



Neutral Citation: [2025] UKFTT 1188 (TC)

Case Number: TC09654

**FIRST-TIER TRIBUNAL
TAX CHAMBER**

Taylor House, London

Appeal reference: TC/2023/08870

*CORPORATION TAX – section 22(1)(c) Taxation of Chargeable Gains Act 1992 – surrender
– termination fee – merger agreement – Delaware law – appeal allowed*

Heard on: 16 and 18 June 2025

Further written submissions: 12 September 2025

Judgment date: 3 October 2025

Before

**TRIBUNAL JUDGE BLACKWELL
MR M BELL**

Between

DIALOG SEMICONDUCTOR LIMITED

Appellant

and

THE COMMISSIONERS FOR HIS MAJESTY’S REVENUE AND CUSTOMS

Respondents

Representation:

For the Appellant: Mr David Goldberg KC and Mr Harry Winter, instructed by Reynolds
Porter Chamberlain LLP

For the Respondents: Mr Simon Pritchard of counsel, instructed by the General Counsel and
Solicitor to HM Revenue and Customs

DECISION

INTRODUCTION

1. Dialog Semiconductor Limited (“Dialog”) is a specialist microchip company that produces mixed signal, connectivity and power management products for mobile and “internet of things” devices.

2. Dialog entered into an Agreement and Plan of Merger dated 19 September 2015 (the “Merger Agreement”). The dispute between the parties is whether a sum, called in the Merger Agreement the “Company Termination Fee”, (the “Termination Fee”) of USD 137.3m (about £97m), received by Dialog pursuant to the Merger Agreement constitutes a disposal of assets under section 22(1)(c) of the Taxation of Chargeable Gains Act 1992 (“TCGA 1992”) thereby giving rise to a chargeable gain that is chargeable to corporation tax.

Preliminary Issue

3. On 23 January 2025 the parties made a joint application that:

“1. The First-tier Tribunal will, in the first instance, decide only the preliminary issue (i.e. whether the [Termination Fee] does fall within section 22(1)(c) Taxation of Chargeable Gains Act 1992).

2. If the preliminary issue is resolved finally in [Dialog]’s favour, then the closure notice will be withdrawn such that there is no additional tax due from [Dialog].

3. If the preliminary issue is resolved finally in the Respondents’ favour, then the parties will seek to agree the correct amount of tax due (in light, inter alia, of the various losses that can be deducted) with both parties having the right to apply to the First-tier Tribunal for a further hearing in the event no such agreement is possible.”

4. Those draft directions were endorsed by Judge Blackwell on 23 January 2025. The purpose of the hearing was, thus, solely to determine whether the Termination Fee falls within s 22(1)(c) TCGA 1992.

STATUTORY FRAMEWORK

5. Corporation Tax Act 2009 (“CTA 2009”) s 2 provides:

“2 Charge to corporation tax

(1) Corporation tax is charged on profits of companies for any financial year for which an Act so provides.

(2) In this Part “profits” means income and chargeable gains, except in so far as the context otherwise requires.

...”

6. The circumstances in which corporation tax is charged in respect of chargeable gains are set out at TCGA s 2, being:

“2 Corporation tax on chargeable gains

(1) As a result of section 2(1) and (2) of CTA 2009, corporation tax is charged on chargeable gains accruing to a company on the disposal of assets.

(2) The charge to corporation tax on chargeable gains has effect in accordance with this Act and all other relevant provisions of the Corporation Tax Acts.

7. Section 15 TCGA 1992 provided as follows at all material times:

“15 Computation of gains

(1) The amount of the gains accruing on the disposal of assets shall be computed in accordance with this Part, subject to the other provisions of this Act.

(2) Every gain shall, except as otherwise expressly provided, be a chargeable gain.”

8. Section 21 TCGA 1992 provided as follows at all material times:

“21 Assets and disposals

(1) 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, and

(b) currency, with the exception (subject to express provision to the contrary) of sterling,

(c) any form of property created by the person disposing of it, or otherwise coming to be owned without being acquired.

(2) For the purposes of this Act—

(a) references to a disposal of an asset include, except where the context otherwise requires, references to a part disposal of an asset, and

(b) there is a part disposal of an asset where an interest or right in or over the asset is created by the disposal, as well as where it subsists before the disposal, and generally, there is a part disposal of an asset where, on a person making a disposal, any description of property derived from the asset remains undisposed of.”

9. Section 22 TCGA 1992 provided as follows at all material times:

“22 Disposal where capital sums derived from assets

(1) Subject to sections 23 and 26(1), and to any other exceptions in this Act, 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—

(a) capital sums received by way of compensation for any kind of damage or injury to assets or for the loss, destruction or dissipation of assets or for any depreciation or risk of depreciation of an asset,

(b) capital sums received under a policy of insurance of the risk of any kind of damage or injury to, or the loss or depreciation of, assets,

(c) capital sums received in return for forfeiture or surrender of rights, or for refraining from exercising rights, and

(d) capital sums received as consideration for use or exploitation of assets.

(2) In the case of a disposal within paragraph (a), (b), (c) or (d) of subsection (1) above, the time of the disposal shall be the time when the capital sum is received as described in that subsection.

(3) In this section “capital sum” means any money or money’s worth which is not excluded from the consideration taken into account in the computation of the gain.”

FINDINGS

10. We make the following initial findings, before discussing the parties' submissions. We then make further findings.

Witnesses and Evidence

11. The hearing bundle was of 1,407 pages together with a bundle of authorities of 201 pages.

12. We heard from Dr Jalal Bagherli, who at the relevant time, was Dialog's Chief Executive Officer. He stated in his witness statement that he was not specifically involved around negotiating the clause concerning the Termination Fee. This is surprising given that Dialog's expert witness expressed the view that termination fee provisions are "typically among the most heavily negotiated terms of a merger agreement".

13. Dr Bagherli in cross examination initially said the Termination Fee was a penalty fee. When the relevant part of the Merger Agreement was put to him which expressly stated that it was not a penalty fee, he stated he was "using regular English, not law English" and that (following the language of the passage read to him) it "constitutes compensation to Parent". He then suggested it was to cover out-of-pocket costs that Dialog had incurred (such as securing debt funding and upgrading accounts to US standards). When asked to itemise these costs, they were so far below USD137.3m that they could not be seen, realistically, to be a pre-estimate of out-of-pocket expenses. Figures given were "5 million" (it is unclear whether USD or GBP) for payment to the bank (which "wasn't massive" as it "normally works on a contingent fee"), and "a few million dollars on a complete five-year accounting review, audit, and preparation for NASDAQ listing." Dr Bagherli then suggested that thinking in terms of "detailed expense" was not right and the Termination Fee was set on the basis of an "almost formulaic" table of what the "going rate" is, agreed by the investment banks: which was "about 3 per cent of the deal value". He then suggested that this was agreed as a deterrence. Given these inconsistencies and changes of tack, we do not find Dr Bagherli a helpful or reliable witness. While we accept he honestly tried to assist the Tribunal we place little weight on his testimony.

14. We also heard live evidence from Jeffrey R. Wolters (the expert witness called by Dialog) and Catherine G. Dearlove (the expert witness called by HMRC). We had the benefit of an expert report from Mr Wolters and a report and supplemental report from Mrs Dearlove. In addition to these they prepared a joint statement of areas of agreement and disagreement.

15. The expert witnesses gave concurrent evidence (sometimes known as "hot-tubbing") with judicial led questioning following an agenda proposed by the parties. After the judicial led questioning on each topic the experts were tendered for cross-examination.

