

CAPITAL GAINS TAX - Gift of unquoted shares by donor to his children - Failure of donor to notify Inland Revenue of gift of shares in his return - Extended time limit assessments raised by Inland Revenue - Whether donor's failure to notify amounted to negligence - Valuation of those shares - Section 36 Taxes Management Act 1970; sections 150 and 152 Capital Gains Tax Act 1979

THE SPECIAL COMMISSIONERS

LEONARD KAY BILLOWS Appellant

- and -

MRS GILLIAN ANNE HAMMOND

(HM INSPECTOR OF TAXES) Respondent

Special Commissioner: MR T H K EVERETT

Sitting in London on 26, 27 and 28 July 2000

The Appellant appeared in person

Mr Christopher Tidmarsh of Counsel, instructed by the Solicitor of Inland Revenue, appeared for the Respondent

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DECISION

Mr Leonard Kay Billows ("Mr Billows") appeals against an assessment to capital gains tax for the year ended 5 April 1987 in the estimated sum of £205,000. That assessment was made more than six years after the end of the relevant tax year and accordingly was made pursuant to the provisions of section 36 Taxes Management Act 1970.

1. The assessment was made following a gift of unquoted shares in his company Billows Ltd to each of his two children in December 1986.

The questions for my determination are as follows:

1. Following the gift of the shares to his children was Mr Billows guilty of negligent conduct resulting in a loss of tax to the Crown?

2. If the answer to question one is in the affirmative, what was the value of the shares transferred by Mr Billows to his son and daughter, at the date of the transfer?

2. The evidence before me consisted of the sworn testimony of the following persons:

(a) Mr Billows

(b) Mrs Avril Whitfield, HM Inspector of Taxes. Whilst working at the Milton Keynes District Tax Office between March 1986 and August 1997, she dealt with Mr Billows' capital gains tax file.

(c) Mr Michael Alan Fowler, HM Inspector of Taxes. He is an employee of the shares valuation division of the Inland Revenue's Capital Taxes Office and attended a meeting with Mr Billows at the premises of Billows Ltd in company with two colleagues from the share valuation division on 11 April 1996. His note of that meeting was annexed to his witness statement.

3. I also received sworn evidence of opinion from Mr Thomas Frame Vassie, A chief examiner in the shares valuation division of the Inland Revenue Capital Taxes Office.

4. The witness statements of each of the four witnesses will be available to the Court should this appeal proceed further.

5. In addition to the oral testimony I received two bundles of documents put in evidence by the Inland Revenue and one bundle of documents put in evidence by Mr Billows. Lengthy negotiations between the parties covering the period from 1996 to the date of the appeal hearing produced little, if any agreement between them. Mr Billows for his part maintained that the shares had very little, if any value at the date of the transfer from him to his children, whilst the Inland Revenue maintains that their intrinsic value was significant.

6. Mr Billows is an elderly gentleman who suffers from deafness. Prior to the appeal hearing he had mislaid his hearing aid. On this becoming apparent on the first morning of the appeal I indicated to him that if he wished to apply for an adjournment until such time as he had replaced his hearing aid, I would consider such an application sympathetically. I record this offer in my decision as on several occasions during his submissions Mr Billows complained that he had had very little time to prepare his case as a copy of Mr Vassie's witness statement, giving his opinion as to the value of the shares transferred reached him only a few days before the appeal hearing. On each occasion I renewed my suggestion to Mr Billows that he should apply for an adjournment, but on each such occasion he refused to make such an application and indicated that he wished the appeal hearing to continue without an adjournment.

7. Insofar as it was possible, arrangements were made within the courtroom, by a re-arrangement of the furniture, for Mr Billows to be aware of what was being said by witnesses, by Mr Tidmarsh and by myself. In addition, his daughter Mrs Buckley and the company accountant Mr Christopher Coote seated on either side of Mr Billows in the courtroom explained to him any points of difficulty which he encountered owing to his poor hearing. I am satisfied that in all the circumstances, Mr Billows was fully aware of what was taking place in the courtroom and did not suffer because of his disability and was enabled to respond to the Inland Revenue's submissions to the best of his ability.

