HIGH COURT OF JUSTICE (CHANCERY DIVISION)—
11, 12, 13, 14, AND 17 JUNE AND 22 JULY 2002

COURT OF APPEAL—12, 13 AND 14 NOVEMBER AND 13 DECEMBER 2002

HOUSE OF LORDS—12 AND 13 OCTOBER AND 25 NOVEMBER 2004

Barclays Mercantile Business Finance Ltd. *v.* Mawson (H.M. Inspector of Taxes)([1])

*Corporation tax—Capital allowances—Writing down allowances—Plant and machinery—Composite transaction—*Ramsay *principle—Expenditure—Expenditure on provision of asset—Finance leasing—Asset owned by a non-UK company—Series of transactions of finance leasing nature starting with sale of the asset and ending with that company having use of the asset but not having use of the purchase price of the asset—Whether* Ramsay *principle applied—Whether writing down allowances due—Capital Allowances Act 1990, ss 24(1) and 75(1).*

By 31 December 1993 BGE (the Irish Gas Board) had constructed a pipeline for the transportation of gas from Scotland to Ireland. The construction was financed by bank loans and a grant from the EEC.

BZW (a Barclays Bank company), which had been advising BGE about finance matters, proposed a finance leasing structure, and on 31 December 1993 several transactions occurred. BMBF (a Barclays Bank company) bought the pipeline from BGE for some £91 million (a sum borrowed by BMBF from the Group Treasury of Barclays Bank), leased it back to BGE on finance lease terms, and BGE sub-leased it to BGE (UK), the sub-lease mirroring the head lease. The rentals under the head lease were calculated to recoup BMBF, over 31 years, its outlay and to provide a worthwhile margin. To simplify movements of money BGE (UK) were to pay direct to BMBF. Barclays Bank guaranteed BGE (UK)'s obligations to BMBF. BGE (UK) agreed to provide to BGE services in relation to the transportation of gas, and the minimum payments for those services were large enough to cover BGE (UK)'s rental liabilities. BGE was obliged to deposit the £91 million with D, a Jersey company managed by another Barclays Bank company but owned by a charitable trust. D deposited the £91 million with a Barclays Bank Isle of Man company, and that company deposited the sum with the Group Treasury of Barclays Bank. Various additional transactions were of a security nature. BMBF's rental receipts were insufficient to cover its obligations under the loan made to it by Barclays Bank, but capital allowances on its expenditure would enable BMBF fully to finance the borrowing and to make an attractive commercial margin.

On appeals against notices of determination of trade losses for accounting periods ended 31 December 1993 and 1994, BMBF contended that it qualified

([1]) [2002] EWHC 1527 (Ch); [2002] STC 1068; [2002] EWCA Civ 1853; [2003] STC 66; [2004] UKHL 51; [2005] STC 1.

A for capital allowances under s 24(1) Capital Allowances Act 1990. The Inspector of Taxes contended, in reliance on the principle established in *W T Ramsay Ltd.* v. *Commissioners of Inland Revenue* (1981) 54 TC 101, that capital allowances were not due because (1) BMBF did not incur expenditure of £91 million, (2) if BMBF did incur that expenditure, it was not expenditure on the provision of the pipeline, and (3) if BMBF did incur expenditure of £91 million on the provision B of a pipeline, then it was not expenditure incurred wholly and exclusively for the purposes of BMBF's trade on the grounds that it was not a trading transaction at all. Dismissing BMBF's appeals, the Special Commissioners upheld the Inspector's second argument. BMBF appealed.

The Chancery Division held, dismissing BMBF's appeal, that:
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(1) for the Crown to succeed, it was not necessary for BZW's scheme to be found to be a convoluted tax avoidance transaction, and it was not such a transaction;

(2) the scheme did not comprise standard commercial finance leasing; in D such cases the finance lessor provides upfront finance to the lessee, and the finance so provided is used in one way or another in the lessee's business; but in the present case no upfront finance was provided; BGE already owned, and had paid for, the pipeline, and, after the transaction, was still able to use the pipeline as before and was still indebted to the banks in respect of the loans which funded the original purchase; the £91 million was not available to BGE for it to use in E any other way to finance transactions or activities of its business;

(3) as regards finance leasing the underlying purpose of Parliament, in relation to s 24(1) was to enable capital allowances to be used so as to provide to lessees at attractive rates finance for them to use and to develop their real business activities; the underlying purpose was not to enable cash payments to F be made annually to third parties who are able to provide a major item of machinery or plant which satisfies one of the conditions for a finance lessor to claim the allowances;

(4) s 24, and in particular the words "has incurred capital expenditure on the provision of machinery or plant", plainly embodied a commercial concept, not a legal (or juristic) concept;
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(5) the correct approach was to look at all the events of 31 December 1993, and this applied even though BMBF knew only the nature, and not the details, of several steps in the scheme;

(6) on that approach BMBF did not incur expenditure on the provision of H the pipeline; the expenditure incurred by BMBF was on the rights to the money flows under the network of agreements of 31 December 1993.

per curiam: as to the Crown's first and third arguments, BMBF did incur expenditure, but the leasing transaction was not a trading transaction and therefore not within BMBF's trade.

I

BMBF appealed.

The Court of Appeal held, allowing BMBF's appeal, that, on the facts and the legislation properly understood, BMBF qualified for capital allowances, and in particular:— A

(1) the Special Commissioners could not properly have concluded on the evidence before them that certain of the payments under the terms of the deposit with D "would be financed entirely by UK taxpayers by means of the hoped-for capital allowances", or that the other payments under those terms, although earmarked to be passed to BMBF, did not benefit BGE; whether the transaction was viewed as a whole or step by step, its commerciality was plain; B

(2) the purpose of the capital allowances legislation was to encourage the expenditure of capital and machinery; there was nothing in the legislation to substantiate the view that s 24 was enacted so that capital allowances could be used to provide lessees with finance at attractive rates to use and to develop their real business activities; s 24 focused on the incurring of expenditure by the trader on the provision of plant or machinery wholly and exclusively for the purposes of his trade; it was necessary to look only at what the taxpayer did; for the purposes of s 24 it was immaterial how the trader acquired the funds to incur the expenditure or what the vendor of the provided plant or machinery did with the consideration received; the express limitation in s 75(1) suggested that s 24 was not subject to a corresponding limitation; in any event s 75(1) was aimed at artificial transactions, and the present case did not involve any artificial transaction designed to create a tax allowance; C D E

(3) there was no scope for application of the *Ramsay* approach; the incurring by BMBF of the expenditure was wholly and exclusively for the purposes of its trade of providing asset-based finance; there was no basis for re-characterising the transaction, which was a genuine trading transaction; F

(4) there was expenditure by BMBF, and the circular movement of money and the intention of BMBF to obtain and pass on capital allowances did not stamp the transaction as something different from that contemplated by Parliament as giving rise to an entitlement to capital allowances under s 24; G

The Crown appealed.

Held, in the House of Lords, dismissing the Crown's appeal, that:—

(1) the essence of the new (*Ramsay*) approach was to give the statutory provision a purposive construction in order to determine the nature of the transaction to which it was intended to apply, and then to decide whether the actual transaction (which might involve considering the overall effect of a number of elements intended to operate together) answered to the statutory description; of course that did not mean that the courts had to put their reasoning into the straitjacket of first construing the statute in the abstract and then looking at the facts; it might be more convenient to analyse the facts and then ask whether they satisfy the requirements of the statute; but however the matter were approached, the question was always whether the relevant provision of statute, upon its true construction, applied to the facts as found; the simplicity of that question, however difficult it might be to answer on the facts of a particular case, H I

A showed that the *Ramsay* case did not introduce a new doctrine operating within the special field of revenue statutes; some cases had given rise to a view that, in the application of any taxing statute, transactions or elements of transactions which had no commercial purpose were to be disregarded; but that was going too far; it elided the two steps which were necessary in the application of any statutory provision, namely, first, to decide, on a purposive construction, exactly B what transaction would answer to the statutory description and secondly, to decide whether the transaction in question did so;

(2) in the present case a close analysis of what, on a purposive construction, the statute actually required, showed that the object of granting the allowance was to provide a tax equivalent to the normal accounting deduction from profits C for the depreciation of machinery and plant used for the purposes of a trade; consistently with that purpose, s 24(1) required that a trader should have incurred capital expenditure on the provision of machinery or plant for the purposes of his trade; when the trade was finance leasing, that meant that the capital expenditure should have been incurred to acquire the machinery or plant for the purpose of leasing it in the course of the trade; in such a case, it was the D lessor as owner who suffered the depreciation in the value of the plant and was therefore entitled to an allowance against the profits of his trade; those statutory requirements were, in the case of a finance lease, concerned entirely with the acts and purposes of the lessor; the Act said nothing about what the lessee should do with the purchase price, how he should find the money to pay the rent or how he should use the plant;

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(3) the finding of the Special Commissioners that the transaction "had no commercial reality" depended entirely upon an examination of what happened to the purchase price after BMBF paid it to BGE; but those matters did not affect the reality of the expenditure by BMBF and its acquisition of the pipeline for the F purposes of its finance leasing trade.

W T Ramsay Ltd. v. *Commissioners of Inland Revenue* [1982] AC 300; (1981) 54 TC 101, *Commissioners of Inland Revenue* v. *McGuckian* (1997) 69 TC 1; [1997] 1 WLR 991, *MacNiven* v. *Westmoreland Investments Ltd.* [2003] 1 AC 311; (2001) 73 TC 1, and *Collector of Stamp Revenue* v. *Arrowtown Assets Ltd.* [2003] G HKCFA 46 considered.

Dictum of Ribeiro P.J. in *Collector of Stamp Revenue* v. *Arrowtown Assets Ltd.* [2003] HKCFA 46, para 35, *viz*. "[T]he driving principle in the *Ramsay* line of cases continues to involve a general rule of statutory construction and an H unblinkered approach to the analysis of the facts. The ultimate question is whether the relevant statutory provisions, construed purposively, were intended to apply to the transaction, viewed realistically" approved.

I The Company appealed against the following decision of the Special Commissioners dated 18 October 2001.

Decision ([1]) A

Barclays Mercantile Business Finance Ltd. ("BMBF") appeals against notices of determination of trading losses for BMBF's accounting periods ended 31 December 1993 and 1994 and notices of assessment to corporation tax for the same periods. B

In substance there is only one issue in dispute: Is BMBF entitled to writing-down allowances in respect of its expenditure of £91,292,000 allegedly on the acquisition of a section of the gas pipeline running beneath the Irish Sea from Scotland to the Republic of Ireland?

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The evidence before us consisted of numerous agreed bundles of documents together with oral evidence from each of the following persons given on behalf of BMBF:

Mr. Christopher Leslie Richard Boobyer, a member since 1992 of the BMBF Board of Directors and the executive group, which is the group of senior officers who are collectively responsible for the strategic management of BMBF's business. D

Mr. Patrick Perry, group treasurer of Barclays Bank Plc from 1991 to 2000.

Mr. Francis Donald Wilson, a director of BGE (UK) Ltd. ("BGE (UK)"), a wholly-owned UK subsidiary company of Bord Gais Eireann ("BGE"). E

Witness statements were provided by each of the witnesses and in addition a full transcript of the proceedings is available to the Court should these appeals proceed further. F

The Facts

Bundle G put in evidence contains (*inter alia*) an Agreed Statement of Facts which states as follows: G

A. The Parties and the Pipeline

1. BMBF is a company within the Barclays Plc group. It was incorporated in England and Wales under company number 898129 on 14 February 1967 and its registered office is at Churchill Plaza, Churchill Way, Basingstoke, Hampshire RG21 7GP. Its principal activity is the provision of asset-based finance, and it is a leading UK supplier of finance and operating leasing and lease purchase agreements in the business finance sector. With its subsidiaries it has a current turnover of approximately £2 billion, assets of approximately £7 billion and over 700 staff located in the UK, France, Germany and Italy. H I

2. BGE is a statutory corporation established in 1976 under the Irish Gas Act and having its principal office at Inchera, Little Island, County Cork,

([1]) [2002] STC (SCD) 78.

A Ireland. It is responsible for the supply, transmission and distribution of natural gas in Ireland.

3. Between 1991 and 1993 BGE built, with the assistance of a 35 per cent. grant from the EEC, a high pressure natural gas pipeline running from Moffat in Scotland to Ballough in the Republic of Ireland ("the pipeline"). The B construction was financed by loans from a consortium of banks. The pipeline consists of three sections, as follows:—

(a) a 30 inch onshore pipeline, 80 km in length and running from the compressor station at Moffat to the Scottish coast at Brighouse Bay ("the Scottish section");

(b) a 24 inch sub-sea pipeline, 208 km in length and running from C Brighouse Bay to Loughshinny on the Irish coast north of Dublin ("the middle section");

(c) a 30 inch onshore pipeline, 8 km in length and running from Loughshinny to Ballough in North County Dublin ("the Irish section").

4. BGE UK is a wholly-owned subsidiary of BGE. It was incorporated in D England and Wales under company number 02827969 on 17 June 1993. Its registered office is at 35 Thomas Street, London SE1. Its objects (as rehearsed by clauses (1) and (2) of its Memorandum of Association) are:—

(a) to manufacture, purchase or otherwise acquire natural or other gases from any source and to liquify, compress, or otherwise prepare, process, treat or reform natural gas; and

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(b) to produce, store, transmit and distribute natural gas and to sell and supply natural gas produced, manufactured or required by it, whether or not such gas has been prepared, processed or treated.

B. The Acquisition Agreement

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5. Under the terms of two acquisition agreements between BMBF and BGE dated 31 December 1993 ("the Acquisition Agreements") BMBF agreed to acquire certain plant and machinery from BGE ("the Plant and Machinery"). Acquisition Agreement No. 1 related to the Irish section of the pipeline and that part of the middle section of the pipeline which lies in Irish territorial waters. Acquisition Agreement No. 2 related to certain compressors on the Scottish G mainland and that part of the middle section of the pipeline which passes through the territorial waters of the Isle of Man and international territorial waters. The total purchase price specified in the Acquisition Agreements was £91,292,000.

6. On 31 December 1993 BMBF made a CHAPS payment of £91,292,000 plus VAT to BGE, BMBF having borrowed the sum of £91,784,000 from H Barclays Bank plc at a fixed rate of interest of 10.95 per cent. per annum.

C. The Lease, the Sublease and the Assumption Agreement

7. Under the terms of a lease agreement dated 31 December 1993 between BMBF and BGE ("the headlease") BMBF agreed to lease the plant and I machinery to BGE for a pre-primary period running from 31 December 1993 to 30 September 1995 and for a primary period running from 1 October 1995 to

30 September 2025. Thereafter, subject to the fulfilment of certain conditions, the headlease provides that the lease may be renewed for successive one year periods. A

8. Under the terms of a sublease agrrement between BGE and BGE (UK) dated 31 December 1993 ("the sublease") BGE agreed to sublet the plant and machinery to BGE (UK). B

9. Under the terms of an agreement between BMBF, BGE and BGE (UK), ("the Assumption Agreement"), BMBF agreed that it would make out invoices to BGE (UK) in respect of payments falling due from BGE under the headlease ("the assumed payment") and that BGE (UK) would settle such invoices, thereby discharging BGE's monetary obligations due to BMBF under the headlease. In turn BGE agreed that direct payments from BGE (UK) to BMBF would, to the extent of the amounts so paid, satisfy BGE (UK)'s monetary obligations to BGE under the sublease. C

D. Arrangments for the Transportation of Gas D

10. Under the terms of an agreement between BGE and BGE (UK) ("the Transportation Agreement") dated 31 Decmber 1993, it was agreed that BGE (UK) would transport, handle and deliver gas to BGE's order and receive payment from BGE therefor. Payments due to BGE (UK) under the Transportation Agreement fall to be made into a specified account held in the name of BGE (UK) ("the Transportation Account"). E

E. Security for the Lease and Transportation Agreements.

11. Under the terms of a guarantee facility agreement and Deed of Guarantee between Barclays Bank Plc ("Barclays") and BMBF, Barclays guaranteed to BMBF direct payment by BGE (UK) to BMBF of the assumed payments ("the Barclays guarantee"). F

12. Under the terms of a deposit agreement ("the deposit agreement") concluded between BGE and a company called Deepstream Investments Ltd. ("Deepstream"), BGE deposited the sum of £91,542,000 ("the Deposit Sum") with Deepstream ("the BGE Deposit"). G

13. As security for its obligation to BGE (UK) under the Transportation Agreement, BGE assigned its interest in the BGE Deposit to BGE (UK) ("the BGE Assignment") and charged a current account held in the name of BGE ("the BGE Account") in favour of BGE (UK). H

14. BGE (UK) executed a Deed of Indemnity in favour of Barclays and in support thereof:

(a) it assigned to Barclays:— I

(i) its interest in the BGE Deposit;

(ii) its interest in the BGE Account;

(iii) its rights under the Transportation Agreement

(b) it charged the Transportation Account in favour of Barclays.

A 15. Under the terms of a deposit agreement concluded between Deepstream and Barclays Bank Finance Co. (Isle of Man) Ltd. ("BBFCIOM") (a subsidiary of Barclays resident in the Isle of Man) on 31 December 1993, Deepstream placed an amount equal to the deposit sum with BBFCIOM ("the cash deposit").

16. Deepstream executed a Deed of Idemnity in favour of Barclays in B respect of Barclays obligations under the Barclays guarantee and in support thereof, Deepstream:—

(1) assigned to Barclays its rights to the cash deposit;

(2) granted Barclays fixed and floating charges over all its assets; and

(3) charged in favour of Barclays the account with BBFCIOM containing the cash deposit.

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17. The existence of the cash deposit held by BBFCIOM (the benefit of which was assigned to Barclays by Deepstream) had the effect that the finance provided by the Barclays group was weighted at 0 per cent. in Barclays Plc's consolidated capital adequacy return when the leasing transaction was entered into.

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We make the following additional findings of fact based on the evidence before us.

On 8 April 1992 Mr. George Hudson, the Corporate Finance Director of Barclays European Corporate Group, wrote to BGE, for the attention of Eamon E Nicholson, BGE's financial director with a proposal. Its first paragraph reads as follows:

> "Re: The inter-connector pipeline from the Republic of Ireland to the United Kingdom (the Project). Further to our discussions regarding the above project we outline below and in the attached diagram and documents our proposal for achieving 1) medium term funding at a substantial margin F below the current commercial cost of funds, and 2) an effective up-front substantial discount in the capital cost of the project."

On a date unknown but believed to be subsequent to Barclays's proposal to BGE on 8 April 1992, Barclays de Zoete Wedd Ltd. ("BZW"), the investment banking arm of the Barclays group, made a presentation to British Gas in G relation to the inter-connector pipeline from the Republic of Ireland to the UK. The first page of the proposal contains the following:

> "Further to our discussions regarding the above project we outline below, and in the attached diagrams and documents our proposal for the involvement of British Gas as a financial investor.
>
> At this stage our proposal is a preliminary structure which will need to H be adapted and tailor made to suit British Gas and BGE in the light of your reaction and objectives concerning particular elements of our proposal. We would hope to achieve this through further discussion with yourselves over the coming weeks, so that appropriate commitment to the structure from the relevant parties may be in effect by the end of July 1992. Our proposal, although using a number of projects which have the benefit of being I relatively standard in the financial markets, combines them in a way which is proprietorial to Barclays, and accordingly we should request you to treat

the structure and transaction with an appropriate level of confidentiality. We should also state that our proposed role is that of arranger of the transaction, and British Gas should therefore seek its own legal, accounting and financial advice as it deems appropriate.

We have made the following basic assumptions:

(1) The total cost of the project is circa £250,000,000

(2) BGE requires funding for circa eight years

(3) BGE is willing to involve another party in the legal and economic ownership of the project

(4) There is an underlying commercial logic for the company in British Gas' line of business to invest in this project

(5) British Gas is prepared to consider a financial investment and the commitment of tax capacity should the terms prove attractive."

BMBF and BZW were each subsidiaries of Barclays Bank Plc at the relevant time.

The proposed deal with British Gas did not proceed.

Subsequently BZW suggested to BGE that it might consider entering into transactions with either Powergen Leasing Ltd. or Abbey National. Powergen was rejected as it had been established for less than six months.

On 23 March 1993 a presentation was made by the Barclays group of companies incorporating Barclays and BZW to Abbey National.

The first page of the executive summary of that document reads as follows:

"Proposal

BZW and Barclays are proposing that an Abbey National subsidiary enter into a finance lease as the lessor of a Gas pipeline ('the Pipeline') which is being constructed between Moffat in Scotland and Ballough in Eire, known as 'the Inter-connector Project'. The Pipeline would be leased to a UK incorporated company which would be wholly-owned by BGE. BGE would assume responsibility for all risks associated with the ownership and operation of the Pipeline.

In addition, BZW and Barclays will arrange funding and related agreements which will ensure that the substance of the following objectives are achieved for Abbey National:

(1) The investments are priced such that they are both remunerative and tax efficient, and will enable Abbey National to preserve a fixed level of return over its cost of funds;

(2) The principal credit risks involved in the lease are effectively transferred to third parties;

(3) BZW and Barclays will arrange and/or provide all the funding required for the investments;

(4) Risk asset weighting of the finance lease will be minimised."

A At that time the total cost of the pipeline and facilities was to be circa £270,000,000. The finance lease envisaged a primary period ending in 2022.

The proposed transaction with Abbey National did not proceed owing to legal advice to the effect that under its construction BGE was unable to give a guarantee.

B

On 15 September 1993 David Thompson and Tom Clark of BMBF wrote to the directors of the Bank's Risk Management Department with a credit proposal. It reads as follows:

"BORD GAIS EIREANN ('BGE')

(100 per cent) Irish State owned)

C Attached is a £25 million credit proposal bearing our qualified support in respect of a 31 year lease of an undersea Gas Pipeline to the above.

I apologise for the urgency of this application—BZW require an answer by Friday—but as you will see from the attached papers BZW's original lessor was dismissed by BGE and in order to protect the Barclays' groups involvment in this remunerative and prestigious transaction we have

D been asked to step into their shoes.

The rationale for the proposal and the detail is set out in the attached papers. In summary we are being asked to provide a gross lease facility peaking at £177 million (2010) of which the majority of the 'quantified' exposure will be guaranateed by Barclays Bank (*cash collateralised*) [our emphasis] but nevertheless involving a direct 'strip' risk to the lessor

E culminating at £25 million in the first few years of the next century. As with any lease we will in addition be exposed contingently to the lessee for adverse tax charges which cannot be specifically quantified but might involve an additional £15 million exposure for each 5 per cent. increase in tax rate.

F Whilst we wish to support the Group effort in consummating the transaction BMBF are not in a position to analyse or recommend on exposure against Irish sovereign/country risk either in amount or time frame. To that end our recommendation is qualified on the basis that that credit approval must be forthcoming from the appropriate specialist team within RMD. It is also fair to say that we would not normally wish to contemplate such a lengthy lease profile, but that as an exception we

G somewhat reluctantly support the term.

I can confirm however, and recommend on the following points:—

(1) That BMBF has the specialist team that will enable us to structure and document the lease in order to provide the maximum protection under the lease. (Wilde Sapte will act as our advisors)

H (2) Provided BZW supply the appropriate option then interest rate risk has been neutralised by fixed funding over the period.

On the above basis, and subject to clearance on Irish state and country risk, the proposal carries our recommendation. Tax aspects are being covered separately."

I BGE (UK) has a board consisting of three directors (Mr. Wilson and two others) but apparently only one other employee. Most of its operations are

carried out by the means of contracts with independent contractors. It is a £100 company. A letter dated 7 May 1993 from the financial controller of BGE to the Irish Department of Transport, Energy and Communications contains the following paragraph:

> "Re: Sale/ Lease Back of the Gas Interconnector Ireland-UK
>
> As previously discussed, the structure of the above requires BGE to set up a subsidiary company incorporated in England that will lease the pipeline from the Lessor and will thereafter control all aspects of the pipeline over its useful life."

It is apparent from the evidence of Mr. Boobyer that BMBF was aware that there were to be security arrangements for the lease and transportation agreements. In particular, BMBF knew at the time that the transaction was entered into that there were to be a cash collateral equivalent to the price paid for the pipeline.

Two versions of one document appear in the bundles. The document in question is a corporate certificate issued by BGE. One version is to be found behind divider 40 in bundle B2 whilst the other version is to be found behind divider 35 in bundle C1. Each of the documents has exhibited to it an extract from the minutes of a meeting of the members of BGE held on 14 December 1993. That extract refers to a further exhibit entitled "Inter-Connector Proposal—Summary" to be found at pp 566 and 567 in bundle B2 and at pp 262 and 263 in bundle C1. Those two versions are very different. The version in bundle B2 deals only with the sale of the pipeline, the lease and sublease, the guarantee by Barclays, the details of the eventual disposal of the pipeline by BMBF and details of an access licence to be granted by BGE to BGE (UK). The version of the document in bundle C1 refers in detail to the security arrangements and contains (*inter alia*) the following:

> "1. Deposit—BGE will deposit the purchase price (to be paid to BGE by BMBF pursuant to the terms of two acquisition agreements in respect of the sale of certain sections of (and certain compressors relating to) a natural gas inter-connector pipeline between Ireland and the United Kingdom, with Deepstream pursuant to a deposit agreement. The deposit is in legal terms a debt owed to BGE by Deepstream i.e. a loan.
>
> 2. Deposit taker—Deepstream is to be a Jersey Limited liability company. The shares of Deepstream will be held by a Jersey charity trust. Deepstream is to deposit the BGE deposit moneys with Barclays Isle of Man (this document is not available to BGE).
>
> 3. Deposit Repayments—Under the deposit agreement, Deepstream will repay to a BGE account with Barclays (respectively the 'BGE account' and 'Barclays') sums intended *to match (both in timing and amount)* [our emphasis] the rental and termination sums payable under an assumption agreement to be entered into between BMBF, BGE and BGE (UK). In addition, on each rental payment date between October 1995 and October 2002 Deepstream will pay the BGE 'subsidy' to a separate BGE account. Barclays Isle of Man will be required to repay Deepstream's deposit with it in order to fund payments due to BGE.
>
> 4. Transportation Agreement—BGE (UK) will transport gas to BGE through the Pipeline pursuant to a transportation agreement. Certain of the

A amounts payable by BGE under such agreement are intended *to match* (*both in amount and timing*) [our emphasis] deposit repayments from Deepstream. Such amounts will be paid into a BGE (UK) account with Barclays (the 'BGE (UK) account'). As pre-conditions to the entry into of this agreement, BGE (UK) is requiring BGE to make its deposit with Deepstream and to charge its interest and rights in respect thereof and BGE account in favour B of BGE (UK).

8. Cashflows—On each lease/sub-lease rental payment date the following payments intended to be of equal amount, will be made:

(a) Barclays Isle of Man to Deepstream in respect of Deepstream deposit into Deepstream's account;

C (b) Deepstream to BGE in respect of BGE deposit into BGE's account;

(c) BGE to BGE (UK) under the Transportation Agreement into BGE (UK)'s account;

(d) BGE (UK) to Lessor under the Assumption Agreement into the Lessor's account with Barclays."

D

The distribution list on each of the above documents includes BMBF. In a second witness statement of Mr. Boobyer he has stated his belief that "BMBF was named as an addressee of this certificate by mistake and that it was never sent to BMBF." He further stated "to the best of my recollection I had not seen the document (contained in bundle C1) before the hearing of this appeal."

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As Mr. Boobyer was not cross-examined on the contents of his second witness statement referring to the above documents we must accept his supplementary evidence at face value.

The document contained in bundle C1 is dated as follows "dated as of F 31 day of December 1993". The document contained in bundle B2 is dated 31 December 1993.

The Deposit Agreement dated 31 December 1993 and made between BGE as Depositor and Deepstream as Deposit Taker contains the following provisions: (Bundle C1 at pp 110-111):

G "3. DEPOSIT PAYMENTS

3.1 Subject to the Initial Deposit Amount being deposited in accordance with the provisions of Clause 2, the Deposit Taker hereby agrees, subject to the provisions of Clause 3.2, to repay the Deposit as follows:

H (a) on each Payment Date which has an amount set opposite it in the second column of the Schedule, the applicable amount therein specified (a '**Scheduled Repayment Amount A**');

(b) (i) on each Payment Date which has an amount set opposite it in the third column of the Schedule, the applicable amount therein specified (a '**Scheduled Repayment Amount B**'); and

I (ii) on each Payment Date which has an amount set opposite it in the fourth column of the Schedule, the applicable

amount therein specified (a '**Scheduled Repayment Amount C**'); and A

(c) on any day on which the Depositor and the Deposit Taker agree that the entire amount of the Deposit shall be prepayable (the '**Early Termination Date**'), the net amount equal to the value of the Deposit less the aggregate amount of the Early Termination Fees and the Breakage Costs (each determined as of such date). B

3.2 Save as set forth in this Clause 3, the Deposit Taker shall not be required to make any payment of any nature to the Depositor.

3.3 All payments to the Depositor pursuant to Clause 3.1 shall be made to account no. 13570109 of the Depositor with The Bank of Ireland of 83 South Mall, Cork, Ireland or to such other account or accounts as the Depositor may notify to the Deposit Taker from time to time." C

The Account Charge Agreement dated 31 December 1993 and made between BGE as chargor and BGE (UK) as chargee contains the following provisions: (Bundle C1 at pp 194-5): D

"4. Restriction on Withdrawals from the Charged Account

Subject only as is hereafter mentioned, BGE shall not be entitled to withdraw or transfer any sums comprising the Charged Property. E

5. Continuing Security and Enforcement of Security

5.1 BGE hereby covenants with the Chargee that until the Chargee is satisfied that the Secured Obligations have been discharged in full, BGE shall not withdraw any amount standing to the credit of the Charged Account nor shall it sell, assign, discount, pledge, charge or otherwise deal with or grant or permit third party rights to arise over or against the same or any part thereof or attempt to agree to do so; **Provided Always** that the Chargee may in its absolute discretion and upon such terms as it may agree consent to BGE making a withdrawal of an amount from the Charged Account and **Provided Always** further that the Chargee shall consent to any withdrawal (each a '**Permitted Withdrawal**') from the Charged Account if: F G

(a) on the proposed date for the Permitted Withdrawal an amount shall be due and payable pursuant to the Transportation Agreement in respect of (a) Transportation Payment(s); H

(b) the amount of the proposed Permitted Withdrawal is equal to the lesser of the amount the standing to the credit of the Charged Account and the aggregate amount of the Transportation Payment(s) due and payable on such day; and

(c) the full amount of the proposed Permitted Withdrawal shall be transferred directly from the Charged Account to the Chargee's Account." I

A letter dated 31 December 1993 (Bundle C1 at p 224) signed on behalf of BGE, Barclays Bank plc and BGE (UK) and addressed to Barclays Bank plc at 54 Lombard Street, London EC3 contains the following:

A "We refer to (i) the account charge agreement (the 'Charge') dated even date herewith between Board Gais Eireann ('BGE') as chargor and BGE (UK) Limited ('BGE UK') as chargee in respect of our account (the 'BGE Account') no. 4077-3638 with the Bank at the Branch and (ii) the assignment agreement (the 'Assignment') also dated even date herewith between BGE UK as assignor and the Bank as assignee in respect, *inter alia*, of the BGE B Account.

