the defined exceptions in 471(3)(a) and (b) are met. The purpose of sec 471(3) was to clarify that where an employer has made an option available, it falls within the general rule of section 471(1) unless either of these exceptions apply. The FTT had erred by looking beyond the ordinary meaning of section 471(3) and considering the *causa* of the grant of the 2007 option. In so far as the FTT had adopted a purposive approach to interpreting section 471, it had erred (*WT Ramsay v IRC* [1982] AC 300; *Advocate General for Scotland* v *Murray Group Holdings Limited* [2018] SC(UKSC) 15, *Marshall (Inspector of Taxes)* v *Kerr* [1995] AC 739. *Steven Price (and others)* v *HMRC* [2013] UKFtT 297(TC) was not binding on the Upper Tribunal and in any event was distinguishable on the facts.

36. In response to Senior Counsel for the Taxpayer's argument that it was not open to HMRC to argue the first ground, Counsel for HMRC submitted that the first ground had been included in the Grounds of Appeal and referred to in the application for permission to appeal.

Submissions for the Taxpayer

37. Senior Counsel for the Taxpayer submitted that the substance of the transaction that created the 2007 Option was a reduction in Mr Noble's rights, notwithstanding that the form included the creation of new rights. The First-tier Tribunal had found in fact that the "right or opportunity to acquire" the 2007 option was "made available" because Mr Noble held the 2006 option, and was willing to surrender part of that to enable the respondent to receive the further funding it needed to survive. It was not "made available by" the respondent. Section 471(3) therefore did not encompass the facts of the present case. Even if it did, the 2007 Option should nonetheless be excluded from the scope of section 471(3). Deeming provisions were to be interpreted to limit their scope insofar as the literal reading would give rise to absurdity (*Murphy* v *Ingram* [1974] 1 CH 363 at 369F; *Marshall* v *Kerr* at 164, *Jenks Dickinson* [1997] SDC 853 at 862, *DCC Holdings (UK) Limited* v *HMRC* [2011] 1 WLR 44 at 57F. The purpose of section 471 was to

ensure that the rewards of employment were made liable to income tax and to prevent tax avoidance. The 2007 Option was not the rewards of employment: on the contrary it involved taking value away from Mr Noble. There was no suggestion of tax avoidance. It would be absurd if the 2007 Option were held to be within section 471(3) as it represented a reduction in Mr Noble's rights. Section 471(3) should be interpreted to prevent that absurdity.

38. In relation to the HMRC's first ground, Counsel further submitted that it was not open to HMRC to argue that the grant of the 2007 options was within section 471(1) without the need to rely on section 471(3) as this was a new point. In any event, HMRC's reasoning was that the 2007 Option was granted by Vermilion, Vermilion was the employer and therefore the 2007 Option made available by reason of his employment. There was a gap in that reasoning. Further, and in any event, the FTT's findings in fact precluded the conclusion that the "right or opportunity to acquire" the 2007 Option was granted by reason of Mr Noble's employment, and there was no challenge to these findings (*Hochstrasser* v *Mayes* [1960] AC 376 at 392; *Wicks* v *Firth* [1982] 1 CH 355 at 363F (CA) [1983] 2 AC 214 at 234(HL).

39. In relation to HMRC's second ground, Counsel submitted that (a) sec 471(3) did not apply on the facts of the case and (b) as sec 471(3) was a deeming provision it should be interpreted to avoid the absurdity that Mr Noble was in effect being taxed for having given up a previous reward from self-employment, which had been given up solely by the accident that a new option had been granted instead of amending the previous one.

Discussion and decision on the first ground: the meaning of sec 471(1)

40. The argument which HMRC advances under the first ground is that on the facts of the case the requirements of section 471(1) have been satisfied and section 471(3) does not apply.

41. In response Senior Counsel for the Taxpayer says firstly that it is not open to the HMRC to make that argument in this appeal and secondly that the argument is wrong on the merits.

Whether open to HMRC to advance first ground in this appeal

42. Senior Counsel for the Taxpayer categorises this case as being only about sec 471(3) and not about sec 471(1). This can be seen from his submission to the FTT, which is recorded in para 61 of the decision as follows:

"61. Mr Simpson submitted that the legal issue is whether the 2007 Option over 1.5% of the Company was 'made available by [Mr Noble's] employer' within the meaning of s 471 ITEPA. His submissions, as I understand them, focused on making the case that the 2007 Option was not 'made available' by Vermilion, as a matter of fact, and as a matter of law."

43. This is a submission only on sec 471(3). The words "made available" appear only in sec 471(3) and do not appear in sec 471(1). He is not recorded as having made any submission on sec 471(1).

44. The FTT accepted Senior Counsel's categorisation. The FTT's reasoning is to be found in paras 98-144. That reasoning proceeds under the heading "The application of the deeming provision under sec 471(3)". The FTT does not consider sec 471(1).

