[2019] UKFTT 0558 (TC)

TC07351

Corporation tax – capital allowances – transfer of trade using leased satellites whose launch costs had been separately incurred by transferor – whether successor entitled to writing down allowances on an apportioned part of the market value at the time of transfer based on predecessor's launch costs of the satellites – sections 78(1) & 61(4) CAA 1990 – held no

FIRST-TIER TRIBUNAL
TAX CHAMBER

Reference number: TC/2017/01134

BETWEEN

INMARSAT GLOBAL LIMITED — **First Referrer**

-and-

THE COMMISSIONERS FOR HER MAJESTY'S REVENUE AND CUSTOMS — **Second Referrers**

TRIBUNAL: JUDGE KEVIN POOLE

Sitting in public at the Royal Courts of Justice, London on 14-16 & 19 November 2018

Kevin Prosser QC and Barbara Belgrano, counsel, instructed by Stephenson Harwood LLP, for the First Referrer

Michael Gibbon QC, Richard Vallat QC and Ronan Magee, counsel, instructed by the General Counsel and Solicitor to HM Revenue and Customs, for the Second Referrers

DECISION

INTRODUCTION

1. This decision addresses a joint referral by the parties to the Tribunal for determination of a question arising in the course of an enquiry into the corporation tax self-assessment returns of the First Referrer ("Inmarsat") for the accounting period ended 31 December 1999 and subsequent periods.

2. The question (and the surrounding factual circumstances to which it relates) are set out in full below, but in essence the issue is as follows.

3. Inmarsat succeeded to the activities previously carried on by the International Maritime Satellite Organisation (a body corporate established pursuant to an international convention) ("IMSO"). IMSO had contracted for the purchase of six satellites ("the Satellites"), which were subsequently acquired (and paid for) by lessors and leased to IMSO. It arranged for all six Satellites to be put into service by launching them. IMSO itself incurred the costs of launching the Satellites into their respective orbits. IMSO was exempt from UK corporation tax. The lessors of the Satellites had claimed capital allowances on their capital expenditure incurred in the acquisition of the Satellites (but not on the expenditure incurred by IMSO on their launch), and accordingly whilst IMSO itself was not directly entitled to the benefit of those capital allowances, the availability of those allowances to the lessors would no doubt have been taken into account in setting the rental payments under the leases of the Satellites.

4. IMSO subsequently transferred its business to Inmarsat, and the lease agreements relating to the Satellites were (along with certain other contracts) novated, such that from the time of the business transfer the Satellites were leased to Inmarsat, which was responsible (in place of IMSO) for making the rental payments.

5. As a result of these transactions, Inmarsat claims to be entitled, by virtue of section 78(1) Capital Allowances Act 1990 ("CAA90"), to writing down allowances on some part of the open market value of the Satellites as at the date of the business transfer. In reply to the objection that the Satellites "belonged" at all relevant times to the lessors, meaning that one of the fundamental requirements for the availability of writing down allowances was absent, Inmarsat claims that section 61(4) CAA90 provides a complete answer, effectively deeming the Satellites to have belonged to IMSO before the business transfer; and accordingly, it maintains, by virtue of section 78(1) CAA90 the Satellites were deemed to be sold to Inmarsat as a result of the business transfer on the basis of their open market value at that time, thus entitling Inmarsat to capital allowances on a proportion of that open market value.

THE FACTS

Introduction

6. The facts are complex, but are not in dispute.

7. I received witness statements made by Mark Dickinson, Inmarsat's "Deputy Chief Technology Officer and Vice President of the Space Segment"; and from Darren Hawkins, a chartered accountant with MDT (UK) Limited, specialising in lease finance especially in the aviation and shipping sectors, who had spent some time on secondment to IMSO and subsequently provided leasing advice to it (and Inmarsat), including in relation to at least some of the satellites under consideration in this reference. The Second Referrers ("HMRC") accepted the witness statements made by Mr Dickinson and Mr Hawkins, who were not required to give oral testimony. There was no witness evidence from HMRC.

Background

8. The Convention on the International Maritime Satellite Organization (INMARSAT) ("the Convention") was entered into in London on 3 September 1976. It was ratified by the United Kingdom on 30 April 1979 and came into force on 16 July 1979. The main maritime nations were parties. The Convention established IMSO, whose purpose was set out as being to "make provision for the space segment necessary for improving maritime communications[1], thereby assisting in improving distress and safety of life at sea communications, efficiency and management of ships, maritime public correspondence services and radiodetermination capabilities." The Council of IMSO was established, with power to "perform all appropriate functions, including…adoption of policies, plans, programmes, procedures and measures for the design, development, construction, establishment, acquisition by purchase or lease, operation, maintenance and utilization of the INMARSAT space segment, including the procurement of any necessary launch services to meet such requirements."

9. Article 5(3) of the Convention provided that IMSO "shall operate on a sound economic and financial basis having regard to accepted commercial principles" and under Article 19 of the Convention, it was provided that IMSO should charge for the use of its system, and that:

> "These charges shall have the objective of earning sufficient revenues for the Organization to cover its operating, maintenance, and administrative costs, the provision of such operating funds as the Council may determine to be necessary, the amortization of investment made by Signatories, and compensation for use of capital in accordance with the Operating Agreement."

10. The headquarters of IMSO were established in the United Kingdom, and the Inmarsat (Immunities and Privileges) Order 1980 recognised IMSO as having "the legal capacities of a body corporate" and confirmed that "[w]ithin the scope of its official activities, [it] shall have exemption from taxes on income and capital gains." Notwithstanding such exemption, at all material times until 15 April 1999 IMSO was a body corporate (and therefore a company for corporation tax purposes) which was resident in the UK. Mr Prosser submitted that IMSO was carrying on a trade of operating a telecommunications satellite system on a commercial basis and Mr Gibbon did not contest the point, which I accept.

11. As a key part of its activities, IMSO commissioned the construction and launch of the six Satellites which are the subject of this reference.

The commissioning of the six Satellites

12. IMSO commissioned three so-called second generation satellites ("the I-2 Satellites") and three so-called third generation satellites ("the I-3 Satellites")[2]. All were leased from third party lessors (the leasing arrangements being put in place well after IMSO had contracted to acquire the Satellites) and IMSO separately incurred expenditure (which is agreed to be capital expenditure) on procuring their launch and placement into the correct orbits.

13. The respective finance lessors claimed capital allowances on the capital expenditure incurred by them on the provision of the various Satellites for their (actual or deemed) leasing trades. No such allowances were claimed on any costs of launching the Satellites (which costs were incurred and paid by IMSO and formed no part of the leasing arrangements).

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[1] Amended to include aeronautical services by an amendment to the Convention which entered into force on 13 October 1989.

[2] It also commissioned other satellites, but those are not relevant to these proceedings.

The I-2 Satellites

14. By a contract dated 15 April 1985 between British Aerospace plc ("BAe") and IMSO ("the BAe Contract"), BAe agreed to construct and sell to IMSO the three I-2 Satellites, with title and risk to pass at intentional ignition of any first stage engine of the launch vehicle for each satellite. If any of the satellites was delivered for storage prior to launch, then title (but not risk) was to pass earlier.

15. By a contract dated 15 October 1986 between IMSO and Arianespace (a French limited company) it was agreed that the I-2 Satellite subsequently designated F3 would be launched into orbit from Kourou, French Guiana.

16. By a contract dated 31 July 1987 between IMSO and McDonnell Douglas Corporation ("MDC") it was agreed that the I-2 Satellite subsequently designated F1 would be launched into orbit from Cape Canaveral, USA.

17. By a contract dated 31 March 1988 between IMSO and MDC it was agreed that the I-2 Satellite subsequently designated F2 would be launched into orbit from Cape Canaveral.

18. Subsequent arrangements were made on 28 September 1988 for the three I-2 Satellites being built by BAe to be purchased by North Sea Marine Leasing Company ("NSM") (a firm comprising BMI Marine Limited, Lloyds Leasing (North Sea Transport) Limited, Lombard Facilities Limited and Midland Gillett Leasing (North) Limited) and leased by it to IMSO. This involved the execution of a series of agreements all dated 28 September 1988, most crucially:

(1) an Agreement to Acquire and Lease between NSM and IMSO under which NSM agreed to acquire and lease the three I-2 Satellites being built by BAe to IMSO pursuant to finance leases;

(2) a Novation Agreement between BAe, IMSO and NSM under which NSM assumed the rights and obligations of IMSO under the BAe Contract regarding the passing and acceptance of title and risk, and payment in respect of the same three satellites;

(3) a Master Lease Agreement between NSM and IMSO under which NSM agreed to lease the three I-2 Satellites being built by BAe to IMSO for an initial period of not less than 10 years and 9 months (and not longer than 11 years 6 months) (subject to possible annual extensions), and three associated Lease Schedules (one for each satellite) setting out the detailed financial terms of each letting; and

(4) a Supervision Agreement between NSM and IMSO under which IMSO agreed to supervise the construction, supply and delivery of the three I-2 Satellites on behalf of NSM.