The Bank and BGE UK have agreed, notwithstanding any provision of the Charge or the Assignment to the contrary, that Barclays Mercantile Business Finance Limited may pay £91,292,000 (the 'Funds') into the Account for value 31 December 1993 through the medium of CHAPS.

C The Bank and BGE UK have further agreed that, upon receipt of the full amount of the Funds, the full amount thereof may be debited from the BGE Account provided that the same is immediately transferred to the account (the 'Deepstream Account') no. 7010-3748 of Deepstream Investments Limited ('Deepstream') with the Bank at the Branch.

Accordingly we hereby instruct you that upon receipt in the BGE D Account of the full amount of the Funds, please debit the full amount thereof from the Account and pay this to the Deepstream Account."

A Memorandum of BZW dated October 1993 (Bundle D2 at pp 403-5) contains the following:

E "(II) BGE Deposit with Deepstream Investments Ltd, Deepstream Deposit with BBFCIoM, Deepstream Indemnity and Security for Indemnity.

A. BGE Deposit with Deepstream Investments Ltd

(i) BGE will place a fixed rate deposit with Deepstream Investments Ltd ('Deepstream') a company incorporated in the Isle of F Man. Deepstream is a single purpose company owned by Hill Samuel as trustee for a charitable trust. Hill Samuel will appoint Barclaytrust to provide company management.

(ii) The terms of that deposit will be such that BGE will be entitled to withdraw principal from time to time and receive interest and fees earned on the deposit during its life. This deposit will represent senior G unsecured obligations of Deepstream.

(iii) BGE can generate a cash flow through withdrawals of principal and receipt of income from the deposit sufficient to meet both its base case rental payments over the life of the Lease and also to provide it with some additional income.

H B. Deepstream Deposit with BBFCIoM

Deepstream will place a deposit with Barclays Bank Finance Company Isle of Man ('BBFCIoM').

Deepstream will provide an indemnity to Barclays Bank PLC ('BB PLC') in respect of BB PLC's Guarantee of certain of the Lease obligations I of BGE. Deepstream will grant a charge to BB PLC over its deposit with BBFCIoM as security for its indemnity obligations to BB PLC.

In the normal course of its business, and as a matter of policy, all of BBFCIoM's deposit raisings are placed with BB PLC IoM Branch which in turn places its funds with GTS. The funds raised from the deposit by Deepstream with BBFCIoM will become part of the normal BBFCIoM raisings and will be dealt with in the usual manner described above. A

In order to hedge its obligations to pay a fixed rate on the funds placed with it by BBFCIoM, BB PLC IoM Branch will purchase a floor and will enter a swaption agreement with Barclays Swaps. B

The result of the substitution of BMBF in the structure is that the complications of the funding of Abbey National are no longer required. The swaption written by Barclays Swaps and Options for BMBF is hedged by the swaption written for BB PLC IoM Branch. However, we require confirmation of your approval for the provision of a cash secured guarantee to BMBF for the fixed rental obligations of BGE in the revised structure as described above." C

(GTS represents Barclays Bank's Global Treasury Services).

D

A BGE Memorandum dated 14 December 1993 (Bundle D2 pp 415A-415E) contains the following:

"UK Interconnector—Lease/Deposit Proposal

Introduction E

(all figures in the Introduction are present value at 6.75 per cent.).

Relative to the lease/deposit proposal discussed with the Board at its meeting on 30 November 1993, the current proposal is less attractive to BGE because Irish stamp duty of circa £1.8 million will be payable which is partially offset by an increased subsidy of £0.9 million. F

From an Ireland Inc. perspective the proposal is financially more attractive by the following:

(a) Net benefits have increased by £0.5 million in the first 8 years and by a further £0.4 million over the life of the lease.

(b) BGE is not contributing to the cost of the floor. G

(c) BGE will receive the value of the floor in the event of termination of the lease due to significant adverse rental movements.

(d) Barclays will guarantee a minimum value for the floor of £1.5 million in the event of termination due to denial of capital allowances in October 1995. H

The package is worse from an Ireland Inc. prospective to the extent that termination cost has increased by £1.1 million (due to the cost of the floor).

The main elements of the lease/deposit proposal are outlined below.

1. Amount: I

U.K. £91.3 million

2. Effective Saving:

The gross value of the saving is estimated at £12.6 million over the life of the lease (£11.7 million over years 1-8) and the present value at

A £9.9 million (discounted at 6.75 per cent.). Out of these benefits BGE must pay £1.8 million of stamp duty. The net present value is therefore projected at £8.1 million.

3. Lessor:

Barclays Mercantile Business Finance Group ('BMBF'), a leasing B company ultimately controlled by Barclays Bank plc.

4. Structure:

Lease

(a) BGE sells identified parts of the Interconnector to BMBF.

(b) BMBF leases the above to BGE under a finance lease for a C period of 31 years.

(c) BGE will sub-lease these parts of the Interconnector to BGE (UK) Limited, under a finance lease for 31 years.

Guaranty & Deposit

(a) BGE will place a fixed rate deposit of £91.3 million (the sale D proceeds) with Deepstream Investment Ltd, a Jersey company owned by a Jersey charitable trust. This deposit will service the lease rentals as set out in the lease agreement and provide the income of £12.6 million to BGE over the life of the lease.

(b) Barclaytrust will provide company management to Deepstream and the money will be deposited in a Barclays subsidiary E in the Isle of Man.

(c) Lease payments by BGE to BMBF (as set out in the lease agreement) will be guaranteed by Barclays Bank. Any changes to the lease rentals because of Writing Down Allowances or Corporation tax changes will not be covered.

F (d) Barclays will have a charge over the deposit as support for the Barclays guarantee of the lease payments.

5. Transportation Agreement:

BGE will enter a take or pay agreement with BGE UK Ltd, for the transport of gas. Payments will be made under this agreement irrespective G of gas flows.

6. Comments

(a) Ownership of the Interconnector

(1) For tax reasons BGE cannot have a right to buy the Interconnector. BGE does have the right, assuming it is not in default H of its obligations, to act as the exclusive sales agent and can thereby sell it at market value to a BGE subsidiary.

(2) If BGE is in default of its lease obligations then BGE can lose control over the pipeline.

(b) Deposit Risk

I Risks attach to the security of BGE's deposit. This risk would most likely arise in the event of the collapse of Barclays.

(c) Benefit Risks A

While the expected net present value of the benefits of the scheme is £8.1 million (net of stamp duty) the actual benefits may vary. The major reasons for variation are:—

(1) Denial of allowances.

(2) Change in level of capital allowances. B

(3) Changes in the tax rates.

(4) Imposition of Withholding Tax.

While the size of the benefits may either increase or decrease they are likely to remain positive provided: (See Annex A). C

(1) Allowances are not denied.

(2) Tax rates do not fall to below 20 per cent. in the first few years (currently 33 per cent.) or go above 50 per cent. in 2010 (see graph).

The major downside in the next three years occurs if capital allowances are denied and the lease is terminated. If this happened in October 1995 the D maximum cost would be £7.5 million. (Assumes no residual value in the floor to BGE).

In the event that capital allowances were reduced to 10 per cent. in 1995 (currently 25 per cent.) or tax rates reduced to 25 per cent., the net benefit to BGE of the scheme would be reduced from £10.8 million to about E £6.2 million. If Corporation Tax rates increase to 50 per cent. in the year 2010 then the benefit from the lease/deposit would be eliminated.

In the middle to latter part of the lease (1998–2025) a reduction in the rate of Corporation Tax will increase BGE's benefit whilst an increase will reduce BGE's benefits.

F

For changes in tax rates in this period to eliminate BGE's benefit, tax rates would need to be greater than 60 per cent. in 2000 or greater than 50 per cent. in 2010 and sustained at these levels for the duration of the lease. (The graph in the Appendix shows the range of tax rates which would need to prevail to result in a net loss to BGE from the transaction).

It would be extremely expensive for BGE to arbitrarily terminate the G lease during the first seven years of its operation.

Accounting Issues

In economic terms the present value of the lease payments and the amount on deposit are the same. However while in economic terms these items are offsetting for reporting purposes it will be necessary to show the H level of the deposit and the amount outstanding under the lease in the balance sheet. In addition it may be necessary to note certain contingent liabilities. Craig Gardner are satisfied that the lease will not impact on BGE's Profit and Loss account.

Overview I

The expected benefits to BGE of the lease proposal amount to £8.1million. Ireland Inc. receives an additional benefit of £1.8 million.

There are risks associated with receiving these benefits, because BGE is tied to a very long (31 year) lease. Over the next 5 years the benefits are likely to be positive provided capital allowances are not denied. In the long term

A (10 years plus) there is much greater uncertainty, and then benefits could be eliminated in the event of sustained high tax rate regime e.g. because of tax rates increasing to over 60 per cent. in the year 2000 or 50 per cent. in the year 2010, and staying at those levels.

Documentation

B Final documentation has today gone to the Department of Transport, Energy and Communications. Some schedules have been revised as late as today. It may not be feasible to complete before the deadline of Monday 20 December.

Recommendation

It is recommended that the proposal be finalised."

C BMBF receives rental payments under the terms of its lease, but has to pay higher amounts to Barclays Bank under the terms of its borrowings. The difference, according to the terms of the scheme prepared by BZW is to be funded by the capital allowances claimed.

D The Transportation Agreement is designed to ensure that BGE (UK)'s rental payments can always be met. The transportation payments by BGE are designed never to be less than the amounts of rent due under the terms of the lease. Admittedly higher transportation payments can, and probably will be made. However, the effect of the agreement is that effectively BGE finances the payment of its sub-lessee's rental payments.

E Under the terms of the deposit with Deepstream, the only moneys which leave the Barclays Bank Group are payments B and C, which are small in comparison with payments A. Payments A return to Barclays.

We find as a fact that the events of 31 December 1993 were pre-ordained and designed by BZW to be a composite whole.

F By virtue of two put options each dated 31 December 1993 and made between Sudinor Ltd., BMBF and BGE, BGE is given the right in return for payments of nominal consideration to sell the Pipeline and its equipment to Sudinor at the conclusion of the term of the lease to BGE. On the evidence of Mr. Boobyer, Sudinor was formed "specifically for the purpose of being able to G grant a put option to Barclays Mercantile in the event that we wished to exit the lease. The constraints we put around that and we satisfied ourselves on the fact that within the lease that Sudinor must remain wholly-owned subsidiary of BGE for the entire period that the put option is live."

The transfer of ownership of the Pipeline was effected by two bills of sale, H each referable to the respective acquisition agreements. The bills of sale were not produced at the hearing as they remained outside the jurisdiction and in an unstamped condition. After hearing argument we indicated at the conclusion of the hearing that in the absence of the original stamped documents we were not satisfied that either a legal or equitable title to the Pipeline had been made out by BMBF and we adjourned the hearing to enable BMBF to consider its position. I Shortly thereafterwards BMBF's solicitors Messrs. Denton Wilde Sapte gave an unconditional undertaking to present the bills of sale for adjudication and

stamping and to pay the *ad valorem* duty assessed together with any penalty due. A
In the circumstances the ownership of the Pipeline is no longer in issue.

Prior to the hearing there was the possibility that the Crown might put forward contentions on the basis of s 42 Capital Allowances Act 1990. Before the hearing commenced however it was agreed between the parties that the Revenue would take no point in relation to s 42 as such had been their practice at the time of the relevant transactions in 1993. B

The Contentions of the Parties

C

Mr. Aaronson's approach to this case is very simple as is illustrated by the opening paragraph of his skeleton argument where he says "there is nothing in this case, once the facts are sorted and understood." He says that what took place in 1993 was an ordinary finance lease transaction to be taxed and treated like any other.

D

Mr. Goy, for the Crown, accepts that if we are to look at the transaction solely by reference to what BMBF did then BMBF must succeed in this appeal but the Revenue say that this is a wholly incorrect approach. The effect of the steps that BMBF took in this transaction must be judged by reference to the entire transaction of which those steps form part, including the security arrangements. Mr. Goy has submitted that when the entire transaction is looked at it can be said that this is no ordinary finance lease transaction, principally because in the view of the Inland Revenue there was no finance. BGE received the sum of £91,292,000 plus VAT for perhaps a millisecond but it was never able to get its hands on the money. Mr. Goy does not allege sham but seeks to use the "new approach", as propounded in *W T Ramsay Ltd.* v. *Inland Revenue Commissioners* [1982] AC 300; *Furniss* v. *Dawson* [1984] AC 474 and subsequent cases. E F

Both Mr. Aaronson and Mr. Goy submitted written skeleton arguments which will be available to the Court should these appeals proceed further.

G

The law

Subsection 24(1) Capital Allowances Act 1990 provides as follows:

"(1) Subject to the provisions of this Part, where— H

(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, I

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

The appropriate allowance claimed by BMBF is an entitlement to a 25 per cent. writing down allowance.

A **Conclusions**

When making his submissions Mr. Goy characterised the acts and events relative to these appeals as "financial engineering". It is apparent that he did not intend that description to be complimentary but it is possible that such a description may not be entirely rejected by BMBF. Those same words "financial B engineering" are to be found adorning the document detailing the presentation by Barclays Bank plc to BGE in April 1992 (Bundle D2 at pp 265-276).

However, Mr. Aaronson has submitted throughout that all that his client did in 1993 was to engage in perfectly normal everyday finance leasing. What then is finance leasing? Mr. Boobyer defined it in his evidence at para 17 of his C witness statement in the following terms:

> "The basic premise of the finance leasing industry is that lessors pass on the value of the capital allowances available to them in respect of the asset being financed to the customer. The customer gets the use of the asset concerned and pays rent at a rate which reflects the margin required by the Bank and the reduced funding cost to the Bank of providing lease finance D as a result of the tax deferral benefit available."

It is common ground in this appeal that if we look at and are concerned with only what BMBF did in 1993 it is inevitable that it will succeed in its appeals before us. Accordingly Mr. Goy, for the Revenue, has maintained throughout that we must look at the whole of the events which took place on 31 December E 1993 and that if we look at the whole transaction it will be seen not to be a normal everyday simple finance leasing transaction. He has rejected any attempt to use pejorative language but it is inevitable that if the Crown is to succeed in these appeals it must establish that what occurred was a complicated, convoluted tax avoidance transaction.

F It is plain on the face of the documents that the arrangements were organised and set in motion by BZW.

After several false starts involving British Gas, PowerGen Leasing Ltd. and Abbey National we find the details of the scheme laid out with precision in BZW's memo of October 1993, to be found in Bundle D2 commencing at p 403. G It refers to the lease and the BMBF funding from Barclays Global Treasury Services. If refers to the deposit by BGE. It refers to the terms of the deposit. It refers to how BGE can obtain a benefit. It states at the top of p 405:

> "BGE can generate a cash flow through withdrawals of principal and receipt of income from the deposit sufficient to meet both its base case rental payments over the life of the lease and also to provide it with some H additional income."

Thereafter it refers to the deposit by Deepstream with BBFCIoM. It further states that the BBFCIoM deposit will be placed with Barclays Bank.

In addition, there is a BGE Memorandum dated 14 December 1993 to be I found in the same bundle commencing at p 415A and at the top of p 415B details of the effective saving to BGE is stated as follows:

"The gross value of the saving is estimated at £12.6 million over the life of the lease (£11.7 million over years 1-8) and the present value at £9.9 million (discounted at 6.75 per cent.). Out of these benefits BGE must pay £1.8 million of stamp duty. The net present value is therefore projected at £8.1 million."

A

In the light of all the evidence placed before us we must reject Mr. Aaronson's submission that we should look no further than the actions of BMBF. We accept Mr. Goy's submissions in the light of the decisions in *Ensign Tankers (Leasing) Ltd.* v. *Stokes* (1992) 64 TC 617 and *MacNiven* v. *Westmoreland Investments Ltd.* [2001] STC 237 that s 24 is looking at a commercial concept. We also accept his submission that we must look at the whole of the transaction; all the documents, acts and events of 31 December 1993 and not merely what BMBF did: *Overseas Containers (Finance) Ltd.* v. *Stoker* (1989) 61 TC 473.

B

C

Although BMBF took no active part in the "security arrangements", we have found from the evidence of Mr. Boobyer that BMBF knew that there were such arrangements, including the 100 per cent. cash collateral (Day 2 p 60 lines 7-11). We accept that BMBF may not have known all the intricate details of the security arrangements put in place but it was part of a larger organisation, namely the Barclays Bank Group of Companies, for both BMBF and BZW, although operating to a considerable extent independently, were each subsidiaries of Barclays Bank plc. We also accept Mr. Goy's submissions that in the light of the decision in *Moodie* v. *Commissioners of Inland Revenue* (1993) 65 TC 610 detailed knowledge of all the subsequent transactions is not required of BMBF. At (1993) 65 TC 610 p 622D of the report there is the finding by the Special Commissioners that;

D

E

"Mr. Moodie did not know the full details of the circular movement of debits and credits in the books of the Slater Walker Companies; but he knew that the financial arrangements would take place within the Slater Walker Group."

F

Mr. Moodie's lack of detailed knowledge did not assist him in attempting to win his appeal before the House of Lords. We believe that for us to ignore the security arrangements merely because BMBF may not have had full knowledge of the details of them would be to look at the transactions before us wearing blinkers and we reject Mr. Aaronson's attempts to persuade us to do so.

G

It is common ground in these appeals that money by way of security was held in a loop. Mr. Aaronson submits that it was by way of security only. Mr. Goy accepts that security was involved but that that was only part of the story.

H

We also understand that there is no dispute that BGE was unable, in Mr. Goy's words, to get its hands on the money. In relation to that we are grateful to Mr. Perry, a very experienced banker, who said in relation to a loan on a cash secured basis where the security covers the whole of the loan that such a borrower "has not got any more money at the end than he had at the beginning". (Day 2 p 151 line 25).

I

A Accordingly it is apparent that BGE acquired no funds by selling its pipeline to BMBF. The purchase price having been borrowed by BMBF from Barclays left BMBF and lodged momentarily in a designated account of BGE. Thence it travelled by way of deposit to Deepstream and eventually returned to Barclays Global Treasury via BBFCIoM. Those facts are not disputed by BMBF but we do not accept the argument put forward on behalf of BMBF that such a circular B route followed by the money represented no more than was required in order to provide the necessary security.

The only benefit which BGE obtained from the very complicated arrangements choreographed by BZW were amounts B and C paid to it under the terms of the deposit agreement. Payments of amount A returned eventually C to BMBF and from BMBF to the Bank. BGE was to benefit to an extent of £8.1 million net and the Irish government was to receive £1.8 million in stamp duty. Those payments would be financed entirely by UK taxpayers by means of the hoped-for capital allowances. Without the capital allowances BGE would receive nothing, for the amounts of the rents would increase to take account of the non-availability of capital allowances.

D

Looking at the matter in round we accept Mr. Goy's primary submission that the payment of money by BMBF, even if it is said to have involved BMBF incurring expenditure, cannot be said to have been expenditure on the pipeline.

The payment by BMBF to BGE achieved no commercial purpose. E Commercially driven finance leasing is designed to provide working capital to the lessee. But BGE could not get its hands on the money. It parted with a valuable asset allegedly for £91,292,000 but received no immediate benefit from that transaction. It provided no finance to BGE simply because the amounts had to be deposited as part of the arrangements with Deepstream to be repaid only in accordance with the deposit agreement with Deepstream.

F

Lord Templeman in *Ensign Tankers (Leasing) Ltd.* v. *Stokes* said (1992) 64 TC 617 at p 742I, when dealing with the predecessor of s 24:

> "The section is not concerned with the purpose of the transaction but with the purpose of the expenditure."

G

In our judgment the purpose of the expenditure by BMBF on 31 December 1993 was not the acquisition of the Pipeline but the obtaining of capital allowances which would result in ultimately a profit to BGE and fees payable to BMBF and BZW. The transaction had no commercial reality.

H What actually occurred was that BMBF parted with money to Deepstream and received back in return payments from Deepstream. Certainly BGE was never able to enjoy the alleged purchase price of over £92,000,000. What is more it never expected to do so as is plain from the documents put in evidence.

We do not say that BMBF did not make any expenditure but any I expenditure it made was not on the Pipeline and thus BMBF cannot satisfy the conditions laid down by s 24.

The appeals fail and we adjourn these proceedings to enable the parties to agree figures. A

THK Everett
MP Cornwell-Kelly

B

The Company's appeal was heard in the Chancery Division before Park J. on 11, 12, 13, 14 and 17 June when judgment was reserved. On 22 July 2002, judgment was given in favour of the Crown, with costs.

Graham Aaronson Q.C. and *Malcolm Gammie Q.C.* for the Company. C

David Goy Q.C. and *David Ewart* for the Crown.

The cases referred to in the judgment are as follows:—*Barclays Mercantile Industrial Finance Ltd.* v. *Melluish* (1990) 63 TC 95; [1990] STC 314; *Bird* v. *Inland Revenue Commissioners* [1989] AC 300; (1988) 61 TC 238; [1988] 2 All ER 670; [1988] STC 312; *Commissioners of Inland Revenue* v. *Burmah Oil Co. Ltd.* (1982) 54 TC 200; [1982] STC 30; *Countess Fitzwilliam & others* v. *Commissioners of Inland Revenue* (1993) 67 TC 614; [1993] 1 WLR 1189; [1993] 3 All ER 184; [1993] STC 502; *Craven* v. *White* [1989] AC 398; (1988) 62 TC 1; [1988] 3 All ER 495; [1988] STC 476; *Delta Finance Newco* v. *Inland Revenue Commissioners* [2002] STC (SCD) 274; *Ensign Tankers (Leasing) Ltd.* v. *Stokes (HMIT)* [1992] 1 AC 655; (1992) 64 TC 617; [1992] 2 All ER 275; [1992] STC 226; *Finsbury Securities Ltd.* v. *Bishop* (1966) 43 TC 591; [1966] 1 WLR 1402; [1966] 3 All ER 105; *Furniss* v. *Dawson* [1984] AC 474; (1984) 55 TC 324; [1984] 1 All ER 530; [1984] STC 153; *Lupton* v. *FA and AB Ltd.* [1972] AC 634; (1971) 47 TC 580; [1969] 1 WLR 1627; *MacNiven* v. *Westmoreland Investments Ltd.* [2001] UKHL 6; (2001) 73 TC 1; [2001] 2 WLR 377; [2001] STC 237; *McGuckian* v. *Commissioners of Inland Revenue* (1997) 69 TC 1; [1997] 1 WLR 991; [1997] 3 All ER 817; [1997] STC 908; *Moodie* v. *Commissioners of Inland Revenue* (1993) 65 TC 610; [1993] 1 WLR 266; [1993] 2 All ER 49; [1993] STC 188; *R* v. *Commissioners of Inland Revenue* ex parte *Matrix Securities Ltd.* (1994) 66 TC 587; [1994] 1 WLR 334; [1994] 1 All ER 769; [1994] STC 272; *W T Ramsay Ltd.* v. *Commissioners of Inland Revenue* [1982] AC 300; (1981) 54 TC 101; [1981] 1 All ER 865; [1981] STC 174. D E F G

The cases cited in the arguments were as follows:—*Barclays Mercantile Industrial Finance Ltd.* v. *Melluish* (1990) 63 TC 95; [1990] STC 314; *Britax International GmBH* v. *Commissioners of Inland Revenue* [2002] EWCA Civ 806; [2002] STC 956; *Coates* v. *Arndale Properties Ltd.* (1984) 59 TC 516; [1984] 1 WLR 1328; [1985] 1 All ER 15; [1984] STC 637; *Countess Fitzwilliam & others* v. *Commissioners of Inland Revenue* (1993) 67 TC 614; [1993] 1 WLR 1189; [1993] 3 All ER 184; [1993] STC 502; *Delta Finance Newco* v. *Inland Revenue Commissioners* [2002] STC (SCD) 274; *Edwards (HMIT)* v. *Bairstow & Harrison* [1956] AC 14; (1955) 36 TC 204; *Ensign Tankers (Leasing) Ltd.* v. *Stokes (HMIT)* [1992] 1 AC 655; (1992) 64 TC 617; [1992] 2 All ER 275; [1992] STC 226; *Furniss* v. *Dawson* [1984] AC 474; (1984) 55 TC 324; [1984] 1 All ER 530; [1984] STC 153; *Greenberg* v. *Commissioners of Inland Revenue; Commissioners of Inland Revenue* v. *Tunnicliffe* [1972] AC 109; (1971) 47 TC 240; [1971] 3 WLR H I

A 386; [1971] 3 All ER 136; *Lupton* v. *FA and AB Ltd.* [1972] AC 634; (1971) 47 TC 580; [1969] 1 WLR 1627; *MacNiven* v. *Westmoreland Investments Ltd.* [2001] UKHL 6; (2001) 73 TC 1; [2001] 2 WLR 377; [2001] STC 237; *Moodie* v. *Commissioners of Inland Revenue* (1993) 65 TC 610; [1993] 1 WLR 266; [1993] 2 All ER 49; [1993] STC 188; *Overseas Containers (Finance) Ltd.* v. *Stoker (HMIT)* (1989) 61 TC 473; [1989] 1 WLR 606; [1989] STC 364; *R* v. B *Commissioners of Inland Revenue* ex parte *Matrix Securities Ltd.* (1994) 66 TC 587; [1994] 1 WLR 334; [1994] 1 All ER 769; [1994] STC 272; *W T Ramsay Ltd.* v. *Commissioners of Inland Revenue* [1982] AC 300; (1981) 54 TC 101; [1981] 1 All ER 865; [1981] STC 174.

C

Park J.:—

Abbreviations, *Dramatis Personae*, etc.

D 1.

BGE	Bord Gáis Éireann (the Irish Gas Board)
BGE(UK)	BGE (UK) Ltd., a wholly-owned subsidiary of BGE
BZW	Barclays de Zoete Wedd Ltd.
BMBF	Barclays Mercantile Business Finance Ltd., the Appellant company.
Barclays IoM	Barclays Finance Company (Isle of Man) Ltd.
Deepstream	Deepstream Investments Ltd.

E

F **Overview**

2. This is a corporation tax appeal from a decision of the Special Commissioners (Mr. Everett and Mr. Cornwell-Kelly), dated 18 October 2001, delivered after a hearing which lasted for five days in July 2001. The point at issue is whether the Appellant company, BMBF, is or is not entitled to capital G allowances for expenditure of somewhat over £91 million (which I shall round off to £91 million for the purposes of this judgment). BMBF contends that the expenditure was, within the meaning of s 24(1) of the Capital Allowances Act 1990, incurred on the provision for the purposes of its trade of an item of machinery or plant, namely a natural gas pipeline between Scotland and the Irish Republic. BMBF entered into contracts for it to purchase the pipeline from BGE H (the Irish Gas Board) for the sum which I am rounding off as £91 million, and there were bills of sale transferring the ownership of the pipeline to it. BMBF then entered into a lease agreement with BGE leasing the pipeline back to BGE on finance lease terms. BMBF has an established trade which includes finance leasing on a large scale, and it contends that it is entitled to capital allowances for expenditure of £91 million on the pipeline. The Special Commissioners held I that account had to be taken of the entire series of operations of which the purchase contracts and finance lease were only parts. When that was done the

Commissioners' conclusion was that BMBF had not incurred expenditure of £91 million on the pipeline. They therefore dismissed BMBF's appeal. A

3. I agree with the result reached by the Special Commissioners, for reasons which I will explain in the judgment which follows.

4. I record that before me Mr. Graham Aaronson Q.C. and Mr. Malcolm Gammie Q.C. appeared for BMBF, and Mr. David Goy Q.C. and Mr. David Ewart appeared for the Respondent Inspector of Taxes. B

The critical statutory provision C

5. This case turns upon s 24(1) of the Capital Allowances Act 1990, which was the relevant statute in force at the time when the events occurred. It provided as follows:

"24(1) Subject to the provisions of this Part, where— D

(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." E

BMBF contends that that subsection applies to it with reference to expenditure on the pipeline. The arguments arise under para (a), the requirements of which, and the extent to which they are or are not in issue in this case, can be analysed as follows. F

(i) BMBF had to be carrying on a trade. There is no dispute about this. It was. Its main activity, as the Special Commissioners found, was the provision of asset-based finance, and the Revenue accept that the generality of that activity constituted a trade. That does not mean that every transaction which BMBF entered into was necessarily part of its trade. But the requirement that it was carrying on a trade was satisfied. G

(ii) BMBF must have incurred expenditure. There is a dispute about this. BMBF's case is that it incurred expenditure of £91 million. One of the Revenue's arguments (not its main argument) is that on grounds of the circularity of payments, BMBF did not in reality incur any expenditure at all. H

(iii) If BMBF did incur the expenditure of £91 million, the expenditure had to be capital expenditure. There is no dispute about this. The Revenue accept that, if BMBF did incur the expenditure, it was capital expenditure, not revenue expenditure. I

(iv) The parts of the pipeline which BMBF purchased must have been machinery or plant. There is no dispute about this. They were.

