

5 Stone Buildings

When is CGT payable on the settlement of Chancery litigation?

Harry Martin

30 July 2021

www.5sblaw.com

Overview

- Rights to sue
- Rights to an unadministered estate

Rights to sue - where are we now?

Principles

- A right to sue is an asset for CGT purposes.
- A right to sue is usually acquired for £nil.
- A right to sue is disposed of when a court judgment is entered or a settlement is reached.
- The consideration for the disposal is the value of the judgment or settlement.
- CGT may therefore be payable on the entirety of the judgment sum or settlement sum.
- HMRC operate a concession whereby the first £500,000 is not charged to CGT.

Rights to sue

What is an 'asset' for CGT purposes?

- Section 21(1) TCGA:

“All forms of property shall be assets for the purposes of this Act, whether situated in the United Kingdom or not, including-

(a) options, debts and incorporeal property generally ...”
- Section 22(1) TCGA:

“... there is for the purposes of this Act a disposal of assets by their owner where any capital sum is derived from assets notwithstanding that no asset is acquired by the person paying the capital sum, and this subsection applies in particular to -

... (c) capital sums received in return for forfeiture or surrender of rights, or for refraining from exercising rights”
- *O'Brien v Benson's Hosiery* [1980] AC 562: per Lord Russell “*something which he can turn to account*” or per the Crown “*all forms of rights upon whose disposal a capital sum may be received*”.

Rights to sue

Zim Properties v Proctor [1985] STC 90

- Zim claimed against its solicitor in negligence: alleged lost a profitable sale of land because the sale contract was badly drawn. The solicitor settled the claim for £69,000.
- Warner J held that:
 - The right of action constitutes an ‘asset’ for CGT purposes.
 - The £69,000 payment was derived from the right of action, not from the land which was the subject of the sale.
 - Zim acquired the right of action when the defective sale contract was entered into. It was deemed to have acquired the right at its market value at that time. (N.B. the timing point is possibly wrong, and the ‘deeming’ provision was removed with effect from 1981).
 - Zim was therefore liable to CGT on £69,000, with an allowance in respect of the market value of the right of action at the time of contracting.

Rights to sue

Acquisition value

- Section 17 TCGA
 - “(1) ... a person’s acquisition ... of an asset shall for the purposes of this Act be deemed to be for a consideration equal to the market value of the asset -
 - (a) where he acquires ... the asset otherwise than by way of a bargain made at arm’s length ...”
 - (2) Subsection (1) shall not apply to the acquisition of an asset if -
 - (a) there is no corresponding disposal of it, and
 - (b) there is no consideration in money or money’s worth ...”
- Subsection (2) first introduced by S. 90 of the Finance Act 1981 to counter reverse *Nairn Williamson* arrangements (later consolidated in the TCGA).

Rights to sue

Other caselaw

- *Davis v Powell* (1977) - no charge, pre-dated 1981
- *Davenport v Chilver* (1983) - charge, pre-dated 1981
- *Drummond v Austin Brown* (1985) - no charge, pre-dated 1981
- *Gadhavi v HMRC* (2018) - charge
- *Robinson v HMRC* (2019) - charge

Rights to sue

Extra Statutory Concession D33 - the past

- First published in 1988 (4 years after *Zim*).
- *Zim* reversed (probably) by a concession re: rights of action derived from underlying assets.
- Where there is no underlying asset, the disposal of the right was, by concession, exempt from CGT.

Rights to sue

Extra Statutory Concession D33 - the present

- From January 2014:
 - Concession limited to first £500k of gain.
 - Possibility of asking HMRC for a further concession (N.B. right of action must be “acquired in connection with goods or services”)

Rights to sue

Extra Statutory Concession D33 - the future

- HMRC now considers D33 to be beyond the scope of its discretion.
- 2014-2015 consultation:
 - Put concession on a statutory basis.
 - Increase £500k concession to £1m, with no ability to apply for an increase.
 - “Before determining the next course [of] action it is the government’s intention to discuss the issues in more detail with those respondents to ensure that the concerns they raised are fully understood.”
- A dog’s dinner!

Rights to sue - Example

Example (1)

- Example: Boris dies leaving his entire estate to Carrie. His son, Milo, brings a 1975 Act claim against Carrie. Carrie settles the claim by paying £1m to Milo.
- Milo may be liable to pay CGT on £500k of the payment.
- Is it fair that Milo's award (calculated to provide for his maintenance) is subject to CGT?

Rights to sue - Example

Example (2)

- **How could Milo improve his position?**
 - Is a claim under the 1975 Act an “asset” for CGT purposes?
 - Check whether or not Milo is UK resident.
 - Read the settlement back for CGT purposes.
 - Seek a gross settlement sum.

Rights in an unadministered estate

Example - facts

- Boris' purported last will leaves his property to Carrie. Dom claims that the will is invalid, and relies on a prior will which gives the property to him. Carrie settles Dom's claim by a deed of variation which gives half of the property to Dom.

Rights in an unadministered estate

Example - reading back

- If the deal is done within two years of Boris' death, Carrie may seek to read back the variation under s.62(6) TCGA 1992.
- Query whether the variation falls foul of the prohibition on extraneous consideration (s. 62(8) TCGA 1992).

Rights in an unadministered estate

Example - estate administration complete

- If the estate administration is complete and there is no reading back, Carrie makes a disposal of 50% of the property.
- There may not be much CGT to pay:
 - Only potential for CGT on the post-death gain.
 - Carrie may have allowances or exemptions available.

Rights in an unadministered estate

Example - estate administration incomplete (1)

- If the estate administration is ongoing when the deal is done, Carrie has no interest in the property. She has only a right to have the estate properly administered and to have the funds/assets paid/transferred to her at the conclusion.
- One possibility is that Carrie disposes of part of this ‘administration right’ to Dom. As Carrie acquired this right for £nil, the consideration given by Dom will be pure gain.

Rights in an unadministered estate

Example - estate administration incomplete (2)

- HMRC appears to take a different, taxpayer friendly, analysis.
- Carrie disposes of the future proceeds of her ‘administration right’ (i.e. her future right to half of the property).
- When the property vests hindsight is applied to enable a CGT computation to be prepared.
- Carrie will pay CGT only on the difference between the value of 50% of the property at Boris’ death and the consideration provided by Dom.
- HMRC’s view appears to be based upon the erroneous assumption that Carrie is not able to dispose of her ‘administration right’.

Rights in an unadministered estate

Key takeaway

- Treat non-retrospective variations during the administration period with great caution!

5 Stone Buildings

Thank you,
any questions?

t 020 7242 6201

w www.5sblaw.co.uk

 [@5sblaw](https://twitter.com/5sblaw)