The facts

From the evidence before me I find the following relevant facts:

1. Billows Ltd ("the Company") was incorporated on 26 September 1972. Its accounting year ends on 30 April in each year and its first period of trading covered the period from 26 September 1972 to 30 April 1973.
2. The Company capital at all times has been represented by 1,000 ordinary shares of £1 each.
3. On incorporation 700 shares were issued to Mr Billows and 200 shares were issued to his wife, Mrs M J Billows. The remaining 100 shares remained unissued.
4. At or prior to incorporation the Company acquired the assets of an earlier company operated by Mr Billows, namely Billows Graphic Equipment. Those assets included the following:

Plant and machinery £8,995

Motor vehicles £3,340

Special tools and jigs £1,605

Office equipment fixtures and fittings £1,536

(The above figures (which differ in some respects from those shown in Mr Billows' witness statement), are taken from the balance sheet of the Company's opening accounts to the period ended 30 April 1973.)

5. There is no evidence that Mr Billows' shares were issued partly or wholly in return for the acquisition by the Company of the assets of Billows Graphic Equipment. The Company accounts do not contain a share premium account and the Company's return of allotments shows that 898 shares were issued for cash at par. Whilst the return of allotments was made by Mr Billows' accountants, the Company accounts were approved and signed by Mr Billows and his wife.
6. Mr Billows had previously been a major shareholder in another company which carried on a similar trade to that of Billows Ltd, namely Protocol Engineering Ltd ("Protocol"). Before setting up the Company Mr Billows sold his shares in Protocol and left its employment. Some other employees left with him and joined him as employees of his new company.
7. On 28 March 1983 the 100 unissued shares in the Company were allotted to Mr Billows' children. 50 of those shares were allotted to Mrs Sandra Jean Buckley, Mr

Billows' daughter and the remaining 50 to his son Mr Colin David Billows. At about the same time Mrs M J Billows transferred her 200 shares to her children, giving 100 shares to her son and 100 shares to her daughter. Mrs Buckley and her brother are employed full-time with the Company.

8. On 4 April 1986 Mr Billows gave 10 of his shares to his son and a further 10 of his shares to his daughter.

9. In his tax return for the year 1986/87, which he signed on 5 March 1987, Mr Billows gave details of those transfers to his children on 4 April 1986 to the Inland Revenue and stated that the amount of his gains for the year was "none".

10. On 16 December 1986 Mr Billows gave a further 339 of his shares in the Company to his son and a further 339 of his shares in the Company to his daughter. Since 16 December 1986 the shareholdings in the Company have remained unaltered. Of the 1,000 issued shares, Mr Billows retains 2 shares and his son and daughter each hold 499 shares.

11. Mr Billows completed his tax return for 1987/88 on 14 August 1990 and it was received by HM Inspector of Taxes on 23 August 1990. In the section of that return dealing with "chargeable assets disposed of" Mr Billows wrote "none". He sent his return for 1987/88 under cover of his letter dated 21 August 1990 addressed to HM Inspector of Taxes Milton Keynes 1. At the same time he also enclosed his tax returns for the years 1988/89, 1989/90 and 1990/91. The covering letter makes no mention of his transfer of shares to his children on 16 December 1986 or any other date.

12. On 10 January 1991 the Inland Revenue wrote to Mr Billows, referring to his tax returns for the years 1987/88 to 1990/91 inclusive. The letter reported that the Company's accounts for the accounting period ended 30 April 1987 revealed a transfer of 698 shares in total to his children. The letter requested an explanation as to why appropriate entries were not made in Mr Billows' tax return.

13. It appears that nothing happened for a year but on 10 January 1992 the Inland Revenue sent a reminder to Mr Billows seeking a reply to the Inland Revenue's letter dated one year previously.

14. Mr Billows eventually replied on 6 February 1992 in a letter which was received by the Inland Revenue on 10 February 1992. It stated:

"I am in receipt of your letter dated 10 January.

The transfer of shares was done by my accountant of the time Everett Collins & Loosley who I understood supplied all the information to the Revenue. From your letter it appears it was either not done or the information has been misplaced.

You will appreciate that as I did not handle the transfer I have no records of the transaction. Would you therefore please supply me with details of any records of the transfer that you have with all the information necessary to make the calculations you require. I am not an accountant and I am not familiar with the basis of the figures involved."