(v) The capital expenditure of £91 million, if incurred at all, had to be incurred on the provision of the pipeline. This is the main area of dispute. BMBF contends that the expenditure was on the provision of the pipeline.

A The Revenue's main argument is that it was not. The Special Commissioners agreed. In their decision they wrote:

> "... the payment of money by BMBF, even if it is said to have involved BMBF incurring expenditure, cannot be said to have been expenditure on the pipeline".

B (vi) If BMBF did incur capital expenditure of £91 million on the provision of the pipeline, it must have done that wholly and exclusively for the purposes of its trade referred to in (i) above. This also is disputed. BMBF contends that the requirement is satisfied, but the Revenue submit that BMBF's transaction in the pipeline was not a trading transaction at all.

C **The companies involved**

6. Seven different companies were involved in one way or another in the events and transactions which gave rise to the Revenue's decision to refuse capital allowances to BMBF. Four of them were members of the Barclays group, namely: (1) BMBF, the Appellant; (2) Barclays Bank Plc, the main banking D company in the group, sometimes referred to in its roles in this case as Barclays Group Treasury; (3) Barclays IOM, an Isle of Man subsidiary of the group; and (4) BZW. BZW was not a party to any of the individual transactions, but through its Structured Finance Division it devised and organised the entire structure. The policy within the Barclays group is that transactions between group members should be conducted on arm's length terms, and that policy was followed for the E transactions which this case is about. The three other companies involved in the events were BGE, BGE(UK), and Deepstream. BGE is the Irish Gas Board, a statutory body in the Republic of Ireland. BGE(UK) is a UK company, wholly owned by BGE. Deepstream is a Jersey company owned by a charitable trust. I do not know why in this case it was thought necessary or desirable that Deepstream should not be owned by a Barclays company, but no doubt there was a reason. Deepstream was managed by a company in the Barclays group, F and *de facto* I think that it can be regarded as one of the Barclays participants in the entire structure.

Finance leasing

G 7. A major part of BMBF's activity of providing asset-based finance is, and was at the material time, entering into finance leases. I believe that the basic concept of a finance lease is now widely known. Finance leases have come before the courts on many occasions, sometimes in tax cases, sometimes not. Anyone who is sufficiently interested in this case to be a reader of this judgment will almost certainly be familiar with finance leasing. In the circumstances I will not H give a general description of how finance leases are customarily structured. As it seems to me the stage has passed when a judge needs to do that in order to enable his judgment to be followed. I should, however, specifically note that the obtaining of capital allowances for the leasing company's expenditure on acquiring the machinery or plant is fundamental. The lease rates are set at levels which assume that the lessor (or companies grouped with it) will benefit from the I allowances. If the allowances are not obtained after all, the transaction ceases to make financial and commercial sense. The finance lease will still provide for the

leasing company to make its margin, because a rental adjustment clause will provide for the rents to be increased. However, if they are increased the finance lease is no longer advantageous to the lessee: the lessee will find that, instead of it having secured finance at advantageous rates, once the rental adjustment clause has been put into effect the rates are disadvantageous. In practice the termination provisions in the lease will be operated, and the finance lease will be unwound.

8. BMBF's case is that it bought the pipeline from BGE and exploited it in the course of its trade by leasing it back to BGE on a finance lease. It says that the generality of its finance leasing business is undoubtedly undertaken in the course of the trade which the Revenue accepts that it carries on; that it qualifies for and receives capital allowances on expenditure which it incurs on buying machinery or plant for finance leasing; and that this case is no different in principle from the rest of its finance leasing business. The Revenue's case is that, while it entirely accepts (1) that BMBF carries on a trade, (2) that finance leasing transactions are capable of being trading transactions which qualify for capital allowances, and (3) that the general tax treatment of BMBF has been that its purchases of machinery or plant for finance leasing do indeed qualify for capital allowances, nevertheless this case is different and exceptional: when all the detailed transactions which surrounded the finance lease of the pipeline to BGE are taken into account it becomes apparent, as the Special Commissioners correctly decided, that this particular purchase by BMBF did not qualify for capital allowances after all.

9. A witness for BMBF before the Special Commissioners was Mr. Boobyer, a director of the company. The Special Commissioners quote the following passage from his witness statement:

> "The basic premise of the finance leasing industry is that lessors pass on the value of the capital allowances available to them in respect of the asset being financed to the customer. The customer gets the use of the asset concerned and pays rent at a rate which reflects the margin required by the bank and the reduced funding cost to the bank of providing lease finance as a result of the tax deferral benefit available."

It is implicit in Mr. Boobyer's evidence that the transaction which this case is about came within that description, and it is certainly Mr. Aaronson's submission that it did. The Revenue's position is that it entirely accepts the general principle stated by Mr. Boobyer, but it does not accept that the finance leasing transaction between BMBF and BGE was of the kind described. I agree with the Revenue, but I need to describe much more of the case before I can explain why.

The facts, including the structure of the agreements and the payments provided for by them

10. The pipeline runs from Moffat in Scotland to the coast, then under the Irish Sea to a point on the Irish coast just north of Dublin, and from there to installations in the Irish Republic. Its purpose is to transport natural gas from the UK to Ireland. I understand that, because of one or more pipelines running

A across the English Channel or the North Sea, the pipeline to Ireland will be able to transport not just natural gas produced in this country or its offshore waters, but also natural gas originating on the continent of Europe. The pipeline was obviously a major and important infra-structure project.

11. In 1992 BZW's Structured Finance Division began to advise BGE B about financing issues and possibilities connected with the pipeline. From an early stage BZW favoured a finance lease structure. It was in contact with a number of potential lessors which were not members of the Barclays group, but in the end it arranged for BMBF to act as the lessor. All of the agreements were entered into on 31 December 1993. In the following paragraphs I attempt to describe the general structure of them. I should say at the outset that there were C several of them to which BMBF was not a party, and the details of which it (BMBF) did not know. How far this matters is something which I will have to consider later. It is clear, however, that all of the agreements and the events which were to take place pursuant to them were planned as one overall scheme by BZW. (I do not intend the word "scheme" to carry any pejorative connotations. I merely mean that there was one plan which involved several different elements and the participation at different parts of the overall plan of several different D parties.)

12. By 31 December 1993 the pipeline had already been constructed by BGE. BGE owned it. The construction had been financed partly by loans to BGE made by a syndicate of banks and partly by a 35 per cent. grant from the European Economic Community. As far as I know Barclays was not one of the E syndicate banks, but I do not think that it would make any difference if it was.

13. All of the agreements, payments and other transactions which I describe in the following paragraphs happened on 31 December 1993.

14. BMBF entered into two acquisition agreements with BGE for it to F purchase from BGE the parts of the pipeline which were to be involved in the scheme (basically all of the pipeline except the parts onshore in Scotland and in the UK territorial sea off the Scottish coast). There was a reason why two agreements rather than one were required (or if not required, chosen); nothing turns on this detail. The aggregate price was the amount which, for simplicity in this judgment, I am referring to as the round figure of £91 million. (The exact figure was £91,292,000.) That price was chosen because it was the cost of the G pipeline less the grant received from the EEC. BMBF borrowed from Barclays Bank at a fixed interest rate the full amount of the price plus almost £500,000 more. (I am not clear what the extra £500,000 or so was for; perhaps it was to meet some costs and other incidental expenses of the transaction. I do not think that anything turns on this detail.) Using the bank borrowing BMBF paid the price to BGE. What happened to the £91 million after it was paid to BGE is H important, and I will return to it below. First, however, I describe what happened in connection with the pipeline.

15. BMBF and BGE entered into a lease-back of the pipeline on finance lease terms. Finance leases usually provide for a primary period in which substantial rentals are charged, and then a secondary period during which the I lease can continue at very low rentals. In this case there was a pre-primary period, a primary period and a secondary period. The pre-primary period ran until

September 1995 at a low rent of two instalments aggregating to £25,000. The primary period was 31 years from October 1995 to September 2026 (an unusually long period, but the pipeline presumably has a long period of expected use). The secondary period might continue from 2026 onwards. The secondary period rents, if they ever became payable, would be quite significant in amount, but would still be trivial compared to the primary period rentals. The primary period rentals, as in all finance leases, were carefully calculated in order over the 31 years to recoup to BMBF its outlay and to leave it with a worthwhile margin over its own cost of funds. That would only be achievable if capital allowances were obtained. I shall come back to this later, but I should say now that it is not in itself a significant pointer against the availability of capital allowances: virtually all finance leases are similar in this respect. The primary period rentals are payable annually in advance. They are of fixed amounts, not fluctuating with movements in interest rates, but they are calculated on the basis that they escalate at 5 per cent. per annum. There are the usual provisions for the rentals to be adjusted in various events, particularly in the event of changes in UK tax law which affect the tax assumptions on the basis of which the rentals had been calculated. The foremost events which would bring the rental adjustment provisions into operation would be increases or reductions in UK corporation tax rates.

16. BGE, having taken the lease-back of the pipeline, immediately entered into an agreement with BGE(UK) to sublease the pipeline to BGE(UK). In many respects the sub-lease mirrored the head-lease. There were the same pre-primary, primary and secondary periods, and the rentals were fixed at exactly the same amounts as the rentals fixed in the head-lease. That, at any rate, was the position at the outset. A difference between the head-lease and the sub-lease was that the head-lease contained provisions for adjustment of rentals in the event of changes in UK tax law and tax rates, whereas the sub-lease contained no such provisions. So if corporation tax rates changed over the 31 years (realistically a certainty) the head-lease and sub-lease rents would start to diverge from each other.

17. I do not know whether what I am about to mention was the only reason for having a sub-lease to BGE(UK), but there was a tax reason: if BMBF had simply leased the pipeline to BGE (a non-resident company) and BGE had used it in its trade, capital allowances to BMBF would have been either denied or severely restricted by s 42 of the Capital Allowances Act 1990. On the Revenue's published view at the time this would not apply if the pipeline, though directly leased to a non-resident, was sub-leased to an end user which was a UK resident. I understand that the Revenue has in the meantime changed its view on this point, but, since BMBF was presumably relying on the Revenue's published views at the time of the transaction, the Revenue has, fairly and properly, not taken this point against BMBF in the present case. I ought to qualify what I have said so far in this paragraph in the following way. BMBF's evidence, which I have no doubt was accurate, was that at the planning stage it was visualised that there would only be a head-lease, and that it would be from BMBF to BGE(UK). BGE was to give a guarantee to BMBF of BGE(UK)'s obligations. However, advice was received in Ireland that BGE might not have power to give guarantees, so the head-lease/sub-lease structure was adopted to achieve a similar economic effect. If the guarantee problem had not come up and there had simply been a head-lease to BGE(UK), I do not know whether the choice of a UK company rather than an Irish company (perhaps BGE itself) to be the lessee

A would have been made solely because of s 42 of the Capital Allowances Act, or whether there were other good reasons for having a UK company. There might well have been: if there had only been an Irish lessee (like BGE) it would almost certainly have had to have a branch in the UK, so it might have been more convenient in any case (quite apart from the tax imperative of s 42) to locate the sole lessee in this country.

B

18. So far the effect as regards rental payments would have been that on each 1 October BGE (UK) was liable to make a payment of rental to BGE, and BGE was liable to make a payment of rental to BMBF. Unless and until the two payments started to diverge by reason of UK corporation tax rates changing they would have been identical; and even after changes in UK corporation tax rates it was likely that the rentals would still be fairly similar to each other. BGE, BGE C (UK) and BMBF entered into an "Assumption Agreement" the effect of which was that (leaving aside for the moment the complication arising from changes in corporation tax rates) BGE (UK), instead of paying its sub-lease rental to BGE, would pay it directly to BMBF. BMBF would accept it as discharging BGE's liability for the head-lease rent, and BGE would accept that BGE (UK) had discharged its liability for the sub-lease rental. If corporation tax rates changed D the head-lease rent payable to BMBF would change but the sub-lease rent payable by BGE(UK) would remain the same. If I have understood correctly how it would work, if the head-lease rent went up BGE (UK) still paid the full amount of the sub-lease rent to BMBF, and the balance of the (now) increased head-lease rent would be paid by BGE to BMBF; if the head-lease rent went down BGE (UK) would pay part of the sub-lease rent to BMBF (that part being E equal to the (now) reduced head-lease rent) and would pay the balance of the sub-lease rent to BGE.

19. At the point which I have reached so far BGE (UK) had a liability to make large payments of sub-lease rentals (all or most of which would, by virtue of the Assumption Agreement, be paid direct to BMBF). Where was BGE (UK) F going to get the money from to meet its liability to make those payments? This was dealt with by a Transportation Agreement between BGE (UK) and BGE. By this agreement BGE (UK) agreed to provide services to BGE in connection with the transportation of gas for BGE, using the pipeline and onshore facilities in Scotland. (I believe that BGE (UK) owned the onshore facilities rather than leasing them.) BGE agreed to make payments to BGE (UK) for the gas transportation services. The agreement was to continue until the end of G September 2026 (so being coterminous with the primary period under the head-lease and sub-lease). There are minimum payments falling to be made by BGE in any event, regardless of whether any gas was transported through the pipeline or not. The minimum payments are calculated on a complex formula, but I think that I am right in saying that they will always be large enough to cover BGE (UK)'s liabilities to pay its sub-lease rentals to BMBF (by virtue of the H Assumption Agreement), and I imagine that they will also leave BGE (UK) with a profit. I do not know what size of profit BGE (UK) might make from the Transportation Agreement alone, but Mr. Aaronson points out, and I accept, that, quite apart from the profit-potential from that agreement, BGE (UK) has the potential to make significant profits if it is able to make other contracts exploiting parts of the capacity of the pipeline which BGE does not use, for I example by transporting gas for customers in Northern Ireland. Evidence was given to the Special Commissioners on behalf of BMBF to the effect that BGE

(UK) was not a mere vehicle company in a fiscally driven structure, and that BGE (UK) had realistic expectations of being a significantly profitable company in future years. I accept that, but as regards the Transportation Agreement itself, it is, I think, clear that the financial provisions in it are designed to function within the entire scheme devised by BZW. Further indications to that effect are that the payments by BGE to BGE (UK) are payable on 1 October annually (the same date as the date for payments of lease and sub-lease rentals) and that they escalate by 5 per cent. per annum (as do the rental payments).

20. There is one other matter to describe before I return to what happened to the £91 million which BMBF paid to BGE. Under the head-lease BMBF had rights to receive from BGE or (via the Assumption Agreement) BGE (UK) rental payments over a tract of future years. Finance leasing companies commonly wish to obtain bank guarantees of the obligations owed to them by their lessees. In this case it was part of the structure devised by BZW that Barclays Bank would give to BMBF a guarantee of BGE (UK)'s undertaking in the Assumption Agreement to pay its sub-lease rentals to BMBF in discharge of BMBF's right to receive rentals from BGE. A guarantee to that effect was another of the network of agreements which were made on 31 December 1993.

21. I can now turn to what happened to the £91 million. I preface my description by noting that Mr. Aaronson described these aspects of the structure as "the security arrangements". Mr. Goy says, and I agree, that the provision of security was part of them, but that there was more to them than that.

22. Although in simpler finance leasing structures based on a sale and lease-back the seller (the equivalent of BGE in this case) receives the purchase price and can use it to finance other expenditure or to refinance previous borrowing, that was not so in this case. When BGE received the £91 million from BMBF it was obliged to deposit it with Deepstream. This was built into the documentation in such a way that the deposit was inevitable and there was no way that BGE could have prevented it being made. Mr. Goy's expression was that "BGE could not get its hands on the money." In my opinion that was an accurate way of putting it. BGE did get the benefit of its rights against Deepstream under the deposit agreement, but there was no other way in which it could possibly have used the £91 million. The terms of the deposit agreement were most unusual, but it is convenient to describe them later rather than now.

23. When Deepstream received the £91 million by way of deposit from BGE it immediately paid it on by way of deposit to Barclays IoM. There is a complicated deposit agreement between Deepstream and Barclays IoM. Without going into the finer points of it, I can, I think, safely assume that it would ensure that Deepstream would be able to meet its obligations to BGE under the terms of the BGE/Deepstream deposit.

24. Barclays IoM, following normal practice within the Barclays group, placed the £91 million on deposit with the Group Treasury of Barclays Bank.

25. There were other documents executed on 31 December 1993, but for the moment I will pause and review what had happened to the £91 million. It had moved from the Group Treasury of Barclays Bank to BMBF by way of loan; from BMBF to BGE by way of purchase price for the pipeline; from BGE to

A Deepstream by way of deposit; from Deepstream to Barclays IoM by way of onward deposit; and from Barclays IoM to the Group Treasury of Barclays Bank by way of internal group deposit. In that way it can be said that the £91million followed a circular route. There are, however, three comments which should be made in relation to that way of viewing the matter.

B 26. First, BMBF did not know the details of what happened to the £91 million after it had been paid to BGE, and in particular did not know about Deepstream and Barclays IoM. As against that, Mr. Boobyer, the director of BMBF, had been involved at an earlier stage in consulting with BZW about a possible leasing structure for the pipeline. Also, and perhaps more relevantly, he knew that BMBF's outlay of £91 million on the pipeline was fully "cash C collateralised", although he did not know the details of how that was achieved. What the expression means in the present context is that, when Barclays Bank gave a guarantee to BMBF of the obligations of BGE(UK) to pay the lease rentals to BMBF (those obligations having been assumed by BGE(UK) under the Assumption Agreement), there would be some form of counter-guarantee or indemnity to Barclays Bank, provided at the expense of the BGE group and fully backed by cash. I will describe later what form the counter-guarantee or D indemnity took, but Mr. Boobyer's knowledge that there was one in some form and that it was fully cash collateralised meant that he knew, and thus BMBF knew, that the £91 million was not to be freely at BGE's disposal, but was in some way to be routed through other participants in the structure devised by BZW so as to provide cash backing for Barclays Bank's guarantee.

E 27. Second, Mr. Aaronson says that, although the money did in fact move in a circle, it was not inherent in the nature of the transaction that the money had to move in a circle, and to some extent the circularity was "happenstance". The features which might have been different, and if they had been different would not have resulted in a circular movement of funds, were the identities (1) of the bank which lent to BMBF the money to pay to BGE by way of purchase price F for the pipeline, and (2) of the bank which gave the guarantee to BMBF of BGE(UK)'s obligations under the head-lease and Assumption Agreement. In the actual transaction it was Barclays Bank in each case, but it need not have been that way, and if it had not been it would not have been inherent in the structure that the money took a completely circular route. At one stage BZW was planning the scheme on the basis that the finance lessor was to be a leasing company in the Abbey National group. Mr. Aaronson says that, if the transaction had gone G ahead in that way, there would not have been the complete circularity. This was not explored in detail, and I have little doubt that the circular structure which did exist in the event was convenient and attractive to the Barclays group. However, in deference to Mr. Aaronson's submissions on this I will proceed on the assumption that he is right and that the circularity was not inevitable. What was inevitable, however, was that the £91 million, having originated from a financial H participant in the structure (whether Barclays Bank or another lending source) would flow on through a pre-determined route until it ended with another financial participant in the structure: there was no possibility of it ending as funds available for BGE to use in the ordinary activities of its trade.

28. Third, BMBF demonstrated to the Commissioners (through a witness I statement of Mr. Perry, a former Group Treasurer of the Barclays group) that the immediate return of the £91 million to the group (originally by the deposit

made by Deepstream with Barclays IoM) on the same day as the money passed out of the group (by being paid by BMBF to BGE) had considerable advantages to the group under the regulatory capital regime for the control of available funds of banks. Mr. Perry's interesting and informative statement shows clearly how this arose, and I entirely accept it. In my opinion, however, it makes no difference to the issues in the present case. If BMBF would not qualify for capital allowances without this feature of how the regulatory capital system operated, then in my judgment it did not qualify after all because of the feature.

29. I now move on to describe how the structure would operate over the anticipated course of its existence, and in particular over the primary period of 31 years ending in 2026. On 1 October in each year there would be a flow of funds in the opposite direction from the initial flow of the £91 million. I summarise it in the following sub-paragraphs, which assume in the first instance that the Inland Revenue did not put a spanner in the works by denying capital allowances to BMBF (although of course that is what the Revenue has done so far, hence this case). It is somewhat arbitrary where to begin, but I will begin with the deposit of funds which Barclays IoM had made with Barclays Bank's Group Treasury.

(i) The Group Treasury repays to Barclays IoM a part of its deposit sufficient to fund Barclays IoM's payment at (ii) below. (There is, I think, no evidence or express finding by the Special Commissioners about this, but I think that it is inevitable that it would happen.)

(ii) Barclays IoM repays to Deepstream a part of Deepstream's deposit. I assume that the schedules of payments for which the Deepstream/Barclays IoM deposit agreement provides will produce results whereby Deepstream is able to make to BGE the payments referred to in (iii) below.

(iii) Deepstream makes the payments to BGE which are provided for in the BGE/Deepstream deposit agreement. This is a key part of the entire financial structure. The deposit agreement does not, as most deposit agreements do, provide for the depositee to make payments of interest and other payments of principal. It provides for Deepstream to make various payments over the life of the deposit to 2026. At the end of that period the deposit will be fully repaid. The agreement provides that Deepstream has to pay amounts described as A amounts, B amounts, and C amounts. It does not divide any of them into interest and principal. I will describe the B and C amounts later: they are the means by which BGE benefits from the anticipated UK tax savings to BMBF or companies grouped with it from the obtaining of capital allowances on the pipeline. For the present I focus on the A amounts. They are large sums payable on 1 October each year. They escalate by 5 per cent. each year. I will take as an example the first complete year for which a large A amount was payable. On 1 October 1996 Deepstream was liable to pay to BGE an A amount £6,007,883.09. (That figure will recur in some of the following paragraphs.)

(iv) BGE is liable to pay a minimum fee to BGE(UK) under the Transportation Agreement. The amount is worked out each year under a formula in the agreement. As I understand it the formula always produces an annual amount which is at least as large as the A amount received by BGE under the BGE/Deepstream deposit. So on 1 October 1996 BGE(UK) would be entitled to receive from BGE under the Transportation Agreement a fee which would be at least £6,007,883.09. Of the fee, £6,007,883.09 would

A be met out of the A amount payable by Deepstream to BGE, and I assume that any balance would be paid by BGE out of its general resources.

(v) On 1 October in each year BGE(UK) was liable by virtue of the Assumption Agreement to pay to BMBF an amount equal to the sub-lease rental (or, if the head-lease rental had gone down as a result of changes in UK tax rates, the lower head-lease rental). Assuming no reduction in the B head-lease rental by 1 October 1996, both the sub-lease rental and the head-lease rental due on that date were £6,007,883.09. Therefore BGE(UK) would have paid £6,007,883.09 to BMBF, funding the payment out of the minimum fee payable to it under the Transportation Agreement.

(vi) What I say in this sub-paragraph is an assumption, and is not, as far as I can see, formally documented in any of the agreements which were C before the Special Commissioners and which are before me. The assumption seems to me to be inherently likely. When BMBF received payments from BGE(UK) under the Assumption Agreement it would apply them towards servicing its obligations to Barclays Bank in respect of the £91 million which it had borrowed on 31 December 1993 to pay the purchase price for the pipeline. So when on 1 October 1996 BMBF received £6,007,883.09 from D BGE(UK) I assume that it paid it to Barclays Bank.

(vii) Drawing the threads of the foregoing subparagraphs together, the bulk of the payments which would fall to be made year by year over the primary period can be seen to have followed a circular pattern: from Barclays Bank to Barclays IoM, from Barclays IoM to Deepstream, from Deepstream to BGE, from BGE to BGE(UK), from BGE(UK) to BMBF, E and from BMBF to Barclays Bank. That analysis should be seen subject to two comments. First there is the comment which Mr. Aaronson would add, that it was not inevitable in a leasing transaction for the pipeline that there should be a circular flow such as I have described. In particular, if the lessor had been an Abbey National leasing company rather than BMBF, although many of the same payments would still have been parts of the structure, it F was realistically possible that the series of payments would have been linear rather than circular. The second comment is that there were to be elements in the payments made over the years which would not be circular. Although the A payments from Deepstream to BGE would be within the circle (moving on to BGE(UK), thence to BMBF, and thence to Barclays Bank's Group Treasury), the B and C payments would not be. Further, the Transportation Agreement would be likely to mean that the payments from G BGE to BGE(UK) were greater than the amounts which went round the circle (to say nothing of the prospect of BGE(UK) making substantial profits by exploiting the capacity of the pipeline in so far as it was not fully used by BGE). And (an important point which I will pick up a few paragraphs later) BMBF would need more than the receipts which it would get from BGE(UK) under the Assumption Agreement in order fully to H service and repay its borrowing of £91 million from Barclays Bank.

30. Before I come to that important point, there are two matters which I should mention in connection with the documents. First, any finance lease contains provisions for what happens if the lease terminates before the end of the primary period: a termination sum becomes payable to the lessor, reducing in I amount the longer the primary period continues. The termination sum is designed, together with the rentals which have already been paid, to provide to

the lessor the financial return which it expected from the transaction. In the documents in this case there are termination provisions, or other provisions associated with them, in the head-lease, the sub-lease, the Transportation Agreement, and the Deepstream deposit agreement. They are of major commercial importance, but I do not think that I need examine them for the purposes of this judgment.

31. Second, there are various other documents of a security nature, the purpose of which, I assume, was that the network of interlocking contractual and financial obligations which was created by the agreements of 31 December 1993 and which stays in place throughout the existence of the lease cannot be thrown into disarray by commercial events such as the emergence of outside creditors of one or more of the parties involved. I give two examples. First, it will be recalled that Barclays Bank gave a guarantee to BMBF of BGE(UK)'s obligation under the Assumption Agreement to pay the lease rentals to BMBF. When banks give guarantees they usually look for counter-guarantees or indemnities. In this case Deepstream agreed to indemnify Barclays Bank against liabilities under the guarantee. Further, Deepstream's asset was its deposit, originally of £91 million, with Barclays IoM, and Deepstream charged the benefit of that deposit to Barclays Bank to secure the indemnity. This, if I understand the matter correctly, was an important part of the "cash collateralisation" of the finance lease, to which I have referred earlier. Second, BGE had an obligation to make payments to BGE(UK) under the Transportation Agreement. BGE's major asset under the structure devised by BZW was its deposit with Deepstream. BGE charged that deposit to BGE(UK) to secure its obligation to make the payments under the Transportation Agreement.

32. I now come back to the point that BMBF's receipts of rentals (paid by BGE(UK) under the Assumption Agreement) would not be enough to cover its obligations to Barclays Bank under the borrowing of £91 million. Where was the funding going to come from to meet those obligations in full and to leave BMBF with a margin of profit from the lease? The answer, as with all finance leasing, was: from the tax savings accruing to BMBF (or to other companies in its group from surrenders of group relief, for which they would make payments for group relief to BMBF), which tax savings would be obtained if BMBF obtained capital allowances for expenditure of £91 million on the pipeline. Capital allowances give tax relief ahead of the rates of commercial depreciation, and the timing benefits of them have present values when the accelerated tax deductions are obtained. It was from the tax reliefs, which either saved for BMBF money which it would otherwise have had to pay to the Revenue or (more probably) enabled it to receive payments for group relief from other members of the Barclays group, that BMBF was able to finance its borrowing from Barclays Bank and, by the end of the lease, to make an attractive commercial margin. The Special Commissioners express the point tersely but accurately as follows:

> "BMBF receives rental payments under the terms of its lease, but has to pay higher amounts to Barclays Bank under the terms of its borrowings. The difference, according to the terms of the scheme prepared by BZW, is to be funded by the capital allowances claimed."

This is in itself entirely normal, and not some sort of abuse of the tax system, as Vinelott J. pointed out in *Barclays Mercantile Industrial Finance Ltd.* v.

A *Melluish* (1990) 63 TC 95; [1990] STC 314. (The taxpayer in that case was in fact BMBF: it has changed its name by substituting "Business" for "Industrial". At an even earlier stage in its existence it was called Mercantile Credit Ltd.)

33. However, the use of the capital allowances in this case has more effects than those which are customary in all finance leasing. They enable BGE to obtain B and keep for itself the B and C amounts which are payable to it by Deepstream under the terms of the BGE/Deepstream deposit agreement. Under the terms of the BGE/Deepstream deposit agreement the B and C amounts are still payable by Deepstream to BGE even if the capital allowances are not obtained by BMBF, but BGE will be liable to make additional payments to BMBF under the lease, and I believe that the additional payments will be greater than the B and C C amounts. In that situation the finance lease structure will be disadvantageous to BGE rather than advantageous, and the predictable result is that the termination provisions will be put into effect.

34. I now give a few more details of the B and C amounts. I do not know how they are calculated or why there are two sets of amounts rather than one, although I am sure that there is a logical explanation. All that I can do is to D summarise what the BGE/Deepstream deposit provides for. The B amounts are quite large sums. There are eight of them, and they are payable in the early years of the lease, annually on 31 December each year. The one nearest in date to the A amount of £6,007,883.09 payable on 1 October 1996 was the one due on 31 December 1996. It was £1,951,433.37. The C amounts are comparatively smaller sums payable on 1 October in all years to 2025. The amount due on 1 October E 1996 was £33,037.71. The total of the B amounts over the eight years in which they are payable is £11,708,600, and the total of the C amounts over the 32 years for which they are payable is £917,518. I was told that the net present value of those prospective receipts as at 31 December 1993 was £9,066,000, and that the net present value of the A amounts at the same date was £82,468,000. (These amounts of net present values were not, I think, before the Special F Commissioners. I have taken them from a calculation supplied to me by BMBF.)

The Special Commissioners' decision

35. The Special Commissioners described the parties and the facts, summarising the agreements much as I have attempted to do in the foregoing G paragraphs. They made an express finding as follows: "We find as a fact that the events of 31 December 1993 were pre-ordained and designed by BZW to be a composite whole."