45. HMRC on the other hand has not categorised the case as being only about sec 471(3). It has addressed both sec 471(1) and 471(3).

46. In their letter of 14 December 2016 responding to the Taxpayer's clearance application, HMRC set out their position:

    "It is my view that the option granted on 2 July 2006 is not a securities option that falls within s471 ITEPA 2003 as it does not relate to an employment.

    However it is my view that the option granted on 2 July 2007 is an option that falls within s471 ITEPA 2003. The granting of the option does not meet any of the exceptions in s471(3) ITEPA, so the exercise of the option is a chargeable event within s477 ITEPA 2003"

47. That position is that same as that now being advanced under the first ground: the option falls within sec 471(1) as the exceptions in sec 471(3) (a) and (b) do not apply.

48. In their letter of 3 August 2017 informing the Taxpayer that they intended to make a Regulation 80 determination, HMRC states that its position is:

    "It is our belief that the 2007 option acquired by Mr Noble as a securities option made available by you as his employer. That option is to be regarded for the purposes of s471(1) as available by reason of his employment with you because s471(3)(a) and (b) does not apply to it."

49. We note that HMRC makes specific mention of sec471(1). Their position in that letter is exactly the position now being advanced under the first ground.

50. HMRC produced a Skeleton Argument in respect of the hearing before the FTT. HMRC's position in that Skeleton Argument is that the option falls under sec 471(1). The Skeleton Argument specifically mentions sec 471(1):

    "**Respondent's case**
    The non-statutory clearance request and the application of sec 471(1) ITEPA 2003
    …
    31. HMRC decided that the gain fell within the provisions of Chapter 5 Part 7 ITEPA by virtue of sec 417(1) ITEPA 2003."

51. In its Decision the FTT neither records nor addresses HMRC's submission on sec471(1). It does however record HMRC's oral submission on the deeming provision in sec 471(3) (para 74).

52. In its Application for Permission to Appeal HMRC states:

> "7. The Respondents submit that the deeming provisions of section 471(3) are only subject to the exceptions contained in paragraphs (a) and (b). As the said exceptions do not apply in this case..the Tribunal was therefore bound: (i) to find that the deeming provision was met; and thus (ii) to give effect to the provisions of section 471(1).
> 8. Accordingly, by failing to give effect to the provisions of section 471, the Tribunal erred in law"

53. These paragraphs are not particularly clear but they do make specific reference to sec 471(1) and to sec 471(3) (a) and (b) operating as exceptions.

54. In granting permission to appeal, the FTT did not limit the appeal to sec 471(3) but gave permission on sec 471(1). In para 8 the FTT stated:

> "These grounds [ie the grounds in the Application for Leave] seem to converge on the approach adopted by FTT in construing sec 471(3) ITEPA, and on the application of its interpretation of ss471(1) and (3) to the facts of the case. I consider that the Respondent's grounds of appeal, taken together, disclose an arguable point of law"

55. HMRC then lodged formal Grounds of Appeal. The formal Grounds of Appeal addressed both sec 471(1) (para 1) and sec 471(3) (para 2-3).

56. In these circumstances we are satisfied that it is open to HMRC to advance the first ground in this appeal. The FTT granted permission to appeal in respect of sec 471(1). In any event, sec 471(1) was put in issue by the HMRC letters of 14 December 2016 and 3 August 2017 and HMRC's Skeleton Argument and it is in the interests of justice that it is considered in this appeal.

The merits of the first ground

57. Turning now to the merits of the first ground, the starting point is the wording of section 471(1) which sets out the following definition:

> "This chapter applies to a securities option acquired by a person where the right or opportunity to acquire the securities option is available by reason of employment of that person or any other person."

58. There is an exception in sec 471(3) (a) and (b) where:
> "(a) the person by whom the right or opportunity is made available is an individual, and
> (b) the right or opportunity is made available in the normal course of the domestic, family or personal relationships of that person"

59. This exception does not apply in the current case, and so the focus is on the definition in section 471(1).

60. There are two elements to that definition.

61. The first element is “acquired by a person.”

62. It is notable that all that is required in order for an option to fall within this element of the definition is for the option to be “acquired”. There is no reference as to who the granter of the option is. There is no requirement for the operation of section 471(1) that the option is made available by the employer. That is a clear contrast to and difference from section 471(3) which sets out that it is a specific requirement for the operation of section 471(3) that the option is “made available by a person’s employer.”

63. The second element is that the right or opportunity to acquire the option is available “by reason of an employment.”

64. Nothing turns on the distinction between a director and employee as a directorship is treated as employment (s 5(1) ITEPA)

65. Guidance on how to approach the phrase “by reason of an employment” can be found in *Wicks* v *Firth.* That case concerned a situation where an employer, ICI, funded a trust which then gave education grants to the children of employees. The issue in the case was whether the employees were liable to income tax on the grants.