15. On 16 March 1992 the Inland Revenue wrote again to Mr Billows stating that the Company accounts did not include any specific details regarding the transfer of the shares in question. The only information in the accounts was that at 30 April 1986 Mr Billows owned 700 shares in the Company and that a year later he owned 2 shares and that his son and daughter each owned 499 shares. The letter concluded by requesting Mr Billows to inform the Inland Revenue of the value of the shares at the date of their disposal and their original cost.

16. Having received no reply to their letter the Inland Revenue sent a reminder to Mr Billows on 18 September 1992.

17. Mr Billows eventually replied on 13 October 1992 in a letter which was received by the Inland Revenue on 15 October 1992. It states:

"Your letter of 16 March referred to in your letter dated 18 September 1992 did not fully answer my letter dated 6 February 1992.

My letter of the 6th requested from you "all the information necessary to make the calculations you require". This was not received.

I have no information regarding the formula to be used in assessing the value of a private company as used by the Revenue. If you supply the formula I am quite capable of using it.

I would inform you that the shares were transferred by me for which no payment was made so no sale value was obtained. Also my accountant considered the shares had no free market value so no CGT would be payable.

In view of the opinion of the accountant and my own view of the Company value I have therefore not been surprised that no correspondence was received from the Revenue at the time of the transfer or subsequently and the following years' accounts were sent to the Revenue which showed the transfer.

I do not believe that the transaction gave rise to a liability to CGT but on receipt of your basis for calculation I will respond to clear this matter which I was previously informed by my accountant had been cleared."

18. The Inland Revenue responded by letter to Mr Billows on 10 November 1992 quoting section 18 Taxation of Chargeable Gains Act 1992 and seeking further information in order to enable the Inland Revenue to assess the value of the shares transferred.

19. Mr Billows wrote again to the Inland Revenue on 2 December 1992 and for the first time he gave details of the transfers of the shares to his children in December 1986. His letter states as follows:

"I am in receipt of your letter dated 10th Nov. 1992.

I am not aware of Section TGCA 1992 so cannot base any calculations on that Section you say is applicable. Would you please send me the relevant information. I have asked you twice to supply me with the necessary basis you wish me to use to comply with your request to supply a valuation.

As you are "not privy to their method of calculation" would you please request them to send the formula to me?

The answers to your questions are as under which I have extracted from the audited accounts and the filed "Annual Returns".

1. 700
2. 20 on 4.4.86 and 678 on 15.12.86
3. & 4. Please supply a basis of calculation

Referring to leaflet CGT 16 you have sent to me it would appear that the important question is what is the difference in value of the Company shares between 1982 and 1986. The Company made a profit of £35,374 in 1982 and £22,912 in 1986. On this basis of profit to value of the Company shares most people would say that there was no capital gain to be deemed on shares that returned £35,374 in 1982 and £22,912 four years later.

I would therefore on a commercial basis consider that the realisable value of my shareholding was less in 1986 than it was in 1982 - there being no capital gain in the relevant period - presumably a notation or loss.

I believe the foregoing to be a reasonable assessment of the position which is in accordance with the advice I had at the time "that no Capital Gains Tax" was applicable to the share transfer.

Other factors may be relevant i.e. my age at the time of the transfer 62-63.

I look forward to your assessment and any comment from your colleagues at the Shares Valuation Division if you think it necessary."

20. On 10 May 1994 Mr R A Knight of the Inland Revenue Shares Valuation Division wrote to the Inspector of Taxes with his estimated values per share representing his current opinion based on the Company's accounts. He had not been able to reach any consensus with Mr Billows. Mr Knight's estimated values were as follows:

20 x £1 ords @ 4 April 1986 - £15 per share

698 x £1 ords @ 4 April 1986 - £135 per share

679 x £1 ords @ 15 December 1986 - £450 per share

698 x £1 ords @ 15 December 1986 - £450 per share

21. On 6 June 1994 the Inspector of Taxes assessed Mr Billows to capital gains tax pursuant to section 36 Taxes Management Act 1970. The assessment was for the year ended 5 April 1987 and was made in the estimated sum of £205,000. In support of the assessment the Inland Revenue alleged negligent conduct on the part of Mr Billows and that the assessment was made for the purpose of making good to the Crown the loss of capital gains tax attributable to Mr Billows'

negligent conduct. The Crown does not allege fraudulent conduct on the part of Mr Billows.

22. During the six years which have elapsed since the issue of the assessment negotiations have continued between the Inland Revenue and Mr Billows but it has proved impossible to reach agreement as to the value of the Company in 1986 or the value of the shares transferred during that year.