The finding was obvious and not disputed, but it seems to me appropriate that the Commissioners should have spelt it out, since it indicates that they H considered it appropriate to evaluate the scheme in the light of the *Ramsay* principle, deriving from *WT Ramsay Ltd.* v. *Inland Revenue Commissioners* [1982] AC 300; (1981) 54 TC 101 and (by now) a long line of subsequent cases, many of them decided in the House of Lords. In their conclusions the Special Commissioners said that it was plain that the arrangements were organised and set in motion by BZW. They rejected Mr. Aaronson's submission that they I should look no further than the actions of BMBF. They accepted Mr. Goy's submission that they should look at the whole of the transaction; all the

documents, acts and events of 31 December 1993 and not merely what BMBF did. They stated their conclusion in a number of ways, but I think that the heart of it comes in one sentence:

> "Looking at the matter in [the] round we accept Mr. Goy's primary submission that the payment of money by BMBF, even if it is said to have involved BMBF incurring expenditure, cannot be said to have been expenditure on the pipeline."

36. There are other matters covered in the Special Commissioners' decision, but since I intend to give my own reasons for agreeing with their conclusion, I will not go through the contents of the decision in detail. Mr. Aaronson subjected the decision to sustained criticism, but, although there are some things which the Commissioners said about which I have some doubts or which I would express differently, it seems to me that, in a concise decision (and none the worse for being concise), they have said quite a lot. I agree with the general line of their approach.

The *Ramsay* authorities

37. I do not intend to review generally the line of authorities which commenced with *WT Ramsay Ltd.* v. *Inland Revenue Commissioners* [1982] AC 300; (1981) 54 TC 101 and has continued through a substantial number of subsequent cases, many of which went to the House of Lords, the latest being *MacNiven* v. *Westmoreland Investments Ltd.* [2001] UKHL 6; [2001] 2 WLR 277; [2001] STC 237. I do, however, wish to pick out some strands in the line of authorities which appear to me to be of particular relevance to the present case. I shall also look more closely at the *Westmoreland* case: it is the latest word of the House of Lords in this developing area of tax law, and it is heavily relied upon by Mr. Aaronson.

38. The *Ramsay* principle has by now been authoritatively categorised by the House of Lords as a principle of statutory construction: see for example Lord Hoffmann in *Westmoreland* at para 28: "Everyone agrees that *Ramsay* is a principle of construction. The House of Lords said so in *Inland Revenue Commissioners* v. *McGuckian* [1997] STC 908." The same point had been made before, for example by the House of Lords in *Craven* v. *White* [1989] AC 398. There is also validity, in my respectful opinion, in the remark of Nourse L.J. in *Fitzwilliam* v. *Inland Revenue Commissioners* [1992] STC 185 at p 198: "The principle might equally be described as one of statutory application." The principle is certainly relevant in cases where there is an element of fiscal planning involved. In the present case I would not myself think of the scheme devised by BZW as a tax avoidance scheme (although, as I shall explain later, it seems that the Special Commissioners did), but careful tax planning is always involved in finance leasing, and there is, I believe, no dispute that the *Ramsay* principle falls to be considered in this case. The issue is how, if at all, it applies to the facts and the documents.

39. The *Ramsay* principle may come into play where there was a series of transactions with a close nexus between them: "pre-ordained" is a commonly used word here, deriving from the speech of Lord Diplock in *Inland Revenue*

A *Commissioners* v. *Burmah Oil Co. Ltd.* (1981) 54 TC 200 at p 214. All the more clearly the principle applies where, as in this case, there were several different documents, each dealing with its own particular subject matter, but all designed to take effect together and all entered into at the same time as each other. An earlier example of such a case is *Ensign Tankers (Leasing) Ltd.* v. *Stokes* [1992] 1 AC 655; (1992) 64 TC 617, which involved a leasing transaction connected with B a film. In Lord Templeman's words ((1992) 64 TC 617, at p 727): "The scheme was a single composite transaction embodied in 17 documents all of which are dated 14 July 1980." It was common ground that the documents had to be read as a whole. The *Ensign Tankers* case demonstrates that the nature of the transaction when all the documents are taken together may differ from what might have appeared to be the effect of one particular document, which may well have been C the one on which the taxpayer specifically wanted to rely. Lord Hoffmann made an essentially similar point in *Westmoreland* by referring at more than one point to the Court taking a view "which transcended the juristic individuality of the various parts of a preplanned series of transactions."

40. An important strand of the *Ramsay* line of authorities is that, when it D is necessary to consider whether an expression in a taxing statute applies to the situation created by the series of transactions or interconnected set of documents, the Court must consider the question with an eye to reality rather than artificiality. The words "real" or "really", or other words carrying the same idea, make regular appearances in the judgments. For example, in *Ramsay* itself Lord Wilberforce said, in a much-quoted passage [1982] AC 300, at p 187:

E "The capital gains tax was created to operate in the *real* world, not in the world of make-belief . . . [I]t is a tax on gains . . ., it is not a tax on arithmetical differences. To say that a loss (or gain) which appears to arise at one stage in an indivisible process, and which is intended to be and is cancelled out by a later stage, so that at the end of what was bought as, and planned as, a single continuous operation, there is *not such a loss (or gain) as the legislation is dealing with*, is in my opinion well and indeed essentially F within the judicial function." [The italics are mine, as in the further quotations which follow.]

In *Burmah Oil* (at (1981) 54 TC 200 at p 220H and [1982] STC 30) Lord Fraser quoted that passage and said that it was the ratio of the decision in G *Ramsay*. A few lines later he said:

"The question . . . is whether the present scheme, when completely carried out, did or did not result in a loss such as the legislation is dealing with, which I may call for short a *real* loss."

At (1981) 54 TC 200 p 221G Lord Fraser said:

H "The result was that although *Burmah apparently* suffered the loss of almost the whole price it had paid for the new shares, . . . it suffered *no real* loss because . . ." (His Lordship went on to explain the reason on the facts of the particular case.)

I I will give two other examples. In *Ensign Tankers* Lord Templeman said ((1992) 64 TC 617 at p 739G):

"It is crucial, when considering the tax avoidance scheme in the present case to take the analysis far enough to determine where the expenditure on the film is *really* to be found." A

In *Inland Revenue Commissioners* v. *McGuckian* (1997) 69 TC 1 at p 76; [1997] STC 908 at p 913, Lord Browne-Wilkinson said: B

". . . the liability for tax on the indirect receipt of such dividend by Shurltrust has to be determined by stripping out the *artificial* steps and applying the provisions of the Taxes Acts to the *real* transaction, i.e. the payment of a dividend to the shareholder, Shurltrust, which received such dividend as income." C

41. I move now to the most recent case, *MacNiven* v. *Westmoreland* [2001] UKHL 6; (2001) 73 TC 1; [2001] STC 237. It was a case in which the House of Lords held that the Revenue was unable successfully to invoke the *Ramsay* principle to cause an apparent payment of tax-deductible interest to be treated as not being such a payment after all. The importance of the case lies not so much in the specific decision (though that is important in itself) as in the general observations of all the members of the House, particularly of Lord Hoffmann who delivered the principal speech. The central thesis in His Lordship's analysis of the law is to distinguish between two kinds of concepts which might be used in a taxing statute: commercial concepts on the one hand, and purely legal or juristic concepts on the other. Where it appears that Parliament intended to refer to a commercial concept the *Ramsay* approach or principle comes into operation, particularly so given the large body of authority that it is a principle of statutory interpretation. However, not all concepts used in a statutory provision can be approached in that way. "They [many terms in tax legislation] cannot be construed in this way. They refer to purely legal concepts which have no broader commercial meaning. In such cases, the *Ramsay* principle can have no application." (Paragraph 49 of Lord Hoffmann's speech.) His Lordship considered that the statutory term which was in point in *Westmoreland* itself was of that sort, and for that reason the Revenue's *Ramsay* argument failed in that case. D E F G

42. But it is different where the term used in the statute is of a commercial nature. In *Ramsay* itself the key terms were "loss" and "disposal". Lord Hoffmann explained (in para 32) that the innovation in *Ramsay* was to give those statutory concepts a commercial meaning [(2001) 73 TC 1; [2001] STC 237, at para 32]: H

"The new principle of construction was a recognition that the statutory language was intended to refer to commercial concepts, so that in the case of a concept such as a 'disposal', the court was required to take a view of the facts which transcended the juristic individuality of the various parts of a preplanned series of operations." I

Lord Hoffmann expanded on his analysis in various ways. The whole speech should be carefully studied. I will not prolong this judgment by extensive quotations, but I will cite one other passage only, from para 48 where his Lordship explains how his analysis that *Ramsay* is a principle of construction is in line with the celebrated analysis of Lord Brightman in *Furniss* v. *Dawson* [1984]

A AC 474 at p 574, to the effect that fiscally inserted steps in a composite transaction are "disregarded":

> "If the statutory language is construed as referring to a commercial concept it follows that steps which have no commercial purpose but which have been artificially inserted for tax purposes into a composite transaction will not affect the answer to the statutory question. When Lord Brightman B said that the inserted steps are to be 'disregarded for fiscal purposes', I think that he meant that they should be disregarded for the purpose of applying the relevant fiscal concept."

43. In earlier paragraphs I pointed out how in *Ramsay* itself and in several of the subsequent cases the focus has been on whether the loss claimed was a C "real" loss, or otherwise on whether what is relied on by the taxpayer was "really" within the statutory provision concerned. Lord Hoffmann does not use those expressions, but in my view his emphasis that statutory terms which are used in a "commercial" sense should be interpreted so as to have their commercial meaning is not significantly different. Lord Hutton agrees with Lord Hoffmann, and in adding a few observations of his own focuses on the "real" as D opposed to the "artificial".

44. I have concentrated on Lord Hoffmann in *Westmoreland*, since all of the other members of the House said that they agreed with his speech. There are valuable and important, though briefer, speeches by Lords Nicholls, Hope and Hutton. Lord Hobhouse said that he agreed with Lord Hoffmann. I have already E mentioned Lord Hutton's stress on the distinction between the real and theartificial. Lord Nicholls observed that (2001) 73 TC 1; [2001] STC 237, at para 6 : "When searching for the meaning with which Parliament has used the statutory language in question, courts have regard to the underlying purpose that the statutory language is seeking to achieve." (Paragraph 6 of his speech.) He added that "weight is given to the purpose and spirit of the legislation." Lord Hope, having agreed with Lord Hoffmann, added, at para 77:

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> "The only relevant questions are: (1) the question of law: what is the meaning of the words used by the statute? And (2) the question of fact: does the transaction, stripped of any steps that are artificial and should be ignored, fall within the meaning of those words?"

G **Analysis and discussion: some general observations**

45. I have already explained that this case turns on s 24 of the Capital Allowances Act 1990, and in particular on the following words in subs (1)(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." H BMBF submits that it came within those words: it says that it incurred expenditure of £91 million on the provision of the pipeline, and did so wholly and exclusively for the purposes of its trade of providing asset-based finance. The Revenue submit that for three independent reasons, any one of which by itself would be enough, BMBF did not, as respects this particular transaction, come within s 24. Logically the order in which the Revenue arguments arise is: I (1) BMBF did not incur any expenditure at all. (2) If it did the expenditure was not expenditure on the provision of the pipeline. (3) If it did incur expenditure

and the expenditure was on the provision of the pipeline, the expenditure was not incurred wholly and exclusively for the purposes of its trade: the pipeline transaction was a transaction which stood outside BMBF's trade. That is the logical order of the three arguments, but the primary argument is (2), and it has always been presented first. I shall follow that pattern in this judgment.

46. I would like to begin by specifying one thing which I do not say, and which is not any part of my reasoning for deciding this issue against BMBF. I do not regard the pipeline transaction as some sort of unappealing tax-avoidance scheme. In this connection, although I am in general agreement with the Special Commissioners, there is one thing which they say with which I do not agree. They record that Mr. Goy, counsel for the Revenue before them as he has been before me, rejected any attempt to use pejorative language directed against BMBF or the scheme, but they go on to say this: ". . . but it is inevitable that if the Crown is to succeed in these appeals it must establish that what occurred was a complicated, convoluted tax avoidance transaction." Mr. Goy submitted to me that he did not need to establish that BZW's scheme was "a complicated, convoluted tax avoidance transaction." I agree with him, and that is not a description (except for the word "complicated") which I would apply to the scheme. However, contrary to what is implied by the above-quoted words of the Special Commissioners, it does not follow that, if the scheme was not a convoluted tax avoidance transaction, therefore the Revenue have no maintainable argument that the scheme did not come within the wording of s 24(1)(a).

47. BMBF's view of the scheme in which it participated is, in the terms put to me by Mr. Aaronson, that, although the scheme was large and complicated, it was still "standard commercial finance leasing". I do not agree that it was, for reasons which I will explain below, but I do not question that BMBF (and BZW, the overall architect of the scheme) did not think of it as standing apart from the general run of finance leasing business which BMBF has habitually undertaken for many years. I think that there is a danger that pure specialists in asset-based financing structures may become carried away by the details of a structure which they are devising, to the extent that they tend to lose sight of the overall picture. They just take it for granted that, if they can use a lessor which, like BMBF, has an established trade of finance leasing, the capital allowances will be forthcoming. Usually they are right, but not always. I do not know whether something like that happened here, but it would not surprise me if it did. In a detailed way the structure of this scheme is meticulously and imaginatively thought out. I am full of admiration for the drafting of the numerous documents which were required to implement it. But I believe that, if one steps back from the details and reconsiders what they have all achieved, it does become apparent that the overall transaction was not "standard commercial finance leasing" at all, and that it could not be taken for granted that the capital allowances would be forthcoming.

48. The Revenue does not dispute, and nor do I, that, in general, finance leasing transactions carried out by BMBF qualify for capital allowances. However, the Revenue submit, and I agree, that this case is exceptional and possesses unusual features which differentiate it from the general run of BMBF's finance leasing. I quoted earlier in this judgment the description of finance leasing given by Mr. Boobyer, a director of BMBF. It refers to the lessors passing on "the

A value of the capital allowances available to them in respect of *the asset being financed* to the customer". Mr. Boobyer says that the customer "gets the use of the asset concerned". He refers to "the reduced funding cost to the Bank [sic: I think that Mr. Boobyer really means to refer to the leasing company] of *providing lease finance*". Mr. Goy says that the Revenue have no disagreement with what Mr. Boobyer says, but in its submission the present transaction is outside the B description which he gives.

49. Mr. Boobyer describes transactions where the leasing company provides finance to the lessee, and where the finance enables the lessee to have the use of an asset which, absent the lease finance, it would not have. Alternatively (perhaps not precisely covered by Mr. Boobyer's description, but a common kind C of finance leasing) the lessee already has the asset (an item of machinery or plant) but has paid for it with borrowed money on which it is paying full commercial rates of interest; it sells the asset to the leasing company and takes a finance lease-back at more favourable rates; it uses the purchase price to repay its borrowings. Another possibility is for the lessee to sell the asset and lease it back under a finance lease, and to use the purchase price, not to repay the existing borrowing D incurred to acquire the asset, but for other purposes of the lessee's business. In all of those cases the finance lessor provides "up-front" finance to the lessee, and the finance so provided is used in one way or another in the lessee's business. But in the transaction involved in the present case no up-front finance was provided. BGE already owned the pipeline and had paid for it with a loan from a syndicate of banks. After the transaction BGE was still able to use the pipeline as before, E though by then it did so by virtue of the lease, sub-lease and Transportation Agreement, and it still owed to the banks the money which it had borrowed. Nor was the £91 million available to BGE for it to use in any other way to finance transactions or activities of its business.

50. Mr. Goy is right when he says that "BGE could not get its hands on the F money". All that BGE was to get out of the transaction was the annual receipts of the B amounts and the C amounts from Deepstream as the scheme worked its way through the primary period. The financial reality as regards those payments was that they were BGE's share of the value of BMBF's capital allowances, channelled to BGE via Barclays Bank, Barclays IoM and Deepstream under the system devised by BZW. It is true that, in finance leasing as described by G Mr. Boobyer, the lessee benefits from the value of the leasing company's capital allowances, but it does so by raising finance for use in its business at lower rates than it would have to pay on a conventional borrowing: it does not benefit from the value of the allowances by receiving annual cash receipts from other participants in the leasing structure. I have no doubt that to receive the B and C amounts annually for over 30 years would be very attractive to BGE, but it is not remotely characteristic of finance leasing as Mr. Boobyer described it.

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51. In my opinion it is legitimate to have in mind the points which I have made in the last few paragraphs in considering whether the requirements of s 24 have been met by BZW's scheme. In *Westmoreland* (2001) 73 TC 1; [2001] STC 237 Lord Nicholls said (in para 6):

I "When searching for the meaning with which Parliament has used the statutory language in question, courts have regard to the underlying

purpose that the statutory language is seeking to achieve . . . [W]eight is given to the purpose and spirit of the legislation." A

As regards finance leasing the underlying purpose of Parliament, in my view, is to enable capital allowances to be used so as to provide to lessees at attractive rates finance for them to use and to develop their real business activities. The underlying purpose of Parliament is not to enable cash payments to be made annually to third parties who are able to provide a major item of machinery or plant which satisfies one of the conditions for a finance lessor to claim the allowances. Nor is that in accordance with "the purpose and spirit of the legislation". B

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52. The Special Commissioners were clearly conscious of the sorts of matters to which I have referred. They wrote this:

"The only benefit which BGE obtained from the very complicated arrangements choreographed by BZW were amounts B and C paid to it under the terms of the deposit agreement. Payments of amount A returned eventually to BMBF and from BMBF to the Bank. BGE was to benefit to the extent of £8.1million net and the Irish government was to receive £1.8 million in stamp duty. Those payments would be financed entirely by UK taxpayers by means of the hoped-for capital allowances. Without the capital allowances BGE would receive nothing, for the amounts of the rents would increase to take account of the non-availability of capital allowances." D E

[The aggregate of two sums of £8.1 million and £1.8 million in this passage was what, as I understand it, the Special Commissioners were told was the net present value of the amounts to be received by BGE. The net present value supplied to me was rather lower: £9,066,000, as mentioned in para 34 above.] F

The Commissioners express those matters in decidedly waspish terms, but in my opinion the points which they make are all substantially correct. If the question is asked, "So what?", I would answer that, although the points do not of themselves mean that BMBF's payment of £91 million fails to come within the terms of s 24, the obtaining of allowances in such a case is not the sort of thing which Parliament may be supposed to have had in mind when it enacted the section. G

53. I move on. One issue which was disputed before the Special Commissioners was whether they should take into account only the specific transactions to which BMBF was a party, or whether they should take account of the entire scheme. The issue was important, because it was accepted by the Revenue before the Commissioners, as it was also accepted before me, that, if the Commissioners looked only at the specific transactions to which BMBF was itself a party (i.e. the Barclays Bank loan to BMBF, BMBF's acquisition of the pipeline, the head-lease, the sub-lease, the Transportation Agreement, the Assumption Agreement, and Barclays Bank guarantee), the appeal would succeed. The Commissioners held, however, that they should take account of the entire scheme: "We also accept his [Mr. Goy's] submission that we must look at the whole of the transaction; all the documents, acts and events of 31 December 1993 and not merely what BMBF did." I agree with the Commissioners. BMBF H I

knew that the specific things which it was to do were parts of a larger scheme devised and organised by BZW, and it was content to perform its parts of the entire scheme. It knew that the £91 million was fully cash-collateralised, so it must have known that BGE was not going to get £91 million which it could use for purposes of its business of fulfilling the Irish Republic's requirements for gas. I do not accept that BMBF cannot be affected by other steps in the entire scheme, the details of which it did not know.

54. Taxpayers have quite frequently argued that, when they have participated in a scheme devised by another (sometimes by a tax consultancy which specialised in providing avoidance schemes), the tax consequences for themselves ought not to be influenced by steps in the scheme to which they were not parties and of which they had no specific knowledge. The arguments are almost always unsuccessful. The Special Commissioners quote one example from the decision of the House of Lords in *Moodie* v. *Inland Revenue Commissioners* (1993) 65 TC 610; [1993] 1 WLR 266. The Special Commissioners in that case had found that (1993) 65 TC 610 at p 622D

> "Mr. Moodie did not know the full details of the circular movements of debits and credits in the books of the Slater Walker companies, but he knew that the financial arrangements would take place within the Slater Walker group."

As the Special Commissioners in the present case observe, Mr. Moodie's lack of detailed knowledge did not assist him in attempting (unsuccessfully) to win his appeal before the House of Lords. In a similar way there have been quite a lot of reported cases under the present ICTA 1988 ss 703 *et seq* and predecessor enactments (captioned "cancellation of tax advantages from certain transactions in securities") in which taxpayers who have sold shares in a private company to a purchasing company in the tax consultants' organisation have been made liable to income tax partly in consequence of things which happened in the consultants' organisation and of which they had no knowledge (and of which they would probably not have been told if they had asked). See for example the discussion of this aspect by Vinelott J. in *Bird* v. *Inland Revenue Commissioners* [1985] STC 584 at pp 635-6.

55. I mention before moving on that, although I agree with the Special Commissioners that the applicability or otherwise of s 24 to BMBF has to be ascertained by reference to the whole scheme, and not just by reference to what BMBF itself did within the scheme, I agree with that only for the reason which I have explained (that BMBF knew that what it was doing was part of an entire scheme, and was content to fulfil its part of the scheme). I do not agree with a second reason which the Special Commissioners gave, namely that, if knowledge on the part of BMBF of the entire scheme was necessary for the Revenue to succeed, BMBF was somehow fixed with all the knowledge which all the companies in the group of which it was a member possessed, even if some items of it were not knowledge which BMBF itself possessed.

Analysis and discussion: assuming that BMBF incurred expenditure, did it incur it on the provision of the pipeline?

56. I move on to the terms of s 24, and in particular the words "has incurred capital expenditure on the provision of machinery or plant". In view of Lord Hoffmann's speech in *Westmoreland* (2001) 73 TC 1; [2001] 2 WLR 377 I need to consider whether those words embody a commercial concept or a legal (or juristic) concept. In my judgment they plainly embody a commercial concept. Incurring expenditure on the provision of something is not legal terminology. It would be different if terms like "consideration" were used, but they are not. I expect that Mr. Aaronson is right that a reason why the draftsman used the words he did was because he needed to cover, not just the case where a person buys an existing item of machinery or plant, but also the case where a person spends money on creating a new item of machinery or plant by building it or manufacturing it. That does not change the position. The statute is still employing commercial vocabulary, not legal vocabulary. Indeed the explanation underlines the point: the statute needed to cover a considerable range of different commercial ways in which machinery or plant might be acquired. It is therefore not at all surprising that the draftsman used commercial language to cover the whole range.

57. Section 24 refers to incurring expenditure on the provision of machinery or plant. It is true that in a strictly legal sense one can say that BMBF incurred expenditure on the provision of the pipeline. That is what the two Acquisition Agreements said: "The Seller shall sell the Pipeline as beneficial owner, and the Lessor shall purchase the Pipeline ...". Each agreement provides for "the Purchase Price for the Pipeline", and the two purchase prices aggregate to over £91 million. However, in the light of the *Ramsay* authorities I consider that I have to interpret and apply the statute in a wider way. I have to ask: looking at the matter commercially (Lord Hoffmann's term), did BMBF incur expenditure of £91 million on the provision of the pipeline, or did it incur it on something else? I have to ask: on what did BMBF *really* incur its expenditure of £91 million? Was it really incurred on the provision of the pipeline, or was it really incurred on something else? Businessmen are familiar with situations under which, in order to get some advantage which the business wants, it is necessary to achieve it indirectly by buying some other item through which the advantage, which is what the money is really paid for, can be secured.

58. The Special Commissioners held, in a passage which I have already quoted, that "the payment of money by BMBF, even if it is said to have involved BMBF incurring expenditure, cannot be said to have been expenditure on the pipeline". I agree with them, although I would be inclined myself slightly to expand the proposition and say: the expenditure by BMBF, looked at commercially and from the point of view of what it was really for, was not incurred on the provision of the pipeline. That proposition naturally prompts the question: Well, what was it incurred on? The Special Commissioners do not answer the question. My answer is that the expenditure was really incurred on the creation or provision of a complex network of agreements under which, in an almost entirely secured way, money flows would take place annually over the next 32 or so years so as to recoup to BMBF its outlay of £91 million plus a profit. The £91 million never passed out of the network created by the agreements

A (substantially an enclosed network). The £91 million was merely part of what the Special Commissioners record Mr. Goy as describing (not inappropriately, in my view) as "financial engineering". I consider that it was the money flows which mattered, and it was on the rights to the money flows that, as a commercial matter, BMBF really expended the £91 million which it had borrowed.

B 59. In support of my analysis I make some further observations. It is noteworthy that, although BGE warranted that to the best of its knowledge and belief the price of £91 million did not exceed the open market value of the pipeline, as far as I can see no attempt was made to determine the open market value of the pipeline and to adopt that figure as the purchase price. £91 million was the cost of constructing the pipeline less the amount of the EEC grant towards the cost. I appreciate that the pipeline was a particularly difficult item to C value, but the absence of any attempt at the difficult exercise demonstrates that it did not greatly matter what the value was. Usually the ability of a lessee to meet its obligations to pay rents depends to a significant extent on the performance of its business, and that is likely to include the value and income-earning potential of the leased property. In the present case the ability of BGE to meet its obligations to pay rents depended only to a small extent on the performance of D its business. As long as capital allowances were granted to BMBF, then, apart from the possibility that rentals under the head-lease might be adjusted upwards on account of changes in UK tax rates or rules, it is not apparent to me that it mattered what the value of the pipeline was, what its income-earning potential for BMBF was, or what the general commercial performance of BGE in its business was. The deposit of the entire £91 million which BGE had to make E immediately with Deepstream, coupled with the agreement between Deepstream and Barclays IoM, meant that (barring some cataclysm like the total collapse of the Barclays group) the rentals would always be provided through the network of financial agreements. The same applies to the termination sums which would have to be paid if the lease was terminated before it had run for the whole of the primary period.

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60. I accept that finance lessors always wish to limit the credit risk to which they are exposed. But there can be cases where the credit risk is so comprehensively eliminated that it becomes apparent, if one steps back and thinks about it, that the lessor has not really laid out its money on a leasing transaction at all.

G 61. Indeed, in this case it seems to me that the structure would in principle have worked in exactly the same way whether the purchase price had been £91 million or £191 million or, for that matter, £9.1 million. The various figures and the money flows would all have to be scaled up or down, but because the original funding had never moved out of the financial network, the financial structure would always be in place to supply the money flows which the H agreements provided for. Another aspect of this is that, apart from the need to obtain capital allowances, it could be argued that the pipeline was surplus to the requirements of the scheme, analogous to an unnecessary fifth wheel on the coach. I do not suggest for a moment that a major company of the stature of BMBF would be indifferent to whether it really did become the owner of the machinery or plant involved in any leasing transaction. However, let me test the I matter by imagining that there never was a pipeline, or (perhaps more realistically) that there was but that by some disastrous error which had not been

picked up and corrected, BGE had never been the true owner of it. Capital allowances apart, it strikes me that neither of those assumptions would prevent the financial mechanism from operating in exactly the same way as it works if (as of course is actually the case) there is a pipeline and BGE is the owner of it.

62. Why was the pipeline needed for the transaction at all? The answer is: to provide the machinery or plant without which capital allowances could not be obtained. If those allowances are once obtained it hardly matters what happens to the pipeline. Barclays IoM would always have the money needed to pay to Deepstream what Deepstream needed to make its payments to BGE. BGE would always have (from the A amounts paid by Deepstream) most of what it needed to make its payments of the minimum fees due to BGE(UK) under the Transportation Agreement. BGE(UK) would always have (through the amounts received by it from BGE) the amounts which it needed to make its payments to BMBF under the Assumption Agreement. It is true that there were contingencies (principally ones of changes in UK corporation tax leading to upward adjustments of the head-lease rentals) under which BGE could be liable to make some payments to BMBF which would not be provided for by the money flows coming to BGE under the structure. However, the bulk of the rentals payable to BMBF were covered by the pre-arranged money flows, and I cannot think that this detail can affect the principle of the matter.

63. Mr. Aaronson pointed out that there are some sections in which the legislature has described in detail a particular kind of leasing transaction which is regarded as unsuitable to rank for capital allowances. He instances ss 42 and 75(1)(c), neither of which is suggested by the Revenue to apply in this case. He also draws attention to s 76A, which would now apply to this case and prevent capital allowances being claimed, but which was not in force at the time of the pipeline transaction. He does not suggest that the existence of any of these provisions shuts the Revenue out from advancing the argument which they successfully advanced to the Special Commissioners, but he submits that they should make me cautious before accepting it. I see the point, but none of the other sections to which Mr. Aaronson draws attention persuades me that the Special Commissioners were wrong or that I should reach a different conclusion from the one which they reached.

64. For the foregoing reasons I agree with the Special Commissioners' conclusion that the expenditure incurred by BMBF was not incurred on the provision of the pipeline. I believe that my reasons are substantially the same as the Commissioners' reasons, but I have set them out in more detail than the Commissioners did.

65. That is sufficient to mean that this appeal must be dismissed. In the circumstances the Special Commissioners did not deal with the Revenue's two other arguments. I will say something about them, but I will not go into them in the same sort of depth as I have adopted in my examination of the Revenue's main argument.

A **Analysis and discussion: did BMBF incur any expenditure at all?**

66. One of the Revenue's other arguments is that BMBF did not incur any expenditure at all. The basis of this argument is that the apparent payment of £91 million by BMBF to BGE was part of a circle of payments, and there have been several cases in the tax field which have held that circular money movements
B do not involve real payments of money at all. The circle round which the £91 million flowed in this case was from Barclays Bank to BMBF, from BMBF to BGE, from BGE to Deepstream, from Deepstream to Barclays IoM, and from Barclays IoM to Barclays Bank.

67. This is a difficult area. It is true that there have been cases in which
C circular payments have been held for tax purposes to be "nothings" (for example *Moodie* v. *Inland Revenue Commissioners* in the High Court and in the House of Lords: see (1993) 65 TC 610 at p 638 *et seq* and p 657 *et seq*; Lord Templeman's speech in *R* v. *Inland Revenue Commissioners* ex parte *Matrix Securities Ltd.*: see (1994) 66 TC 587 at p 629 *et seq*). But there have also been cases in which circular payments have been held to rank as payments. *Westmoreland* was one of them.
D So, I think, was *Ramsay*, at least in the eyes of Lord Fraser. He said that "'real' money in the form of a loan from Slater Walker was used" ([1982] AC 300 at p 338G). In this case the payment of £91 million from BMBF to BGE was a Barclays Bank payment through the CHAPS system, and it would be a very strong thing to hold that that was a nullity. Further, there is force in Mr. Aaronson's proposition that it was not inevitable that the scheme would be
E wholly circular; for example, if it had proceeded with an Abbey National leasing company instead of with BMBF, the payments might realistically have been linear rather than circular.