19. The F1, F2 and F3 I-2 Satellites were successfully launched on, respectively, 30 October 1990, 8 March 1991 and 16 December 1991.

The I-3 Satellites

20. By a contract dated 1 February 1991 between General Electric Technical Services Company Inc ("GETSCO") and IMSO ("the GETSCO Contract"), GETSCO agreed to construct and sell to IMSO the three I-3 Satellites. Title and risk of loss or damage were to pass at intentional ignition of any first stage engine of the launch vehicle for each satellite or, if earlier, upon expiration of GETSCO's warranty.

21. Subsequent arrangements were made on 20 December 1991 for the three I-3 Satellites to be purchased by Abbey National December Leasing (3) Limited ("Abbey") and leased by it to IMSO. This involved the execution of a series of agreements all dated 20 December 1991, most crucially:

(1) a Lease Facility Agreement between Abbey and IMSO under which Abbey made a commitment to acquire and lease to IMSO the I-3 Satellites;

(2) a Novation Agreement between GETSCO, IMSO and Abbey under which Abbey assumed the rights and obligations of IMSO under the GETSCO Contract regarding the passing and acceptance of title and risk and payment;

(3) a Master Lease Agreement and three Lease Schedules between Abbey and IMSO, under which Abbey agreed to lease the three I-3 Satellites to IMSO pursuant to finance leases for a period ending 13 years after launch in each case; and

(4) a Supervision Agreement (or possibly three separate similar agreements) between Abbey and IMSO in which it was stated that IMSO had agreed to act on behalf of Abbey to supervise the delivery of the satellites to Abbey.

22. By a contract dated 1 May 1992 between IMSO and General Dynamics Commercial Launch Services Inc ("GDCLS"), GDCLS agreed to launch the I-3 Satellites subsequently designated F1 and F3 into orbit from Cape Canaveral.

23. By a contract dated 27 April 1993 between IMSO and Design Bureau Salyut ("DBS"), subsequently novated by contracts dated 8 March 1994 and 17 April 1994 in favour of Krunichev State Research and Production Space Center ("KRSPSC"), DBS/KRSPSC agreed to launch the I-3 Satellite subsequently designated F2 into orbit from Baikonur, Kazakhstan.

24. The three I-3 Satellites were successfully launched on, respectively, 3 April 1996, 6 September 1996 and 18 December 1996.

Transfer of IMSO business

25. Following protracted discussion between all the various interested parties, a decision was taken to transfer the business of IMSO to a new company established for the purpose in exchange for an issue of shares. The transfer was effected on 15 April 1999 and the transferee was Inmarsat (in its then name of Inmarsat Two Company).

26. A large number of contracts and associated documentation were required in order to effect the transfer. The key ones for present purposes were a Business Transfer Agreement between IMSO and Inmarsat (the form of which was laid down in Schedule 8 to the Master Transition Agreement involving all relevant parties) and two Novation Agreements between the respective finance lessors, IMSO and Inmarsat.

27. Pursuant to the Business Transfer Agreement, IMSO transferred its "Business Assets" (as defined, which did not include the Satellites) to Inmarsat in exchange for an allotment of 100,000,000 ordinary shares of £1 each, credited as fully paid. Pursuant to the two Novation Agreements, IMSO was "released from all obligations and liabilities under the Novated Documents[3], whether arising on, before or after" the transfer of IMSO's business to Inmarsat, and Inmarsat became "bound by the Novated Documents as if all references therein to the Lessee or INMARSAT (however expressed) were references to" Inmarsat.

28. Mr Prosser submitted that after the transfer, Inmarsat carried on the same trade as had previously been carried on by IMSO, and again Mr Gibbon did not disagree. It is therefore common ground that the Business Transfer Agreement gave rise to a succession to the trade of IMSO by Inmarsat.

29. Following the succession, Inmarsat sought to claim writing down allowances, effectively in respect of the capital expenditure incurred by IMSO in procuring the launch of the Satellites.

[3] This phrase included the various leasing agreements.

That claim led to enquiries by HMRC into all relevant corporation tax returns of Inmarsat from 1999 onwards. The parties have been unable to agree on the claims, leading ultimately to the referral of the question which is the subject of these proceedings.

THE QUESTION REFERRED

30. The question specified by the parties for referral is as follows:

> "Is Inmarsat Global Limited entitled to capital allowances in respect of the Satellites specified below for its accounting period ended 31 December 1999 and subsequent accounting periods and, if so, in what amount(s)?
>
> The Satellites are each of:-
>
> The Item 1 Protoflight Spacecraft (the "I2-Fl Satellite")
>
> The Item 2 Second Flight Spacecraft (the "I2-F2 Satellite")
>
> The Item 3 Third Flight Spacecraft (the "I2-F3 Satellite")
>
> supplied by British Aerospace Public Limited Company under a contract originally dated 15th April 1985 and entered into originally between British Aerospace Public Limited Company and the International Maritime Satellite Organisation ("IMSO") and launched under a contract originally dated as of 31 July 1987 between McDonnell Douglas Corporation and IMSO (INM/86-213) (the I2-Fl Satellite), a contract dated as of 31 March 1988 between McDonnell Douglas Corporation and IMSO(INM/88-300/GC) (the I2-F2 Satellite), and a contract dated 15 October 1986 between Arianespace and IMSO (INM/86-210/DD) (in respect of the launch of the I2-F2 Satellite, but later amended under an agreement - amendment number 5 - dated 10 April 1989 to launch the I2-F3 Satellite),
>
> and each of
>
> The Item 1 Protoflight Spacecraft (PFM) (the "I3-Fl Satellite")
>
> The Item 2 Second Spacecraft (F2) (the "I3-F2 Satellite")
>
> The item 3 Third Spacecraft (F3) (the "I3-F3 Satellite")
>
> supplied by the General Electric Technical Services Company Inc ("GETSCO") under a contract between GETSCO and IMSO with effective date 1 February 1991 and launched under a contract dated 1 May 1992 (INM/92-786/YW) (the I3-F1 and I3-F3 Satellites) between General Dynamics Launch Services Inc and IMSO, and a contract dated 27 April 1993 between Design Bureau Salyut (DB Salyut) and IMSO (INM/93-972/YW) (the I3-F2 Satellite)"

31. If the question is answered in the affirmative in principle, the parties are agreed that a further hearing would be necessary to determine the amounts of allowances available, if they are not agreed.

THE MAIN RELEVANT LEGISLATION

32. The parties agreed that the main relevant legislation was that contained in CAA90. This provided, in relevant part, as follows:

> **24 Writing-down allowances and balancing adjustments**
>
> (1) Subject to the provisions of this Part, where –
>
> (a) a person carrying on a trade has incurred capital expenditure on the provision of machinery or plant wholly and exclusively for the purposes of the trade, and

(b) in consequence of his incurring that expenditure, the machinery or plant belongs or has belonged to him,

allowances and charges shall be made to and on him in accordance with the following provisions of this section.

…

(6) … the disposal value to be brought into account by a person for any chargeable period is the disposal value of all machinery or plant –

(a) on the provision of which for the purposes of the trade he has incurred capital expenditure;

(b) which belongs to him at some time in the chargeable period; and

(c) in respect of which, in the chargeable period, one of the following events occurs, namely –

(i) the machinery or plant ceases to belong to him,

…

and that is the first such event to occur;

…

61 Machinery and plant on lease

(1) Subject to subsection (2) below, where machinery or plant is first let by any person otherwise than in the course of a trade, then, whether or not it is used for the purposes of a trade carried on by the lessee –

(a) the capital expenditure incurred by the lessor in providing the machinery or plant shall be treated for the purposes of this Part as having been incurred in providing it for the purposes of a trade begun to be carried on by him, separately from any other trade which he may carry on, at the commencement of the letting, and

(b) at the time when the lessor permanently ceases to let the machinery or plant otherwise than in the course of a trade, the machinery or plant shall be treated for the purposes of this Part as being used wholly for purposes other than those of the trade referred to in paragraph (a) above.