16. We find that Mrs Dearlove's expert reports, and the presentation of her evidence, was more detailed, more closely reasoned and she more sought to corroborate her opinions with principles of Delaware law. Where there is disagreement between the experts, we prefer the views of Mrs Dearlove for the following reasons, which are essentially those stated by HMRC in their written closings:

(1) Mrs Dearlove was careful to explain her expressed opinions by references to concepts that she said arise under Delaware law. By way of contrast, Mr Wolters tended to refer to general commercial expectations, no doubt reflecting his experience advising boards and corporations. Mr Wolters' evidence therefore lacked as detailed an analysis of the requirements of Delaware law and consideration of how Delaware courts would approach an agreement such as the Merger Agreement.

(2) Comparing the two written reports, there was a far greater referencing of caselaw and other authorities in Mrs Dearlove's report.

(3) In their oral testimony, one example of this was Mr Wolters' evidence about the parties' express agreement that the Termination Fee was compensatory in nature. Despite accepting that under Delaware law the focus of contractual interpretation is the words of the contract Mr Wolters suggested that the parties were merely "*signalling to a court, like, this is not a penalty...*" and that if he was advising a client who was defending such a clause, he would not spend a lot of time showing loss or "*with expert witnesses on financial arguments about potential loss.*" However, when the reasoning at [6] of *Brazen v Bell Atlantic* 695 A.2d 43 (Del. 1997) ("*Brazen*") was put to him, he had no option but to accept that in that case the Delaware Supreme Court had expressly relied upon "*the analysis of the parties concerning lost opportunity costs*".

(4) Mr Wolters did not refer to *Brazen* at all in his written report or in his section of the joint report. In contrast the case was identified by Mrs Dearlove.

(5) Mr Wolters repeatedly referred to a 3% termination fee as being permitted. Whilst 3% may be a useful "rule of thumb" for the purposes of commercial negotiations, it says little, if anything, about the underlying legal principles that the Court will consider when deciding whether a particular fee is lawful. Mrs Dearlove's evidence explored these in detail.

(6) When asked to comment on Mrs Dearlove's opinion that under Delaware law contracts can be discharged or extinguished by performance, breach or termination, Mr Wolters did not disagree. He said that he could "follow the point" {d.1,p.180,l.13}. But he also said that he was not in a position to comment {d.1,p.180,l.10}. Given that the experts were instructed to opine on Delaware law and their third agenda item referred specifically to whether the Termination Fee was paid in performance of the Merger Agreement, this omission was surprising (indeed, he even said that he "just thought that wasn't a part of the questions asked of the experts..."). Similarly, when asked by the Tribunal whether Delaware had a concept of "discharged by performance", he replied that he believed so but he did not know "if it would be phrased in exactly those words so I hesitate to go too far into that." This was notwithstanding the centrality of "performance" to Dialog's arguments and the third issue in the Agenda.

Background

17. In 2015, Dialog entered into a bidding process to acquire Atmel Corporation ("Atmel").

18. Atmel was a producer of microchips and microcontrollers based in the United States (US) and the attempted acquisition of Atmel presented Dialog with the opportunity to combine technologies, access Atmel's client base and streamline operations to make a more profitable company.

Merger Agreement

19. In making these findings we have drawn heavily on the experts' joint statement of areas of agreement and disagreement and Mrs Dearlove's reports.

20. On 19 September 2015 the Merger Agreement was entered into between (1) Dialog; (2) Avengers Acquisition Corporation (Avengers) (a US company that had been newly incorporated by Dialog and was a wholly owned subsidiary of Dialog); and (3) Atmel (the target company, incorporated in Delaware and unconnected with Dialog).

21. By way of summary only, the Merger Agreement provided that the consideration for the merger would be a combination of cash and shares in Dialog. The consideration was worth approximately USD 4.577 billion at the time the merger was announced, based on the fully diluted value of Dialog's shares at the time and represented Dialog's agreement to pay USD 4.65 per Atmel share in cash and 0.1120 Dialog shares for each Atmel share.

22. The Merger Agreement could not, by itself, effect the merger. This is because a merger cannot occur under Delaware law unless the merger agreement is approved by stockholders.

23. The Merger Agreement was governed by Delaware law.

24. The agreement begins with Recitals. Those recitals state that the parties have determined that the transactions set out in the agreement are in the best interests of their respective companies and stockholders. They also state that the directors of the parties have determined that the Merger is “advisable and fair” to their respective companies.

25. The Merger Agreement created enforceable rights and obligations when signed by the parties. These include the following.

Ordinary Course Covenant (§5.1)

26. Atmel was obligated to, among other things, conduct its business in the ordinary course of business, consistent with past practice. There were limitations on Atmel relating to the payment of dividends, issuing shares, setting the compensation of its directors and employees, making loans to directors, taking out loans, changing accounting standards, making tax elections, acquiring stock and assets, altering material contracts, alienating IP and engaging in litigation.

No-Shop Provision (§ 5.4(a))

27. Atmel was obligated not to, among other things, take any action to solicit or initiate other bids, engage or participate in any discussions with prospective bidders, or pursue a different bid, subject to exceptions.

28. ***Exceptions:*** Atmel could, among other things, engage in discussions with respect to an unsolicited proposal if Atmel’s board determined that such proposal was, or was reasonably expected to result in, a bid superior to the Dialog transaction, Atmel’s board determined that failure to engage in such discussions would reasonably be expected to be inconsistent with directors’ fiduciary duties, and Atmel was not otherwise in material breach of the No-Shop Provision.

Atmel Board Recommendation Covenant (§ 5.4(d))

29. Atmel was obligated to recommend that its stockholders approve and adopt the Merger Agreement, subject to exceptions.

30. ***Exceptions:*** Atmel could change its recommendation in a manner adverse to Dialog if:

(1) an unexpected event occurred causing the failure to do so to be inconsistent with directors’ fiduciary duties; or

(2) Atmel received a competing proposal, did not breach the No-Shop Provision, and the Atmel board determined such proposal to be superior to Dialog’s offer and that failure to change its recommendation would be inconsistent with directors’ fiduciary duties.

31. ***Match Right:*** both exceptions, however, were subject to Dialog’s right to change its transaction terms or offer other arrangements. In either instance, Atmel was required to give Dialog four business days’ advance notice before it changed its recommendation and to consider in good faith Dialog’s proposed changes or other arrangements. Atmel had the right to change its recommendation only if the board determined in good faith thereafter that doing so was still required to comply with directors’ fiduciary duties notwithstanding Dialog’s revisions. Further, Atmel could only change its recommendation in favour of a competing proposal if Atmel entered into the competing transaction and paid the Termination Fee concurrently with the termination.

Best Efforts Covenant (§ 5.6)

32. The obligation of each of the parties to use reasonable best efforts to do all things necessary to “consummate” (this is the expression used in the Merger Agreement) the Merger, including making required antitrust filings, defending against legal proceedings challenging the transaction, and using best efforts to obtain Committee on Foreign Investment in the United States approval.

Other Provisions

33. The Merger Agreement contained other rights and obligations including Atmel’s obligation to take actions in furtherance of closing and convene a stockholder meeting to secure approval of the Merger Agreement (§5.8), Dialog’s information rights (§5.9) and Dialog’s consultation rights over Atmel public statements (§5.10).

Specific Performance (§8.9)

34. The terms of the Merger Agreement, including the foregoing provisions listed above, were enforceable by the parties by specific performance, i.e., injunction or other equitable relief.