23. As part of its effort to reach agreement with Mr Billows the Inland Revenue officers attended a meeting with Mr Billows (and briefly with his daughter) at the offices and factory of the Company on 11 April 1996. The Inland Revenue was represented at that meeting by Mr Fowler who gave evidence before me, Mr Knight (the author of the letter dated 10 May 1994) and a third inspector named Mr Richardson.

The visit produced no meeting of minds between the Inland Revenue and Mr Billows. Mr Richardson made a final offer to settle at £275,000 but Mr Billows did not respond.

24. During the course of the negotiations which took place between the Inland Revenue and Mr Billows Mr Knight sought to establish the value of the Company as at 4 April 1986 on the occasion of Mr Billows' gift of 10 shares to his son and 10 shares to his daughter. Whilst pursuing that line of enquiry Mr Knight wrote to Mr Billows on 6 October 1994 and his letter contains the following:

"My main concern however, has been to establish a whole Company value and it is in this area that we have experienced considerable difficulty. This case primarily concerns a majority shareholding of almost 70%, and I think it reasonable to assume that a prospective purchaser would have had access to virtually all relevant accounts together with any associated information. It would be in the vendor's interest to furnish him with this information if he wished a sale to progress.

Further, I did not say that the shares disposed of were worth £150,000, but that the Company would have been worth in the region of that figure based on a maintainable profit of around £20,000 and a multiple of 7.5. We cannot possibly calculate a share price until we have agreed upon a value for the entire concern.

If you believe my maintainable profit figure to be over optimistic, then perhaps we could adopt the figure of £13,819 as outlined in your letter of 3 June 1994. My adopted multiple of 7.5, very much on the low side given the averages in evidence during 1986/87, would value the Company at around £100,000."

Unfortunately, both Mr Billows' accountants and Mr Billows assumed, wrongly, that Mr Knight was offering to agree a value of the Company in the figure of £100,000 as at December 1986, and not, as Mr Knight's previous correspondence made clear, an offer to value the Company at that figure as at April 1986. That, probably genuine, misapprehension on the part of Mr Billows' accountants and the Appellant himself has muddied the waters in negotiations which have taken place between the Inland Revenue and Mr Billows. He has sought throughout to maintain a value of nil £ for each of the shares as at December 1986 although he has been willing to accept a value for the whole Company of £100,000. Such a valuation would produce no capital gains tax liability for Mr Billows.

25. Another factor which has bedevilled the negotiations between the Inland Revenue and Mr Billows is the history of the relationship between the two parties. In 1987 Mr Billows and his Company each appeared before the General Commissioners for Income Tax for the division of Bletchley in order to appeal against assessments to income tax under Schedule E, in the case of Mr Billows, for the years 1972/73 to 1985/86 inclusive and in the case of the Company assessments to corporation tax for the accounting periods ended 30 April 1973 to 1986 and a determination under Regulation 29 of the Income Tax (Employment) Regulations 1973 for 1978/79. Although the Commissioners discharged the assessments on Mr Billows up to and including 1977/78 they determined that he had received undeclared income for the years 1978/79 to 1985/86 inclusive. Most of the assessments on the Company were discharged. Mr Billows appealed both to the High Court and to the Court of Appeal unsuccessfully and his witness statement in this appeal makes plain that he "still has a deep sense of grievance". He was particularly unhappy with the allegation by the Inspector before the General Commissioners that the Company's accounts were unreliable and that Mr Billows' tax returns were also unreliable. Full details of the appeals by Mr Billows and the Company are to be found in the report of *Billows v Robinson* 64 TC 17.

26. I take the following description of the Company's business from paragraphs 11 to 15 of Mr Billows' witness statement, which paragraphs I accept, as follows:

"The business was founded, to design, manufacture and sell register equipment to the graphic arts industry. It also modified existing equipment being used by customers i.e. printing presses, cameras, step and repeat machines and other pre-press equipment to make compatible with the equipment the Company supplied.

The customers were widespread being approximately one-third overseas and two-thirds home market. A typical monthly customer list would be spread around 40. From the Company's inherited expertise it had built up a very specialised business. In the UK there was only one serious competitor being, Protocol Engineering Ltd. This was the company started by L K Billows in his own home in Potters Bar in 1950 of which he was a 50% shareholder when he left and sold his entire shareholding in 1972.