…

(4) Where –

(a) a lessee incurs capital expenditure on the provision for the purposes of a trade carried on by him of machinery or plant which he is required to provide under the terms of the lease, and

(b) the machinery or plant is not so installed or otherwise fixed in or to a building or any other description of land as to become, in law, part of that building or other land,

then, if the machinery or plant would not otherwise belong to him, the machinery or plant shall be treated for the purposes of this Part as belonging to him for so long as it continues to be used for the purposes of the trade; but, as from the determination of the lease, section 24(6) shall have effect as if the capital expenditure on providing the machinery or plant had been incurred by the lessor and not by the lessee.

…

> (8) In this section "lease" includes an agreement for a lease where the term to be covered by the lease has begun, and any tenancy, but does not include a mortgage, and "lessee" and other cognate expressions shall be construed accordingly.
>
> …
>
> **78 Succession to trades where no election made under section 77**
>
> (1) Where a person succeeds to any trade which until that time was carried on by another person and, by virtue of section 113 or 337(1) of the principal Act (changes in persons carrying on a trade, and special rules for corporation tax), the trade is to be treated as discontinued, any property which, immediately before the succession takes place, was either in use or provided and available for use for the purposes of the discontinued trade and, without being sold, is, immediately after the succession takes place, either in use or provided and available for use for the purposes of the new trade shall, for the purposes of this Part be treated as if –
>
> (a) it had been sold to the successor when the succession takes place, and
>
> (b) the net proceeds of the sale had been the price which that property would have fetched if sold in the open market;
>
> but no first-year allowance shall be made by virtue of this subsection.
>
> …

33. It is common ground that s 337(1) Income and Corporation Taxes Act 1988 ("TA88") (as referred to in s 78(1) CAA90) applied so as treat IMSO's trade as discontinued. References in this decision to sections and subsections refer to CAA90 unless otherwise stated.

ARGUMENTS

Outline arguments for Inmarsat

34. Mr Prosser's argument, in outline, was as follows.

35. Inmarsat had succeeded to the trade of IMSO on 15 April 1999. Under s 337(1) TA88, IMSO's trade was treated as discontinued. The Satellites were, immediately before the succession, in use for the purposes of IMSO's trade. They were not sold. Immediately after the succession, they were in use for the purposes of Inmarsat's new trade. Accordingly, under s 78(1) CAA90, for the purposes of plant and machinery allowances each Satellite should be treated as if it had been sold to Inmarsat on 15 April 1999 at a net sale price equal to its open market value.

36. It followed from this that Inmarsat was entitled to writing down allowances under s 24 on such open market value; however, in recognition of the fact that the lessors of the Satellites in fact owned them throughout the whole period, the allowances available to Inmarsat should be calculated on an apportioned part of their market value, the apportionment to reflect the respective amounts of capital expenditure incurred by the lessors on their acquisition of the Satellites and by IMSO on launching the completed Satellites and placing them into the correct orbits. As Mr Prosser put it:

> given that [each] Satellite is treated as belonging to IMSO and to the Lessors in relation to the capital expenditure incurred by them, Inmarsat submits that the market value for s 78(1) purposes should be calculated as a fraction (x/x+y) of the market value of the Satellite, where x is the amount of Launch Expenditure incurred by IMSO, and y is the amount of capital expenditure incurred by the relevant Lessor.

37. Some of the intermediate steps in this argument were amplified as follows.

38. Mr Prosser accepted that, for s 78(1) to apply, it was a requirement that assets in question must have belonged to the predecessor trader (in this case IMSO): "after all, the predecessor cannot sell what does not belong to him".

39. On the face of it, this requirement was not satisfied here, as the Satellites belonged throughout to the lessors. This apparent problem was, however, overcome in the present case by virtue of the deeming provision contained in s 61(4) which, in his submission, deemed the Satellites to have belonged to IMSO for the purposes of plant and machinery allowances up to the time of the succession on 15 April 1999.

40. IMSO, in incurring the capital costs of launching the Satellites, had in Mr Prosser's submission incurred capital expenditure on the provision for the purposes of its trade of the launched and operational Satellites, having been required to provide them under the terms of the lease documentation. As a result, the Satellites were to be treated as belonging to it by virtue of s 61(4) up to the succession on 15 April 1999. That was all that was necessary to satisfy the "belonging" requirement of s 78(1).

41. It did not matter that the Satellites actually belonged throughout to the lessors. Notwithstanding the general position that sole ownership of the relevant asset was an essential prerequisite to the availability of allowances, there were other examples in the capital allowances code of allowances being available without ownership. Here, he pointed in particular to the "contribution" provisions in ss 153 to 155.

42. Mr Prosser submitted that this argument gave "a sensible result, indeed more sensible than any alternative", and was "wholly consistent with a purposive construction" of the provisions: it did not "give rise to any possibility of double allowances in respect of the same expenditure, or produce any other results which Parliament cannot have intended".

Outline arguments for HMRC

43. Mr Gibbon attacked Mr Prosser's analysis at a number of points. First, it was clear that the "rational scheme [of capital allowances] in relation to machinery and plant has as a central feature the concept of ownership." There were certain very carefully crafted exceptions to this central feature, but the present case fell outside them. Inmarsat's case relied extensively on various deeming provisions in the legislation, beyond the point that was legitimate in the light of the authorities on such provisions.

44. Second, he argued that allowances were available for expenditure on "the provision" of machinery or plant. It was accepted that this extended beyond the bare purchase cost and covered ancillary costs such as transport and installation; however it did not extend to transport and installation costs incurred in isolation from the acquisition of the relevant machinery or plant.

45. Third, he submitted that s 61(4) could not apply in the present case because it could not fairly be said that the launch expenditure costs incurred in isolation by IMSO were on the "provision" of the Satellites; because there was no contractual obligation imposed by the lease documents to "provide" the Satellites; and because any effect of s 61(4) would have ceased upon novation of the various leases at the time of the succession on 15 April 1999, treating the lessors as having incurred the relevant expenditure thereafter.

46. Fourth, he submitted that it was implicit in s 78(1) that for it to apply (and certainly for s 78(1) to have any effect so far as the successor is concerned), the successor must become the owner of the relevant plant or machinery. That was not the case here, either in fact or on the basis of any deeming effect of s 61(4).

47. Fifth, if the preconditions for s 78(1) to apply were satisfied, its effect focused on the nature of the transfer from the predecessor to the successor, not on the state of affairs brought

about by the deemed sale. In particular, it did not expressly deem the property to belong to the successor, it was not a necessary consequence of the predecessor's deemed sale that it should do so, and crucial questions about the supposed deemed ownership of the successor were left unaddressed. Accordingly, the section should not be taken to deem the successor to be the owner of the asset in question if it was not the owner "in the real world".

48. Sixth, even if it applied, s 78(1) did not deem Inmarsat to have satisfied the other requirements of s 24; in particular it did not deem Inmarsat to have incurred expenditure on the provision of machinery or plant wholly and exclusively for the purposes of its trade, nor did any such purpose flow inevitably from the deemed sale. In his submission, this indicated that s 78(1) was dealing with a much more limited question, namely how the transfer value between two parties was to be determined where there had not been a sale at the time of the transfer of the relevant asset from the predecessor to the successor.

DISCUSSION

Preliminary points

49. It must not be forgotten that Inmarsat's claim for allowances rests primarily on s 24(1). In order to succeed, it must establish (a) that it has (or is deemed to have) incurred capital expenditure on the provision of machinery or plant wholly and exclusively for the purposes of its trade, and (b) that in consequence of incurring that expenditure (actual or deemed), the machinery or plant belongs or has belonged to it (or is to be treated as such).

50. Since Inmarsat has neither incurred relevant capital expenditure nor at any point have the Satellites actually belonged to it, in order to succeed it must establish both that it should be deemed to have incurred the relevant capital expenditure and that in consequence the Satellites should be treated as belonging (or having belonged) to it.

51. With regard to the extent to which statutory deeming provisions should be "followed through", Mr Prosser made brief reference to the statement of Lord Asquith of Bishopstone in *East End Dwellings Co Ltd v Finsbury Borough Council* [1952] AC 109 at 132:

> If you are bidden to treat an imaginary state of affairs as real, you must surely, unless prohibited from doing so, also imagine as real the consequences and incidents which, if the putative state of affairs had in fact existed, must inevitably have flowed from or accompanied it.