66. In discussing the meaning of section 61 of the *Finance Act 1976*, which referred to benefits being provided to the taxpayer or the taxpayer’s family “by reason of his employment” Denning MR said:

    "By reason of his employment"

    “It seems to me that the words "by reason of" are far wider than the word "therefrom" in section 181 (1) of the *Income and Corporation Taxes Act 1970* . They are deliberately designed to close the gap in taxability which was left by the House of Lords in *Hochstrasser v. Mayes* [1960] A.C. 376 . The words cover cases where the fact of employment is the causa *sine qua non* of the fringe benefits, that is, where the employee would not have received fringe benefits unless he had been an employee. The fact of employment must be one of the causes of the benefit being provided, but it need not be the sole cause, or even the dominant cause. It is sufficient if the employment was an operative cause - in the sense that it was a condition of the benefit being granted. In this case the fact of the father being employed by ICI was a condition of the student being eligible for an award. There were other conditions also, such as that the student had sufficient educational attainments and had a place at a university. But still, if the father's employment was one of the conditions, that is sufficient. If two students at a university were talking to one another - both of equal attainments in equal need - and the one asked the other "Why do you get this scholarship and not me?" He would say "Because my father is employed by ICI." That is enough. The scholarship was provided for the son "by reason of" the father's employment” (p363 C-F).

67. Watkins LJ agreed with Denning MR’s construction of section 61 (para 372 E)

68. Oliver LJ stated:

    “Speaking only for myself I do not, in the case of this legislation, find the philosophical distinction between a "*causa causans*" and a "*causa sine qua non*" helpful. I see no

reason why a benefit "derived" from the employment (to use the words of the chapter title) necessarily has to be invested with an intention on the part of the employer to remunerate the employee for the performance of his duties. One is directed to see whether the benefit is provided by reason of the employment and in the context of these provisions that, in my judgment, involves no more than asking the question "what is it that enables the person concerned to enjoy the benefit?" without the necessity for too sophisticated an analysis of the operative reasons why that person may have been prompted to apply for the benefit or to avail himself of it." (p370H -371B)

69. The decision of the Court of Appeal was reversed in the House of Lords on another ground. The only speech to address the meaning of "by reason of employment" was that of Lord Templeman who said, in the context of the particular statutory provisions applicable to that case:

"If the person [at whose cost the scholarship is provided] is not the employer then the employee is only to be charged with tax under section 61(1) [of the Finance Act 1976] if the scholarship was provided "by reason of his employment" that is to say if there is a relevant connection between the award of the scholarship and the employment" (p233H)

70. He went on to say:

"Your Lordships were invited by counsel for the taxpayers to express a view as to the meaning of the expression "by reason of his employment" for the purposes of section 61 [of the Finance Act 1976] and to determine whether tax would have been chargeable if the true construction of section 61 (3) had been different from that which I have indicated. I do not feel tempted to accept this invitation to decide a hypothetical question on the basis of a construction of the Act which I have rejected. Whether a benefit provided at the cost of a third party is provided by reason of his employment must depend on a variety of circumstances including the source of the benefit and the relationship, rights and expectations of the employer, the employee and the third party respectively. I decline to speculate." (p233H)

71. What we take from *Wicks* v *Firth* is that the phrase "by reason of employment" is to be given its ordinary meaning and must be considered in the circumstances of the particular case. We note also that the employment need not be the sole reason: it is enough that the employment was a condition of a benefit being granted.

72. The question which has to be decided in this case is whether the requirements of section 471(1) are satisfied in the circumstances of this case. In other words, whether on the facts of the case, the opportunity to acquire the 2007 Option was available by reason of the employment of Mr Noble.

73. This question is not specifically addressed by the FTT. The FTT does not address section 471(1). However the FTT does address the question of the meaning of "by reason of an employment" in the context of its discussion of sec 471(3). It does so under the heading "The application of the deeming provision under s471(3)" (para 98) and the subheading "The meaning of "by reason of employment" (paras 98-110).

74. The FTT quotes the *dicta* of Denning MR, including the part in which he explains that the fact of the employment need not be the sole cause but it is sufficient that it was a condition of the benefit being granted. It goes on to say:

"105. As a matter of fact, I find Mr Noble's directorship was not the *causa* for the grant of the 2007 Option, but for the same reason as Dickson Minto being granted a 2007 Option. Without their respective Supplier Options granted in 2006, neither Mr Noble nor Dickson Minto would have been granted (via their nominees companies) the right to the 2007 Options. The right to acquire the 2007 Option in each case emanated from the right under the Supplier Option received in 2006.