68. Reverting to *Ramsay*, Lord Wilberforce said ([1982] AC 300 at pp 332–3; (1981) 54 TC 101 at p 184):

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"In some cases one may doubt whether, in any real sense, any money existed at all . . . but facts as to this matter are for the commissioners to find. I will assume that in some sense money did pass as expressed . . ."

In the present case the Special Commissioners have quoted an Agreed
G Statement of Facts which includes the following: "On 31 December 1993 BMBF made a CHAPS payment of £91,292,000 plus VAT to BGE . . ." They make no finding as respects the Revenue's argument that, because of the circularity, BMBF did not pay the £91 million after all. They only hint that there is an issue about this, doing so by their passage, which I have quoted already: ". . . the payment of money by BMBF, even if it is said to have involved BMBF incurring
H expenditure . . ." If they had expressly held or found that, on account of circularity, BMBF did not incur expenditure I might not have been prepared to interfere with their decision. But equally, the Commissioners not having made any finding of such a nature, and having dealt only with the Revenue's main argument (which proceeds on the assumption that BMBF did incur expenditure), I am not prepared positively to conclude that BMBF did not incur
I the expenditure. To put the matter another way, if I had been against the Revenue on their other two arguments (which I am not), I would not have been

prepared to uphold the Commissioners' result on the sole ground that, although the Commissioners did not say so, in my judgment BMBF did not incur any expenditure. A

Analysis and discussion: was any expenditure by BMBF incurred for the purposes of its trade? B

69. I turn finally to the Revenue's third argument, that, even if BMBF did incur expenditure on the provision of the pipeline, it did not do that wholly and exclusively for the purposes of its trade. I agree with this argument. In my judgment the transaction involved in the present case stands apart from the generality of BMBF's finance leasing transactions to an extent such that, whereas the generality of transactions are in the course of BMBF's trade, this one was not. I have no doubt that it would have come as a shock to Mr. Boobyer if someone had said to him in 1993 that the leasing transaction with BGE relating to the pipeline would not be a transaction within BMBF's trade, but that is nevertheless my opinion. C D

70. The Revenue argument on this aspect of the case rests on principles established by a line of "dividend-stripping" cases of the 1960s and 1970s, culminating in *Lupton* v. *FA & AB Ltd.*, (1971) 47 TC 580; [1972] AC 634 (House of Lords); [1968] 1 WLR 1401 (High Court); [1969] 1 WLR 1627 (Court of Appeal). The case went to the House of Lords, but I wish to refer to an important passage in the first instance judgment of Megarry J., which was expressly adopted and approved by Lord Morris of Borth-y-Gest in the House of Lords. The learned Judge was concerned with the drawing of a dividing line between (1) transactions which have fiscal elements in them but which are nevertheless trading transactions, and (2) transactions where the fiscal elements are present to such an extent that the transactions are not trading transactions at all. In a frequently cited passage (at (1971) 47 TC 580 at p 598B) he says this: E F

> "If upon analysis it is found that the greater part of the transaction consists of elements for which there is some trading purpose or explanation (whether ordinary or extraordinary), then the presence of what I may call 'fiscal elements', inserted solely or mainly for the purpose of producing a fiscal benefit, may not suffice to deprive the transaction of its trading status. The question is whether, viewed as whole, the transaction is one which can fairly be regarded as a trading transaction. If it is, then it will not be denatured merely because it was entered into with motives of reaping a fiscal advantage. Neither fiscal elements nor fiscal motives will prevent what in substance is a trading transaction from ranking as such. On the other hand, if the greater part of the transaction is explicable only on fiscal grounds, the mere presence of elements of trading will not suffice to translate the transaction into the realms of trading. In particular, if what is erected is predominantly an artificial structure, remote from trading and fashioned so as to secure a tax advantage, the mere presence in that structure of certain elements which by themselves could fairly be described as trading will not cast the cloak of trade over the whole structure. In speaking of the greater part of the transaction I am not, of course, referring to mere bulk. A long document, like a long speech, may do and say remarkably little. What seems G H I

A to me to be of particular importance is the relative extent of the significant provisions which are made."

71. It is necessary to apply the distinction which Megarry J. explains to the facts of this case. The Special Commissioners do not deal with the point at all, and, unless I leave the question undecided as they did, I have to decide it myself B on the basis of the materials before me, including the witness statement of Mr. Boobyer. I do not think that it would be appropriate for me to remit the case to the Special Commissioners for them to decide whether the transaction was a trading transaction or not: if my decision on the main argument (that the expenditure was not incurred on the provision of the pipeline) is correct the trade/no trade argument is not necessary to the determination of the case. There would C also be the practical difficulty that both of the Special Commissioners who decided this case have now retired.

72. In my judgment, looking at the transaction as a whole and weighing up the matters described by Megarry J., the transaction was not one which was mainly trading but with fiscal elements. Rather it was one which was heavily dominated by fiscal elements, although it did have "the presence of elements of D trading". Megarry J. says that the transaction must be "viewed as a whole", and in my judgment that requires the Court to consider, not just the parts of the whole transaction to which BMBF was specifically a party, but the other parts of the transaction as well. I have already considered that point (see paras 53 and 54 above), and I will not repeat what I said there. I referred in the previous paragraph to Mr. Boobyer's witness statement, but he describes only the steps in E which BMBF was directly involved. He does not mention that BGE was obliged to deposit the £91 million with Deepstream (so that, in Mr. Goy's words, BGE could not get its hands on the money), nor does he refer to the terms of the Deepstream deposit, in particular to the payments of the B and C amounts, which were the real benefit of the transaction to BGE.

F 73. There are always fiscal elements present in any finance leasing transaction, but that does not prevent the generality of such transactions being trading transactions on the part of the lessor. Most finance leasing transactions are ones where the lessor provides finance to the lessee. Further, the finance is up-front finance, that is finance which is available for the lessee to use in its business at the time of the lease. In this case, for reasons which I have explained earlier, BMBF did not provide any up-front finance to BGE. Normal finance leasing G transactions involve, as a central element in the structure, the leasing of the machinery or plant at a rent—something which I have no difficulty in accepting is at least very likely to be a trading operation. In the present case there was a lease of the pipeline to BGE, but in my judgment, despite its apparent prominence it was not really a central element: it was not what the transaction was really about. The transaction was really about creating a complex and H sophisticated structure which enabled BGE every year to receive payments representing its share of the tax savings (or group relief payments) received by BMBF from the capital allowances. The underlying thinking was, as it seems to me, that BGE had the pipeline, which was a big item of machinery or plant and thus a potential subject matter for a big claim for capital allowances, and that BMBF had an established status and know-how as a finance lessor. The two I items would be utilised in combination within the structure devised by BZW, with the real end product being, not the provision of finance at rates which were

both profitable to the provider (BMBF) and attractive to the recipient (BGE), but fiscal savings to be shared between the two of them and to be provided at the expense of the UK Revenue. A

74. It is in my view important that the sharing of fiscal benefits in this case went significantly beyond the type of sharing which is found in all finance leasing. That type of sharing is that the leasing company is able to provide finance to the lessee at lower rates than it would have to charge if it did not get capital allowances on its expenditure. I do not see anything in sharing of that nature which is an indication against trading on the part of the leasing company. In this case, however, there is the additional and striking feature of the B and C amounts which fall to be paid by Deepstream to BGE. They amount to a straight cash sharing of tax savings. In the dividend stripping cases cash sharing of the intended fiscal benefits was regarded as a significant indication against trading (see especially *Finsbury Securities* v. *Bishop* (1966) 43 TC 591; [1966] 1 WLR 1402, and also the decision in *Lupton* v. *FA and AB (supra)* itself), and I take the same view of it in this case. B C D

75. For those reasons I agree with the Revenue's argument that this was not a trading transaction on the part of BMBF, so that, even if it did involve expenditure being incurred by BMBF on the provision of the pipeline, it would still not come within s 24. If necessary I would dismiss this appeal on that ground as well. E

Conclusion

76. For the foregoing reasons I dismiss this appeal. I have nothing of substance to add, but there is one matter which I should briefly mention. I was told that a decision of a differently constituted panel of Special Commissioners in a somewhat similar case has recently been released in anonymised form. I was supplied with a copy of the decision, which is made public under the name of *Delta Finance Newco* v. *Inland Revenue Commissioners.* Mr. Gammie and Mr. Ewart helpfully explained the main strands of the case to me. It has similarities to the present case, but there are differences as well. It may itself come on appeal to this Court at some time. In the circumstances I say nothing more about it in this judgment. F G

Appeal dismissed, with costs. H

The Company's appeal was heard in the Court of Appeal before Peter Gibson, Rix and Carnwath L.JJ. on 12, 13 and 14 November, when judgment was reserved. On 13 December 2002, judgment was given against the Crown, with costs. I

Graham Aaronson Q.C. and *Camilla Bingham* for the Company.

David Goy Q.C. and *David Ewart* for the Crown.

A The cases referred to in the judgment are as follows:—*Barclays Mercantile Industrial Finance Ltd.* v. *Melluish (HMIT)* (1990) 63 TC 95; [1990] STC 314; *Beauchamp (HMIT)* v. *FW Woolworth plc* [1990] AC 478; (1989) 61 TC 542; [1989] STC 510; *Commissioners of Inland Revenue* v. *Burmah Oil Co. Ltd.* (1982) 54 TC 200; [1982] STC 30; *Countess Fitzwilliam & others* v. *Commissioners of Inland Revenue* (1993) 67 TC 614; [1993] 1 WLR 1189; [1993] 3 All ER 184; [1993] B STC 502; *Craven* v. *White* [1989] AC 398; (1988) 62 TC 1; [1988] 3 All ER 495; [1988] STC 476; *Ensign Tankers (Leasing) Ltd.* v. *Stokes (HMIT)* [1992] 1 AC 655; (1992) 64 TC 617; [1992] 2 All ER 275; [1992] STC 226; *Furniss* v. *Dawson* [1984] AC 474; (1984) 55 TC 324; [1984] 1 All ER 530; [1984] STC 153; *Gisbourne* v. *Burton* [1989] QB 390; *Lupton* v. *FA and AB Ltd.* [1972] AC 634; (1971) 47 TC 580; [1971] 3 WLR 670; *MacNiven* v. *Westmoreland Investments Ltd.* [2001] C UKHL 6; (2001) 73 TC 1; [2001] 2 WLR 377; [2001] STC 237; *McGuckian* v. *Commissioners of Inland Revenue* (1997) 69 TC 1; [1997] 1 WLR 991; [1997] 3 All ER 817; [1997] STC 908; *Overseas Containers (Finance) Ltd.* v. *Stoker (HMIT)* (1989) 61 TC 473; [1989] 1 WLR 606; [1989] STC 364; *Re Charge Card Services Ltd.* [1987] Ch 150; *Shiu Wing* v. *Commissioner of Estate Duty* [2000] HKFCA 64; *W T Ramsay Ltd.* v. *Commissioners of Inland Revenue* [1982] AC 300; (1981) D 54 TC 101; [1981] 1 All ER 865; [1981] STC 174.

The cases cited in the arguments were as follows:—*Barclays Mercantile Industrial Finance Ltd.* v. *Melluish (HMIT)* (1990) 63 TC 95; [1990] STC 314; *Commissioners of Inland Revenue* v. *Burmah Oil Co. Ltd.* (1982) 54 TC 200; [1982] E STC 30; *Commissioners of Inland Revenue* v. *Willoughby* (1997) 70 TC 57; [1997] 1 WLR 1071; [1997] 4 All ER 65; [1997] STC 995; *Coates* v. *Arndale Properties Ltd.* (1984) 59 TC 516; [1984] 1 WLR 1328; [1985] 1 All ER 15; [1984] STC 637; *Countess Fitzwilliam & others* v. *Commissioners of Inland Revenue* (1993) 67 TC 614; [1993] 1 WLR 1189; [1993] 3 All ER 184; [1993] STC 502; *DTE Financial Services Ltd.* v. *Wilson* [2001] EWCA Civ 455; (2001) 74 TC 14; [2001] STC 777; F *Edwards (HMIT)* v. *Bairstow & Harrison* [1956] AC 14; (1955) 36 TC 207; *Ensign Tankers (Leasing) Ltd.* v. *Stokes (HMIT)* [1992] 1 AC 655; (1992) 64 TC 617; [1992] 2 All ER 275; [1992] STC 226; *Furniss* v. *Dawson* [1984] AC 474; (1984) 55 TC 324; [1984] 1 All ER 530; [1984] STC 153; *Greenberg* v. *Commissioners of Inland Revenue; Commissioners of Inland Revenue* v. *Tunnicliffe* [1972] AC 109; (1971) 47 TC 240; [1971] 3 WLR 386; [1971] 3 All ER 136; *Inland Revenue* G *Commissioners* v. *John Lewis Properties plc* [2001] STC 1118; *Lupton* v. *FA and AB Ltd.* [1972] AC 634; (1971) 47 TC 580; [1971] 3 WLR 670; *MacNiven* v. *Westmoreland Investments Ltd.* [2001] UKHL 6; (2001) 73 TC 1; [2001] 2 WLR 377; [2001] STC 237; *Melluish (HMIT)* v. *BMI (No.3) Ltd. & others* [1996] 1 AC 454; (1995) 68 TC 1; [1995] 3 WLR 630; [1995] 4 All ER 453; [1995] STC 964; *Moodie* v. *Commissioners of Inland Revenue* (1993) 65 TC 610; [1993] 1 WLR 266; [1993] 2 All ER 49; [1993] STC 188; *Overseas Containers (Finance) Ltd.* v. *Stoker* H *(HMIT)* (1989) 61 TC 473; [1989] 1 WLR 606; [1989] STC 364; *R* v. *Commissioners of Inland Revenue* ex parte *Matrix Securities Ltd.* (1994) 66 TC 587; [1994] 1 WLR 334; [1994] 1 All ER 769; [1994] STC 272; *Stokes (HMIT)* v. *Costain Property Investments Ltd.* (1984) 57 TC 688; [1984] 1 WLR 763; [1984] 1 All ER 849; [1984] STC 204; *W T Ramsay Ltd.* v. *Commissioners of Inland Revenue* [1982] AC 300; (1981) 54 TC 101; [1981] 1 All ER 865; [1981] STC 174.

I

Peter Gibson L.J.:— A

1. The taxpayer, Barclays Mercantile Business Finance Ltd. ("BMBF"), appeals against the order made on 22 July 2002 by Park J., dismissing with costs BMBF's appeal against the decision on 18 October 2001 of the Special Commissioners (Mr. THK Everett and Mr. MP Cornwell-Kelly). The Special B Commissioners dismissed BMBF's appeals against notices of determination of trading losses for accounting periods ended 31 December 1993 and 1994 respectively and notices of assessment to corporation tax for the same periods.

2. The issue in dispute is whether BMBF is entitled to capital allowances in respect of what it claims was its expenditure on the acquisition of a gas pipeline C for the purposes of its trade. But in resolving that dispute questions arise as to the applicability of the approach laid down in the House of Lords in *WT Ramsay Ltd.* v. *Commissioners of Inland Revenue* [1982] AC 300 ("*Ramsay*") as explained by the House of Lords in *MacNiven* v. *Westmoreland Investments Ltd.* (2001) 73 TC 1; [2001] 2 WLR 377 ("*MacNiven*"). The Revenue accepts that if one looks D only at what BMBF did, it would be entitled to capital allowances. But it says that if the transaction involving the acquisition of the pipeline is looked at in its entirety, on the *Ramsay* approach BMBF did not incur the claimed expenditure on the provision of the pipeline and accordingly it was not entitled to capital allowances. That submission was upheld by the Special Commissioners and, on appeal, by the Judge, who further agreed with another submission by the E Revenue that this was not a trading transaction by BMBF at all. BMBF says that this was a standard commercial finance leasing transaction giving rise to the ordinary availability of capital allowances. We are told by Mr. Aaronson Q.C., appearing for BMBF, that the decisions thus far have caused widespread concern within the asset-leasing sector of the financial market. Chadwick L.J., in giving permission to appeal, said that the appeal raised an important point of principle F which required early guidance from this Court. Hence the expedited hearing of the appeal.

The statutory provisions G

3. Before I turn to the facts it is convenient to set out the statutory provisions in force at the material time governing capital allowances. Section 24(1) Capital Allowances Act 1990 provided:

"Subject to the provisions of this Part, where— H

(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, I

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

It is unnecessary to refer to the details of the writing-down and other allowances and balancing charges provided for in the other parts of s 24.

A 4. There are other provisions which restrict the availability of capital allowances in particular circumstances. Thus s 75(1) provides (so far as material):

"... where a person incurs capital expenditure on the provision by purchase of machinery or plant, and—

(a) he and the seller are connected to each other, or

B (b) the machinery or plant continues to be used for the purposes of a trade carried on by the seller, or

(c) it appears with respect to the sale, or with respect to transactions of which the sale is one, that the sole or main benefit which, but for this subsection, might have been expected to accrue to the parties or any of them was the obtaining of an allowance under C this Part,

a first-year allowance shall not be made in respect of the expenditure or any additional VAT liability incurred in respect of it or, if made, shall be withdrawn, and these shall be disregarded for the purposes of section ... 25 ... so much (if any) of the aggregate of the expenditure and any such additional VAT liability as exceeds the disposal value to be brought into D account under those sections by reason of the sale."

The *Ramsay* approach

5. It is also convenient to say a few words about the *Ramsay* approach in E the light of the authorities. Lord Nicholls in *MacNiven* said ([2001] 2 WLR 377 at pp 379, 380; (2001) 73 TC 1 at p 56):

"1 ... In the *Ramsay* case the House did not enunciate any new legal principle. What the House did was to highlight that, confronted with new and sophisticated tax avoidance devices, the courts' duty is to determine the legal nature of the transactions in question and then relate them to the fiscal F legislation: see Lord Wilberforce at page 326.

2. The *Ramsay* case brought out three points in particular. First, when it is sought to attach a tax consequence to a transaction, the task of the courts is to ascertain the legal nature of the transaction. If that emerges from a series or combination of transactions, intended to operate as such, it is that series or combination which may be regarded. Courts are entitled to look at G a prearranged tax avoidance scheme as a whole ...

4. Second, this is not to treat a transaction, or any step in a transaction as though it were a 'sham' ... What this does is to enable the court to look at a document or transaction in the context to which it properly belongs.

5. Third, having identified the legal nature of the transaction, the courts must then relate this to the language of the statute. For instance, if H the scheme has the apparently magical result of creating a loss without the taxpayer suffering any financial detriment, is this artificial loss a loss *within the meaning of the relevant statutory provisions?*"

6. Lord Hoffmann (with whom all the other members of the House agreed) in *MacNiven* ([2001] 2 WLR 377, at p 391 para 44) regarded as the *Ramsay* I principle the decision of the House of Lords to construe particular statutory terms ("disposal" and "loss") in a commercial sense which transcended the

individuality of intermediate circular book entries. He referred to what Lord Brightman had stated in *Furniss* v. *Dawson* [1984] AC 474 at p 572C; (1984) 55 TC 324, at p 401 where, paraphrasing what Lord Diplock had said in *Commissioners of Inland Revenue* v. *Burmah Oil Co. Ltd.* [1982] STC 30 at p 33, Lord Brightman set out the limitations of the *Ramsay* approach: A

"First, there must be a series of pre-ordained transactions; or, if one likes, one single composite transaction. This composite transaction may or may not include the achievement of a legitimate commercial (i.e. business) end. The composite transaction does, in the instant case; it achieved a sale of the shares in the operating companies by the Dawsons to Wood Bastow. It did not in *Ramsay*. Secondly, there must be steps inserted which have no commercial (business) *purpose* apart from the avoidance of a liability to tax—not 'no business effect'. If those two ingredients exist, the inserted steps are to be disregarded for fiscal purposes. The court must then look at the end result. Precisely how the end result will be taxed will depend on the terms of the taxing statute sought to be applied." B C

7. Lord Hoffmann commented ([2001] 2 WLR 377 at pp 392 and 393; (2001) 73 TC 1 at pp 69 and 70): D

"48. My Lords, this statement is a careful and accurate summary of the effect which the *Ramsay* construction of a statutory concept has upon the way the courts will decide whether a transaction falls within that concept or not. If the statutory language is construed as referring to a commercial concept, then it follows that steps which have no commercial purpose but which have been artificially inserted for tax purposes into a composite transaction will not affect the answer to the statutory question. When Lord Brightman said that the inserted steps are to be 'disregarded for fiscal purposes', I think that he meant that they should be disregarded for the purposes of applying the relevant fiscal concept . . . E F

49. For present purposes, however, the point I wish to emphasise is that Lord Brightman's formulation in the *Furniss* case, like Lord Diplock's formulation in the *Burmah* case, is not a principle of construction. It is a statement of the consequences of giving a commercial construction to a fiscal concept. Before one can apply Lord Brightman's words, it is first necessary to construe the statutory language and decide that it refers to a concept which Parliament intended to be given a commercial meaning capable of transcending the juristic individuality of its component parts. But there are many terms in tax legislation which cannot be construed in this way. They refer to purely legal concepts which have no broader commercial meaning. In such cases, the *Ramsay* principle can have no application." G H

8. Lord Nicholls ([2001] 2 WLR 377 at p 381; (2001) 73 TC 1 at p 58, para 7) referred to Lord Brightman's remarks as describing the factual situation where typically the *Ramsay* approach will be a valuable aid but not as laying down the factual prerequisites for the application of the *Ramsay* approach. I

9. Lord Hoffmann ([2001] 2 WLR 377 at pp 395 and 396; (2001) 73 TC 1 at p 72) under the heading "The limits of *Ramsay*" gave further guidance on the distinction he was drawing between commercial and legal concepts in taxing statutes:

A "58 The limitations of the *Ramsay* principle therefore arise out of the paramount necessity of giving effect to the statutory language. One cannot elide the first and fundamental step in the process of construction, namely to identify the concept to which the statute refers. I readily accept that many expressions used in tax legislation (and not only in tax legislation) can be construed as referring to commercial concepts and that the courts are today B readier to give them such a construction than they were before the *Ramsay* case. But that is not always the case. Taxing statutes often refer to purely legal concepts. They use expressions of which a commercial man, asked what they meant, would say 'You had better ask a lawyer'. For example, stamp duty is payable upon a 'conveyance or transfer on sale' (Schedule 13, paragraph 1(1) to the Finance Act 1999). Although slightly expanded by a C definition in paragraph 1(2), the statutory language defines the document subject to duty essentially by reference to external legal concepts such as 'conveyance' and 'sale'. If a transaction falls within the legal description, it makes no difference that it has no business purpose. Having a business purpose is not part of the relevant concept. If the 'disregarded' steps in *Furniss* v. *Dawson*... had involved the use of documents of a legal description which attracted stamp duty, duty would have been payable.

D 59. Even if a statutory expression refers to a business or economic concept, one cannot disregard a transaction which comes within the statutory language, construed in the correct commercial sense, simply on the ground that it was entered into solely for tax reasons. Business concepts have their boundaries no less than legal ones."

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10. In accordance with that guidance the *Ramsay* approach is applicable where it is sought to attach a tax consequence to a transaction which typically consists of a series of pre-ordained transactions or a single composite transaction, in which steps have been inserted which have no business purpose apart from the avoidance of tax. The Court gives effect to the statutory language, F where the concept to which the statute refers is a commercial one, by disregarding the artificial steps. If the concept is a legal one, there is no scope for the application of the *Ramsay* approach. I will return later to what seems to me to be the difficult dichotomy between legal and commercial concepts.

G **The uncontroversial facts**

11. A Statement of Facts was agreed between the parties. It is recited in full in the Special Commissioners' decision ([1]). At this point it is sufficient that I set out the uncontroversial salient facts, which I take from the Agreed Facts, the documents and the findings of the Special Commissioners.

H (1) BMBF is a very substantial company within the Barclays plc banking group. Its principal activity is the provision of asset-based finance.

(2) Bord Gáis Éireann ("BGE") is an Irish corporation owned by the Irish Government and responsible for the supply, transmission and distribution of natural gas in Ireland.

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([1]) Pages 450 to 468 *ante*.

(3) Between 1991 and 1993 BGE built a gas pipeline ("the Interconnector") running from Scotland to Ireland with the assistance of a 35 per cent. grant from the EU, the construction being financed by loans from a consortium of banks. A

(4) On 8 April 1992 Barclays de Zoete Wedd Ltd. ("BZW"), the investment banking arm of the Barclays group, put a proposal to BGE. This included the purchase by a UK company of the Interconnector or part of it, the grant of a 20-year lease of it to a UK subsidiary of BGE, the guarantee by Barclays Bank plc ("BB") of the rental payments under the lease, a long term supply contract between the subsidiary and BGE and a cash deposit of a sum a little below the expected purchase price of £250 million by BGE with BB as security for its guarantee, the deposit to provide BGE with the cashflow needed by the subsidiary to service the lease. BZW said that the proposal would need to be adapted to suit BGE's needs. BZW was awarded a financing mandate by BGE. B C

(5) In May 1993 BZW submitted a more detailed proposal to its Credit Risk Management Division for sanction. Under it BGE would sell the Interconnector to Abbey National which would lease it to the UK subsidiary of BGE; the subsidiary would sell gas to BGE under a "take or pay" agreement on terms providing the subsidiary with sufficient means to meet the rental payments and to generate a margin of profit; BB would guarantee to the lessor the fixed rental payments payable under the loan but, in view of the proposed length of the lease, BB would require security from BGE in the form of cash deposited with a Barclays subsidiary. BZW said that Abbey National would be able to take advantage of capital allowances by investing in a finance lease of the Interconnector and that those benefits would also be reflected in a level of rental payments attractive to the lessee. Of the cash deposit it was said: D E F

> "This will also serve the purpose of fixing and crystallising the benefits to the BGE Group of the finance lease to the extent that the scheduled interest payments and repayments of the deposit exceed the rental payments i.e. BGE will set aside a certain amount of funds at the outset which will generate a cash flow which will cover the element of BGE's obligations under the Take or Pay Agreement corresponding to the rental payments, and in addition provide a subsidy reflecting the benefits to the BGE Group of the finance lease." G

(6) BGE (UK) Ltd. ("BGE (UK)") was incorporated in England and Wales on 17 June 1993 as a wholly-owned subsidiary of BGE. H

(7) Negotiations with Abbey National reached an advanced stage, but then broke down owing to legal advice that under its constitution BGE was unable to give a guarantee of the lease obligations of BGE (UK), and in October 1993 it was decided that BMBF should be the lessor.

(8) Other changes to the scheme, interposing BGE as the lessee and providing for a sublease to BGE (UK), increasing the length of the lease and reducing the size of the transaction to a purchase of parts of the Interconnector for £91,292,000, were agreed before 31 December 1993. I

(9) On 31 December 1993 the following transactions were entered into pursuant to the scheme devised by BZW:

A (a) by two acquisition agreements BMBF agreed to acquire from BGE certain specified plant and machinery relating to specific parts of the Interconnector for £91,292,000 (I refer to the acquired plant and machinery as "the Pipeline");

(b) by a lease agreement ("the Headlease") BMBF agreed to lease the Pipeline to BGE for a pre-primary period from 31 December 1993 B to 30 September 1995, and for a primary period from 1 October 1995 to 30 September 2025, with possible annual renewals during a secondary period thereafter; there was a low fixed rental for the pre-primary period, but the primary period rentals were of substantial fixed amounts, not fluctuating with movements in interest rates but calculated on the basis that they escalated by 5 per cent. per annum; C further they were to be adjusted in the event of changes to UK tax law and tax rates; the secondary period rentals were small but not insignificant;

(c) by a sublease agreement ("the Sublease") BGE agreed to sublet the Pipeline to BGE (UK) for the same periods as in the Headlease, the rentals being the same (save that the Sublease contained D none of the provisions in the Headlease for the adjustment of rentals in the event of changes in UK tax law and tax rates);

(d) by an agreement ("the Assumption Agreement") between BMBF, BGE and BGE (UK), BMBF agreed to make out invoices to BGE (UK) in respect of payments ("the assumed payments") falling due from BGE under the Headlease and that BGE (UK) would settle E such invoices, thereby discharging monetary obligations due to BMBF under the Headlease; in turn BGE agreed that payments from BGE (UK) to BMBF would correspondingly satisfy monetary obligations to BGE under the Sublease;

(e) by an agreement ("the Transportation Agreement") between BGE and BGE (UK), BGE (UK) agreed to transport, handle and F deliver gas to BGE's order in return for specified payments from BGE, such payments to be made into a BGE (UK) account ("the Transportation Account");

(f) by a guarantee facility agreement and Deed of Guarantee ("the Barclays Guarantee") BB guaranteed to BMBF direct payment by BGE (UK) to BMBF of the assumed payments;

G (g) BMBF borrowed from BB £91,784,000 which came from its Treasury at a fixed rate of interest of 10.95 per cent. per annum and made a CHAPS payment of £91,292,000 to BGE and ownership of the Pipeline was transferred by BGE to BMBF by two bills of sale;

(h) a letter signed on behalf of BGE, BB and BGE (UK) H instructed BB to debit £91,292,000 from BGE's account with BB as soon as it was received from BMBF and to pay that sum to an account of a Jersey company, Deepstream Investments Ltd. ("Deepstream"), with BB;

(i) by an agreement ("the Deposit Agreement") between BGE and Deepstream BGE agreed to deposit £91,542,000 with Deepstream and I Deepstream agreed to repay to BGE amounts falling into three categories, A, B and C; the A payments matched the rental payments

payable to BMBF and in the primary period rose from £2.8 million in 1995 to nearly £25 million in 2025; the B and C payments were for BGE itself, the B payments being of reducing amounts from £2.6 million in 1994 to £325,000 in the last year of the payments, 2001, while the C payments were of much smaller sums never exceeding £35,000 and payable from 1994 to 2025.