Termination Rights (§7.1–7.4)

35. Both parties had rights to terminate the agreement unilaterally in specified circumstances, or by mutual agreement. The agreement was also terminable by either Atmel or Dialog if the merger was not consummated before 30 June 2016.

36. At issue in this case is Atmel’s right to terminate unilaterally in order to concurrently enter into an “Alternative Company Acquisition Agreement” (as that term is defined in the Merger Agreement) under §7.3(a), (the “Fiduciary Out Termination Provision”). This is expressly conditional on:

- (1) Atmel having complied with §5.4(d) (the match rights); and
- (2) Atmel paying the Termination Fee “substantially concurrently” with termination.

37. Atmel was obligated to pay the Termination Fee to Dialog if the Merger Agreement was terminated by Atmel in certain circumstances, which included a termination for a superior proposal: § 7.5(b)(i). The Termination Fee of USD 137.3m, was 3% of the fully diluted equity value of Dialog’s offer at the time the Merger Agreement was entered into.

38. Broadly, a superior proposal was an unsolicited written company acquisition proposal that the Atmel board determined in good faith, by majority vote, after taking into account any counter-proposal by Dialog, (i) would have been reasonably capable of being timely consummated on the terms proposed; and (ii) would, if consummated in accordance with its terms, result in a transaction that is more favourable from a financial point of view to Atmel stockholders than the merger with Dialog.

39. While not at issue in this appeal, Dialog was obligated to pay a termination fee of USD 41.1m to Atmel if the Merger Agreement were terminated by Atmel in certain circumstances, which included if Atmel exercised its right to terminate in response to a breach of the agreement by Dialog after which Dialog entered into an agreement for an alternative acquisition: §7.5(c).

40. Upon termination of the Merger Agreement in accordance with its terms, the Merger Agreement was void and of no effect, provided that the provisions with respect to the termination fees, certain reimbursement and indemnification provisions, and certain confidentiality and non-disclosure obligations survived termination, and termination did not relieve any party of potential liability for intentional breach of the Merger Agreement:).

41. We accept Mrs Dearlove's evidence that the obligation to pay the Termination Fee survives termination, since if the agreement were not to say it survived then it would not be possible to enforce payment if there was a breach.

42. The Merger Agreement's termination provision also provided at §7.5(g):

"Each of the Company, Parent, and Merger Sub acknowledges that (i) the agreements contained in this Section 7.5 are an integral part of the transactions contemplated by this Agreement, (ii) without these agreements, Parent, Merger Sub and the Company would not enter into this Agreement, (iii) the Company Termination Fee is not a penalty, but rather constitutes damages in a reasonable amount that will compensate Parent and Merger Sub in the circumstances in which such Company Termination Fee is payable, and (iv) the Parent Termination Fee is not a penalty, but rather constitutes damages in a reasonable amount that will compensate the Company in the circumstances in which such Parent Termination Fee is payable."

Delaware Law Context

43. In making these findings we have drawn heavily on the experts' joint statement of areas of agreement and disagreement and Mrs Dearlove's reports.

44. Terms similar to the above-described provisions of the Merger Agreement negotiated by the parties at issue in this case, including the Fiduciary Out Termination Provision and the Termination Fee Provision, are typical in merger agreements entered into by public companies under Delaware law.

45. However, these features are not required by Delaware law in every merger agreement, whether by Delaware's merger statute (Section 251 of the Delaware General Corporation Law, "DGCL") or Delaware contract law. In addition, whether a selling board's fiduciary duties may require them to obtain these features in a particular merger is a contextual case-by-case determination based on all relevant facts. The specific terms and conditions of such provisions are typically negotiated by the parties.

Fiduciary duties under Delaware law

46. Under Delaware law directors' fiduciary duties are context-specific. The Delaware Supreme Court established in *Revlon Inc. v MacAndrews & Forbes Holdings, Inc.* 506 A.2d 173 (Del. 1986) ("*Revlon*") that in a sale of the corporation involving a change of control (like the Merger), directors' fiduciary duties require directors to maximise value not in the long-term, but rather immediately such that stockholders will receive the highest price reasonably available in the sale. However, there is no single blueprint that a board must follow to fulfil its duties: *Barkan v Amsted Indus Inc.* 567 A.2d 1279, 1286 (Del. 1989).

47. The foregoing paragraph summarises the fiduciary standard of conduct that Delaware law imposes on corporate directors. However, Delaware courts do not apply the standard of conduct when determining whether corporate directors are liable for a breach of fiduciary duty. Instead, they apply one of three standards of review: being, in increasing order of stringency (i) the business judgment rule; (ii) entire fairness enhanced scrutiny; and (iii) entire fairness.

48. Two enhanced scrutiny triggers are relevant for purposes of these proceedings:

(1) The first is transactions involving a change of control, oftentimes shorthand for *Revlon* scenarios. Where stockholders challenge a change of control transaction, directors must show that "(i) they sought to obtain the best transaction reasonably available, (ie, they pursued a legitimate end), and (ii) they followed a process that fell within a range of reasonableness (ie, they selected a reasonable means)": *In re Columbia*

Pipeline Group, Inc. Merger Litig 299 A.3d 393, 457 (Del. Ch. 2023) (“*Columbia Pipeline*”).

(2) The second relevant enhanced scrutiny trigger is the board’s adoption of so-called “defensive measures” that make it more difficult for third parties to take control of the corporation. Because a board’s adoption of defensive measures presents “the omnipresent spectre that a board may be acting primarily in its own interests”, for example, to entrench themselves in office, these types of transactions are subject to enhanced judicial scrutiny: *Unocal Corp. v Mesa Petroleum Co* 493 A.2d 946, 954 (Del. 1985) (“*Unocal*”). Accordingly, where a stockholder challenges a board’s adoption of defensive measures, the board must demonstrate that:

“(i) they had acted in good faith to identify and respond to ‘a danger to corporate policy and effectiveness’ (ie, they pursued a legitimate end), and (ii) they had implemented a response that was ‘reasonable in relation to the threat posed’ (ie, they selected a reasonable means).”: *Columbia Pipeline*, 456-57.

49. Deal protection provisions in merger agreements are subject to the enhanced scrutiny standard of review both because they are considered defensive measures animating the inherent conflicts identified in *Unocal* and because they limit target directors’ ability to maximise value by pursuing superior proposals, thereby animating the concerns addressed in *Revlon*.

50. When applying enhanced judicial scrutiny to defensive devices designed to protect a merger agreement, a court must first determine that those measures are not preclusive or coercive before its focus shifts to the reasonableness assessment described above: *Omnicare Inc. v NCS Healthcare, Inc.* 818 A.2d 914, 932 (Del. 2003). Protections are “coercive” if they have “the effect of causing the stockholders to vote in favour of the proposed transaction for some reason other than the merits of that transaction”: *Orman v Cullman*, 2004 WL 2348395 (Del. Ch. Oct. 20, 2004). Protections are “preclusive” if they unreasonably restrict superior proposals from emerging: *In re Cogent, Inc. S’holder Litig* 7 A.3d 487, 501 (Del. Ch. 2010).

Why merger parties typically include a non-solicitation provision, subject to a fiduciary out termination provision

51. In public company mergers like the Merger, there is typically a fairly long interim period in between signing (when the merger agreement is executed) and closing (when the merger occurs and the acquiror takes ownership of the target company). This is for a variety of reasons, including the time it takes public target companies to convene the special meeting at which the target corporation’s stockholders must vote on whether to approve the merger agreement, as is required by s 251(c) DGCL.