In his submission, on this basis the "inevitable consequence" flowing from any deemed sale under s 78(1) was that Inmarsat must be regarded as having acquired each Satellite for a net price equal to its open market value at the time.

52. Mr Gibbon referred to the more recent and detailed commentary on the interpretation of deeming provisions contained in *DCC Holdings Limited v HMRC* [2010] UKSC 58, in the light of which he submitted that whilst it was correct to consider the consequences <u>inevitably</u> flowing from the statutory hypothesis, it was appropriate also to take account of ascertainable policy and purposes of the legislation, and one should be readier to identify the limit to a "deeming provision" than to a "non-deeming provision". Further, citing Peter Gibson LJ in *Hoare v National Trust* (1998) 77 P&CR 366 at 386-387 (in part endorsing earlier authorities), he submitted that the "real world" should only be interfered with to the extent strictly necessary to give effect to the deeming provision:

> It is important that this statutory world of make-believe should be kept as near as possible to reality. No assumption of any kind should be made unless provided for by statute or decided cases.
>
> …

> I would emphasise the necessity to adhere to reality subject only to giving full effect to the statutory hypothesis… I would call this the principle of reality.

53. Standing back and looking at this claim in the round, Mr Gibbon pointed out that the Tribunal was being asked, as a result of the combination of two "deemings", to confirm the availability of allowances arising from a supposed sale between two parties where in fact at all relevant times the property was owned by third parties, with the amount of the allowances not being calculated on any expenditure actually incurred but by reference to an apportionment of a market value for which there was no statutory warrant. This, in his submission, illustrated the extent to which the present claim breached the "principle of reality".

54. Both parties were agreed on the requirement to apply the legislation purposively and in accordance with a rational overall scheme, if one could be found. Both then sought to persuade me of the existence of a rational scheme which supported their respective cases. In the main, I did not find this line of argument to be particularly fruitful. Whilst "belonging" is undoubtedly a very important feature of plant and machinery allowances, there are clearly exceptions and in seeking to decide whether this case was such an exception, I did not find general assertions about the centrality of this feature (or indeed the reasonableness or otherwise of the claim being put forward) to be particularly illuminating.

Main areas of contention

Section 78(1)

55. It was common ground that the present case at least fell within the scope of s 78(1): Inmarsat had succeeded to the trade previously carried on by IMSO and that trade was treated as discontinued by virtue of s 337(1) TA 88.

56. It was also common ground that the Satellites were in use for the purposes of IMSO's trade immediately before the succession took place on 15 April 1999, and that they were not sold (although the parties gave different reasons for the latter conclusion – Mr Prosser arguing it was because Inmarsat had simply assumed the rights and obligations under the leases without paying any money or transferring any property in exchange, and Mr Gibbon arguing it was because the Satellites belonged at all times to the lessors).

57. Mr Prosser argued that it was an implicit requirement in s 78(1) that the Satellites should have belonged (or be deemed to have belonged) to IMSO before the succession and he acknowledged that for this purpose he had to rely on s 61(4) in seeking to establish "deemed belonging" (as to which, see [62] *et seq* below). Mr Gibbon agreed.

58. As to the question of "belonging" immediately after the succession on 15 April 1999, Mr Prosser argued that this followed naturally from the operation of s 78(1), if it applied; in his submission, as the Satellites were undoubtedly in use for the purposes of Inmarsat's trade after the succession, the requirements for the operation of s 78(1) were met and accordingly the Satellites should be treated as belonging to Inmarsat as an inevitable consequence of the deemed sale provided for in s 78(1)(a). Mr Gibbon on the other hand argued that just as s 78(1) implicitly required the Satellites to belong (or be deemed to belong) to IMSO before the succession, it also required them to belong (or be deemed to belong) to Inmarsat after the succession and this second implicit requirement was not satisfied.

59. At first sight, Mr Prosser's argument appears attractive, on a plain reading of the words of s 78(1). By including the words "but no first-year allowance shall be made by virtue of this subsection" at the end, it is clear (as he argued) that the draftsman was contemplating the position of the successor as well as that of the predecessor; however, those words do not necessarily imply that the assets are to be treated as belonging to the successor, they can operate just as meaningfully to deprive the successor of any first-year allowances to which it might

otherwise be entitled as a result of its actual ownership of the assets in question following their deemed sale at market value; and whilst s 78(1)(a) does specifically provide that there is not just a deemed sale, but a deemed sale to the successor, s 78(1)(b) talks only of the "net proceeds of sale" (i.e. considering matters from the predecessor's point of view). Given the fact that (as the parties agreed) the draftsman assumed (without feeling it necessary to state explicitly) that the assets would have belonged to the predecessor before the succession, I consider that the same implicit assumption is made in respect of the successor, so that the provisions only apply where the assets in question actually belong (or, potentially, are deemed by some other provision to belong) to the successor after the succession. This point interacts with my views on the effect of the "tailpiece" to s 61(4) (as to which, see [118] below), and is reinforced by the fact that on Mr Prosser's own argument, his approach would require me to read into the statute provisions for apportioning the market value between the lessor and lessee which are simply not there.

60. It follows that since it is common ground the Satellites did not actually belong to Inmarsat after the succession on 15 April 1999, and I have been referred to no other provision which would confer on it a "deemed" belonging of them, I do not consider s 78(1) operates in the way Mr Prosser submits so as to confer entitlement to writing down allowances on Inmarsat based on the market value of the Satellites at the time of the succession on 15 April 1999. I am reinforced in this conclusion by the fact that there is no statutory machinery to accommodate a case such as the present, where the Satellites have, as a matter of fact, remained owned throughout by third party lessors who have no doubt been claiming writing down allowances on their original acquisition cost, and for whom the potential consequences of the Satellites being deemed to belong to Inmarsat from 15 April 1999 would appear to me to fall outside any rational scheme of the legislation.

61. On this basis, whether or not Inmarsat succeeds in its arguments on s 61(4) (as to which, see below), I consider the answer to the question referred should be that Inmarsat is not entitled to capital allowances in respect of the Satellites for its accounting period ended 31 December 1999 and subsequent accounting periods.

Section 61(4)

62. In case I am wrong in the conclusion I have reached above, I now turn to a consideration of s 61(4).

Were the launch costs incurred by IMSO on the provision of machinery or plant for the purposes of its trade?

63. Looking at the conditions required to be satisfied before the subsection applies, the first question is whether the capital expenditure incurred by IMSO in launching the Satellites was incurred "on the provision for the purposes of a trade carried on by [it] of machinery or plant".

64. Mr Gibbon argued that the launch expenditure incurred by IMSO was more properly regarded as "ancillary" expenditure rather than expenditure truly incurred on the "provision" of the Satellites: it was not, he submitted, a "natural use of words to suggest that someone who has paid freestanding amounts on ancillary expenditure has thereby paid for the provision of the plant and machinery itself." He likened the costs incurred by IMSO to the financing costs referred to in *Ben-Odeco Limited v Powlson (H.M. Inspector of Taxes)* (1978) 52 TC 459, which were held to be too remote from the plant itself to count as part of the cost incurred in providing it; instead, they were incurred on providing the money which was used in the acquisition of the relevant plant. He also submitted that the use of the phrase "is required to provide [plant and machinery] under the terms of the lease" connoted a requirement more closely focussed on the asset itself than the phrase "has incurred capital expenditure on the

provision… of plant and machinery" in s 24: at most, he submitted, all that that IMSO was required to provide under the leases was "launch services" rather than the Satellites themselves.

65. Mr Prosser's response was to refer to the comments made by Lord Wilberforce and Lord Russell in *Ben-Odeco*:

> The words "expenditure on the provision of"… focus attention on the plant and the expenditure on the plant – not limiting it necessarily to the bare purchase price, but including such items as transport and installation… (Lord Wilberforce at 473H)
>
> I do not seek to confine qualifying capital expenditure to the price paid to the supplier of the plant. I should have thought, for example, that if the cost of transport from the supplier to the place of user is directly borne by the taxpayer it would be expenditure on the provision of plant for the purposes of the taxpayer's trade. And there may well be other examples of expenditure, additional to the price paid to the supplier, which would qualify on similar grounds… (Lord Russell at 481F).