106. The respondents would not dispute that these are the facts in relation to the 2007 Option either. However, their contention is that the deeming effect of s 471(3) means that the grant of the 2007 Option 'is to be regarded' as having been made available by reason of Mr Noble's directorship, despite any fact-findings to the contrary."

75. In our opinion the FTT has erred in these paragraphs 105 and 106. We say so for three reasons.

76. Firstly, the FTT has erred in finding that "the respondents would not dispute that these [ie the "matter of fact" set out in para 105] are the facts" This constitutes speculation as to what HMRC "would" not dispute which is not based on HMRC's position as set out in its Skeleton Argument nor its oral argument as recorded by the FTT at paras 74-5. Indeed it is clear from these that the Respondent both would and does dispute these matters. HMRC's position in para 31 of the Skeleton Argument is that the 2007 Option falls within s471(1). There is nothing in the FTT's account of HMRC's oral submissions which would constitute a concession that s471(1) does not apply or that the case turns only on sec 471(3).

77. Secondly, the FTT has erred in categorising para 105 as a "matter of fact". In our opinion, it is a matter of mixed fact and law. It consists of the application of the law to the facts and circumstances of the case. It is a conclusion reached by applying the law. As an appellate tribunal, we would be reluctant to disturb the findings of the lower tribunal on matters of fact. However, where the finding is of mixed fact and law we are entitled to consider whether the lower tribunal has erred in law.

78. Thirdly, in our opinion the FTT has erred in law. It has failed to properly apply the guidance given in *Wicks* v *Firth*. In particular it has not applied the guidance in respect of how to approach matters where there is more than one cause. It has not properly applied the guidance of Denning MR that the fact of employment need not be the sole cause or even dominant cause, and that it is sufficient that the employment was a condition of the benefit being granted.

79. At around the time when the 2007 Option was granted Vermilion was in grave financial difficulty. It was about to go bust (FTT decision para 36). The 2006 Option was worthless (para 45). A change of management leadership was required to rescue the Company (para 36). A rescue package was put together. That package was conditional *inter alia* on
    (a) Mr Noble becoming Executive Chairman and devoting not less than 1-2 days per week to Vermilion (Para 3(i) of the Summary Report of Principal Legal Terms)

(b) The 2006 Option being "amended/cancelled" (para (ix). Vermilion and Mr Noble chose to cancel and issue a new option rather than amend.

80. In these circumstances, it seems to us that there was more than one reason why the 2007 Option was granted to Mr Noble. One reason was that there was an existing 2006 Option which could no longer continue in its current form. Another reason was that the 2007 Option was part of a package of measures which included the employment of Mr Noble.

81. The employment of Mr Noble and the grant of the 2007 Option are two of the conditions of the rescue package. The grant of the 2007 Option was conditional on the other conditions (including the employment of Mr Noble) being satisfied before it could go ahead. It was thus a condition of the granting of the 2007 Option that Mr Noble was employed by Vermilion. Accordingly the test set out by Denning MR was met: employment as director was an operative cause in the sense that it was a condition of the option being granted.

82. For these reasons, in our opinion the grant of the 2007 Option was available by reason of Mr Noble's employment. Accordingly, in terms of sec 471(1), the 2007 Option was an option to which Chapter 5 ITEPA applies.

83. Before leaving this part of our opinion, we would comment on two particular arguments made by Senior Counsel for the Taxpayer, albeit that he did so under reference to sec 471(3).

84. Senior Counsel emphasised that the 2007 Option would not have been granted if instead the 2006 Option had been amended. However, we require to proceed on the documentation that the parties chose to enter into, not alternative documentation which they could have been entered into but chose not to.

85. Senior Counsel also emphasised that the 2006 Option had been granted for the value of consultancy services and the 2007 Option was part of the value that Mr Noble had already earned through these services. We do not find this argument persuasive. Immediately prior to the rescue package the 2006 Option was worthless. Mr Noble had already lost the value he had earned through consultancy services. However, under Mr Noble's executive chairmanship from 2007 onwards the performance of Vermilion and the value of the 2007 Option both improved to such an extent that the gain on the exercise of the 2007 Option in 2016 was £636,238.

Discussion and decision on the second ground: the "deeming" provision in sec 471(3)

86. The Decision of the FTT on the "deeming" provision in sec 471(3) (including the alternative finding in para 141 of the FTT decision), is predicated on the 2007 Option not falling within sec 471(1). Issues of deeming only arise when the option does not fall within sec 471(1). As we have held that the 2007 Option falls within sec 471(1) it is not necessary for us to consider the second ground.

Decision

87. For these reasons, the appeal is allowed. The 2007 Option is an employment-related securities option for the purposes of section 471 of ITEPA 2003.

Lord Ericht

Judge Dean

Decision released: 27 May 2020