52. The existence of this interim period gives other interested parties—including, in some cases, other bidders who were outbid in the bidding process an opportunity to attempt to “jump” the original transaction by convincing the target company to terminate the original agreement and pursue a transaction with the competing bidder.

53. This gives buyers strategic incentives to include deal protection mechanisms in a merger agreement preventing or otherwise discouraging the target from entertaining competing offers. That is the principal function of a non-solicitation provision like the No-Shop Provision: enhancing the buyer’s strategic interest in maximising closing certainty: Lou R. Kling & Eileen T. Nugent, *Negotiated Acquisitions of Companies, Subsidiaries and Divisions* (Law Journal Press, 2018) (“Kling & Nugent”), §13.05[1].

54. Thus, non-solicitation provisions are desired by buyers for strategic purposes, but in no sense required by Delaware law. Indeed, non-solicitation provisions are generally frowned

upon under Delaware law in that they are susceptible to at least two subtypes of legal challenges:

(1) first, stockholders could challenge a board of directors' agreement to a non-solicitation provision as breach of fiduciary duty on grounds that the provision is a deal protection device that fails to satisfy enhanced scrutiny.

(2) second, stockholders could challenge the provision as violating the principle, set forth in several Delaware Supreme Court cases, that "[t]o the extent that a contract, or a provision thereof, purports to require a board to act or not act in such a fashion as to limit the exercise of fiduciary duties, it is invalid and unenforceable": *Paramount Commc's Inc. v QVC Network Inc* 637 A.2d 34, 51 (Del. 1994).

55. Fiduciary out termination provisions arose as one particularly common method (but not the only method) to address both concerns.

The role, purpose, and treatment of termination fees under Delaware law

56. In a practical, strategic sense, termination fee provisions in merger agreements function as both a compensation mechanism and as a deal protection device:

(1) as compensation provisions, buyers bargain for termination fee provisions to recoup various losses borne by pursuing the target company, including both the opportunity cost associated with pursuing the target rather than other strategic alternatives and out-of-pocket costs associated with negotiating the transaction: Kling & Nugent §13.05[2].

(2) as deal protection devices, buyers bargain for such provisions to deter competing bidders. The higher the fee, the less attractive the target becomes to prospective bidders, who must price in the reduction in the target's assets caused by its payment of the fee.

57. The function of a termination fee in a more technical contractual sense is somewhat less clear. In *Brazen* the Delaware Supreme Court suggested that termination fee provisions in merger agreements may, depending on the circumstances, be analysed as liquidated damages provisions whose function is to compensate buyers for losing the right to complete the merger.

58. Under Delaware law, liquidated damages are generally defined as "a fixed sum" that "parties to a contract may agree on... to compensate the non-breaching party in the event of breach.": *Wilmington Housing Authority v Pan Builders, Inc*, 665 F.Supp. 351, 354 (D. Del. 1987).

59. Because Delaware law forbids contractual damages from functioning as penalties, liquidated damages provisions are unenforceable unless they satisfy a two-part test:

(1) damages for breach must be difficult to estimate; and

(2) the agreed-upon sum must be reasonable.

60. The *Brazen* court clarified how the liquidated damages test applies to termination fees in merger agreements. In particular, the court held that in that unique context, the first prong requires that "the damages that would result from a breach of the merger agreement must be uncertain or incapable of accurate calculation" and the second prong hinges on an assessment of two factors, including "the anticipated loss by either party should the merger not occur" and "the difficulty of calculating that loss": *Brazen*, 695 at [48]. Notably, the applicable legal standard's express focus on the cost of losing the transaction in the second prong suggests that when termination fees appear in merger agreements, their contractual function under Delaware law is to compensate jilted buyers for the costs associated with giving up the jilted buyer's right and opportunity to acquire the seller.

61. In addition to being analysed as liquidated damages, termination fee provisions are considered deal protection devices subject to enhanced scrutiny: *In re Cogent, Inc. S'holder Litig.*, 7 A.3d 487, 502-04 (Del. Ch. 2010). The enhanced scrutiny inquiry in this context focuses on whether the termination fee is so large as to preclude superior proposals from emerging. Delaware courts routinely uphold termination fees amounting to 2% to 4% of the target corporation's equity value, whereas fees over 5% have been characterised as potentially problematic: *In re 3Com S'holders Litig.*, 2009 WL 5173804, at 7 (Del. Ch. Dec. 18, 2009); *In re Converge, Inc.*, 2014 WL 6686570, at 14 (Del. Ch. Nov. 25, 2014).

62. Like non-solicitation provisions, termination fee provisions are not required in merger agreements governed by Delaware law. To the contrary, they are considered deal protection mechanisms that are subject to enhanced judicial scrutiny, and in that sense are generally disfavoured by Delaware courts.

Possible alternatives to termination fees

63. As already noted, termination fee provisions serve the dual function of deterring unsolicited topping bids and compensating the buyer for losing the right and opportunity to acquire the target company. Accordingly, alternatives to termination fee provisions would theoretically include any structure that serves those same functions. Possible alternatives include:

- (1) topping fees, which generally require the target company to pay the spurned buyer a percentage of any merger consideration sum eclipsing the price provided for in the original merger agreement;
- (2) target stock options, which generally give the buyer the option to acquire a large slug of the target's shares shortly before signing so that the buyer can capitalise on the transaction premium; and
- (3) asset lock-up options, which similarly give the buyer the option to acquire a key asset even if another bidder prevails.

Superior offer

64. By §5.4 of the Merger Agreement (and by way of summary only), Atmel were required to tell Dialog of any superior offer that had been received. On 7 December 2015, Dialog was made aware by Atmel that an unsolicited and potentially higher bid had been made by Microchip Technology Inc ("Microchip"). Microchip's initial offer was USD 9 per share in cash, with an option at shareholders' discretion to receive up to USD 1 billion in Microchip stock.

65. In January 2016, Atmel determined that the offer received from Microchip constituted a "Company Superior Proposal" as defined in the Merger Agreement and decided to pursue the offer from Microchip. Dialog was informed about Microchip's final offer and that Atmel considered this to be a superior offer on 12 January 2016. Microchip's final offer was for USD 7 per share in cash and USD 1.15 per share in Microchip stock, so worth approximately USD 3.6 billion. Due to an approximate 40% decrease in Dialog's share price since September 2015 (which significantly affected the value of the stock component of Dialog's offer), the offer from Microchip was more valuable than Dialog's.

66. Under §5.4(d)(z) of the Merger Agreement, Dialog had (by way of summary only) the right to make a counteroffer. On 14 January 2016, Dialog announced that it would not raise its offer for Atmel. The directors of Atmel accepted the higher offer from Microchip. Atmel sent formal notification to Dialog on 19 January 2016 that the merger would not be going ahead. Atmel then paid the Termination Fee to Dialog.

67. On 20 December 2017, Dialog filed its company tax return for the accounting period ended 31 December 2016 showing the Termination Fee as a capital receipt but not as a chargeable gain. HMRC subsequently enquired into Dialog's return and concluded that receipt of the Termination Fee constituted a disposal of assets for chargeable gains purposes under s 22(1)(c) TCGA 1992, resulting in an additional corporation tax liability for Dialog. A closure notice to this effect was issued on 8 March 2023.

68. On 6 April 2023, Dialog requested postponement of the tax and requested a review of HMRC's closure notice. On 27 April 2023, HMRC provided Dialog with HMRC's view of the matter. Following this, on 9 June 2023, HMRC issued their review conclusion letter which upheld the original decision within the closure notice. On 6 July 2023, Dialog appealed to the First-tier Tribunal against HMRC's decision.