Echoing these comments, in his submission the launch costs were an exact parallel to the various installation costs of the dry dock incurred in *Barclay, Curle & Co Limited v Commissioners of Inland Revenue* (1968) 45 TC 221 and should be treated as such.

66. I acknowledge Mr Prosser's argument that the Satellites were entirely useless for their intended purpose until they had been launched into orbit, however the question before me is whether IMSO incurred capital expenditure (in the form of the launch costs) "on the provision for the purposes of a trade carried on by [it] of machinery or plant…". Here I agree essentially with Mr Gibbon's argument. Any "provision of plant" must have at its heart the plant itself; simply moving someone else's plant from A to B (even if B is the place at which it is to operate in your trade, and however complex and expensive the process of movement may be) cannot in my view amount to the "provision" of that plant. All the cases to which I was referred were concerned with ancillary costs associated with an acquisition (or, in the case of *CIR v George Guthrie and Son* (1952) 33 TC 327, a proposed acquisition) of the plant itself (or of the materials from which the plant was to be created), and none of them would have had in mind a situation such as the present. The comments of both Lord Wilberforce and Lord Russell in *Ben-Odeco* clearly support this analysis. Lord Wilberforce specifically referred to the statutory words "focus[ing] attention on the plant and the expenditure on the plant"; and both their Lordships referred in slightly different terms to the fact that expenditure on the provision of plant would not be "limited" or "confined" to the simple purchase price – both tacitly assuming that the purchase price would generally be at the core of any "provision" of plant.

67. It follows that I do not consider IMSO to have incurred capital expenditure (in the form of its costs of launching the Satellites) on the provision for the purposes of its trade of those Satellites and that accordingly s 61(4) cannot assist Inmarsat's case, even if I am wrong about s 78(1) above.

Was IMSO required to provide machinery or plant under the terms of the leases?

68. In case I am wrong in that conclusion, I now go on to consider whether IMSO's launch costs were incurred on the provision of plant which it was "required to provide under the terms of" each relevant lease.

69. Mr Prosser argued along two broad lines here, which could be characterised as "express obligation" and "practical requirement". His "express obligation" argument in relation to the I-3 Satellites also rested upon an additional "implied term" argument, as can be seen below.

Express obligation – the I-2 Satellites (explicit obligation to launch)

70. First, he argued that at least in relation to the I-2 Satellites, a clear and explicit contractual obligation to launch the Satellites could be found in clause 6 of the Agreement to Acquire and Lease dated 28 September 1988 between NSM and IMSO, which provided as follows:

> 6. LAUNCH
>
> As between the Lessor and the Lessee, the Lessee shall be exclusively responsible for the launch of each Spacecraft and the placing of each Spacecraft into geosynchronous transfer orbit and for the provision of the necessary launch and early orbit phase services in order to achieve Satisfactory Operation[4] of each such Spacecraft. The Lessee undertakes that it will use all reasonable endeavours to achieve Successful Injection[5] and Satisfactory Operation in a timely fashion.

71. The Agreement to Acquire and Lease was defined as one of the "Operative Documents" in the Master Lease Agreement between NSM and IMSO of the same date, which in turn contained the following provision (thereby incorporating the commitment from the Agreement to Acquire and Lease into the Master Leasing Agreement):

> 6.6 Performance of the Essence
>
> The Lessee acknowledges and agrees that… prompt and full performance by the Lessee of each of its obligations under this Agreement or under any other Operative Document shall, subject to applicable grace periods, be of the essence and shall be conditions of this Agreement.

72. Additionally, the Master Lease Agreement contained the following provisions:

> 2. ACCEPTANCE AND LEASING OF LEASED EQUIPMENT
>
> 2.1 Subject to the provisions of this Agreement, the Lessor agrees to lease to the Lessee hereunder, and the Lessee agrees to take on lease from the Lessor hereunder, each Spacecraft and the Ancillary Equipment in each case for the Lease Period applicable thereto. Each Spacecraft and the Ancillary Equipment is leased on the terms and conditions contained in this Agreement and in addition, in the case of a Spacecraft, the terms and conditions contained in the Lease Schedule applicable thereto…

73. Finally, the separate Lease Schedules entered into in relation to each I-2 Satellite contained the following provision:

> 3. By execution and delivery by each of the Lessor and the Lessee of this Lease Schedule (together with the Financial Schedule), the Lessor agrees to lease to the Lessee and the Lessee agrees to take delivery of, and take on lease from the Lessor, the Spacecraft, details of which appear in paragraph 4 below, and its related Ancillary Equipment, on the Delivery Date[6] and on and subject to

[4] Defined by incorporation of the relevant provisions from the BAe Contract, essentially referring to the satellite being capable of performing in accordance with specification. The term was defined for the purposes of an incentive clause which placed at risk certain sums due to BAe, contingent upon the satellite performing in accordance with specification. If a satellite were not launched (or if the launch failed due to launch vehicle malfunction) then the sums were to be paid in any event.

[5] Defined by incorporation of the relevant provisions from the BAe Contract, essentially referring to the attainment of a satisfactory geosynchonous orbit.

[6] This was defined in the Master Leasing Agreement, essentially to mean the time when title and risk passed to NSM in accordance with the novated purchase contract with BAe.

> the terms and conditions of the Agreement to Acquire and Lease, the Master Lease Agreement, this Lease Schedule and the other Operative Documents.

74. In Mr Prosser's submission, the obligation in clause 6 of the Agreement to Acquire and Lease, under which IMSO undertook to "use all reasonable endeavours to achieve Successful Injection and Satisfactory Operation in a timely fashion" amounted to a clear contractual obligation on IMSO to incur the relevant launch costs in relation to the three I-2 Satellites. As that commitment was incorporated by reference into both the Master Lease Agreement and the individual Lease Schedules, it was clearly an obligation "under the terms of the lease" of each of the I-2 Satellites. He was submitting that the incurring of launch costs was a necessary element of complying with that obligation.

Express obligation – the I-2 Satellites (obligation to comply with the Convention)

75. In addition, he referred to clause 7.3 of the Master Leasing Agreement, which included the following:

> 7.3 Compliance with Law
>
> The Lessee shall have and maintain all permits, licences and approvals required under any Applicable Laws and shall satisfy the requirements of all Applicable Laws….

76. In his submission, this clause also imposed an express obligation of some kind on IMSO to procure the launching and placing into orbit of the I-2 Satellites. This was because "Applicable Laws" was defined in the Master Leasing Agreement itself as including the Convention; the Convention (Article 3) required IMSO to "make provision for the space segment" and (Article 5) to "operate on a sound economic and financial basis having regard to accepted commercial principles"; by the time IMSO entered into the Master Leasing Agreement it had already entered into contracts for the construction and launch of the three I-2 Satellites; and accordingly in Mr Prosser's submission IMSO would not be complying with its obligations under the Convention unless it took appropriate steps to procure their launch.

Express obligation – the I-3 Satellites (obligation to comply with the Convention)

77. In relation to the I-3 Satellites, he made similar submissions regarding compliance with the Convention. In this case, the relevant clause was clause 7.03 of the Master Lease Agreement dated 20 December 1991, under which IMSO was required to "satisfy the requirements of all Pertinent Laws" (which was defined to include "Applicable Laws", which in turn was defined to include the Convention).

78. Each Lease Schedule relating to the I-3 Satellites (all dated 20 December 1991) included a clause by which "the Lessee agrees to take on lease… the Spacecraft…on and subject to the terms and conditions of the Master Lease Agreement, this Lease Schedule and the other Relevant Documents".

79. Although IMSO had not yet entered into the launch services contracts for the I-3 Satellites by 20 December 1991, it had already commissioned the construction of the I-3 Satellites under the GETSCO Contract and it would not be "making provision for the space segment" or "operating on a sound economic and financial basis having regard to accepted commercial principles" unless it took appropriate steps to procure the launch of those Satellites.

Express obligation – the I-3 Satellites (obligation to comply with implied term in GETSCO Contract)

80. In the absence of an explicit clause similar to clause 6 in the Agreement to Acquire and Lease the I-2 Satellites (the obligation to "use all reasonable endeavours to achieve Successful Injection" referred to at [70] to [74] above) his lengthier submission on the "express obligation" point in respect of the I-3 Satellites was a little more circuitous. This entailed a new argument

which had only been communicated to HMRC for the first time the day before the hearing started. In essence, it involved arguing that the GETSCO Contract for the supply of the I-3 Satellites should be read as containing an implied commitment on the part of IMSO to procure the launch of the Satellites. He phrased the nature of this putative commitment in various ways during argument, but finally settled on the formulation that it was "to use best efforts (as defined in Article 1C of the GETSCO Contract) to procure launch services (as referred to in Article 21A) for any spacecraft which is to be delivered for launch or removed from storage for launch." The obligation imposed on IMSO by this implied term was in his submission also incorporated by reference as an obligation under the lease documents for the I-3 Satellites.

