ENHANCEMENT EXPENDITURE

Blackwell v HMRC TC03243

Practical point 81 in April 2014 *TAXline* reported the decision of the FTT in *Blackwell v HMRC* TC03243 where the meaning of enhancement expenditure for CGT purposes under s38(1)(b), Taxation of Chargeable Gains Act 1992 was considered. The tribunal found for the taxpayer, but an appeal has now been heard in the UT and the decision overturned.

Simply stated, Mr Blackwell was proposing to sell shares in his family company. He entered into certain agreements regarding the possible sale of his shares but a little while later a third party appeared who offered him a great deal more. This placed him in difficulty in respect of the earlier agreements and he ended up making a payment of £17.5m to get out of the earlier agreements so he could accept the higher offer for the shares. In computing the capital gain on the sale of his shares he claimed a deduction for the £17.5m which had put him in a position to proceed with the sale.

Instinctively one feels that a deduction should be permitted for this expenditure, but the terms of s38 are not very helpfully worded. To be entitled to relief he had to show that the expenditure was incurred on the asset "for the purpose of enhancing the value of the asset, being expenditure reflected in the state or nature of the asset at the time of disposal".

Mr Blackwell believed that the expenditure would enhance the value of his shares because it would enable the higher bid to be accepted. However, that is not enough. It is necessary for the expenditure to be incurred "on the asset" and to be "reflected in the state or nature of the asset at the time of disposal".

The UT has now denied him the relief. It did acknowledge that the result appears somewhat unfair because Mr Blackwell would be taxed on a profit that exceeds his commercial profit - but that was an inevitable result of the restrictive nature of the provisions of s38. The expenditure was not incurred on the shares, nor did it have the effect of changing the state or nature of the shares. The UT concluded that at the time of their disposal, the state or nature of Mr Blackwell's shares did not reflect the money paid to get out of the earlier agreement, and a deduction for the expenditure was not allowed.

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