(j) as security for its obligations to BGE (UK) under the Transportation Agreement, BGE assigned its interest in the deposit with Deepstream to BGE (UK) and charged a BGE current account in favour of BGE (UK);

(k) BGE (UK) executed a Deed of Indemnity in favour of BB and assigned to BB its interest in the deposit with Deepstream, the BGE account and its rights under the Transportation Agreement and charged the Transportation Account in favour of BB;

(l) by a further deposit agreement between Deepstream and Barclays Bank Finance Company (Isle of Man) Ltd. ("Barclays (IOM)"), another company in the Barclays group, Deepstream placed £91,542,000 with Barclays (IOM);

(m) Deepstream executed a Deed of Indemnity in favour of BB in respect of BB's obligations under the Barclays guarantee and assigned to BB its rights to the sum deposited with it, granted BB fixed and floating charges over all its assets and charged in favour of BB the account with Barclays (IOM);

(n) the £91,292,000 deposited by Deepstream was returned to BB's Treasury by Barclays (IOM);

(o) by two put options made between another BGE subsidiary, Sudanor Ltd. ("Sudanor"), BMBF and BGE, BMBF was given the right to sell the Pipeline to Sudanor on the termination of the Headlease, BGE acting as BMBF's sales agent.

(10) The purchase price of £91,292,000 represented the net cost to BGE (after deduction of the EU grant) of the Pipeline;

(11) The existence of the deposit held by Barclays (IOM), the interest in which Deepstream had assigned to BB, had the effect that the finance provided by the Barclays group was weighted at 0 per cent. in BB's capital adequacy return to the Bank of England (i.e. the transaction was treated as being of no risk and so did not affect the capital adequacy of the Barclays group);

(12) BGE saw the benefits to it of the arrangements as being the following:

"The gross value of the saving is estimated at £12.6 million over the life of the lease (£11.7 million over years 1-8) and the present value at £9.9 million (discounted at 6.75 per cent.). Out of these benefits BGE must pay £1.8 million of stamp duty. The net present value is therefore projected at £8.1 million." (BGE Memorandum dated 14 December 1993)

It was recognised that there were risks associated with receiving those benefits because BGE would be tied to a very long lease, but it was said that in

A the first 5 years the benefits were likely to be positive provided capital allowances were not denied; in the long term there was much greater uncertainty and the possibility of the benefits being eliminated if taxes were to go up.

The Special Commissioners' decision

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12. The Special Commissioners (in para 36 of their decision) said that BMBF had to pay higher amounts to BB under the terms of its borrowing than it would receive from the rental payments payable to it under the Headlease. The difference, they said, was to be funded by the capital allowances claimed according to the terms of the scheme prepared by BZW.

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13. The Special Commissioners, in para 37, said that the Transportation Agreement was designed to ensure that BGE (UK)'s rental payments could always be met, the effect of the agreement being that BGE financed the payment of BGE (UK)'s rental payments. Having noted that under the terms of the deposit with Deepstream the only moneys which left the Barclays group were the comparatively small B and C payments, the Special Commissioners found as a D fact that the events of 31 December 1993 were pre-ordained and designed by BZW to be a composite whole (para 39).

14. In the passage in para 48 of their decision where they stated their conclusions the Special Commissioners took the view that what occurred was "a complicated, convoluted tax avoidance transaction." They rejected a submission E by Mr. Aaronson that they should look no further than the actions of BMBF. They accepted the submissions by Mr. Goy Q.C., for the Revenue, that s 24 was looking at a commercial concept and that they had to look at the whole of the transaction. They noted that it was common ground that money by way of security was held in a loop. They continued:

> "We also understand that there is no dispute that BGE was unable, in F Mr. Goy's words, to get its hands on the money. In relation to that we are grateful to Mr. Perry, a very experienced banker, who said in relation to a loan on a cash secured basis where the security covers the whole of the loan that such a borrower 'has not got any more money at the end than he had at the beginning.'
>
> Accordingly it is apparent that BGE acquired no funds by selling its G pipeline to BMBF. The purchase price having been borrowed by BMBF from Barclays left BMBF and lodged momentarily in a designated account of BGE. Thence it travelled by way of deposit to Deepstream and eventually returned to Barclays Global Treasury via [Barclays (IOM)]. Those facts are not disputed by BMBF but we do not accept the argument put forward on behalf of BMBF that such a circular route followed by the money H represented no more than was required in order to provide the necessary security.
>
> The only benefit which BGE obtained from the very complicated arrangements choreographed by BZW were amounts B and C paid to it under the terms of the deposit agreement. Payments of amount A returned eventually to BMBF and from BMBF to the Bank. BGE was to benefit to I an extent of £8.1 million net and the Irish government was to receive £1.8 million in stamp duty. Those payments would be financed entirely by

UK taxpayers by means of the hoped-for capital allowances. Without the capital allowances BGE would receive nothing, for the amounts of the rents would increase to take account of the non-availability of capital allowances. A

Looking at the matter in round we accept Mr. Goy's primary submission that the payment of money by BMBF, even if it is said to have involved BMBF incurring expenditure, cannot be said to have been expenditure on the pipeline. B

The payment by BMBF to BGE achieved no commercial purpose. Commercially driven finance leasing is designed to provide working capital to the lessee. But BGE could not get its hands on the money. It parted with a valuable asset allegedly for £91,292,000 but received no immediate benefit from that transaction. It provided no finance to BGE simply because the amounts had to be deposited as part of the arrangements with Deepstream to be repaid only in accordance with the deposit agreement with Deepstream. C

Lord Templeman in *Ensign Tankers (Leasing) Ltd.* v. *Stokes* [[1992] 1 AC 655] said at p [677E], when dealing with the predecessor of s 24: D

> 'The section is not concerned with the purpose of the transaction but with the purpose of the expenditure.'

In our judgment the purpose of the expenditure by BMBF on 31 December 1993 was not the acquisition of the Pipeline but the obtaining of capital allowances which would result in ultimately a profit to BGE and fees payable to BMBF and BZW. The transaction had no commercial reality. E

What actually occurred was that BMBF parted with money to Deepstream and received back in return payments from Deepstream. Certainly BGE was never able to enjoy the alleged purchase price of over £92,000,000. What is more it never expected to do so as is plain from the documents put in evidence. F

We do not say that BMBF did not make any expenditure but any expenditure it made was not on the Pipeline and thus BMBF cannot satisfy the conditions laid down by s 24."

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15. Accordingly, the Special Commissioners dismissed BMBF's appeal.

Park J.'s judgment

16. On the appeal to the High Court the Judge in a careful and detailed judgment, the lucidity of which was rightly acknowledged by Mr. Aaronson, upheld the decision of the Special Commissioners. He pointed out how the £91,292,000 had followed a circular route starting with the Treasury of BB from which it went on loan to BMBF and ending with the Treasury after Barclays (IOM) had received Deepstream's deposit, all in the course of the same day. He described as inevitable the movement of the money through a predetermined route until it ended with another financial participant in the structure, commenting "there was no possibility of it ending as funds available for BGE to use in the ordinary activities of its trade." He also stated that the bulk of the payments, which would fall to be made year by year over the primary period, follow a circular pattern, though he drew attention to those elements in the H I

A payments which would not be circular: first, the B and C payments by Deepstream to BGE; second, the fact that the payments by BGE to BGE (UK) under the Transportation Agreement would be likely to be greater than the amounts which went round the circle; third, the fact that BMBF would need more than the receipts which it would receive from BGE (UK) under the Assumption Agreement in order fully to service and repay its borrowing from B BB. The Judge said that the further funding would be expected to come from the tax savings accruing to BMBF if capital allowances were obtained for the expenditure of £91,292,000 on the Pipeline. He said (in para 32 of his judgment ([1])):

> "Capital allowances give tax relief ahead of the rates of commercial depreciation, and the timing benefits of them have present values when the C accelerated tax deductions are obtained. It was from the tax reliefs, which either saved for BMBF money which it would otherwise have had to pay to the Revenue or (more probably) enabled it to receive payments for group relief from other members of the Barclays group, that BMBF was able to finance its borrowing from Barclays Bank and, by the end of the lease, to make an attractive commercial margin."

D

17. The Judge said (in para 32) that this was in itself entirely normal in finance leasing and not an abuse of the tax system. But he said (in para 33) that the use of the capital allowances in this case had more effects than those which are customary in all finance leasing, the B and C payments still being payable by Deepstream to BGE even if the capital allowances are not obtained by BMBF, E but BGE would be liable to make additional payments, greater than the B and C payments, under the Headlease. That, he said, was likely to cause the provisions allowing termination of the Headlease to be put into effect by BGE.

18. The Judge (in para 46) said that he did not regard the transaction as some sort of unappealing tax avoidance scheme. He (in para 47) accepted that F BMBF and BZW did not think of the scheme in which BMBF participated as standing apart from the general run of finance leasing business, and (in para 48) that, in general, finance leasing transactions qualify for capital allowances. But he said (in para 49) that this was not a case where the finance enabled the lessee to have the use of an asset which, absent the lease finance, it would not have, nor was it a case where the lessee uses the proceeds of sale to repay borrowings or for other purposes of the lessee's business. He described all those cases as being G where the finance lessor provided "up front" finance to the lessee and the finance so provided is used in the lessee's business. He contrasted that with the present case where BGE already owned the Pipeline, and after the transaction it was still able to use it as before, though by virtue of the Headlease, the Sublease and the Transportation Agreement, and it still owed the banks the money which it had borrowed, nor was the £91,292,000 available for BGE to use in any other way H to finance transactions or activities of its business. He agreed (in para 50) with Mr. Goy's comment that "BGE could not get its hands on the money" and said that the only money BGE was to get out of the transaction was the B and C payments, the financial reality being that those payments were BGE's share of the value of BMBF's capital allowances channelled to BGE via BB, Barclays (IOM) and Deepstream under the system devised by BZW.

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([1]) Page 480 *ante*.

19. The Judge (in para 51) expressed the view that as regards finance leasing the underlying purpose of Parliament is "to enable capital allowances to be used so as to provide to lessees at attractive rates finance for them to use and to develop their real business activities". A

20. The Judge (in para 56) considered whether the words of s 24, "has incurred capital expenditure on the provision of machinery or plant", embodied a commercial or a legal concept. He said that they plainly embodied a commercial concept, incurring expenditure on the provision of something not being legal terminology. He said (in para 58): B

> "the expenditure was really incurred on the creation or provision of a complex network of agreements under which, in an almost entirely secured way, money flows would take place annually over the next 32 or so years so as to recoup to BMBF its outlay of £91 million plus a profit . . . I consider that it was the money flows which mattered, and it was on the rights to the money flows that, as a commercial matter, BMBF really expended the £91 million on which it had borrowed". C

D

The Judge accepted (in para 60) that finance lessors always wish to limit the credit risk to which they are exposed, but he said that there can be cases where the credit risk is so comprehensively eliminated that it becomes apparent that the lessor has not really laid out its money on a leasing transaction at all. He said (in para 61) that the structure would have worked whatever the purchase price and that it could be argued that the Pipeline was surplus to the requirements of the scheme, analogous to an unnecessary fifth wheel on the coach. E

21. The Judge then considered an argument for the Revenue that BMBF did not incur any expenditure at all but, in the absence of a finding by the Special Commissioners accepting or rejecting that argument, he was not prepared positively to conclude that BMBF did not incur the expenditure. However, he did accept a further argument for the Revenue that even if BMBF did incur expenditure on the provision of the Pipeline, it did not do that wholly and exclusively for the purposes of its trade. After considering the distinction drawn in *Lupton* v. *FA & AB Ltd.* (1971) 47 TC 580; [1968] 1 WLR 1401 by Megarry J. between (1) transactions which have fiscal elements in them but which are nevertheless trading transactions and (2) transactions where the fiscal elements are present to such an extent that the transactions are not trading transactions at all, the Judge held that the transaction in the present case fell into the latter category. The Judge said (in para 73): F G

> "The transaction was really about creating a complex and sophisticated structure which enabled BGE every year to receive payments representing its share of the tax savings (or group relief payments) received by BMBF from the capital allowances. The underlying thinking was, as it seems to me, that BGE had the pipeline, which was a big item of machinery or plant and thus a potential subject matter for a big claim for capital allowances, and that BMBF had an established status and know-how as a finance lessor. The two items would be utilised in combination within the structure devised by BZW, with the real end product being, not the provision of finance at rates which were both profitable to the provider (BMBF) and attractive to the recipient (BGE), but fiscal savings to be shared between the two of them and to be provided at the expense of the UK Revenue." H I

A **The rival arguments**

22. On this appeal Mr. Aaronson does not dispute that there was a composite scheme including not only the sale and leaseback but also the security arrangements. But he submits that the Judge erred in concluding that BMBF did not incur expenditure on the provision of the Pipeline for four principal reasons:

B (1) the *Ramsay* approach does not permit the re-characterisation of BMBF's expenditure on the acquisition of the Pipeline as "expenditure on the provision of a complex network of agreements";

(2) the concept of incurring expenditure on the provision of machinery or plant as it is found in s 24 is not a commercial but a legal concept;

C (3) it is not an essential feature of finance leasing either that the vendor of the asset to be leased back should be able to "get its hands on" the sale proceeds immediately or that the lessor should be exposed to some (unspecified) degree of credit risk;

(4) it was not the underlying purpose of Parliament in enacting s 24 "to enable capital allowances to be used so as to provide to lessees at attractive D rates finance for them to use and to develop their real business activities".

23. Mr. Aaronson further submits that the Judge erred in concluding that BMBF did not incur the expenditure in question wholly and exclusively for the purposes of its trade.

E 24. By a Respondent's Notice the Revenue repeats the submission that BMBF did not incur expenditure at all by reason of the circular and self-cancelling movement of money.

25. Mr. Goy supports the reasoning and conclusion of the Judge. His submissions were as follows:

F (1) on the assumption that BMBF incurred expenditure, it did not do so on the provision of machinery or plant;

(2) if it did, it did not do so wholly and exclusively for the purposes of its trade;

(3) it did not incur expenditure at all.

G 26. All three submissions depend on the correctness of the Special Commissioners' view of the transaction as having "no commercial reality", the purpose of the expenditure by BMBF being not the acquisition of the Pipeline but the obtaining of capital allowances resulting ultimately in a profit to BGE and fees payable to BMBF and BZW. That view was in turn largely dependent on its conclusion that, because BGE could not get its hands on the purchase H price, the only benefits which BGE obtained from the arrangements were the B and C payments and that those payments were financed by the capital allowances. These views and conclusions were accepted uncritically by the Judge.

27. However Mr. Aaronson challenged the correctness of those findings in the light of the evidence before the Special Commissioners. I return therefore to I the Special Commissioners' decision. The Special Commissioners had in addition to the Agreed Statement of Facts a large number of documents and the

evidence, written and oral, of three witnesses called by BMBF. The first was Christopher Boobyer. He was the director of BMBF primarily responsible for the transaction and has vast experience in what is known as big ticket leasing, that is to say leasing (generally finance leasing) arrangements made direct with customers for individual asset values above £20 million. Among his many distinctions he has since 1998 been chairman of the Inland Revenue Panel, a joint Finance Leasing Association and Inland Revenue forum set up to discuss national issues affecting tax, accounting and regulatory policy in the leasing field with senior Treasury and Inland Revenue officials, and is the editor and co-author of *Leasing Finance*, now in its third edition. The second was Patrick Perry who from 1991 until his retirement in 2000 was Group Treasurer of the Barclays group. The third was Donald Wilson who after working for 42 years for British Gas became a director of BGE (UK) shortly after its incorporation. Apart from recording the fact that the three witnesses provided evidence the Special Commissioners make only brief references to their evidence.

28. First, they said that from Mr. Boobyer's evidence it was apparent that BMBF was aware that there were to be security arrangements for the lease and transportation agreements and that there was to be a cash collateral equivalent to the price paid for the Pipeline. Second, they accepted his written evidence that a corporate certificate issued by BGE was never sent to BMBF. Third, they referred to his evidence that Sudanor was formed so that the put option could be granted to BMBF if it wished to exit the Headlease. Fourth, Mr. Boobyer's description in his witness statement of finance leasing is quoted, *viz.*

> "The basic premise of the finance leasing industry is that lessors pass on the value of the capital allowances available to them in respect of the asset being financed to the customers. The customer gets the use of the asset concerned and pays rent at a rate which reflects the margin required by the Bank and the reduced funding cost to the Bank of providing lease finance as a result of the tax deferral benefit available."

29. The Special Commissioners make no reference to other material parts of Mr. Boobyer's evidence. He made clear that what he meant by finance leasing was a form of asset financing whereby asset-owning companies enter into a sale and leaseback transaction with a purchaser/lessor and indirectly benefit from the capital allowances available, which are passed on by the lessor in lower rentals and the lessor recoups the cost of acquisition and obtains a profit margin through those rentals, taking security by acquiring title to the asset. In his oral evidence Mr. Boobyer was adamant that this was a standard commercial finance leasing transaction for BMBF, negotiated at arm's length first with BB from which BMBF borrowed the purchase price, second with BZW which put the scheme together, and third with BGE which insisted on the transaction being a fixed rate transaction from the start. He explained that the profit which BMBF derived from the deal was calculated by giving it a net after tax margin of 0.8965 per cent. applied to the day-to-day balance of the capital outstanding, those being the same terms as had been negotiated between BGE and Abbey National. As Mr. Boobyer put it, "we literally stepped into their shoes". In cross-examination it was put to him that BMBF entered into documents that would effectively ensure that the purchase price went straight into the deposit account. He replied: "No we did not. BMBF paid the acquisition price to BGE. What BGE did with it did not have involvement or concern with BMBF." Although pressed by Mr. Goy

A that a provision in each acquisition agreement for the purchase price to go into a specified account was to facilitate the taking of security, Mr. Boobyer said he could not accept that: it was on BGE's instructions that BMBF was to make payment into the account that BGE specified; for the vendor to specify an account to receive payment was a standard provision. He reaffirmed that this transaction was an ordinary, straightforward, commercial leasing transaction B and denied a suggestion by Mr. Goy that it was somewhat unusual.

30. Mr. Perry's evidence is only referred to in one respect by the Special Commissioners and that is only for his oral evidence that on a loan on a cash secured basis where the security covers the whole of the loan, such a borrower C "has not got any more money at the end than he had at the beginning". The Special Commissioners do not record that that was said in answer to the question whether, on the hypothesis that the loan is made on terms that the lender requires the borrower to deposit the money lent and that the deposit must be used to repay the loan, any *additional* funds had been made available to the borrower. They also do not refer to his evidence that the fact that the loan from BB to BMBF D contained interest and principal payment terms matching the rents payable under the leasing arrangements with BGE was entirely normal for a finance lease transaction, that cash secured lending was by no means unknown, nor that as Group Treasurer he did not see BMBF, Barclays (IOM), Deepstream and BZW as all part of the same operation, the responsibility of the directors of each company being confined to that company. The Special Commissioners do not refer to the explanation given by Mr. Perry of the regulatory requirements E imposed on banks whereby banks have to maintain minimum levels of capital depending on the risk weighting of transactions which they undertook, those requirements causing banks to try to negotiate security in the form which will best improve the weighting position of each transaction. The relevance of that is, of course, that BB's insistence on BGE providing a cash collateral which would result in the transaction in question being zero-rated, so far from being a matter F to excite suspicion, was driven by normal banking considerations.

31. Mr. Wilson's evidence is not referred to at all. The Special Commissioners say of BGE (UK) that it is a £100 company with a board consisting of three directors but apparently only one other employee, most of its G operations being carried out by means of contracts with independent contractors. The Special Commissioners appear to have overlooked Mr. Wilson's written evidence that BGE (UK)'s capital was £400,000 and that it had a board of five directors. Insofar as the Special Commissioners are suggesting that this was an insubstantial company with no purpose other than as part of a structure to ensure the availability of capital allowances (as Mr. Goy H had put to Mr. Wilson), they ignore Mr. Wilson's written evidence that in addition to being the sublessee of the Pipeline it owned other parts of the Interconnector and had assets well in excess of £30 million under construction, and his oral evidence flatly denying that its only purpose was as part of the structure to obtain capital allowances. Further his oral evidence was that the intention and expectation were that the Interconnector would be a profitable I operation with pre-tax profits ultimately of £40 million per annum and that BGE (UK) would very soon be a profitable company.

32. In the light of that evidence from apparently impeccable witnesses whose evidence is not said by the Special Commissioners to be disbelieved, it is not apparent to me on what evidence the findings to which I have referred in para 26 above are based. They appear to be an acceptance of the Revenue's assertions that the B and C payments represent the benefit of the capital allowances, that this was no ordinary finance lease transaction and served no commercial purpose, and that it was aimed only at obtaining capital allowances which would result in a profit to BGE and fees payable to BMBF and BZW. That the capital allowances were taken by BGE in the form of the B and C payments does not appear from any document. On the contrary, as is apparent from the BZW document referred to in para 11(5) above it was recognised that the cash deposit required by BB as security for its guarantee would produce a benefit for BGE over and above the covering of the rental payments. That benefit is not linked to the capital allowances. Further the Special Commissioners' conclusion runs counter to Mr. Boobyer's insistence that this was an ordinary finance leasing transaction and that in finance leasing the benefit of the capital allowance obtained by the lessor is passed on to the lessee in the form of lower rentals. Yet if the Special Commissioners are right, they were not passed on in that form but were taken out of the deposit with Deepstream in the form of the B and C payments. Of course it was open to the Special Commissioners to reject the evidence of a witness, but they would have been bound to explain why they did so. I can see no basis on which they could properly have rejected the evidence of Mr. Boobyer, given the extent of his experience in the field of lease financing.

33. Further, Mr. Aaronson was able to demonstrate that of the £91,534,000 deposited with Deepstream by BGE only £82,468,000 needed to be invested (at the rate implicit in the Deepstream deposit of 9.641 per cent.) to fund the rental stream (at the implicit interest rate of 8.6 per cent.), and that the balance of £9,066,000 could be invested at 9.641 per cent. to provide a return over and above that required to cover the interest payments. That return would account for the B and C payments. The A payments total £402,042,725, the B payments £11,708,600 and the C payments £917,548. Unfortunately no evidence was given to the Special Commissioners in respect of the figures Mr. Aaronson now gives. Mr. Goy however, very fairly, accepts as mathematically accurate that the purchase price received by BGE was greater than the sum which it would need to invest in order to fund the payment of the rental stream. It would be astonishing if a major Irish corporation with its own advisers would not exploit the deposit, which it had to make to obtain BB's guarantee of the rental payments, as far as it could for its own benefit. There is no inconsistency, in my opinion, between the view that the benefit of the capital allowances would be passed on to the lessee in the form of lower rentals in the ordinary way and the BGE memorandum of 14 December 1993 referring to the "effective saving" as £12.6 million over the life of the lease and "the net present value of the benefits" as £8.1 million. Nowhere in the memorandum are that saving and those benefits to BGE equated with the capital allowances intended to be obtained and indirectly passed to BGE (UK).

34. This is not a case where the Special Commissioners were choosing between conflicting evidence. The Revenue produced no evidence. Despite the great respect which it is appropriate to accord to a specialist and experienced

A tribunal, particularly when its findings are adopted by a judge as knowledgeable as Park J., I have reached the clear view that the Special Commissioners could not properly conclude on the evidence before them that the B and C payments "would be financed entirely by UK taxpayers by means of the hoped-for capital allowances." That is simply not substantiated by any written or oral evidence.

B

35. Further I cannot accept that the only benefits which BGE obtained were the B and C payments. BGE sold the Pipeline for £91,292,000. It received that sum, but for its own commercial purposes it agreed to deposit it on the terms of the Deposit Agreement. Effectively it thereby purchased three annuities corresponding to the A, B and C payments, the A payments matching C obligations arising annually under the Headlease. Implicit in those payments is the fact that interest will have been earned on the deposit. It seems to me quite unrealistic to say that BGE received no benefit from its entitlement to the A payments. True it is that they were earmarked to be passed to BMBF, but that was in discharge of obligations incurred by BGE to BMBF for the purposes of BGE's business. Nor is it realistic to say that BGE never enjoyed the sales D proceeds: they were invested in the deposit with Deepstream.

36. As for the commercial reality of the transaction, whether the sale and leaseback transaction or that transaction with the security arrangements, I have found it very difficult to understand what was thought by the Special Commissioners and the Judge not to be commercial about it. I say that, whether E it is viewed as a composite whole or step by step. It is hardly surprising that in relation to a transaction involving such large sums of money and intended to be in operation for a very long period, all the parties would want to make provision to reduce the risks of the obligations they were respectively undertaking as far as possible. But it should be borne in mind that this was not an entirely risk-free transaction for either BMBF or BGE. BMBF, in order to secure its 0.8965 per F cent. profit via the rental payments, was agreeing to invest a very substantial sum, well in excess of the minimum for big ticket leasing, on acquiring a new unproved pipeline which it was to let on an unusually long lease to a non-UK corporation owned by a foreign state, the rents under the lease in effect to be paid by a new company starting up. Whilst BMBF was protected against any risk arising from changes in tax rates or capital allowances, not surprisingly it sought to ensure G that it would receive the covenanted rental payments which would give it its profit, but it had no security other than the Pipeline for the "strip risk" estimated at £25 million, being the difference between the maximum sum payable by BMBF on termination and the amount of the guarantee by BB. BGE, to achieve its saving with a present value of £8.1 million, was conscious that it too was exposed to risks. They would arise if capital allowances were refused or reduced, and if H tax rates changed. Nevertheless it chose to go ahead with the transaction on the terms negotiated not with a company in the Barclays group but with Abbey National, into whose shoes BMBF stepped. The other participants in the scheme devised by BZW, *viz*. BB, Deepstream and Barclays (IOM), all did so on ordinary commercial terms. To my mind the commerciality of the transaction is plain. I respectfully disagree with the contrary inferences of the Special I Commissioners and the Judge on this point: they seem to me to be based on an incorrect appreciation of the facts.

Conclusions A

37. I now come to the statutory provisions. The purpose of the capital allowances legislation would appear to be to encourage the expenditure of capital on plant and machinery. The fact that the trader incurring the expenditure would not himself use the plant or machinery but would lease it and B pass on the benefit of the capital allowances to the lessee was not seen to be any reason for not conferring capital allowances on that trader who had incurred the expenditure. I can see nothing in the legislation which substantiates the Judge's view that s 24 was enacted so that capital allowances could be used to provide lessees with finance at attractive rates to use and to develop their real business activities. Section 24 focuses on the incurring of expenditure by the trader on the C provision of plant or machinery wholly and exclusively for the purposes of his trade. It therefore requires one to look only at what the taxpayer did. To the test posed in s 24 it is immaterial how the trader acquires the funds to incur the expenditure or what the vendor of the provided plant or machinery does with the consideration received. Provided that the expenditure is incurred on the provision of plant or machinery and is so incurred wholly and exclusively for the D purposes of the trader's trade, subject to s 75(1) it is irrelevant to the operation of s 24(1) whether or not the trader's object is or includes the obtaining of capital allowances. The express reference in s 75(1)(c) to the disallowance of a first-year allowance where the sole or main benefit that might have been expected to accrue was the obtaining of an allowance suggests that save in a case to which that E provision applies, the expectation of, or the intention to obtain, such benefit is not a reason for denying the capital allowances.

38. Further in *Barclays Mercantile Industrial Finance Ltd.* v. *Melluish* (1990) 63 TC 95; [1990] STC 314 Vinelott J. said, in respect of a film finance lease, that what became s 75(1)(c) was not satisfied even though the lessor could not F offer a lease back at an acceptable rent unless it could obtain a capital allowance; that was because the lessor's main object and purpose in that case was to make a profit on a purchase and lease of the film. Vinelott J. said at [1990] STC 314 p 343 that the provision was aimed at artificial transactions designed wholly or primarily at creating a tax allowance. He gave as an instance of an artificial G transaction the case of a company purchasing machinery or plant which is used for a brief period and then sold. In the present case on Mr. Boobyer's evidence BMBF's sole purpose was to enter into the sale and leaseback to obtain the net 0.8965 per cent. profit, which Abbey National had negotiated and which it would obtain regardless of any changes to capital allowances, as part of its ordinary finance leasing trade, and there was no artificial transaction designed to create a H tax allowance. I do not accept that the Pipeline was some sort of unnecessary fifth wheel to the transaction coach. Of course the scheme for a finance leasing transaction with security arrangements can be adapted to any plant or machinery of any value, but the asset is of essential importance, providing as it does security to the purchaser/lessor as Mr. Boobyer said. If capital allowances are to be obtained in full for the expenditure on the provision of the asset, that expenditure I must not exceed the value of the asset.

39. The Special Commissioners and Park J. appeared to think that the inability of BGE to "get its hands on the money" showed that there was no expenditure on the provision of the Pipeline. Park J. further considered that the

A provision of "up front" finance to the lessee in the terms which I have described in para 13 above was an essential feature of the requirements of s 24(1) and that there must be some degree of credit risk to the lessor. I cannot accept any of these glosses on the simple statutory language. The Revenue accepts that in a sale and leaseback transaction where the vendor sells the plant or machinery to a lessor like BMBF on the basis that the proceeds will be applied in extinguishing a debt B to the lessor, capital allowances are available. In such a case the vendor can never get his hands on the money. Such a transaction does not produce any "up front" money in any normal sense. I cannot see how what the vendor does with the purchase moneys can affect the availability of the allowances when s 24 is directed only at the actions of the incurrer of the expenditure.

C 40. The Revenue's chief point appears to be that because the £91,292,000 went round in a circle, the *Ramsay* approach applies. Mr. Goy placed particular reliance on the *Ensign* case in this context. That case involved a complex tax avoidance scheme aimed at providing to English investors forming a limited partnership, VP, an entitlement to capital allowances for expenditure of $14 million on a film although the partners were never liable to spend more than D $3,250,000 of their own money. An essential part of the scheme was what purported to be two loans of $9,750,000 and $1 million borrowed by the film producer, LPI, from its bank and passed to the partnership by way of non-recourse loans. They were purportedly applied immediately by VP as expenditure on the film by repayment into LPI's bank account, leaving no balance outstanding at the end of the day's trading. The loans were repayable to E LPI by payment out of the net profits of the film under arrangements which the House of Lords found to be inconsistent with the concept of a commercial loan, involving repayment out of profits from the film. Lord Templeman said that the expenditure of $10,750,000 was really to be found to have been incurred by LPI ([1992] 1 AC 655 at p 674C) and VP neither borrowed nor spent $10,750,000 (p 678D). In contrast VP's actual expenditure of $3,250,000 was real and not F magical and so qualified for the capital allowance (p 677F).