81. Clause 12.03 of the Lease Facility Agreement relating to the I-3 Satellites provided as follows:

> The Lessee acknowledges and agrees that punctual payment of all amounts payable by the Lessee under this Agreement or under any other Operative Document and prompt and full performance by the Lessee of each of its obligations under this Agreement or under any other Operative Document shall, subject to applicable grace periods, be of the essence and shall be conditions of this Agreement.

82. Clause 6.05 of the Master Lease Agreement provided as follows:

> 6.05 Performance of the Essence
>
> The Lessee acknowledges and agrees that punctual payment of Rent by the Lessee hereunder and prompt and full performance by the Lessee of each of its obligations under this Agreement or under any other Operative Document shall, subject to applicable grace periods, be of the essence and shall be conditions of this Agreement and of any other such Operative Document.

83. Each Lease Schedule included the following provision:

> By execution and delivery by each of the Lessor and the Lessee of this Lease Schedule, the Lessor agrees to Lease to the Lessee and the Lessee agrees to take on lease from the Lessor, the Spacecraft… and its related Ancillary Equipment, on the Delivery Date for that Spacecraft and on and subject to the terms and conditions of the Master Lease Agreement, this Lease Schedule and other Relevant Documents.

84. The GETSCO Contract was both an "Operative Document" and a "Relevant Document", and accordingly in Mr Prosser's submission all of the Lease Facility Agreement, the Master Lease Agreement and the Lease Schedules required IMSO to discharge any implied obligation arising under the GETSCO Contract.

85. It followed, he submitted, that if the GETSCO Contract were found to contain an implied term obliging IMSO to use its best efforts as referred to at [80] above, then that obligation would become an express requirement "under the terms of the lease" of each I-3 Satellite, which would necessarily involve IMSO in incurring the relevant launch costs.

86. So Mr Prosser sought to establish that such a term should be implied into the GETSCO Contract. For the legal principles governing the importing of implied terms into a contract, he referred to *Marks and Spencer plc v BNP Paribas Securities Trust Co (Jersey) Limited and another* [2015] UKSC 72, in particular the review of the law in this area given at [14] to [31] by Lord Neuberger JSC. In that case, the summary given on behalf of the majority by Lord Simon of Glaisdale in the earlier Privy Council case of *BP Refinery (Westernport) Pty Ltd v Shire of Hastings* (1977) 180 CLR 266 at 283, as extended by Bingham MR in *Philips Electronique Grand Public SA v British Sky Broadcasting Ltd* [1995] EMLR 472, was endorsed, subject to six additional "comments". The passage from *BP Refinery* was as follows:

> "for a term to be implied, the following conditions (which may overlap) must be satisfied: (1) it must be reasonable and equitable; (2) it must be necessary to give business efficacy to the contract, so that no term will be implied if the contract is effective without it; (3) it must be so obvious that it 'goes without saying'; (4) it must be capable of clear expression; (5) it must not contradict any express term of the contract."

87. The extensional statements made by Bingham MR in the *Philips* case were summarised in *BP* as follows:

> Bingham MR then explained… that it was 'difficult to infer with confidence what the parties must have intended when they have entered into a length and carefully-drafted contract but have omitted to make provision for the matter in issue', because 'it may well be doubtful whether the omission was the result of the parties' oversight or of their deliberate decision', or indeed the parties might suspect that 'they are unlikely to agree on what is to happen in a certain… eventuality' and 'may well choose to leave the matter uncovered in their contract in the hope that the eventuality will not occur. Bingham MR went on to say…
>
> > 'The question of whether a term should be implied, and if so what, almost inevitably arises after a crisis has been reached in the performance of the contract. So the court comes to the task of implication with the benefit of hindsight, and it is tempting for the court then to fashion a term which will reflect the merits of the situation as they then appear. Tempting, but wrong…. it is not enough to show that had the parties foreseen the eventuality which in fact occurred they would have wished to make provision for it, unless it can also be shown either that there was only one contractual solution or that one of several possible solutions would without doubt have been preferred…'

88. Lord Neuberger's six "additional comments" were as follows:

> First…Lord Steyn [in *Equitable Life Assurance Society v Hyman* [2002] 1 AC 408] rightly observed that the implication of a term was 'not critically dependent on proof of an actual intention of the parties' when negotiating the contract. If one approaches the question by reference to what the parties would have agreed, one is not strictly concerned with the hypothetical answer of the actual parties, but with that of notional reasonable people in the position of the parties at the time they were contracting. Secondly, a term should not be implied into a detailed commercial contract merely because it appears fair or merely because one considers that the parties would have agreed it if it had been suggested to them. Those are necessary but not sufficient grounds for including a term. However, and thirdly, it is questionable whether Lord Simon's first requirement, reasonableness and equitableness, will usually, if ever, add anything: if a term satisfies the other requirements, it is hard to think that it would not be reasonable and equitable. Fourthly… although Lord Simon's requirements are otherwise cumulative, I would accept that business necessity and obviousness, his second and third requirements, can be alternatives in the sense that only one of them needs to be satisfied, although I suspect that in practice it would be a rare case where only one of those two requirements would be satisfied. Fifthly, if one approaches the issue by reference to the officious bystander, it is 'vital to formulate the question to be posed by [him] with the utmost care'…Sixthly, necessity for business efficacy involves a value judgment. It is rightly common ground on this appeal that the test is not one of 'absolute necessity', not least because the necessity is judged by reference to business efficacy. It may well be that a more helpful way of putting Lord Simon's second requirement is… that a term can only be

implied if, without the term, the contract would lack commercial or practical coherence.

89. In the light of this authority, Mr Prosser produced a list of provisions in the GETSCO Contract which he said all pointed to the existence of an implied term of the type he was arguing for. These included obligations on the part of IMSO:

(1) to co-ordinate the activities of the launch vehicle and spacecraft contractors at the launch site;

(2) to designate launch vehicles, identify the particular launch vehicle to be used for each Satellite and to inform GETSCO of the selected mission orbit inclination and mode;

(3) to conduct an Acceptance and Launch Readiness Review at the launch site prior to integration of the Satellite with the launch vehicle;

and on the part of GETSCO:

(1) to support the satellite operations carried out by IMSO during and after launch operations;

(2) to ensure compatibility of the Satellite design with the required launch engines, and to prepare the Satellites for launch;

(3) to deliver complete Satellites for launch, compatible with the launch vehicles;

(4) to furnish launch support services; and

(5) to conduct all activities to prepare the Satellites at the launch sites.

90. Other relevant express terms included, in his submission, the following:

(1) prices included compatibility with the launch vehicles;

(2) milestone payments linked to "completion of launch readiness review";

(3) title and risk to pass at intentional ignition of the launch vehicle engines; and

(4) time being of the essence as to delivery, in view of IMSO's intention to procure launch services in reliance on the delivery schedule.

91. By way of example, Mr Prosser asked, rhetorically, how IMSO could designate a launch vehicle unless it had made arrangements for a launch with a particular launch agency? Then again, there were numerous obligations of GETSCO under the contract which it could only perform if it were enabled to do so by IMSO arranging a launch. He invited me to consider the whole picture of obligations on both sides and agree with him that the GETSCO Contract would lack commercial or practical coherence unless there were an implied obligation on IMSO of the kind he was arguing for to procure the necessary launch services. An alternative way he put it was to refer to an implied obligation to co-operate with GETSCO in enabling them to perform the various obligations imposed on them by the contract. He also pointed to express terms of the contract which presupposed there would be a launch, such as the fundamental provision that title and risk would pass on intentional ignition of the engines of the first stage launch vehicle.

Required "as a practical matter"

92. Mr Prosser also submitted that the use of the word "required" in s 61(4) connoted a requirement that was broader than simply a legal requirement. In his submission, if the lease (viewed in the wider factual matrix) required "as a practical matter" that the expenditure be incurred, that was sufficient for the purposes of s 61(4). In his submission, it clearly did.