THE PARTIES' SUBMISSIONS ON THE ISSUES IN DISPUTE

69. Dialog has three arguments as to why the Termination Fee does not fall within s 22(1)(c) TCGA 1992:

(1) the Termination Fee was not received "in return for" Dialog's forfeiture of, surrender of, or refraining from exercising any rights. Instead, the Termination Fee was paid to Dialog by Atmel, unilaterally, to give effect to a term of the Merger Agreement.

(2) there was no "forfeiture" of rights, "surrender" of rights, or "refraining from exercising" rights by Dialog. Instead, as is normal in commercial situations where both sides perform their obligations under a contract and thereby discharge it, some of Dialog's contractual rights were executed by the counterparty and other rights fell away without Dialog forfeiting them, surrendering them, or refraining from exercising them.

(3) Dialog's bundle of rights under the Merger Agreement was not an asset for CGT purposes.

70. HMRC's skeleton essentially conflates Dialog's issues (1) and (2) and, in addition to addressing Dialog's issue (3) also raises the issue as to whether the Termination Fee is a capital sum.

"IN RETURN FOR"

Dialog's case

71. Dialog say these words imply reciprocity. They say this is evident from *British Telecommunications plc v HMRC* SpC 535; [2006] STC (SCD) 347 ("*BT*"), where at [9] Dr John Avery-Jones CBE remarked:

"I think that it is common ground that if the reason for the payment was to give effect to a term of the Merger Agreement rather than because the appellant gave up its rights under the agreement, the sum would not be derived from assets; and if the reason for the payment was in return for the appellant's giving up its rights under the agreement, the sum would be derived from the asset."

72. Dialog say the Termination Fee was not paid for Dialog giving up or refraining from exercising its rights under the Merger Agreement, since:

(1) on a true analysis, all that happened was that the Merger Agreement was discharged by performance.

(2) Dialog did not give up any of its rights under the Merger Agreement, Dialog's contingent right to a merger fell away.

(3) when the Specified Sum became payable, Dialog had no material enforceable rights (other than the right to receive the Specified Sum) which were capable of being given up.

(4) Dialog's right to Atmel's reasonable best efforts to consummate the merger is not particularly important in the circumstances, because Atmel was fully entitled to recommend a superior alternative merger: Merger Agreement, §5.4(d). Accordingly, the Specified Sum was not paid in return for Dialog giving up that right. This follows the analysis in *BT* at [14].

(5) all of Dialog's rights under the Merger Agreement (other than to be paid the Termination Fee) were "very slight" and "not worth much" (referencing *BT* at [15]). The reality is therefore that Dialog was not being paid to surrender its rights against Atmel. Dialog was instead simply being paid in pursuance of a term in the Merger Agreement. Dialog elaborate on this in their written closing, stating that:

"when Microchip came on the scene and made a Company Superior Proposal, the value started to leach out of the promise to merge and into the promise found in Section 7.5(b) to pay \$137.3m which was quite distinct, and a fallback, to the provisions concerning the implementation of a merger. Accordingly, when the \$137.3m came to be paid, the only remaining valuable right of any practical value – and thus the true and real source of the \$137.3m – was the payment obligation in Section 7.5(b) which gets fulfilled in accordance with its terms and in a way which does not bring about a disposal."

When there is a right (whether contingent or not) to receive a payment and the payment is, as here, simply received pursuant to that right, the requirements for the application of s 22 TCGA 1992 are not fulfilled. In such a case there is no sum derived from an asset: the right to the sum and the payment of the sum are one and the same thing: *IRC v Laird Group plc* [2003] UKHL 54; [2003] STC 1349 at [37].

(6) The Termination Fee was a consequence or effect of termination, not a price paid for termination, and that is all the more so as (i) §7.3(a) of the Merger Agreement requires payment only substantially concurrently with termination and (ii) the right to payment of the USD 137.3m is specifically said in §7.5(a) of the Merger Agreement to survive termination.

(7) Dialog took no active steps to receive the Termination Fee. It was a consequence of Atmel's unilateral termination of the Merger Agreement following the Company Superior Proposal from Microchip. The Termination Fee is paid pursuant to a promise made between the third party and Atmel (§5.21 Microchip's merger agreement) and it is paid in part to compensate for expenses and time spent in pursuing a bid.

(8) All of these things emphasise that the real source of the Company Termination Fee is not the conditional promise to merge Atmel and Dialog. Both since (i) as a matter of form, the rights to a merger have been already been terminated by the time the capital sum was received; and (ii) as a matter of commercial reality, the only remaining valuable asset of Dialog when it gets paid is the right to be paid itself under section 7.5(b) and the payment is simply pursuant to that right.

(9) In their skeleton argument they rely on a homely example whereby a greengrocer contracts with a vehicle manufacturer for the provision of a lorry but where, in certain circumstances, the vehicle manufacturer must instead provide a van. A similar homely example is provided in their written closing, where they give an example of X and Y contracting to marry, with them entering into an agreement containing two distinct promises operating separately from each other (1) how the parties will behave while they are engaged and, should the marriage go ahead, the terms of that marriage; and (2) that

if, before the marriage takes place, Y receives a better offer of marriage, Y may terminate the engagement but if Y does so Y will pay X USD 137.3m.

HMRC's case

73. In summary, HMRC's case is that (1) Dialog had various contractual rights under the Merger Agreement and these were assets; (2) the Termination Fee was a capital sum; (3) the Termination Fee was paid to release Dialog from its contractual rights and therefore the real source of the capital sum was the termination of the Merger Agreement; and (4) it follows, that the payment was made in return for Dialog forfeiting/surrendering/refraining from exercising its rights.

74. HMRC note how in *Zim Properties Ltd v Proctor* [1985] STC 90, 106j, (ChD) ("*Zim*") Warner J observed that:

“a capital sum may be derived from assets within the meaning of the general words in s 22(3) even though those assets may not be the immediate source of that sum.”

and whether a capital sum derived from an asset in each case requires consideration of “the real (rather than the immediate) source of the capital sum”: *Zim* 107b.

75. HMRC rely on *Welbeck Securities Limited v Powlson* [1987] STC 468 (CA) ("*Welbeck Securities*"). There Welbeck had an option to acquire an interest in a property development but proceedings to enforce the option were compromised in the form of a Tomlin order by which Welbeck received £2m and in consideration thereof released and abandoned the option. Welbeck argued (amongst other things) that the £2 million payment was not received in return for disposal of the option. Instead, it was received in return for Welbeck's right, under the Tomlin order, to receive that sum. The Court of Appeal disagreed, holding that the asset that was disposed of was the option: *Welbeck Securities* per Slade LJ, 474e.

76. Similarly HMRC rely on *Kirby v Thorn EMI plc* [1988] 1 WLR 445; [1987] STC 621 (CA). There Thorn and a wholly owned subsidiary entered into an agreement whereby the subsidiary sold shares in three companies to a third party and Thorn covenanted that for a period of five years neither it nor any of its subsidiaries would engage in any of the businesses carried on by the three companies. Thorn received the sum of £575,000 in return for the covenant. The Court of Appeal held that the promise not to compete could not be an asset at the time of the sale because it did not exist at the time of the agreement. Also, a right to carry out business in the marketplace was not an “asset” within the meaning of the legislation. However, the Court explained that goodwill in a particular business was an “asset” and Thorn's covenant amounted to a promise not to exploit its goodwill. That promise was a disposal of its goodwill. It followed that the sum paid to Thorn was, at least in part, a capital sum derived from assets and was therefore within the charge to tax.