The Company's business was in 1986 self-contained in that it conceived, designed and marketed its own exclusive products. The Company sold its products in the UK but direct to printers and through distributors. Overseas products were almost exclusively sold through agents. Manufacture was largely done in-house.

The Company occupied premises in Milton Keynes rented at £36,000 per annum from Kelloran Ltd a company equally owned by S J Buckley and C D Billows." [It should be noted that the shares valuation division estimated that the rent should be £40,000. This would have the effect of reducing the Company profit by another £4,000 per annum. My comment]

"The Company's only meaningful competitor in the UK was the former company of L K Billows, Protocol Engineering Ltd. Overseas there were a few competitors. They were insignificant in the UK but had a stronghold in their home markets in the USA and Germany."

27. In 1986 the Company's main business was Film Montage. It provided a very accurate hole-punching and plate-bending service for the photographic industry. The main item produced was a manually operated pump which, remarkably, the Company was able to sell throughout the world. Since then the Company has

moved with the times and is now a highly technical concern and produces computer controlled graphic equipment.

28. At the meeting between the Inland Revenue and Mr Billows which took place on 11 April 1996 he was asked about his view of the trading outlook of the Company as at December 1986. The relevant paragraph of the note of the meeting prepared the following day by Mr Fowler and approved by Mr Richardson and Mr Knight and which I accept, states as follows:

"[Mr Billows] was not very specific regarding the outlook as at December 1986 but implied that with development work and customer expansion being ongoing features there was no reason not to expect the trend of increasing turnover and growth profit to continue."

29. The growth profits of the Company and its turnover for the years 1983 to 1987 inclusive as provided by the Company's accountants are as follows:

1983 1984 1985 1986 1987

Turnover £377,799 £470,609 £723,452 £958,315 £1,705,933

Growth profit £141,312 £193,097 £267,604 £434,038 £ 548,436

Gross margin 37.4% 41.0% 37.0% 45.3% 50.9%

30. Protocol made substantial profits in the years up to and including 1989. In 1990 and 1991 it suffered very large losses (£624,623 before tax in 1991) and was put into receivership. Attempts by the receiver to sell Protocol as a going concern failed. Several companies showed interest initially but no offers to buy were made. Eventually Mr Billows purchased the assets of Protocol and also employed some of its staff.

The evidence of Mr T F Vassie

8. Mr Vassie noted the upward trend in both turnover and gross profit from 1983 to 1987 inclusive and calculated the net profit before tax and before the management charge for the directors as follows:

1983 : £69,433

1984 : - £784 (loss)

1985 : £43,972

1986 : £111,712

1987 : £178,368

9. Viewing these figures both in the light of the guided optimism shown by Mr Billows as recorded in Mr Fowler's note of the meeting which took place on 11

April 1996 and alternatively in the light of Mr Billows' less optimistic forecast as shown in his witness statement, Mr Vassie gave it as his opinion that a purchaser would estimate the future maintainable profit for the Company before allowing for a management charge as being at least £145,000 as at 15 December 1986.

10. Taking into account the District Valuers' opinion that the rent for the factory should be £40,000 per annum rather than the actual rent paid of £36,000 Mr Vassie estimated that on commercial lines, £78,000 would be a reasonable estimate of the Company's future maintainable profit before tax as at 15 December 1986 made up as follows:

Profit, before adjustments : £145,000

Less

Directors' remuneration 45,000

Directors' pension contributions 9,000

Interest on outstanding loans 9,000

Rental adjustment (£40,000 - £36,000) 4,000

£ 67,000

£ 78,000

11. To that figure Mr Vassie applied a multiple, a figure which he described as "somewhat arbitrary".

12. Mr Vassie stated in cross-examination that it was "difficult to find a comparable to Billows".

13. The only comparable figure to which Mr Vassie was able to refer was a sale in June in 1987 of an 80% holding in Dale Graphic Equipment Ltd ("Dale"). Dale was a company in the same general field of business as the Company having been set up by two ex-salesmen formerly employed by the Company.

14. From the latest results available for Dale Mr Vassie annualised the figure for turnover and pre-tax profit as at 31 December 1987 and from that produced a multiple of 5.43. That figure applied to the (calculated) pre-tax profit of £45,554 for Dale produced the "calculated" turnover of £833,838.