93. He referred to a decision of the Court of Appeal refusing permission to appeal from a decision of the EAT in *Grant v Kent County Council* [2003] EWCA Civ 1917. The "single issue" before the Court as described by Sedley LJ was:

> …whether the hours in excess of his standard working week of 37 hours which the applicant had worked on standby as the respondent's manager of out-of-hours social services for the Medway and Swale area fell to be remunerated as time spent on "duties" which he had been "required to undertake". These key words come from paragraphs 3-11(b) of the Blue Book which contains the applicant's terms and conditions of employment.

94. The detailed facts do not need to be recounted; Mr Prosser's submission was based on the following comment by Sedley LJ:

> …Mr Pitt-Payne has submitted first that the natural ordinary meaning of "required" is "contractually required". It is enough to say that, like the EAT and Sir Martin Nourse, I disagree. Millions of things in life are required without being the subject of contractual or legal obligation.

95. Mr Prosser also referred to *Reynolds v Coleman* (1887) 35 ChD 453, where the Court of Appeal construed the phrase "which according to the terms thereof ought to be performed in the jurisdiction" in the then Rules of the Supreme Court, concerning the jurisdiction of the English Courts over an alleged breach of a contract where there was a large foreign element. Cotton LJ said this:

> … in my opinion those words mean, that you must look at the contract and at the facts which existed at the time when the contract was made, and then determine whether, having regard to the terms, the contract was one which ought to be performed within the jurisdiction, and do not mean that there must be an express provision that the contract is to be performed within the jurisdiction.

Mr Prosser submitted that the words "required under the terms of the lease" should be approached in a similar way here, whilst acknowledging the words themselves and the context were different.

HMRC's response on Inmarsat's various arguments about "required to provide under the terms of the lease"

96. In response to the various routes by which Mr Prosser had submitted it could be said that IMSO was "required under the terms of" the various leases to provide the Satellites by incurring the launch costs, Mr Gibbon had a number of objections.

97. First, he submitted that in seeking to create, from general "compliance with all laws" clauses, a contractual obligation of some kind to procure launch services in relation to both the I-2 and I-3 Satellites, Mr Prosser was simply placing more weight on the words than they could fairly bear. The clause (in either of the versions under consideration here) amounted to "the broadest possible cross-reference to what could be a room full of relevant material". Insofar as it did refer to the Convention, that was really nothing more than a high level statement of objectives, and not something to be read as creating a specific contractual obligation.

98. As to the existence of a contractual term to be implied into the GETSCO Contract imposing some kind of obligation on IMSO to launch the I-3 Satellites, he referred to a number of provisions in that contract which contradicted any such suggestion, chiefly the existence of Article 28 entitled "Termination for Convenience", which started with the following quite clear statement:

> INMARSAT may terminate this Contract, in whole or in part, for INMARSAT's convenience, at any time prior to completion.

The Article then went on to set out the consequences of such termination, most notably GETSCO's entitlement to termination charges based on a "cost plus 10%" starting point.

99. In the context of seeking to establish what the BAe Contract might tell us about the general industry approach to an obligation to launch a satellite once commissioned and built, he pointed out that that contract contained a similar "termination for convenience" article, which again allowed IMSO to terminate the contract at any time, a provision entirely inconsistent with there being some kind of implied obligation for it to launch the I-2 Satellites either. His submission was that "against the background at the time, making assumptions about what might be fair between the parties is very hard". He did not formulate his response on the point by direct reference to the analysis at [86] to [90] above (having been somewhat taken by surprise by Mr Prosser's list), but the essence of his submissions was that Mr Prosser's proposed implied term satisfied none of the requirements there considered.

100. As to the question of whether a "practical" requirement under the lease would satisfy s 61(4), Mr Gibbon referred to *Fiona Trust & Holding Corporation and others v Privalov and others* [2007] UKHL 40 and *Ennstone Building Products Ltd v Stanger Ltd* [2002] EWCA Civ 916, particularly the latter, which considered the phrase "under the terms of the contract" in the Rome Convention on the Law Applicable to Contractual Obligations (1980) as scheduled to the Contracts (Applicable Law) Act 1990 – a legislative as opposed to a contractual context. He submitted that in the context of a highly technical legislative provision such as the present, it was clearly appropriate to have regard only to legal obligations.

Discussion of whether IMSO was required to provide machinery or plant under the terms of any relevant lease

101. Considering first the "compliance with Applicable Laws" argument, I essentially agree with Mr Gibbon. I cannot accept that a generalised obligation to comply with all relevant laws can be treated in the way Mr Prosser argues as giving rise to a specific obligation to incur expenditure on launching six specific satellites.

102. As to Mr Prosser's "implied term" argument in respect of the I-3 Satellites by reference to the GETSCO Contract, and in spite of his most persuasive efforts to manufacture an entire edifice of bricks with an extremely limited supply of straw, I must again agree with Mr Gibbon. To the extent there is any guidance in the GETSCO Contract on the point, I consider it could hardly be clearer, by reason of the existence of an unfettered right on the part of IMSO to terminate the contract without needing any reason, that no obligation of the type argued for by Mr Prosser can be implied. The GETSCO Contract as it stood was perfectly workable and effective (or, to put it another way, had perfectly adequate commercial and practical coherence) without the need to imply any such obligation; given the right of termination for convenience, it would not be correct that it would "go without saying" that it should be implied; the various different formulations of the proposed obligation that Mr Prosser advanced at various different times illustrated very clearly that the supposed implied obligation was not capable of clear expression; and in short I would consider it as "wrong" (without even being "tempting") to imply such an obligation. There could hardly have been a more detailed set of commercial contracts and Mr Prosser has not persuaded me that the parties wished to impose any specific obligation in relation to the launch of the I-3 Satellites that cannot be found in the specific wording they used in the GETSCO Contract.

103. Turning to his argument based on IMSO being subject to a "practical requirement" to procure the launch services, again I prefer Mr Gibbon's submissions. We are here concerned with highly technical legislation, not a review of the broad commercial imperatives. In the search for an obligation "under the terms of the lease", I do not consider it legitimate to look at the wider commercial picture and include obligations which might in practical terms have to

be incurred, in the light of wider commercial considerations, by reason of the existence of the lease. The legislation is clear that the lessee must be required to provide the relevant machinery or plant "under the terms of the lease" in order to fall within s 61(4), and that is not this case.

104. Finally, addressing Mr Prosser's argument in relation to the I-2 Satellites based on the specific obligation in clause 6, that clause clearly imposed an obligation on IMSO to "use all reasonable endeavours to achieve Successful Injection", and I agree with Mr Prosser that it is necessary, in order to comply with that obligation, to incur the costs involved in procuring the launch services for those Satellites. One must remember, however, that the statutory language of s 61(4) refers to a lessee who "incurs capital expenditure on the provision… of machinery or plant which he is required to provide under the terms of the lease". On the basis of the reasoning set out at [66] above, I do not consider that expenditure incurred on launch costs can, in a case such as the present, be equated to expenditure incurred "on the provision of" the Satellites themselves. Therefore, in spite of the existence of a specific obligation, I do not consider the nature or subject matter of the obligation to be of the right sort to fall within s 61(4).

Whether obligations arising by reference to the various lease agreements could satisfy s 61(4) in any event

105. A further point arose, relevant to all of Mr Prosser's above lines of argument. This was the question of whether any requirements referable to the various leasing documents were relevant at all for the purposes of s 61(4), bearing in mind that:

(1) IMSO had entered into the contracts for the launch of all three I-2 Satellites (in October 1986, July 1987 and March 1988) well before the leasing arrangements of those Satellites were put in place in September 1988; and

(2) all of the lease documentation for the Satellites (entered into on 28 September 1988 for the I-2 Satellites and on 20 December 1991 for the I-3 Satellites) was entered into at a time when the relevant Satellites did not yet exist and in each case the lease term was expressed to commence only (effectively) on launch of the completed Satellites, which did not in fact take place until between approximately two and five years later.

106. The essential question was whether it could properly be said, in such circumstances, that IMSO had been "required to provide" the launched Satellites under the terms of the lease in each case.