77. HMRC say that *BT* is to be distinguished. In that case BT owned a 20% shareholding in another company, MCI. In 1996, BT entered into a merger agreement with MCI. Unless terminated, the merger agreement required MCI and BT (as a shareholder in MCI) to support the BT/MCI merger. The merger agreement contained an express termination provision which provided for termination (amongst other things):

- (1) by mutual consent;
- (2) if all the conditions and steps necessary to implement the merger had not been implemented by a specified date; or
- (3) where a superior offer had been received and the board of directors conclude that the superior offer must be accepted.

78. The payment of a termination fee was a condition for termination pursuant to circumstance (3). MCI subsequently received a superior proposal from another company, Worldcom, with its best and final offer being made on 9 November 1997. On the same day, BT entered into an agreement with MCI and Worldcom. The recitals to the agreement provided expressly that the merger agreement had been terminated “by mutual agreement” and that Worldcom (not MCI) had agreed to pay a sum, equivalent in size.

79. HMRC note that the Special Commissioner, Dr Avery Jones CBE, found that the payment to BT was made to it (as a shareholder) to support the merger with Worldcom. The relevant paragraph in his decision states:

“17. What was the real source of the capital sum? Was the appellant paid for giving up the rights it had against MCI under the Merger Agreement, or for being relieved from its obligation to vote its MCI stock in favour of its merger? In my view in reality the appellant was not being paid to surrender its rights against MCI because in the circumstances these were very slight since MCI could in accordance with s 5.7 of the Merger Agreement recommend the Worldcom merger to its stockholders, and so the appellant’s rights were not worth much. The appellant was paid by Worldcom to support the merger with Worldcom for which it was necessary first to terminate the Merger Agreement containing its obligations to MCI support the merger with itself, for which it was worth Worldcom paying the equivalent of the Alternative Transaction Fee. I do not consider that it is a capital sum derived from assets. The appellant was being paid for supporting the Worldcom merger and in consequence for being relieved from an obligation, not for giving up any asset.”

80. In their written closing HMRC summarise the differences between BT and Dialog’s position as follows:

- (1) In *BT* there was no payment of a termination fee. Instead, the relevant merger agreement was terminated by mutual consent. Also, the party who paid a capital sum to BT was not the proposed merger counterparty (MCI) but the person who made the superior proposal (Worldcom).
- (2) BT’s rights under the merger agreement were weak – MCI could change its recommendation to its shareholders at any point and, in such circumstances, MCI could terminate the agreement without payment on 31 December 1997.
- (3) BT was a shareholder in MCI. BT could not vote its MCI shares in favour of the Worldcom merger unless it was released from its obligations under the BT/MCI Merger Agreement and Worldcom paid BT to vote for the new merger.

NO FORFEITURE, SURRENDER OR REFRAINING

Dialog’s case

81. Dialog say there was no “forfeiture” of rights, “surrender” of rights, or “refraining from exercising” rights, since:

- (1) The ordinary meaning of “forfeiture” of a right is losing that right as a result of either (i) taking an action that one should not or (ii) failing to take an action that one should.
- (2) The ordinary meaning of “surrender” of a right is taking an action that leads to the loss of that right.
- (3) The ordinary meaning of “refraining from exercising” a right is choosing not to make use of that right.

Dialog have done none of these. It was Atmel, not Dialog, that took the actions that led to Dialog's contingent right to a merger falling away.

82. Dialog say, as is normal in a commercial case, where both sides perform their obligations under a contract and thereby discharge it, some of Dialog's contractual rights were satisfied by the counterparty and other rights fell away in accordance with their terms without Dialog forfeiting them, surrendering them, or refraining from exercising them. The contract was discharged by performance.

83. Dialog note the analysis would be very different if there were no provision in the Merger Agreement for Atmel to withdraw from the merger and Atmel had subsequently agreed with Dialog, in return for a substantial sum, to discharge the Merger Agreement.

84. We asked to be addressed, in closing submissions, on whether how the terms surrender and forfeiture are used in English contract and land law may inform the interpretation of this provision. Dialog comment:

“The contract and land law concepts of ‘surrendering’ and ‘forfeiting’ are helpful guides to the interpretation of s 22(1)(c) TCGA. Given s 22(1)(c) is evidently not restricted only to leases, contracts with forfeiture clauses, and so forth, there is a bit more interpretative ‘wriggle-room’. But Parliament chose to use words with significant land law / contract ‘backgrounds’ for a reason. In Dialog’s submission, the consideration of these words’ land law and contract meanings supports the submissions on those words in §47 of Dialog’s skeleton – and indeed, those submissions refer to land law and contract. Bennion, Bailey and Norbury on Statutory Interpretation at 25.2 discusses the position, holding:

‘An Act sometimes uses language which describes a concept in terms that are similar but not identical to an existing legal concept. The question then is whether the legislative intention was to incorporate or attract the common law rules, wholly or in part, or to start afresh’.

In Dialog’s submission, there can be no doubt that the land law and contract meanings were intended to assist in what those words mean in s 22(1)(c) but not limit their meanings only to leases, contracts with forfeiture clauses, or similar.”

HMRC’s case

85. At the hearing we pressed HMRC to specify which of the three possibilities contemplated by s 22(1)(c) HMRC said was in issue. In their written closing they say that they “rely primarily” on the phrase “surrender of rights”, continuing:

“As for the meaning of ‘surrender of rights’, in [*Welbeck Securities*] at 473d, Slade LJ explained that the phrase was intended to bring into charge, among other transactions, ‘surrenders of rights in such manner as to extinguish them or the receipt of capital-sums as consideration for such releases’. A surrender of rights therefore occurs where rights are extinguished in return for capital sums.”

86. HMRC say the Termination Fee was paid to release Atmel from its obligations to Dialog and to render Dialog’s rights under the agreement void: that is a surrendering of rights.

87. HMRC say that it is common ground that if the agreement did not contain a break provision then a payment for terminating the agreement after it had been entered into would be a forfeiture or a surrender. It therefore makes no sense that an *ex ante* agreement to terminate the contract in certain circumstances would not also be a surrender.

88. HMRC also suggest that there could be a “forfeiture”. The relevant part of their written closing states:

“As for ‘forfeiture’, HMRC says that this connotes losing something because of an act or omission. The concept of ‘refraining to exercise’ refers to a person who chooses not to use a right. Whilst HMRC’s primary position is that this appeal fails because Dialog surrendered its rights, in circumstances where Dialog ultimately lost its rights after decided not to exercise its matching rights, the Termination Fee could also be a capital sum in return for ‘forfeiture’ or ‘refraining to exercise’.”

89. HMRC say that if it is the case (as Dialog contend) that surrender, forfeiture or refraining from exercising rights requires some kind of positive step by the person losing their rights, agreeing to the termination clauses in the Merger Agreement was a positive step taken by Dialog and the subsequent receipt of money in return for termination was a surrender. Alternatively, Dialog not exercising its matching rights was such a positive act.

90. Regarding whether how the terms surrender and forfeiture are used in English land and contract law may inform the interpretation of this provision, HMRC comment:

“In accordance with the usual rules of statutory interpretation, when ascertaining the intention of Parliament expressed in the language of a statute, the appropriate starting point is that language is to be taken to bear its ordinary meaning in the general context of the statute. That means that the FTT should approach s 22(1)(c) by having regard to the ordinary and natural meaning of the legislative words. Here, it is not necessary, or appropriate, to import principles and doctrines from land law or contract law in order to interpret the statutory words.”