41. Lord Hoffmann in *MacNiven* ([2001] 2 WLR 377 at p 398; (2001) 73 TC 1 at p 75 para 68) said that for the purposes of some concepts in tax legislation the circularity of the cash flow and the fact that the transaction took place entirely for tax purposes would stamp the transaction as something different G from that contemplated by the legislature. But he does not say that the circularity of the movement of money would in itself be enough. I do not accept that the circulation of money in the present case means that the transaction is to be treated like the scheme in *Ensign*. In our case there is nothing comparable with the artificial self-cancelling payments found in that case. There is no non-recourse or other uncommercial loan nor any immediate payment back to the H same purported lender. Each step taken was properly commercial and on arm's length terms. On a true construction of the documents and on a proper analysis of the facts as urged by Lord Templeman to be the task of the Courts (see [1992] 1 AC 655 at p 611B) there was a real expenditure by BMBF on the acquisition of the Pipeline, and it is irrelevant to the application of s 24 that the purchase money originated in a borrowing from BB out of BB's Treasury and that it ended up I back in BB's Treasury after passing through the hands of BMBF, BGE, Deepstream and Barclays (IOM).

42. Mr. Goy suggested that there were four clear indications of artificiality in the arrangements. Two of them, BGE's inability to get its hands on the money and BGE's benefits being limited to the B and C payments, I have already discussed. The third indication was said to be the unusual Deepstream deposit, providing as it did that the deposit could not be terminated for 31 years. The fourth was said to be the fact that the purchase price of the Pipeline was not based on a valuation but was the expenditure by BGE on the Pipeline less the EU grant. Mr. Goy also posed the question: why did not BGE deposit the cash collateral directly with BB?

43. Whether or not the Deepstream deposit was unusual was not explored in any evidence. There is no indication anywhere in the evidence that the terms of the deposit were not commercial; the bargain was struck between two arm's length companies, BGE and Deepstream. As for the purchase price of the Pipeline, Mr. Boobyer did accept in cross-examination that the EU grant was deducted from the expenditure so as to be sure of BMBF getting the capital allowances, but it was not suggested to Mr. Boobyer that the resultant price was not a price which two arm's length companies, BGE and BMBF, could properly arrive at in a sale and leaseback transaction of an asset as difficult to value as the Pipeline. There is no evidence as to why BGE itself did not deposit the cash with BB; BMBF does not know. But Mr. Aaronson was able to draw our attention to two commercial reasons (one relating to the uncertainties created by the much debated views expressed by Millett J. in *Re Charge Card Services* [1987] Ch 150, and the other arising out of the Irish insolvency rules known as the Examinership Procedure which might have affected the zero-weighting of the BB guarantee) which might have operated on the minds of those taking the decision whether BGE should make a direct deposit with BB. He further referred to *Charge Card* and to doubts about the applicability of the exemption under s 349(3) Income and Corporation Taxes Act 1988 from deducting tax from payments of yearly interest as constituting commercial constraints militating against Deepstream making a deposit directly with BB in London. It is not profitable to speculate on those matters. It is sufficient to say that I am not persuaded that any of the points relied on by Mr. Goy establishes artificiality in the arrangements.

44. On the view I have reached on the facts and s 24 it is hard to see any scope for the application of the *Ramsay* approach. But if in accordance with Lord Hoffmann's guidance in *MacNiven* it is necessary to determine whether the concept of incurring expenditure on the provision of an asset is legal or commercial, I would hold that it was legal by analogy with the concept of "payment" which in *MacNiven* was held to be a legal concept. I do not doubt that it is due to my own failings that I find Lord Hoffmann's dichotomy of concepts a difficult one to apply. The touchstone appears to be whether the commercial man would say of a statutory expression "You had better ask a lawyer" (see [2001] 2 WLR 377 at p 395; (2001) 73 TC 1 at p 72 para 58). It is far from obvious to me that the commercial man, knowing anything of the dozens of cases in which the distinction between capital and income has been explored, would say that those concepts are commercial; whether a transaction is of an income or capital nature is normally treated as a question of law (see *Beauchamp* v. *F W Woolworth plc* [1990] AC 478 at p 491A *per* Lord Templeman). Yet income and capital are described by Lord Hoffmann as business concepts ([2001] 2 WLR 377 at p 396 para 60.) On any view, as it seems to me, the fundamental question is the true construction of the statutory provisions, and the application of the

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A meaning so ascertained to the facts. I take refuge in the fact that the expression "incurring expenditure" archetypally would include a payment. In my judgment, just as in *MacNiven* it was immaterial to the meaning of "payment" that the company borrowed money from its shareholder to whom it promptly paid the borrowed money, so in the context of s 24 it is irrelevant to the meaning of "incurred . . . expenditure" that the money used in the expenditure was borrowed B by BMBF from BB out of the Treasury and was used by BGE in a way which eventually brought it back to the Treasury from Barclays (IOM). On that footing, the *Ramsay* approach does not apply.

45. If that is wrong and the relevant concept is a commercial concept, then in accordance with *MacNiven* one must identify the legal nature of the transaction, stripping out artificially inserted steps. Looking at the pre-ordained C events of 31 December 1993 as a composite whole I would regard the legal nature of the transaction as a sale by BGE of the Pipeline to BMBF, the lease of it back to BGE and thence, by the Sublease, to BGE (UK), and the giving by BGE of security to BB for BB's guarantee to BMBF of the fixed rental payments. What is the artificially inserted step which has no business purpose apart from the avoidance of tax? Mr. Goy's answer was the payment by BMBF to BGE. For the D reasons already given, I cannot accept that. There was a plain business purpose for that step, *viz.* the acquisition of the Pipeline so that it could be leased back to provide the rental stream and thereby to enable BMBF to earn the profit which it invariably seeks, and which Abbey National intended to obtain, on such a finance leasing transaction and to provide BMBF with security. The fact that BMBF intended to obtain capital allowances which it would pass on to the lessee E and thence to BGE (UK) does not, in my judgment, detract from the genuineness of that business purpose.

46. In my judgment, the incurring by BMBF of the expenditure was wholly and exclusively for the purposes of its trade of providing asset-based finance. With respect to the Judge, in the light of the evidence, and in particular that of F Mr. Boobyer, I can see no basis for re-characterising the transaction in the way the Judge did. It seems plain to me that BMBF incurred expenditure on the provision of the Pipeline by a transaction which, despite having a fiscal element in it, in that capital allowances were to be obtained and passed on to the lessee in the form of lower rentals, was a genuine trading transaction. I would hold that the facts of the present case are far removed from the artificial structure employed in a dividend-stripping scheme such as that used in the *Lupton* case.

G

47. For the reasons already given, I would reject Mr. Goy's third submission that there was no expenditure at all by BMBF. In the present case the circular movement of money and the intention of BMBF to obtain and pass on capital allowances do not stamp the transaction as something different from that contemplated by Parliament as giving rise to an entitlement to capital allowances H under s 24. That circularity, which arose through BB insisting on security in the form of a cash collateral being provided by BGE, was not of direct concern to, still less under the control of, BMBF and is irrelevant to the fact that expenditure was incurred through BMBF paying BGE for the Pipeline. Parliament has provided for capital allowances to be available on a purchase of plant or machinery, even though the plant or machinery is then leased, and, as I Mr. Boobyer said in his witness statement, the Revenue has long been aware of the practice of finance lessors utilising capital allowances through passing them

on to lessees in the form of lower rentals. That cannot affect the fact that there was expenditure by BMBF. A

48. For these reasons I would allow this appeal and set aside the order of the Judge and the decision of the Special Commissioners.

B

Rix L.J.:—

49. I agree.

C

Carnwath L.J.:—

50. I also agree. I add my own comments in deference to the contrary views of the experienced Commissioners, and of the Judge, whose practical knowledge of this field is second to none.

D

51. The issue in the present case can be shortly stated. BMBF, whose trade was that of providing asset-based finance, entered into a transaction which, viewed on its own, would have attracted capital allowances (I shall refer to it as "the BMBF transaction"). It comprised the acquisition of a pipeline for £91 million from BGE, its lease-back to BGE, and a sub-lease from BGE to BGE (UK). It is common ground that, if one stops there, capital allowances can be claimed. The Revenue's argument, which succeeded below, is that the BMBF transaction should not be seen in isolation, but should be seen as part of a wider scheme ("the BZW scheme"), effected solely to gain a tax advantage; and that, if it is looked at in that light, then for fiscal purposes nothing happened. There was no expenditure, no provision of an asset, and no trade. This is said to be the effect of applying the "*Ramsay* principle", as interpreted in subsequent cases most particularly *MacNiven.* E F

52. In my view, there are two main difficulties with this approach. The first is that the tax advantage, which is said to have infected the whole scheme, is one which is a normal and accepted part of BMBF's finance leasing trade. As the Judge recognised, in this trade: G

> ". . . the obtaining of capital allowances for the leasing company's expenditure on acquiring the machinery or plant is fundamental. The lease rates are set at levels which assume that the lessor (or companies grouped with it) will benefit from the allowances. If the allowances are not obtained after all, the transaction ceases to make financial and commercial sense." (para 7 [1]) H

In other words, the availability of capital allowances provides the "bed-rock" of the trade (to use Mr. Goy's term, accepted in cross-examination by Mr. Boobyer). I

53. Furthermore, the entitlement to capital allowances is not confined to investments in what one might call investment in *new* plant. As the Judge also

(1) Page 471 *ante*.

A recognised, finance-leases are commonly used to restructure the financing arrangements on existing plant. He mentioned, as "a common kind of finance leasing", the case where:

> "the lessee already has the asset . . . but has paid for it with borrowed money on which it is paying full commercial rates of interest; it sells the asset to the leasing company and takes a finance lease-back at more favourable
B rates; it uses the purchase price to repay its borrowings" (para 49) ([1])

Mr. Goy accepted that this was a typical form of finance lease, which would attract capital allowances; and that it would do so, even if the "more favourable rates" were attributable to nothing other than the availability of capital allowances.

C

54. On that analysis, which is not disputed, the mere fact that the essential purpose of the arrangement was to obtain a tax advantage in the form of capital allowances, cannot, under this statutory scheme, be a ground of objection. The Judge distinguished the examples of typical finance leases, on the basis that—

> "in all of these cases the finance lessor provides 'up-front' finance to the
D lessee, and the finance so provided is used in one way or another in the lessee's business. But in the transaction involved in the present case, no up-front finance was provided."

However, there is nothing in the statute to suggest that "up-front finance" for the lessee is an essential feature of the right to allowances. The test is based
E on the purpose of the lessor's expenditure, not the benefit of the finance to the lessee. Nor, as the Judge recognised, should it make any difference whether the arrangements by which the tax advantage was achieved were simple or, as the Commissioners thought in this case, "complicated and convoluted."

55. The other main difficulty with the Revenue's argument is that it treats
F as irrelevant the viewpoint of the taxpayer, in this case BMBF, although it is that to which the section directs attention. The Commissioners took the same view. They said that it was necessary to look "at the whole of the transaction; all the documents, acts and events of 31 December 1993 and not merely what BMBF did"; the Judge agreed (para 53). The justification given by the Commissioners for this approach was, not anything in the evidence before them, but reference to
G another case, *Overseas Containers (Finance) Ltd.* v. *Stoker* (1989) 61 TC 473; [1989] 1 WLR 606. However, in that case, it is clear that attention was paid to the group as a whole, because on the facts that was the true analysis of the position; the taxpayer company was inserted purely for the purposes of the scheme and had no separate trading life.

H 56. In this case, BMBF was an established trading company. It gave apparently credible evidence that it had a distinct business purpose for this transaction, which was seen as identical in kind to its normal finance leases, and that it was not concerned with the details of the BZW scheme. Both the Commissioners and the Judge seemed to have ignored that evidence. In my view, on the basis of the evidence we have been shown, there were no reasonable

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([1]) Page 487 *ante*.

grounds for treating the "purpose" of the BMBF transaction as other than a true trading purpose of BMBF itself.

57. Against that background, the section leaves very little room for application of the *Ramsay* principle. The Judge thought that the pipeline transaction could be disregarded as simply "the fifth wheel of the coach". I find that difficult to follow, even if one looks at the BZW scheme as a whole. One cannot ignore the reality of the pipeline, nor can one ignore the fact that ownership was transferred to BMBF, with whom it remains, and that leases were granted to BGE and BGE (UK). On any view, those are real transactions with lasting consequences in the real world.

58. There might be more room for argument as to whether there was "expenditure", given the apparent circularity of the payments. However, once one accepts the transfer of ownership, it is difficult to question the reality of the expenditure by which the purchase price was discharged. Furthermore, BMBF gave evidence that it financed the purchase price in the normal way by a loan from its parent Bank, in accordance with its standard drawing facility, and that it was not concerned with the security arrangements made by the Bank. There is no indication that this evidence was disbelieved.

59. In any event, there seems to me a close analogy with the issue, which was decided by the House of Lords in *MacNiven*. The ratio was that, for the purposes of s 338 of the Taxes Act, there had been "payment" of yearly interest, in the ordinary meaning of that term, and that the *Ramsay* principle could not alter that simple fact. This was explained succinctly by Lord Nicholls ([2001] 2 WLR 377; (2001) 73 TC 1, at para 15):

> "In the ordinary case the source from which a debtor obtains the money he uses in paying his debt is immaterial for the purposes of s 338. It matters not whether the debtor used cash in hand, sold assets to raise the money, or borrowed money for the purpose. Does it make a difference when the payment is made with money borrowed for the purpose from the very person to whom the arrears of interest are owed? In principle I think not. Leaving aside sham transactions, a debt may be discharged and replaced with another even when the only persons are the debtor and the creditor. Once that is accepted, as I think it must be, I do not see it can matter that there is no business purpose other than gaining a tax advantage. The genuine discharge of a genuine debt cannot cease to qualify as payment for the purpose of s 338 by reason only that it was made solely to secure a tax advantage. There is nothing in the language or context of s 338 to suggest that the purpose for which a payment of interest is made is material."

Similarly, under the BMBF transaction, BMBF obtained ownership of a pipeline and incurred an obligation to pay for it. That obligation was discharged by the expenditure of the £91 million. There is nothing in the section to suggest that it matters what is the source of the £91 million, or alternatively what is to be done with the £91 million by the recipient, once the obligation has been discharged.

60. Those considerations are in my view sufficient to dispose of the appeal in favour of the taxpayer. However, I should add some comments on the

A submissions of the Revenue on the *Ramsay* principle, in the light of the speeches in *MacNiven*. Implicit in those submissions seemed to be a view that, once one has categorised a statutory concept as "commercial" in the sense used by Lord Hoffmann, then it is possible and appropriate to undertake a free-ranging inquiry into the "commerciality" of the particular scheme, unconstrained by the limitations set in previous cases. For the reasons I shall outline, I do not believe B that to be so.

61. It is striking that some 20 years after *Ramsay*, and even with the assistance of at least five major House of Lords decisions explaining or reinterpreting *Ramsay*, there should be such a wide divergence of views as to the nature of the principle. The arguments in this case were "ships that pass in the C night" (Mr. Aaronson's words) or "chalk and cheese" (Mr. Goy's words). To understand why that should be so, it is helpful to look at the development of the principle in the earlier cases in the House of Lords, before considering whether there is anything in the two most recent (*McGuckian* and *MacNiven*) which changes the position.

62. *Ramsay*, of course, represented a breakthrough, but the facts were D extreme. In the memorable description of Templeman L.J. in the Court of Appeal ([1979] 3 All ER 213, p 214; (1981) 54 TC 101 at p 128, it was—

> "Yet another circular game in which the taxpayer and a few hired performers act out a play; nothing happens save that the Houdini taxpayer appears to escape from the manacles of tax."

E

That was an "off-the-peg" scheme. *Burmah* showed that the same approach could be applied to a bespoke version, carefully crafted by respectable professional advisors. *Furniss* v. *Dawson* [1984] AC 474; (1984) 55 TC 324 represented both the consolidation of the principle and a significant extension. The speech of Lord Brightman, with which all the other members of the House agreed, reads as though intended to be a definitive statement of the essential F criteria and limits of the principle, and it has been so regarded in all the subsequent cases, at least until *McGuckian*.

63. Thus, in *Craven* v. *White* [1989] AC 398, at p 500 Lord Oliver (giving the majority speech) asked—"are those criteria definitive as they appear to have been intended by Lord Brightman to be . . .?" to which question he arrived (after G fourteen pages of painstaking analysis) to an affirmative answer (see p 514 F-H). His analysis made clear that Lord Brightman's formulation of the principle represented a significant advance on *Ramsay*. Lord Oliver's view is of particular interest, coming from one who was as he said "a reluctant convert" (cf his judgment in the Court of Appeal in *Furniss* itself (reported in [1984] AC 474 at p 477). He said (*Craven* v. *White* [1989] AC 398 at p 501E; (1988) 62 TC 1 at H p 191):—

> "The *Ramsay* principle is simply that you look at the result which the parties actually intended to and did produce and apply to it the ordinary fiscal consequences which flow from that result. *Furniss* involved going a considerable step further than this and, by reconstituting the actual constituent transactions into something that they were not in fact, I attributed to the parties an intended result which they did not in fact intend. To that unintended result there are then attached the fiscal consequences

which would have flowed if the transaction had actually taken the form into which it is deemed to be reconstituted." A

64. His subsequent analysis made clear that the critical factors which enabled the Courts to make this breakthrough were two matters: first, the inter-dependence of the transactions which enabled the Court to apply the analogy of a tri-partite contract (p 501H, 508C-G); and secondly the lack of commercial motive for the inserted steps: B

> ". . . the absence of any commercial motive underlines the artificiality of the inter-related transactions and entitles the Court to disregard them because they are not intended to produce anything other than an artificial fiscal result." ([1989] AC 398 at p 507C-D) C

Lord Oliver's analysis was endorsed by the majority of the House of Lords in *Fitzwilliam* v. *Inland Revenue Commissioners* [1993] 1 WLR 1189 (see p 1201, *per* Lord Keith).

D

65. As appears from the last passage, the principle is essentially one of fiscal statutory interpretation (even though it may be extended by analogy to other contexts—see e.g. *Gisbourne* v. *Burton* [1989] QB 390). The transactions are "reconstituted" for fiscal purposes but not for other purposes. It has been described as an application of ordinary principles of "broad purposive interpretation" to taxing statutes, by giving effect "to the purpose and spirit of the legislation" (see *per* Lord Steyn and Lord Cooke, in *McGuckian* [1997] STC 908, at pp 915, 910). However, it is difficult to see it as a pure rule of statutory interpretation, in the normal sense. The way in which the House of Lords got over the obvious conceptual hurdles in *Furniss* was, not by re-interpreting the statutory words, but by "reconstituting" the facts (to use Lord Oliver's term). E F

66. Thus, the "purposive" approach is applied, not just to the construction of the statute, but also to the characterisation of the facts. As Sir Anthony Mason NPJ said (in adopting the *Ramsay* principle in the Hong Kong Court of Final Appeal) it is "both a rule of statutory construction . . . and an approach to the analysis of the facts." (*Shiu Wing* v. *Commissioner of Estate Duty* [2000] HKFCA 64). As such, it can perhaps be justified as statutory interpretation in the broader sense. It recognises the underlying characteristic of all taxing statutes as parasitic in nature. They draw their life-blood from real world transactions with real world economic effects, to which the Revenue is not a party. To allow tax treatment to be governed by transactions which have no real world purpose of any kind is inconsistent with that fundamental characteristic. G H

67. The speeches in *McGuckian* [1997] STC 908 itself do not involve any departure from Lord Brightman's formulation of the rule. Lord Browne-Wilkinson thought the case "fell squarely" within Lord Brightman's statement of "the classic requirements for the application of (the *Ramsay*) principle" (p 912f); Lord Steyn quoted the same passage as summarising "the limits of the principle" (p 918 a-c); Lord Cooke also thought the case fell within the limitations stated by Lord Brightman (p 921a); Lord Lloyd agreed with all three speeches (p 914 h; he also agreed with Lord Clyde who made no express reference to *Furniss*). However, Lord Cooke added [1997] STC 908 at p 921 a-b; (1997) 69 TC 1 at p 85: I

A "The present case does fall within these limitations, but it may be as well to add that, if the ultimate question is always the true bearing of a particular taxing provision on a particular set of facts, the limitations cannot be universal. Always, one must go back to the discernible intent of the taxing act."

B He went on to suggest that "the journey's end may not yet have been found," a thought echoed by Lord Steyn ([1997] STC 908 at p 916g).

68. Against this background one returns to *MacNiven*. The ratio, as I have said, was that there had been "payment" of interest, and that the statutory context left no room for application of the *Ramsay* principle. Thus, the limits of C that principle did not arise directly for decision. The principal speeches in the House of Lords have already been referred to by Peter Gibson L.J., and it is unnecessary to repeat them. As he noted, Lord Hoffmann, with the agreement of the other members of the House, reviewed the cases since *Ramsay* itself, which he described as the "fountainhead". He described Lord Brightman's formulation in *Furniss* as

D "... a careful and accurate summary of the effect which the *Ramsay* construction of a statutory concept has upon the way the Courts will decide whether a transaction falls within that concept or not ...

It is a statement of the consequences of giving a commercial construction to a fiscal concept. Before one can apply Lord Brightman's words, it is first necessary to construe the statutory language and decide that E it refers to a concept which Parliament intended to be given a commercial meaning capable of transcending the juristic individuality of its component parts. But there are many terms in tax legislation which cannot be construed in this way. They refer to purely legal concepts which have no broader commercial meaning." ([2001] 2 WLR 377; (2001) 73 TC 1, paras 48-9)

F On this view, therefore, the first step is to decide whether the statutory concept is "legal" or "commercial", one guide being whether a commercial man, asked what it means, would say "you had better ask a lawyer" (para 58).

69. Like Peter Gibson L.J., and with similar respect to its source, I find some difficulty in understanding this dichotomy. It was a difficulty shared by G both leading counsel before us. Lord Hoffmann clearly regarded *McGuckian* and *Furniss*, as illustrations of "commercial" concepts, in the sense he used the term, and as therefore susceptible to *Ramsay* analysis. However, in each case, there seems a strong case for regarding the statutory concept as one of law, or certainly one on which a commercial man would look to a lawyer for advice.

H 70. In *McGuckian*, Lord Hoffmann thought the Crown's argument, based as it was on *Furniss*, had created "unnecessary difficulties", since it required an intervening assignment as part of the scheme to be disregarded, without which one could not explain how any money had been received by the assignor (para 53). In his view, the question in *McGuckian* was—

"... not whether the assignment should be disregarded but whether, I from a commercial point of view, it amounted to an exchange of income for capital." ([2001] 2 WLR 377; (2001) 73 TC 1 at para 54)

He considered that the payment had retained its "commercial" character as revenue, in spite of the scheme designed to turn it into capital. A

71. However, as has been pointed out by Peter Gibson L.J., the distinction between capital and revenue has been regarded, at least in recent House of Lords authority, as an issue of law. Certainly, it is not one which a commercial man would be likely to approach without the assistance of a lawyer. As Lord Cooke said in *McGuckian*: B

> ". . . the line can be notoriously difficult to draw, as the division is necessarily to some degree artificial, and has to be worked out pragmatically by courts, lawyers, and accountants." ([1997] STC 908 at p 918 j). C

72. *Furniss* also needed to be fitted into Lord Hoffmann's dichotomy. Since the *Ramsay* principle was clearly held to apply in that case, the statutory concept had to be treated as falling on the "commercial" side of the line. Lord Hoffmann saw it as an extension of *Ramsay*:

> "Thus while the question in *Ramsay* had been whether there was a disposal giving rise to a loss, the question in *Furniss* v. *Dawson* was whether the disposal had been to one person rather than another." ([2001] 2 WLR 377; (2001) 73 TC 1 at para 46). D

Again, this interpretation is not without difficulty. The facts of *Furniss* were summarised by Lord Hoffmann ([2001] 2 WLR 377; (2001) 73 TC 1 at para 45): E

> "The Dawsons wanted to sell their shares in the family business to a company called Wood Bastow Holdings Ltd. But they wanted to postpone the payment of capital gains tax. So they formed an Isle of Man company (Greenjacket) and exchanged their shares in the company owning the business for an allotment of shares in Greenjacket. The advantage of this transaction was that by para 6 of Sch 7 to the 1965 Act, a disposal of shares to Greenjacket in exchange for an allotment of its shares was treated as a reorganisation of share capital and by para 4 of the same Schedule a disposal of shares forming part of a reorganisation was not treated as a disposal for the purposes of capital gains tax. By a preplanned transaction, Greenjacket then sold the shares to Wood Bastow for cash. But the Revenue claimed that there had been no 'real' disposal to Greenjacket. It was merely a preplanned stage in a disposal from the Dawsons to Wood Bastow and fell outside the exception for a reorganisation of share capital." F G

H

73. As this summary makes clear, the question under the statute was not strictly whether there had been a "disposal" to one person or another; it was whether what would otherwise have been a disposal was to be treated as no disposal by virtue of specific provisions in the statute, applicable to a "share exchange" as defined. Neither of the leading counsel before us felt able to explain or support the characterisation of that issue as "commercial" rather than "legal". Nor was there anything in the speeches in *Furniss* to suggest that the decision turned on that distinction. (The House did not apparently have any concern that, if one ignored the disposal to Greenjacket, one could not explain how Greenjacket received the money. The answer, presumably, was that it did not matter, since the interposition of Greenjacket was purely tax-driven.) I

A 74. For the reasons already given, I do not find it necessary for the purposes of this case to reach a concluded view on how the new line is to be drawn. I can well understand that the term "payment" in s 338 of the Taxes Act was deemed to be too precise to admit of any broader interpretation; whereas the term "loss" in *Ramsay* was more flexible. In the present case, if forced to choose, I would have been inclined (unlike the Commissioners and the Judge) to regard the B concept of "expenditure" on the provision of an asset, as analogous to "payment" of interest, and therefore "legal", by analogy with *MacNiven*. However, I find it much more difficult to see how *McGuckian* or *Furniss* are to be fitted into the analysis. No doubt the working out of this distinction will become clearer in future decisions. For the time-being, it would be wrong in my view to see *MacNiven* as marking a significant change of direction, whether by way of C narrowing or expansion of the *Ramsay* principle. As Lord Nicholls said (para 8), it confirms that "the paramount question always is one of interpretation of the particular statutory provision and its application to the facts of the cases."

75. For these reasons, in addition to those already given, I would allow the appeal.

D *Appeal allowed, with costs.*

The Crown's appeal was heard in the House of Lords before Lord Nicholls of Birkenhead, Lord Steyn, Lord Hoffmann, Lord Hope of Craighead and Lord E Walker of Gestingthorpe on 12 and 13 October , when judgment was reserved. On 25 November 2004, judgment was given against the Crown, with costs.

Graham Aaronson Q.C., *Iain Milligan Q.C.*, *Camilla Bingham* and *Paul Farmer* for the Company.

F *David Goy Q.C.* and *David Ewart* for the Crown.

The cases referred to in the speeches are as follows:—*Barclays Mercantile Business Finance Ltd.* v. *Mawson (HMIT)* [2002] STC 1068 (Ch); [2003] STC 66 (CA); *Campbell* v. *Inland Revenue Commissioners* [2004] STC (SCD) 396; *Carreras Group Ltd.* v. *Stamp Commissioner* [2004] STC 1377; *Collector of Stamp Revenue* v. *Arrowtown Assets Ltd.* [2003] HKCFA 46; *Furniss (HMIT)* v. *D.E.R.* G *Dawson* [1984] AC 474; (1984) 55 TC 324; [1984] 2 WLR 226; [1984] 1 All ER 530; *McGuckian* v. *Commissioners of Inland Revenue* (1997) 69 TC 1; [1997] 1 WLR 991; *Commissioners of Inland Revenue* v. *Burmah Oil Co. Ltd.* (1981) 54 TC 200; [1982] STC 30; *MacNiven* v. *Westmoreland Investments Ltd.* [2003] 1 AC 311; (2001) 73 TC 1; *W T Ramsay Ltd.* v. *Commissioners of Inland Revenue* [1982] AC 300; (1981) 54 TC 101.