107. In Mr Gibbon's submission, this necessarily required the lease to be in place before the relevant expenditure was incurred. Mr Prosser submitted that this language of s 61(4) should not be taken to impose such a requirement, any more than s 61(1)(a) required the lease to be in place before a lessor could incur expenditure qualifying for allowances. Mr Gibbon considered this a false comparison, as the two provisions were doing different things and applied to different circumstances. It was to be expected that in the normal case a lessor would buy the asset to be leased before entering into a lease of it, and s 61(1) contained no wording parallel to "required to provide under the terms of the lease" in s 61(4). He also pointed to s 61(8), which provided as follows:

> In this section "lease" includes an agreement for lease where the term to be covered by the lease has begun, and any tenancy, but does not include a mortgage, and "lessee" and other cognate expressions shall be construed accordingly.

108. In his submission, as the term of the lease did not actually commence under any of the leasing agreements until (effectively) the launch of the relevant Satellite, those documents could not amount to "leases" of the Satellites, only as agreements to lease them; and as such, s

61(8) applied to make it quite clear that any obligations contained in the leasing agreements could not amount to requirements "under the terms of the lease" for the purposes of s 61(4), because in each case the term to be covered by the lease would not commence until at least two years later and the various agreements to lease did not therefore fall within the extended meaning of "lease" set out in s 61(8).

109. Mr Prosser argued that this was wrong. In his submission, the various leasing documents either separately or together amounted to a "lease" in each case and it did not matter that the term of the lease commenced at some later date. He argued that it was legally possible to grant a lease of land today with a lease term commencing in three months' time; that was effectively what was happening here in relation to the Satellites. There was therefore no need to look to s 61(8) at all. But even if you did, he argued that because s 61(8) was (like s 61(4)) worded in terms of "where" (rather than "if and when") the term of the lease has begun, it was not intended to take effect as a timing provision, requiring the term of the lease to have begun before the expenditure was incurred; it was simply saying that in circumstances where the lease term has actually begun, it was possible to look back to the terms of the prior agreement for lease to see if they imposed the necessary requirement on the lessee.

110. Part of the overall difficulty in interpreting s 61(4) arises from the fact that, as both parties agree, it was originally enacted before *Stokes v Costain Property Investments Limited* [1984] 1 WLR 763 and was then substantially amended to take account of the "fixtures code" that was brought into force in July 1984 in response to that decision; it is difficult to discern with any clarity what its continuing intended purpose is following that amendment (the rather strained example in HMRC's manuals being somewhat hard to envisage arising as a normal commercial transaction, as was noted by Fox LJ in *Costain* itself (at 770C): "the idea of a simple lease of chattels where the lessee is required to provide the chattels is an odd one"). In the circumstances, where it is difficult to discern any underlying purpose to the provision to assist in its interpretation in the present context, it is necessary simply to interpret the words used in context in accordance with their normal meaning.

111. S 61(4) starts by referring to a "lessee" incurring capital expenditure on the provision of machinery or plant, and it must be machinery or plant "which he is required to provide under the terms of the lease". It seems to me that there is a natural chronological flow about this provision, which necessarily implies that the lease must be in existence before the capital expenditure is incurred. This view is reinforced by the fact that the draftsman has felt it necessary, in s 61(8), to extend the provision so as to apply where there is an agreement for lease (but only where the agreed term of the lease has already begun), rather than an immediately effective lease. If Mr Prosser's argument were correct, this provision would effectively be unnecessary. Nor do I think the wording of s 61(1) assists Mr Prosser. In contrast to s 61(4), s 61(1) makes no reference to the expenditure having to be incurred by the lessor under the terms of the lease, and the references there to the incurring of the relevant expenditure are both in the past (rather than the present) tense. Finally, the whole focus of s 61(1) is different: its purpose is to ensure that a lessor who is not carrying on a leasing trade (and would therefore not qualify for allowances at all) is to be taken as commencing a deemed trade when the letting commences and not to afford allowances for expenditure which would otherwise be entirely outside the scope of the relief.

112. My comments about "provision" at [66] above are also relevant here. S 61(4) only applies in respect of the "provision… of machinery or plant which he is required to provide under the terms of the lease". The plant in this case is the Satellites. Even if some obligation to incur the launch costs were found to have arisen under the lease documentation, it could not in my view properly be said that a requirement to incur launch costs can be equated to a requirement to "provide" the Satellites.

113. For all these reasons, I consider that the expenditure incurred by IMSO could not fall within s 61(4) in any event. Thus even if I were wrong in the views expressed at [101] to [104] above, I still consider Inmarsat's claim would be bound to fail.

Effect of the "tailpiece" of s 61(4) if it applies

114. If I am wrong in all of the above, and s 61(4) does in fact apply, the question then arises as to the effect, if any, of what the parties referred to as the "tailpiece" of s 61(4). This is the provision that reads as follows:

> … but as from the determination of the lease, section 24(6) shall have effect as if the capital expenditure on providing the machinery had been incurred by the lessor and not by the lessee.

115. The particular concern was with whether the novations of the leases brought about their "determination" so as to bring this provision into play. In Mr Prosser's submission, there were two points to be made here. First, the only reason for looking at s 61(4) at all was to establish deemed belonging to IMSO "immediately before the succession takes place" for the purposes of s 78(1); once that objective had been achieved, the rest of s 61(4) had no relevant effect. Second, even if the position following the succession were relevant he referred to *Sargaison v Roberts* [1969] 1 WLR 951 at 958F-G, (*per* Megarry J) as authority for the proposition that I should have regard to "realities at the expense of the technicalities", and that the reality of the position was that the novations had simply brought about a transfer from IMSO to Inmarsat of the leases and not their "determination".

116. Mr Gibbon argued that in a highly technical context such as the present, it was entirely appropriate to have regard to the legal technicalities, which would of course have been well known to the draftsman of the legislation. It was therefore clear that s 61(4) could not possibly have the effect of deeming the Satellites to belong to Inmarsat following the succession on 15 April 1999; in the absence of actual belonging, therefore, it was clear that the implicit requirement of s 78(1) that the relevant assets should belong to the successor after the succession was not satisfied and therefore s 78(1) could not apply for the benefit of Inmarsat.

117. I agree with at least the first part of Mr Prosser's submission: the primary reason for looking at s 61(4) is to establish deemed belonging to IMSO immediately before the succession on 15 April 1999. But I do not consider that the tailpiece set out above can thereafter be ignored altogether. I agree with Mr Gibbon that it is not appropriate in this context to apply the comment made by Megarry J in *Sargaison* set out above. This is highly technical legislation and the draftsman would have been well aware of the legal effects of a novation. The effect of the novations was therefore to cause the "determination" of the leases; it follows that the effect of the tailpiece (if it were to apply) would be to effectively transfer the benefit of the capital expenditure from IMSO as lessee to the various lessors and this, it seems to me, is predicated on the assumption that the property actually belongs to the lessors (the deemed belonging in the earlier part of s 61(4) having been brought to an end as a result of the succession). To the extent the tailpiece applies, therefore, I consider it to be inconsistent with an essential implied pre-requisite of s 78(1) applying for the benefit of Inmarsat – namely that the Satellites should have belonged to it after the succession on 15 April 1999 (see [59] above).

118. It follows that if s 61(4) were to have applied, I consider its tailpiece would have been activated at the time of the succession on 15 April 1999 and that the implicit assumption underlying its operation (to the effect that the Satellites would belong to the various lessors after the succession) would be inconsistent with the requirement implicit in s 78(1) for the Satellites to have belonged to Inmarsat after the succession. To that extent, whilst I do not consider the arguments around the tailpiece to be potentially determinative of the proceedings

in their own right, I do consider that they feed into the analysis of s 78(1) set out at [59] above in favour of Mr Gibbon's view. On this basis, the two provisions taken together do in my view contribute towards a rational scheme of the legislation as a whole.

SUMMARY AND CONCLUSION

119. Because the Satellites neither belonged nor were deemed to belong to Inmarsat after the succession on 15 April 1999, s 78(1) does not operate so as to confer an entitlement to allowances on Inmarsat in respect of any part of the market value of the Satellites at the time of the succession, still less a part of such value apportioned by reference to the respective capital expenditure incurred by the lessors on the acquisition of the Satellites and by IMSO on their launch (see [59] to [60] above).

120. I do not consider IMSO was required to provide any of the Satellites under the terms of any of the leases, accordingly s 61(4) is not engaged (see [101] to [104] and [111] to [113] above).

121. Accordingly the Referred Question must be decided in principle in favour of HMRC.

RIGHT TO APPLY FOR PERMISSION TO APPEAL

122. 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.

KEVIN POOLE
TRIBUNAL JUDGE

RELEASE DATE: 30 AUGUST 2019