NO CGT ASSET

Dialog’s case

91. Dialog say s 22(1) TCGA 1992, of which s 22(1)(c) is a subspecies, requires a capital sum to be “derived from assets”. However the Merger Agreement was not an asset for CGT purposes.

92. Dialog concede that assets are widely defined in s 21(1) TCGA 1992 and that contractual rights are capable of being an asset for CGT provided they can be turned to account (even if they cannot be transferred or assigned): *O’Brien (Inspector of Taxes) v Benson’s Hosiery (Holdings) Ltd* [1980] AC 562, 573 (HL) (“*O’Brien*”).

93. However, not all contractual rights, even if they can be turned to account, are assets for CGT purposes. In *Zim*, it was held that the contractual right to payment of a vendor of property is not a CGT asset. In *Hardy v HMRC* [2016] UKUT 332 (TCC) (“*Hardy*”) this was taken further, where Arnold J and Judge Sinfield explained (at [40]) that not only is the contractual right to payment of a vendor of property not a CGT asset, but neither is the purchaser’s contractual right to acquire the property. In *Sehgal v HMRC* [2022] UKFTT 312 (TC); [2023] SFTD 212 (“*Sehgal*”) at [104(4)] Judge Short summarised the principle from *Hardy* as:

“When looking at a bi-party contract relating to an underlying asset, the rights arising under the contract cannot be separated from the asset which is the subject of the contract”.

94. Dialog say that it had contingent rights under the Merger Agreement that were, in essence, those of a purchaser of property. They point especially to § 1.4, 2.1(a), 2.1(c) and 8.9 of the Merger Agreement. Therefore the rights under the Merger Agreement were not an asset for CGT purposes.

95. Further, to show the impractical consequences that would arise if the contractual rights of a purchaser of property were an asset for CGT purposes, they put forward the example of a taxpayer who contracts to buy rural land for £1m and finds – between exchange of contracts and completion – a gold deposit on the land giving it a new estimated value of £50m.

HMRC's case

96. Contractual rights can be assets: *O'Brien* at 573C-G per Lord Russell; *Marren (Inspector of Taxes) v Ingles* [1980] 1 WLR 983 (HL) at 986A, per Lord Wilberforce; *Zim* at 104d, per Warner J. Not all contractual rights are assets. As Warner J explained in *Zim* at 108c, the “right of a seller of property to payment of its price” is not an asset. This position is in common with the Dialog.

97. HMRC suggest that *Hardy* and *Sehgal* are of limited relevance because they concern contracts for the purchase of land.

98. In *Zim* at 107b and following, Warner J recorded the arguments that were being advanced by the taxpayer's counsel (including the argument that “a right to compensation for loss is not an asset for capital gains tax purpose”). Warner J did not accept those arguments, explaining at 108c that there could not be “a brute application of verbal formulae”. The outcome of *Zim* was that a right to sue the taxpayer's solicitors for damages was an asset – it must follow that a right to compensation for loss can be an asset for capital gains tax purposes.

DISCUSSION

“In return for”

99. We do not consider it realistic to describe the Merger Agreement as discharged by performance, in an equivalent way that would have occurred if the merger was consummated, when the Termination Fee was paid.

100. From a commercial perspective, the purpose of the Merger Agreement was for Dialog and Atmel to set out the steps they would both take to work towards a merger. The business objective was to consummate a merger. The aim of the transaction was not for a termination fee to be paid. That is clear from Dr Bagherli's testimony. It is also clear from the recitals to the Merger Agreement, which Mrs Dearlove confirmed could be an aid to the construction of the Merger Agreement.

101. We do not accept that, immediately prior to the termination of the Merger Agreement, the rights of Dialog were slight. At that point they were able to enforce significant contractual restrictions against Atmel: including by specific performance. Those restrictions included limitations on Atmel relating to the payment of dividends, issuing shares, setting the compensation of its directors and employees, making loans to directors, taking out loans, changing accounting standards, making tax elections, acquiring stock and assets, altering material contracts, alienating IP and engaging in litigation. Furthermore, Atmel were not able to enter into the merger agreement with Microchip without paying the Termination Fee “substantially concurrently” with termination. Accordingly Dialog had the right to prevent Atmel's board from recommending a different proposal.

102. Given that Dialog had decided not to make a counter-offer to outbid Microchip, immediately prior to the moment of termination these rights were of limited inherent utility for Dialog, aside from the ability to extract payment from Atmel/Microchip to free Atmel of these restrictions. However, these were onerous restrictions on Atmel (see [101] above), and therefore these rights had value. Viewed realistically, the Termination Fee was, at least partly, in return for freeing Atmel from these restrictions.

103. The Termination Fee also had an important compensatory function. It was not solely to compensate for out-of-pocket expenses. That is clear from the amount of the fee vastly

exceeding the out-of-pocket expenses incurred by Dialog. The difference is so large it cannot have been a genuine pre-estimate of just out-of-pocket expenses. Rather, some of it must represent compensation for the loss of opportunity. Indeed, that is consistent with the general position on termination fees (see [60] above).

104. We acknowledge that the Termination Fee had a deal protection function too, to deter higher bids: see [63(2)] above. However, we find this to be a secondary function as the Merger Agreement specifically states the function of the Termination Fee is compensation (see [42] above) and, as we were repeatedly told in the experts' testimony, Delaware law supports freedom of contract and seeks to give effect to what the parties have agreed.

105. We therefore find that the real source of the Termination Fee is as a compensatory payment for the loss of opportunity for pursuing the Merger and also to compensate for out-of-pocket expenses. The timing of the payment of the Termination Fee does not alter this – it is not uncommon in commercial agreements for the price to be paid after delivery of goods or performance of services. Thus, even if the rights under the Merger Agreement were not in existence when the Termination Fee was paid, that does not preclude the Termination Fee from having been paid in compensation for their loss.

106. Dialog's arguments seek to characterise payment of the Termination Fee as just an alternative method of performance. Viewed realistically, for the reasons we have stated above, that is inapt characterisation. The Termination Fee is, in essence, a break-fee paid to enable termination of the contract, not an alternative method of performance. We disagree with the arguments made by Dialog in relation to the "in return for" point, for that reason: those arguments are all essentially premised on payment of the Termination Fee being just another form of performance.

107. We agree with HMRC's analysis of the case law in relation to the "in return for" point, which we have summarised at [74] to [80] above and therefore do not repeat.

108. We find that, viewed realistically, the termination fee was paid to compensate Dialog for losing their rights under the Merger Agreement. Viewed realistically it was therefore paid *in return* for the loss of those rights.

No forfeiture, surrender or refraining

109. We agree with Dialog's submission as to the ordinary meaning of "forfeiture", "surrender", and "refraining from exercising" rights, being:

- (1) "forfeiture" of a right is losing that right as a result of either (i) taking an action that one should not or (ii) failing to take an action that one should;
- (2) "surrender" of a right is taking an action that leads to the loss of that right; and
- (3) "refraining from exercising" a right is choosing not to make use of that right.

110. HMRC agree with these definitions of "forfeiture" and "refraining from exercising" (see [88] above), but with regard to "surrender" suggest that "[a] surrender of rights therefore occurs where rights are extinguished in return for capital sums".