15. Mr Vassie acknowledged in his witness statement that he was unaware of the exact circumstances surrounding the sale of Dale in June 1987.

Lacking any other comparable data Mr Vassie sought support for his opinion from the cases of *Hawkings-Byas v Sassen* [1996] STC (SCD) 319 and the *Administrators of the Estate of Caton (deceased) v Couch* [1995] STC [SCD] 34. He also sought support from Mr Christopher G Glover's book entitled "Valuation of unquoted Companies" (second edition). The relevant paragraph in Mr Glover's book relied upon by Mr Vassie contains the following:

"The author has a bench-mark yield for smaller private companies of 20% (i.e., a multiple of 5). This is shaded up or down to reflect positive or negative attributes of the subject company."

16. In the result Mr Vassie applied a multiple of 5 to his estimated figure of £78,000 for the maintainable profits producing a value for the Company of £390,000. From that figure he deducted a sum of £25,000 as the sort of allowance for tax liabilities arising under the Inland Revenue investigation (still ongoing at December 1986 and unresolved) that a purchaser was likely to make. Accordingly Mr Vassie's estimate of the value of the whole Company became £365,000 equivalent to the value of £365 per share. (I note that Mr Richardson, also of the Inland Revenue shares valuation division, was prepared to allow a figure of £50,000, as a deduction to cover the Company's involvement in the tax dispute, when he wrote to Mr Billows on 18 April 1986.)

17. Finally, to that share value he applied a discount of 15% to take account of the fact that the number of shares transferred amounted to slightly less than a 70% holding. Mr Vassie's final valuation therefore became £310.25 per share or £216,554 for a holding of 698 shares.

18. On the final day of the hearing I recalled Mr Vassie to the witness box in order that he might explain the reasons for what appears to be a very rapid increase in value of the Company from Mr Knights's figure of £100,000 at April 1986 to Mr Vassie's figure of £365,000 as at December of the same year, encompassing an interval of only a little over 8 months.

19. Mr Vassie gave it as his opinion that Mr Knight's figure of £100,000 was too low although he conceded that he had "done no real work" on the April 1986 valuation. He suggested what seemed to be an off-the-cuff figure of £200,000 for April 1986 but emphasised that in his view there had been a rapid increase in the value of the Company during the eight months period in question.

Conclusions

20. In coming to a conclusion as to the value of the shares transferred by Mr Billows in December 1986 I must first record that his witness statement contains several factual inaccuracies and, more seriously, allegations that the Inland Revenue lied and made allegations fraudulently. Those allegations were repeated more than once in his witness statement, accompanied by allegations of dishonesty on the part of the Inland Revenue.

21. I would like to make it abundantly clear that from the detailed evidence presented to me in this appeal there is not one iota of truth in Mr Billows' allegations. The various members of the Inland Revenue concerned in this appeal and in the previous income and corporation tax investigations were merely doing their jobs to the best of their ability and they should not have to suffer allegations of mendacity, dishonesty and fraud.

The requirements of section 36 Taxes Management Act 1970

22. The assessment laid on Mr Billows was an extended time limit assessment and in those circumstances Mr Tidmarsh accepted on behalf of the Crown that the

burden of proof lay with his client, in order to establish the validity of the assessment.

Section 36 states as follows, were relevant:

"36.-(1) An assessment on any person (in this section referred to as "the person in default") for the purpose of making good to the Crown a loss of income tax or capital gains tax attributable to his fraudulent or negligent conduct or the fraudulent or negligent conduct of a person acting on his behalf may be made at any time not later than 20 years after the 31 January next following the year of assessment to which it relates."

23. The Crown does not allege fraudulent conduct but Mr Tidmarsh has submitted that in making his return for 1987/88, and stating in the section requiring him to reveal details of chargeable assets disposed of, the word "none" that Mr Billows was indeed negligent. Furthermore, there was no direct admission of the details of the transfer of total of 678 shares to his son and daughter in December 1986 until he wrote to the Inspector on 2 December 1992, almost six years after the event.

24. Mr Tidmarsh countered the accusation that it was possible for an "in-time" assessment to have been made before the expiry of the six year time limit by referring to a dictum of Carswell LCJ in *Re McGuckian* [2000] STC 65 at 78c-d, dealing with a similar submission in relation to Section 41. He said:

"Any default on the part of the Revenue, if Mr Ward's failure to issue an assessment in 1985 could be so described, is only material if it could be regarded as the sole cause of the loss of tax. Once the Revenue has shown that the taxpayer's acts or omissions may have been a causative factor in causing the loss of tax, *caedit quaestio* and the Revenue's omissions are not material for the purposes of s.41."