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The cases cited in the arguments were as follows:—*Alpine Investments BV* v. *Minister van Financien* (Case C-384/93) [1995] 2 CMLR 209; *Barclays Mercantile Industrial Finance Ltd.* v. *Melluish* (1990) 63 TC 95; [1990] STC 314; *Campbell* v. *Inland Revenue Commissioners* [2004] STC (SCD) 396; *Carreras Group Ltd.* v. *Stamp Commissioner* [2004] STC 1377; *Coates (HMIT)* v. *Arndale Properties* I *Ltd.* (1984) 59 TC 516; [1984] 1 WLR 1328; [1985] 1 All ER 15; [1984] STC 637; *Collector of Stamp Revenue* v. *Arrowtown Assets Ltd.* [2003] HKCFA 46; *Danner*

(Case C-136/00; [2002] 3 CMLR 29; *DTE Financial Services Ltd.* v. *Wilson (HMIT)* (2001) 74 TC 14; [2001] STC 777; *Edwards (HMIT)* v. *Bairstow & Harrison* [1956] AC 14; (1955) 36 TC 207; [1955] 3 WLR 410; [1955] 3 All ER 48; *Ensign Tankers (Leasing) Ltd.* v. *Stokes (HMIT)* [1992] 1 AC 655; [1992] 2 WLR 469; *Eurowings Luftverkehrs AG* v. *Finanzamt Dortmund-Unna* Case 294/97; [1999] ECR I-7447; *Furniss (HMIT)* v. *D.E.R. Dawson* [1984] AC 474; (1984) 55 TC 324; [1984] 2 WLR 226; [1984] 1 All ER 530; *In re Bank of Credit & Commerce International SA (No. 8)* [1998] AC 214; *In re Charge Card Services Ltd.* [1987] 1 Ch 150; *Inland Revenue Commissioners* v. *Fitzwilliam (Countess)* (1993) 67 TC 614; [1993] 1 WLR 1189; [1993] 3 All ER 184; [1993] STC 502; *Inland Revenue Commissioners* v. *Scottish Provident Institution* [2003] STC 1035; *Inland Revenue Commissioners* v. *Willoughby* (1997) 70 TC 57; [1997] 1 WLR 1071; [1997] 4 All ER 65; [1997] STC 995; *Lankhorst-Hohorst GmbH* v. *Finanzamt Steinfurt* (Case C-324/00) [2003] 2 CMLR 22; *Lupton (HMIT)* v. *FA & AB Ltd.* [1972] AC 634; (1972) 47 TC 580; [1971] 3 WLR 470; [1971] 3 All ER 948; *McGuckian* v. *Commissioners of Inland Revenue* (1997) 69 TC 1; [1997] 1 WLR 991; *MacNiven* v. *Westmoreland Investments Ltd.* [2003] 1 AC 311; (2001) 73 TC 1; *Moodie* v. *Commissioners of Inland Revenue* (1993) 65 TC 610; *New Angel Court* v. *Adam (HMIT)* [2004] STC 779; *Norman* v. *Golder* (1944) 26 TC 293; [1945] 1 All ER 352; *Overseas Containers (Finance) Ltd.* v. *Stoker (HMIT)* (1989) 61 TC 473; [1989] 1 WLR 606; [1989] STC 364; *W T Ramsay Ltd.* v. *Commissioners of Inland Revenue* [1982] AC 300; (1981) 54 TC 101.

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1. The following is the opinion of the Committee to which all its members have contributed.

Capital allowances

2. The issue in this appeal is whether Barclays Mercantile Business Finance Ltd. ("BMBF") is entitled to capital allowances in consequence of having paid about £91 million for a gas pipeline under the Irish Sea.

3. A trader computing his profits or losses will ordinarily make some deduction for depreciation in the value of the machinery or plant which he uses. Otherwise the computation will take no account of the need for the eventual replacement of wasting assets and the true profits will be overstated. But the computation required by Sch D (whether for the purpose of income or corporation tax) has always excluded such a deduction. Parliament therefore makes separate provision for depreciation by means of capital allowances against what would otherwise be taxable income. In addition, generous initial or first-year allowances, exceeding actual depreciation, are sometimes provided as a positive incentive to investment in new plant.

4. This appeal is concerned with the form of capital allowance called a "writing-down allowance", which, as its name suggests, is intended to be a substitute for deducting depreciation in the computation of profits. The conditions upon which it is allowed are contained in s 24(1) of the Capital Allowances Act 1990:

A "(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 (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."

BMBF

C

5. BMBF is a member of the Barclays group which carries on the trade of finance leasing or providing "asset based finance". It is the UK market leader in this field. The essence of its business is to provide capital for the purchase of an asset for use by its customer in return for a series of periodic payments secured upon the asset itself. The transaction normally takes the form of a purchase of D the asset by BMBF, either from a third party or (by way of "sale and lease back") from the customer himself, followed by the grant to the customer of a lease at a rent calculated to secure BMBF an appropriate return. BMBF has the security of being owner of the asset and entitled in the event of default to sell it and recover the sums outstanding.

E 6. There is no dispute that BMBF, as purchaser of an asset, is ordinarily entitled to a capital allowance under s 24(1). It carries on the trade of leasing and has acquired the asset wholly and exclusively by way of provision for the purposes of that trade. In consequence of its purchase from the third party or the customer, BMBF becomes owner of the asset and remains owner during the subsistence of the lease. Depreciation of the asset is a depreciation in the value F of BMBF's capital assets.

The pipeline

7. Bord Gáis Éireann ("BGE") is an Irish statutory corporation responsible G for the supply, transmission and distribution of natural gas in the Republic of Ireland. Between 1991 and 1993 BGE employed contractors to build a high-pressure pipeline for the transport of natural gas from Moffat in Scotland to Ballough in the Republic. The pipeline consisted of three parts: a 30 inch onshore pipeline 80 km long from a compressor station at Moffat to another compressor station at Brighouse Bay on the Scottish coast; a 24 inch undersea pipeline 208 H km long from Brighouse Bay to Loughshinny on the Irish coast, not far north of Dublin; and a 30 inch onshore pipeline, 8 km in length, from Loughshinny to Ballough. This was an infrastructure project of national importance, intended to meet the need for natural gas in the Republic as its own natural gas fields (off the south coast of Ireland) came to be exhausted. The pipeline was completed by the end of 1993, although there was a lengthy period of commissioning before it was I fully in service. The cost was met, as to part, by a 35 per cent. EEC grant. The rest appears to have been provided by a consortium of banks.

The sale and lease back A

8. On 31 December 1993 BGE sold the pipeline to BMBF for £91.292 million and was granted a lease back. The Judge rounded the purchase price down to £91 million and we shall do the same. The sale was given effect by two acquisition agreements executed between BGE and BMBF providing for the sale B of part of the pipeline in two sections: (i) the section on Irish soil or in Irish territorial waters (the price being £25.018 million plus VAT) and (ii) the section running in international waters (or in Manx territorial waters) and three turbine compressor units at the compressor station at Brighouse Bay on the Scottish coast (the purchase price being £38.363 million plus VAT for the pipeline in Manx waters and the compressors and £27.911 million with no VAT for the C pipeline in international waters between the Isle of Man and Ireland). These prices were based on an apportionment of the actual cost of the pipeline and compressors, with various adjustments, the most important being the deduction of apportioned amounts of the EEC grant. The aggregate assets acquired by BMBF under the acquisition agreements are referred to below as "the plant". D

9. The lease to BGE was for (i) a pre-primary period (covering the initial commissioning of the plant) from 31 December 1993 to 30 September 1995 and (ii) a primary period of 31 years from 1 October 1995. Thereafter the lease could be renewed for a succession of one-year periods. The basic rent was specified in an "initial cash flow", a computer printout annexed to a lengthy financial E schedule forming part of the lease. The rent (which was chargeable to corporation tax in the hands of BMBF) was to be about £2.86 million in 1995 and about £6.01 million in 1996, escalating by 5 per cent. annually in each later year. But Part 3 of the financial schedule provided for the rents to be adjusted (by the mechanism of one or more revised cash flows) if any of the assumptions in Part 2 of the schedule (which centred on corporation tax matters, and in F particular rates of corporation tax and the availability of writing-down allowances) proved incorrect, either initially or as a result of changes during the course of the lease. In the event of default, BMBF became entitled to termination payments intended to put it in the same financial position as if the lease had continued and there were quite elaborate provisions for re-delivery of the plant to BMBF and its sale to enable the termination payments to be recovered. G

10. BGE did not intend to operate the pipeline itself. It incorporated a wholly-owned UK subsidiary called BGE (UK) Ltd. ("BGE (UK)") on 17 June 1993. It is resident and carries on a substantial business in the UK. On the same day as the lease to BGE was executed, it granted a sub-lease to BGE (UK) for H the "Sub Lease Period", an expression which appears (after a lengthy paperchase through a thicket of definitions) to correspond exactly to the period of the lease. (No one has ever taken the point that the sub-lease might have taken effect as an assignment.) In general the terms of the sub-lease followed those of the lease, but there was an important difference as regards rent. The sub-lease provided for the same escalating rental payments as in the initial cash flow, but without any I provision for adjustments.

11. At the same time BMBF, BGE and BGE (UK) entered into an Assumption Agreement by which BGE (UK) assumed direct liability to BMBF to pay the rent due under the head lease. BMBF agreed to accept these payments

A in discharge of BGE's liability and BGE agreed to treat them as discharging BGE(UK)'s liability under the sublease. The only complication arose from the absence of any provision for adjustment of the rent under the sublease. Park J. described what he understood would be the position if the rent under the headlease was adjusted ([2002] STC 1068, pp 1089-90, para 18):

> "If corporation tax rates changed, the headlease rent payable to BMBF B would change but the sublease rent payable by BGE (UK) would remain the same. If I have understood correctly how it would work, if the head lease rent went up BGE (UK) would still pay the full amount of the sublease rent to BMBF, and the balance of the (now) increased head lease rent would be paid by BGE to BMBF; if the headlease rent went down BGE (UK) would pay part of the sublease rent to BMBF (that part being equal to the (now) C reduced headlease rent) and would pay the balance of the sublease rent to BGE."

It has not been suggested that the Judge's understanding was incorrect.

12. As the most important part of BGE (UK)'s business was to be to D transport BGE's gas through the pipeline to Ireland, BGE (UK) and BGE entered into a transportation agreement and an ancillary licence agreement. BGE (UK) undertook the obligation to transport natural gas through the pipeline in consideration of annual payments calculated by various formulae. The details are very complicated and are not relevant, except that it is common ground that (as provisions for 5 per cent. annual escalations suggest) the E payments were intended to ensure that BGE (UK) had sufficient funds to meet the rent payable to BGE under the sublease. BGE's payments to BGE (UK) were to be paid into a designated transportation account.

The scheme

F 13. If the transactions so far described—the sale to BMBF, the lease back, the sublease to BGE (UK) and the assumption and transportation agreements—were all that there was to be said about the transaction, the Inland Revenue would accept that BMBF is entitled to capital allowances. It has acquired the pipeline in the course of its trade and leased it back to BGE at a rent which reflects its entitlement to capital allowances (and provides for an increase if those G allowances are not obtainable). The sublease, assumption agreement and transportation agreement were essentially Irish matters with which BMBF was not particularly concerned.

14. The challenge by the Inland Revenue arises from the fact that all these transactions formed part of a larger scheme devised by Barclays de Zoete Wedd H Ltd. ("BZW"), another company in the Barclays group. It carried on the business of investment banking and acted as adviser to BGE. As the Special Commissioners found, it was plain on the documents that all the arrangements were organised and set in motion by BZW as part of a co-ordinated scheme. The relevant parts of the scheme which have not so far been described concerned the disposal of the £91 million which BMBF paid for the pipeline. From the point of I view of BMBF, these were described as the "security arrangements", since they supported a guarantee of the rent payable under the lease and assumption

agreement. The Inland Revenue, on the other hand, say that if one looks at the scheme as a whole, they were not security arrangements. They neutralised the effect of the transaction in providing finance to BGE and took it outside the scope of s 24(1). A

15. BMBF required a guarantee of BGE (UK)'s liability to pay the rent. This guarantee was provided by Barclays Bank itself pursuant to a guarantee facility agreement made with BGE (UK). As counter-security for its potential liability under the guarantee, Barclays Bank required BGE (UK) to provide a charge over the £91 million. For this purpose, BGE deposited the money with a Jersey company called Deepstream Investments Ltd. ("Deepstream") which was managed by a company in the Barclays group. The deposit agreement, approved by Barclays, provided for Deepstream "to repay the Deposit" by a series of payments, described as "A", "B" or "C" amounts, over a period ending in 2025 (except that the B payments ended in 2001). The amounts totalled—indeed the A amounts by themselves totalled—much more than £91 million. It was expressly provided that Deepstream was not required to make any other payment of any nature to BGE. B C D

16. The security in favour of Barclays Bank was then created by the following transactions:

(a) As security for its obligations to BGE (UK) under the transportation agreement, BGE assigned its interest in the Deepstream deposit to BGE (UK). It also charged a current account held in the name of BGE. E

(b) As security for its obligations to Barclays under the guarantee facility agreement BGE (UK) assigned to Barclays its interest in the Deepstream deposit, its interest in the charged BGE account, and its rights under the transportation agreement, and it also charged its interest in the transportation account provided for by the transportation agreement. F

(c) There was a deposit agreement between Deepstream and Barclays Finance Co. (Isle of Man) Ltd. ("BIoM"), a Barclays company registered in the Isle of Man, under which Deepstream placed with BIoM an amount equal to the sum deposited with Deepstream by BGE. G

(d) Deepstream executed a deed of indemnity in favour of Barclays in respect of Barclays' obligations under its guarantee of BGE (UK)'s obligations to BMBF. As security for the indemnity Deepstream assigned to Barclays its interest in the deposit with BIoM and granted Barclays fixed and floating charges over all its assets. H

17. BMBF had, unsurprisingly, borrowed the £91 million which it paid for the pipeline from Barclays Bank. And BIoM kept its funds on deposit with Barclays Bank. So, as the Special Commissioners and Park J. pointed out, the £91 million passed from Barclays Bank to BMBF, from BMBF to BGE, from BGE to Deepstream, from Deepstream to BIoM and from BIoM back to Barclays Bank again. The effect, as Park J. said, was that BGE, having sold the pipeline, was unable to get its hands on the purchase price. It had to remain on deposit with Deepstream and be paid out, year by year, partly (in the form of A payments) to discharge the liability for rent under the lease and partly (in the I

A form of B and C payments) for the benefit of BGE. And the benefit obtained by BGE was entirely attributable to BMBF being able to pass on the benefit of its capital allowances.

The decisions of the Special Commissioners and the Judge

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18. The Special Commissioners (whose decision is reported in an anonymised form in [2002] STC 1068, p 1070, p 1080h) found as a fact that the events of 31 December 1993 were pre-ordained and designed by BZW to be a composite whole. That finding has not been challenged. The circularity of the payments of the £91 million was not an essential part of the scheme. The terms C upon which BMBF bought and leased back the pipeline were commercial terms negotiated at arms' length and, as a matter of history, the scheme originally contemplated that a company outside the Barclays group would be the purchaser and lessor. Likewise, the terms upon which Barclays Bank provided the guarantee were ordinary commercial terms. It could have been provided by a different bank without affecting the way in which the scheme worked. In fact, however, the payments did circulate within the Barclays group.

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19. Park J., who has great experience in these matters, described the term of the Deepstream deposit agreement between BGE and Deepstream as most unusual. He acknowledged (in para 29) that the circularity was not a necessary part of the scheme and also that the circulation of the £91 million had created a trail of obligations to make periodic payments which would not be entirely E circular:

> "Although the A payments from Deepstream to BGE would be within the circle (moving on to BGE (UK), thence to BMBF, and thence to [Barclays'] group treasury), the B and C payments would not be: BGE would keep them. Further, the transportation agreement would be likely to mean that the payments from BGE to BGE (UK) were greater than the F amounts which went round the circle (to say nothing of the prospect of BGE (UK) making substantial profits by exploiting the capacity of the pipeline in so far as it was not fully used by BGE). And . . . BMBF would need more than the receipts which it would get from BGE (UK) under the assumption agreement in order fully to service and repay its borrowing of £91 million from [Barclays]."

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20. Nevertheless, the Judge concluded, in agreement with the Special Commissioners, that the difference between what BMBF was receiving from BGE (UK) and what it had to pay Barclays to service its borrowing was represented by the benefit of the capital allowances. It was these allowances which provided the only new money introduced into the circular system and H which enabled BGE to receive the only money to leave the system, namely the B and C payments from Deepstream. All the rest was passed round between Barclays companies.

21. The Special Commissioners summed up their views on the effect of the transactions:

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> "The only benefit which BGE obtained from the very complicated arrangements choreographed by BZW were amounts B and C paid to it

under the terms of the deposit agreement. Payments of amount A returned eventually to BMBF and from BMBF to the bank. BGE was to benefit to an extent of £8.1 million net and the Irish government was to receive £1.8 million in stamp duty. Those payments would be financed entirely by UK taxpayers by means of the hoped-for capital allowances. Without the capital allowances BGE would receive nothing, for the amounts of the rents would increase to take account of the non-availability of capital allowances.

Looking at the matter in the round, we accept Mr. Goy's primary submission that the payment of money by BMBF, even if it is said to have involved BMBF incurring expenditure, cannot be said to have been expenditure on the pipeline.

The payment by BMBF to BGE achieved no commercial purpose. Commercially driven finance leasing is designed to provide working capital to the lessee. But BGE could not get its hands on the money. It parted with a valuable asset allegedly for £91,292,000 but received no immediate benefit from the transaction. [BMBF] provided no finance to BGE simply because the amounts had to be deposited as part of the arrangements with Deepstream to be repaid only in accordance with the deposit agreement with Deepstream . . .

In our judgment the purpose of the expenditure by BMBF on 31 December 1993 was not the acquisition of the pipeline but the obtaining of capital allowances which would result in ultimately a profit to BGE and fees payable to BMBF and BZW. The transaction had no commercial reality."

22. Park J. agreed. He said (at para 49) that finance leasing ordinarily involved the provision of "up-front finance" to the lessee: a capital sum used to buy the plant or refinance its previous acquisition:

"But in the transaction involved in the present case no up-front finance was provided. BGE already owned the pipeline and had paid for it with a loan from a syndicate of banks. After the transaction BGE was still able to use the pipeline as before, though by then it did so by virtue of the lease, sublease and Transportation Agreement, and it still owed to the banks the money which it had borrowed. Nor was the £91 million available to BGE for it to use in any other way to finance transactions or activities of its business."

23. In answer to the submission that BMBF had paid the £91 million in consideration of the acquisition of the pipeline and had become its owner under the acquisition agreements, Park J. said (para 57):

"It is true that in a strictly legal sense one can say that BMBF incurred expenditure on the provision of the pipeline. That is what the two acquisition agreements said . . . However, in the light of the *Ramsay* authorities I consider that I have to interpret and apply the statute in a wider way . . . I have to ask: on what did BMBF *really* incur its expenditure of £91 million? Was it really incurred on the provision of the pipeline, or was it really incurred on something else? . . . My answer is that the expenditure was really incurred on the creation or provision of a complex network of agreements under which, in an almost entirely secured way, money flows would take place annually over the next 32 or so years so as to recoup to BMBF its outlay of £91 million plus a profit."

24. The Special Commissioners and the Judge therefore considered that BMBF did not incur expenditure of £91 million in the provision of a pipeline for the purposes of its finance leasing trade because the transaction lacked commercial reality. The Judge went so far as to say that the existence of the pipeline and the amount of the consideration were irrelevant. Because of the circularity of the payments, the scheme would have worked just as well whatever price had been named in the documents and whether there had actually been a pipeline or not.

The Court of Appeal

25. The Court of Appeal (Peter Gibson, Rix and Carnwath L.JJ.) unanimously allowed the appeal and set aside the order of the Judge and the decision of the Special Commissioners. The judgments in the Court of Appeal are reported at [2003] STC 66. We shall return to them in the course of our discussion. The Inland Revenue appeal to this House and ask that the decision of Park J. should be restored.

The *Ramsay* principle

26. In treating the legal effect of the acquisition agreements as irrelevant for the purposes of s 24(1), the Special Commissioners and Park J. said that they were applying the principles of construction first applied by this House in *W T Ramsay Ltd.* v. *Inland Revenue Commissioners* [1982] AC 300. These principles have since been discussed and explained in numerous cases both in lower courts and in your Lordships' House. But these attempts at clarification appear only to have raised fresh doubts and further appeals. Mr. Aaronson Q.C., who appeared for BMBF, said that he spoke on behalf of the profession when he hoped that the House would take this opportunity to give definitive guidance.

27. It is no doubt too much to expect that any exposition will remove all difficulties in the application of the principles because it is in the nature of questions of construction that there will be borderline cases about which people will have different views. It should however be possible to achieve some clarity about basic principles.

28. As Lord Steyn explained in *Inland Revenue Commissioners* v. *McGuckian* [1997] 1 WLR 991, p 999, the modern approach to statutory construction is to have regard to the purpose of a particular provision and interpret its language, so far as possible, in a way which best gives effect to that purpose. Until the *Ramsay* case, however, revenue statutes were "remarkably resistant to the new non-formalist methods of interpretation". The particular vice of formalism in this area of the law was the insistence of the courts on treating every transaction which had an individual legal identity (such as a payment of money, transfer of property, creation of a debt, etc.) as having its own separate tax consequences, whatever might be the terms of the statute. As Lord Steyn said, it was:

"those two features—literal interpretation of tax statutes and the formalistic insistence on examining steps in a composite scheme separately—[which] allowed tax avoidance schemes to flourish." A

29. The *Ramsay* case [1982] AC 300 liberated the construction of revenue statutes from being both literal and blinkered. It is worth quoting two passages from the influential speech of Lord Wilberforce. First, (at p 323) on the general approach to construction: B

"What are 'clear words' is to be ascertained upon normal principles: these do not confine the courts to literal interpretation. There may, indeed should, be considered the context and scheme of the relevant Act as a whole, and its purpose may, indeed should, be regarded." C

30. Secondly (at pp 323-324), on the application of a statutory provision so construed to a composite transaction:

"It is the task of the court to ascertain the legal nature of any transaction to which it is sought to attach a tax or a tax consequence and if that emerges from a series or combination of transactions, intended to operate as such, it is that series or combination which may be regarded." D

31. The application of these two principles led to the conclusion, as a matter of construction, that the statutory provision with which the Court was concerned, namely that imposing capital gains tax on chargeable gains less allowable losses was referring to gains and losses having a commercial reality ("The capital gains tax was created to operate in the real world, not that of make-belief") and that therefore (p 326): E

"To say that a loss (or gain) which appears to arise at one stage in an indivisible process, and which is intended to be and is cancelled out by a later stage, so that at the end of what was bought as, and planned as, a single continuous operation, there is not such a loss (or gain) as the legislation is dealing with, is in my opinion well and indeed essentially within the judicial function." F

32. The essence of the new approach was to give the statutory provision a purposive construction in order to determine the nature of the transaction to which it was intended to apply and then to decide whether the actual transaction (which might involve considering the overall effect of a number of elements intended to operate together) answered to the statutory description. Of course this does not mean that the courts have to put their reasoning into the straitjacket of first construing the statute in the abstract and then looking at the facts. It might be more convenient to analyse the facts and then ask whether they satisfy the requirements of the statute. But however one approaches the matter, the question is always whether the relevant provision of statute, upon its true construction, applies to the facts as found. As Lord Nicholls of Birkenhead said in *MacNiven* v. *Westmoreland Investments Ltd.* [2003] 1 AC 311, p 320, para 8: G H I

"The paramount question always is one of interpretation of the particular statutory provision and its application to the facts of the case."

33. The simplicity of this question, however difficult it might be to answer on the facts of a particular case, shows that the *Ramsay* case did not introduce a

A new doctrine operating within the special field of revenue statutes. On the contrary, as Lord Steyn observed in *McGuckian* [1997] 1 WLR 991, p 999 it rescued tax law from being "some island of literal interpretation" and brought it within generally applicable principles.

34. Unfortunately, the novelty for tax lawyers of this exposure to ordinary B principles of statutory construction produced a tendency to regard *Ramsay* as establishing a new jurisprudence governed by special rules of its own. This tendency has been encouraged by two features characteristic of tax law, although by no means exclusively so. The first is that tax is generally imposed by reference to economic activities or transactions which exist, as Lord Wilberforce said, "in the real world". The second is that a good deal of intellectual effort is devoted to C structuring transactions in a form which will have the same or nearly the same economic effect as a taxable transaction but which it is hoped will fall outside the terms of the taxing statute. It is characteristic of these composite transactions that they will include elements which have been inserted without any business or commercial purpose but are intended to have the effect of removing the transaction from the scope of the charge.

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35. There have been a number of cases, such as *Inland Revenue* v. *Burmah Oil Co. Ltd.* 1982 SC (HL) 114, *Furniss* v. *Dawson* [1984] AC 474 and *Carreras Group Ltd.* v. *Stamp Commissioner* [2004] STC 1377 in which it has been decided that elements which have been inserted into a transaction without any business or commercial purpose did not, as the case might be, prevent the composite transaction from falling within a charge to tax or bring it within an exemption E from tax. Thus in the *Burmah* case, a series of circular payments which left the taxpayer company in exactly the same financial position as before was not regarded as giving rise to a "loss" within the meaning of the legislation. In *Furniss*, the transfer of shares to a subsidiary as part of a planned scheme immediately to transfer them to an outside purchaser was regarded as a taxable disposition to the outside purchaser rather than an exempt transfer to a group F company. In *Carreras* the transfer of shares in exchange for a debenture with a view to its redemption a fortnight later was not regarded as an exempt transfer in exchange for the debenture but rather as an exchange for money. In each case the Court looked at the overall effect of the composite transactions by which the taxpayer company in *Burmah* suffered no loss, the shares in *Furniss* passed into the hands of the outside purchaser and the vendors in *Carreras* received cash. On G the true construction of the relevant provisions of the statute, the elements inserted into the transactions without any commercial purpose were treated as having no significance.

36. Cases such as these gave rise to a view that, in the application of *any* taxing statute, transactions or elements of transactions which had no commercial H purpose were to be disregarded. But that is going too far. It elides the two steps which are necessary in the application of any statutory provision: first, to decide, on a purposive construction, exactly what transaction will answer to the statutory description and secondly, to decide whether the transaction in question does so. As Ribeiro P.J. said in *Collector of Stamp Revenue* v. *Arrowtown Assets Ltd.* [2003] HKCFA 46, para 35:

I "[T]he driving principle in the *Ramsay* line of cases continues to involve a general rule of statutory construction and an unblinkered approach to the

analysis of the facts. The ultimate question is whether the relevant statutory provisions, construed purposively, were intended to apply to the transaction, viewed realistically." A

37. The need to avoid sweeping generalisations about disregarding transactions undertaken for the purpose of tax avoidance was shown by *MacNiven* v. *Westmoreland Investments Ltd.* [2003] 1 AC 311 in which the question was whether a payment of interest by a debtor who had borrowed the money for that purpose from the creditor himself and which had been made solely to reduce liability to tax, was a "payment" of interest within the meaning of the statute which entitled him to a deduction or repayment of tax. The House decided that the purpose of requiring the interest to have been "paid" was to produce symmetry by giving a right of deduction in respect of any payment which gave rise to a liability to tax in the hands of the recipient (or would have given rise to such a liability if the recipient had been a taxable entity.) As the payment was accepted to have had this effect, it answered the statutory description notwithstanding the circular nature of the payment and its tax avoidance purpose. B C D

38. *MacNiven* shows the need to focus carefully upon the particular statutory provision and to identify its requirements before one can decide whether circular payments or elements inserted for the purpose of tax avoidance should be disregarded or treated as irrelevant for the purposes of the statute. In the speech of Lord Hoffmann in *MacNiven* it was said that if a statute laid down requirements by reference to some commercial concept such as gain or loss, it would usually follow that elements inserted into a composite transaction without any commercial purpose could be disregarded, whereas if the requirements of the statute were purely by reference to its legal nature (in *MacNiven*, the discharge of a debt) then an act having that legal effect would suffice, whatever its commercial purpose may have been. This is not an unreasonable generalisation, indeed perhaps something of a truism, but we do not think that it was intended to provide a substitute for a close analysis of what the statute means. It certainly does not justify the assumption that an answer can be obtained by classifying all concepts *a priori* as either "commercial" or "legal". That would be the very negation of purposive construction: see Ribeiro P.J. in *Arrowtown* at paras 37 and 39 and the perceptive judgment of the Special Commissioners (Theodore Wallace and Julian Ghosh) in *Campbell* v. *Inland Revenue Commissioners* [2004] STC (SCD) 396. E F G

39. The present case, like *MacNiven*, illustrates the need for a close analysis of what, on a purposive construction, the statute actually requires. The object of granting the allowance is, as we have said, to provide a tax equivalent to the normal accounting deduction from profits for the depreciation of machinery and plant used for the purposes of a trade. Consistently with this purpose, s 24(1) requires that a trader should have incurred capital expenditure on the provision of machinery or plant for the purposes of his trade. When the trade is finance leasing, this means that the capital expenditure should have been incurred to acquire the machinery or plant for the purpose of leasing it in the course of the trade. In such a case, it is the lessor as owner who suffers the depreciation in the value of the plant and is therefore entitled to an allowance against the profits of his trade. H I

A 40. These statutory requirements, as it seems to us, are in the case of a finance lease concerned entirely with the acts and purposes of the lessor. The Act says nothing about what the lessee should do with the purchase price, how he should find the money to pay the rent or how he should use the plant. As Carnwath L.J. said in the Court of Appeal [2003] STC 66, p 89, para 54:

> "There is nothing in the statute to suggest that 'up-front finance' for the B lessee is an essential feature of the right to allowances. The test is based on the purpose of the lessor's expenditure, not the benefit of the finance to the lessee."

41. So far as the lessor is concerned, all the requirements of s 24(1) were satisfied. Mr. Boobyer, a director of BMBF, gave unchallenged evidence that C from its point of view the purchase and lease back was part of its ordinary trade of finance leasing. Indeed, if one examines the acts and purposes of BMBF, it would be very difficult to come to any other conclusion. The finding of the Special Commissioners that the transaction "had no commercial reality" depends entirely upon an examination of what happened to the purchase price after BMBF paid it to BGE. But these matters do not affect the reality of the D expenditure by BMBF and its acquisition of the pipeline for the purposes of its finance leasing trade.

42. If the lessee chooses to make arrangements, even as a preordained part of the transaction for the sale and lease back, which result in the bulk of the purchase price being irrevocably committed to paying the rent, that is no concern of the lessor. From his point of view, the transaction is exactly the same. No one E disputes that BMBF had acquired ownership of the pipeline or that it generated income for BMBF in the course of its trade in the form of rent chargeable to corporation tax. In return it paid £91 million. The circularity of payments which so impressed Park J. and the Special Commissioners arose because BMBF, in the ordinary course of its business, borrowed the money to buy the pipeline from Barclays Bank and Barclays happened to be the bank which provided the cash F collateralised guarantee to BMBF for the payment of the rent. But these were happenstances. None of these transactions, whether circular or not, were necessary elements in creating the entitlement to the capital allowances.

43. For these reasons, which are substantially the same as those of the Court of Appeal, we would dismiss this appeal.

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Appeal dismissed, with costs.

[Solicitors:— Messrs. Denton Wilde Sapte; Solicitor of Inland Revenue.]

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Printed in the United Kingdom by The Stationery Office Limited
ID176270 3/2005 C15