111. We do not agree with that definition, which we note essentially paraphrases the introductory part of s 22(1) TCGA 1992 ("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"), except that it narrows it somewhat, essentially by replacing "notwithstanding that" with "and". There is no particular reason why a surrender need necessitate rights being extinguished, they may simply be transferred to the person to whom the surrender is made. That is apparent from the general legal use of the term surrender: for example a person surrendering to bail.

112. HMRC's definition of surrendered would essentially render redundant the introductory part of s 22(1) TCGA 1992, if it is accepted, as it must be, that surrender does not require property rights to be extinguished. Such a definition would be inconsistent with the structure of the subsection, which specifies "surrender" as a particular example.

113. More fundamentally we agree that surrender implies that the person making the surrender takes the action that leads to the loss of that right. Such an interpretation is consistent with the structure of subsection s 22(1)(c) TCGA 1992, as it provides a contrasting circumstance to the other two definitions that HMRC agree with.

114. Applying these definitions to the facts, we first address HMRC's submission that there was "forfeiture" or "refraining from exercising" a right, as Dialog did not exercise its matching rights (see [89] above).

115. We find there was no forfeiture, as Dialog was not required to exercise those matching rights, they were just an option available to Dialog. Accordingly, Dialog did not fail to do something it should have done.

116. It is true that, for the Termination Fee to be paid, Dialog had to refrain from exercising its matching rights. But we find the Termination Fee was not, viewed realistically, "in return for... refraining from exercising" the matching rights. Indeed, Atmel had no reason to disincentivise Dialog from exercising those rights, as it would drive up the offer price, offering better value to its shareholders. It is not something that they would pay for. Rather, as we have already found, viewed realistically the Termination Fee was paid to Dialog for the loss of their rights under the Merger Agreement.

117. There was no surrender, as there was no action that Dialog took that led to the loss of their rights under the Merger Agreement. Rather termination came about because it *did not exercise* its matching rights. HMRC suggest that including the termination provision in the Merger Agreement was an act that amounted to a surrender. However, that cannot be right. Including the termination provisions did not lead to the loss of the rights under the Merger Agreement, it only brought about the possibility of the loss of those rights. Something more was required – an unsolicited superior proposal that Dialog did not match.

118. It is common ground that if the agreement did not contain a break provision then a payment for terminating the agreement after it had been entered into would be a forfeiture or a surrender. HMRC submit that it makes no sense that an *ex ante* agreement to terminate the contract in certain circumstances would not also be a surrender. However, the crucial distinction is that one leads to the loss of the rights and the other only possibly does. Further, in *Barrett v Morgan* [2000] UKHL 1; [2000] 2 AC 264 at 270H, 272B, 273C Lord Millet repeatedly emphasised that a "surrender" takes place other than in accordance with the terms of the agreement. Whilst this was a land law case, we consider that this can legitimately inform the interpretation of s 22(1)(c) TCGA 1992, especially because a lease can be an asset falling within this provision.

119. Similarly, in *Davis v Powell* [1977] 1 WLR 258; [1977] STC 32, Templeman J considered a payment of statutory compensation, following a notice to quit, payable pursuant to section 34 of the Agricultural Holdings Act 1948:

"this s 34 compensation is not a capital sum received in return for the surrender of rights. It is not paid as a result of a bargain in which the tenant says, 'If I get out, will you pay me £591?' It is a sum paid where a tenant is faced with a notice to quit and must get out."

120. This again suggests a surrender requires action on the part of the surrendering party, which leads to the loss of the right.

121. Our interpretation of “surrender” is reinforced by the fact that, in land law, it is generally treated as a concept distinct from a break clause. This distinction is evident in the treatment of the topics under separate headings in Megarry & Wade, *The Law of Real Property* (10th Ed, 2024) Chapter 17 and Gray & Gray, *Elements of Land Law* (5th Ed, 2008) “Termination of leases and tenancies” 4.2.103 et seq., as well as in the passages from *Barrett v Morgan* to which we have already referred.

122. Furthermore, we observe that while the inclusion of a break clause is not a “surrender” its operation may, at least arguably, lead to a charge under a part of s 22 TCGA 1992 other than s 22(1)(c) – perhaps the introductory part of s 22(1) TCGA 1992 or perhaps s 22(1)(a) TCGA 1992. At the hearing HMRC explained they did not make the assessment under the introductory part of s 22(1) TCGA 1992 as they wished to take advantage of the timing under s 22(2) TCGA 1992, which did not apply unless the disposal fell within one of the particular examples in s 22(1)(a)-(d) TCGA 1992. At the hearing HMRC also explained that they had not considered s 22(1)(a) TCGA 1992.

123. We mention this because HMRC’s case is implicitly based on an argument that excluding the exercise of a break clause from the definition of a surrender results in the exercise of a break clause being taxed differently than a payment for terminating the agreement after it had been entered. However, we consider it arguable that this is not the case.

124. The issue was raised by the panel at the hearing but we have not heard extensive argument on this point. We record this as, for the reason given at [123] above, the issue informs our interpretation of s 22(1)(c) TCGA 1992. However, other than that, it cannot alter the outcome of this appeal – as the preliminary point we have been asked to rule on solely concerns s 22(1)(c) TCGA 1992.

125. We therefore allow the appeal on the basis that there was no forfeiture, surrender or refraining.

126. We however disagree with Dialog in that we do not regard the contract as “discharged by performance” (see [82] above), but rather terminated in accordance with the break-clause. This is essentially for the reasons we have discussed in the previous section. We also note that the textbooks we referenced at [120] above treat break-clauses as instances of termination rather than performance, which reinforces our view that a break clause is not simply an alternate means of performance (see [106] above).

No CGT asset

127. It is common ground that assets are widely defined in s 21(1) TCGA 1992 and that contractual rights are capable of being an asset for CGT provided they can be turned to account (even if they cannot be transferred or assigned).

128. Contractual rights can be assets. However the contractual right to payment of a vendor of property is not a CGT asset. Neither is the purchaser’s contractual right to acquire the property: *Hardy*. The outcome of *Zim* shows that a right to compensation for loss can be an asset for capital gains tax purposes.

129. Here Dialog characterise the Merger Agreement as akin to a contract to acquire property, namely the shares in Atmel. We reject that characterisation. At its simplest this is shown by how the shares were owned by the stockholders, yet the Merger Agreement was with Dialog. The Merger Agreement simply cannot be a contract to acquire property. We accept the Merger Agreement is to facilitate the acquisition of the shares in Atmel. However that is a different matter. It therefore falls outside the *ratio* of *Hardy*.

130. We do not consider it relevant that *Hardy* and *Sehgal* concern land. Nothing in those decisions suggest that their reasoning is so restricted.

131. Rather, the Termination Fee is, as we have already found, compensatory in nature. We therefore find it to be a capital asset in line with HMRC's submissions on *Zim*.

CONCLUSION

132. We have found the Termination Fee does not fall within s 22(1)(c) TCGA 1992, but have found in Dialog's favour only in relation to the question of there being no forfeiture, surrender or refraining. This decision is not authority that the Termination Fee would not otherwise fall within s 22 TCGA 1992 – that is a question outside the preliminary issue, other than as potentially relevant as discussed at [120]-[123] above.

133. It was agreed that if the preliminary issue is resolved finally in Dialog's favour, then the closure notice will be withdrawn such that there is no additional tax due from Dialog.

134. It follows that the appeal is allowed.

RIGHT TO APPLY FOR PERMISSION TO APPEAL

135. This document contains full findings of fact and reasons for the decision. Any party dissatisfied with this decision has a right to apply 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 this Tribunal not 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.

Release date: 03rd OCTOBER 2025