25. In my judgment the Crown has discharged the burden of proof laid upon it by section 36. I take into account that Mr Billows must have been aware of the obligation placed upon him by his tax return, for in the previous year in relation to his tax return for 1986/87, he had given very full details of the transfers of 20 shares in total to his children in the appropriate section of his return form.

26. The question of whether there has been a loss of capital gains tax to the Crown depends upon my eventual decision as to the value of the shares transferred but it is clear that the purpose of the assessment, once negligence has been established was to make good a loss of capital gains tax to the Crown in the light of the valuation advice received by the Inspector from the shares valuation division.

The base value of the shares transferred

27. Mr Tidmarsh, who appeared for the Inspector, very fairly pointed out that there was a possibility, to put it no higher, that Mr Billows' shares were issued to him initially in return for the assets put into the Company by Mr Billows. Unfortunately for Mr Billows there is no evidence whatsoever that that is what took place. It is possible that his advisers did not consider the possibility of issuing shares in return for the assets introduced but it is plain from the

documentary evidence that the shares were issued to Mr Billows in return for cash. In addition, there was no share premium account. The evidence therefore is all in favour of an issue of shares at par and I find on the facts that Mr Billows' 700 £1 shares in the Company were issued at par.

The value of the shares transferred in December 1986

28. I can do no better in dealing with this question than to quote from a decision of my colleague Dr Nuala Brice in *Caton's Administrators v Couch* [1995] STC (SCD) 34 where she said at page 51d:

"In reaching a decision about the value of the shares I have in mind the dicta of Lord Fleming in *Salvesen's Trustees* when he said ((1930) 9 ATC 43 at 45):

"the estimation of the value of shares by a highly artificial standard which is never applied in the ordinary share market must be a matter of opinion and does not admit of precise scientific or mathematical calculation."

I have also borne in mind certain dicta of Danckwerts J in *Holt* from which I conclude that I am entitled to find a value either of 35p, as proposed by the Revenue, or 88p as proposed by the administrators, or of some other value somewhere in between. Also, after carefully considering the evidence, I must make the most intelligent guess that I can."

29. Under those perhaps less than helpful guidance comments I must first recognise that Mr Vassie, who gave evidence of opinion on behalf of the Crown, although striving to be disinterested, is a long serving employee of the Inland Revenue and as such cannot be viewed strictly as a totally independent expert witness. In coming to that conclusion I rely upon dicta in the judgment of Cresswell J in the "*Ikarian Reefer*" [1993] 2 Ll. L.Rep. 68 at page 81 where he enumerated the duties and responsibilities of expert witnesses. He laid particular stress on the independent status of expert witnesses.

30. I am also conscious that Mr Vassie had no experience of the trade and manufacturing processes carried on by the Company, that he reached his conclusions entirely from documentary evidence and that he did not visit the premises. I have some sympathy with Mr Billows' contention that at the very least Mr Vassie should have visited the offices and factory of the Company although I am well aware that by the time that Mr Vassie was instructed, the Company's operations had changed markedly from what they were in December 1986. Mr Knight did visit the premises in company with Mr Fowler and Mr Richardson but he did so only after giving his opinion that in April 1986 the Company's value was only £100,000.

31. Throughout this hearing and beforehand during the negotiations with the Inland Revenue, Mr Billows has maintained that the Company shares were valueless in December 1986 although he was willing to accept Mr Knight's valuation of £100,000 if that valuation were to be applied at December 1986 instead of April 1986.

32. Mr Billows has laid great stress upon the fact that at the time when the shares were transferred to his children the Inland Revenue investigation was still under way, for the first hearing before the General Commissioners did not take

place until 30 April 1987 and the litigation which followed was not concluded until the Court of Appeal gave judgment on 31 January 1991. In the light of the Inland Revenue allegations that the Company's accounts were unreliable and that Mr Billows' tax returns were also unreliable Mr Billows contended that any intending purchaser of the Company would be unable to make reasoned judgments as to its value. As against this, it was never alleged by the Inland Revenue that the Company's profits were lower than the figures which appeared in the Company's accounts. The allegation was that the profits were understated. And Mr Tidmarsh contended that any intending purchaser would realise that it was possible that the Company's profits were understated and would therefore be able to make his valuation on the basis that the profits would certainly not be lower than shown in the Company's accounts. He would, however, have to make allowance for the very substantial costs incurred by the Company in resisting the assessments laid on it by the Inland Revenue and I suspect that such a purchaser might well make a larger allowance than the sum of £25,000 included in Mr Vassie's calculations. Mr Richardson was prepared to accept an allowance or deduction of £50,000 for this purpose when he wrote to Mr Billows on 18 April 1996. In the event, the total additional tax payable by the Company amounted to about £16,500 and no interest was paid and penalties were not levied, but the putative purchaser at December 1986 would not know the eventual outcome of the litigation and might well reasonably suppose that were the Inland Revenue to be successful, substantial interest payments could be demanded and penalties levied. He might well decide to make an allowance of as much as £100,000 as a deduction from the Company's value for the cost of the tax investigation and litigation.

33. In cross-examination Mr Vassie agreed that it was "difficult to find a comparable to Billows". It is an unusual Company with few competitors in this country. Mr Billows discounted the comparison with Dale. He submitted that Dale's trade was very different from that of the Company and that the sale of the 80%

holding in Dale was exceptional, as the purchaser was a Swedish company which had been connected with Dale through its trade for some time.

34. Mr Billows contended that it would not have been possible to find a purchaser for the Company in December 1986 and cited in support the fact that when Protocol was in receivership the receiver was unable to find a purchaser for that Company. Eventually Mr Billows purchased the assets of Protocol and the Company took on some of Protocol's staff. However, it is apparent that Protocol was in dire financial straits when it went into receivership and yet, despite this fact, there were several interested enquirers when the receiver placed the Company on the market, even though those enquirers did not produce a purchaser for the Company .

35. In any event, I am required by the statute to assume the existence of a willing purchaser as at December 1986 and to arrive at a value for the shares such as would have governed the sale and purchase between an arms length vendor and purchaser in the open market.

36. Mr Billows has made much of the fact that Mr Knight offered a valuation for the whole Company of £100,000. Mr Billows believed at the time that the offer related to December 1986 but in fact it related, as the correspondence clearly shows, to April 1986 when Mr Knight was trying to establish whether the 20 shares transferred by Mr Billows in April 1986 gave rise to any chargeable gain.

37. That value of £100,000 in April 1986 has never been withdrawn insofar as I am aware, although it was criticised briefly by Mr Vassie in his evidence on being recalled to the witness stand. However, he freely admitted that he had done no real work on an April 1986 valuation and therefore I discount his criticism and his suggested value of £200,000 as a more realistic value for April 1986.

38. Although it is true that turnover and gross profits were increasing throughout the period from 1984 to 1987 it seems to me incredible that the Company's value should almost quadruple in a period of eight months. I am dealing here with a private company with unquoted shares and factors such as a possible takeover which might produce a very rapid rise in the share value of a public limited company do not arise. The suggested steep rise in the Company's value seems particularly unlikely bearing in mind the two substantial problems highlighted by Mr Billows but largely discounted by Mr Vassie. First there is the problem of the Inland Revenue investigation of the Company which was nearing its conclusion in December 1986, only three months or so before the first hearing before the General Commissioners. Secondly, there is the accepted fact that at the relevant time, towards the end of 1986, a rapid change was occurring in the Company's trade and manufacturing processes. Film Montage at that time was a dying art which was rapidly being replaced by digital electronic equipment and the Company's plate punch market was also disappearing. With the benefit of hindsight it has become apparent that the Company has successfully adapted to the new electronic age but the hypothetical purchaser would not be able to be certain of such success as at December 1986.

39. Looking at the amount in the round in the light of the evidence and taking into account the almost unique position in which the Company found itself at the relevant date I have come to the conclusion that a fair open market value for the shares transferred in December 1986 would be £195 per share.

40. I adjourn this hearing to enable the parties to agree figures and when they are reported to me I will determine the assessment formally.

T H K EVERETT

SPECIAL COMMISSIONER

Date Released: 14th August 2000

Authority cited but not mentioned in the Decision

Clark v Green [1995] STC (SCD) 99

SC 3013/95