[2021] UKUT 0059 (TCC)

Appeal number: UT/2019/0167 (V)

CORPORATION TAX – capital allowances – provision of plant and machinery – s61(4) of Capital Allowances Act 1990 – succession to trade – s78 of Capital Allowances Act 1990

UPPER TRIBUNAL
(TAX AND CHANCERY CHAMBER)

INMARSAT GLOBAL LIMITED **Appellant**

-and-

THE COMMISSIONERS FOR HER MAJESTY'S REVENUE AND CUSTOMS **Respondents**

TRIBUNAL: MR JUSTICE ADAM JOHNSON
JUDGE JONATHAN RICHARDS

Sitting in public by way of remote video hearing treated as taking place at The Royal Courts of Justice, Rolls Building, London on 9 to 11 February 2021 and further written submissions received on 19 and 24 February 2021

Kevin Prosser QC and Barbara Belgrano instructed by Stephenson Harwood LLP for the Appellant

Michael Gibbon QC, Richard Vallat QC and Ronan Magee instructed by the General Counsel and Solicitor for Her Majesty's Revenue and Customs for the Respondents

DECISION

1. This appeal concerns the claim by the taxpayer company ("Inmarsat") to capital allowances for the costs of launching six satellites between 1990 and 1996. Inmarsat has never itself owned those satellites which have, at all material times, been owned by equipment lessors who granted leases containing rights to use them. Moreover, Inmarsat only acquired any rights in the satellites in 1999, after their launch, as part of a process by which it succeeded to the trade of the International Maritime Satellite Organisation ("IMSO"). The appeal raises two inter-related questions as to the availability of capital allowances:

> (1) Whether the launch costs were capable of attracting capital allowances at all.
>
> (2) Whether, if the launch costs in principle attract allowances, Inmarsat is entitled to benefit from them.

2. HMRC and Inmarsat made a joint referral of these issues to the First-tier Tribunal (Tax Chamber) under paragraph 31A of Schedule 18 of the Finance Act 1998 ("FA 1998"). In a decision released on 30 August 2019 (the "Decision"), the FTT determined both issues in favour of HMRC and, with the permission of the FTT, Inmarsat appeals to this Tribunal.

Facts

3. The facts were, as the FTT noted, complicated but relatively uncontroversial. In the summary that follows, we will use defined terms in the Decision and, unless we say otherwise, references to numbers in square brackets are to paragraphs of the Decision. In particular, we refer to the six satellites, around which this dispute centres, as the "Satellites", the defined term being used to distinguish those satellites from others whose tax treatment is not in issue.

4. IMSO was an international organisation established by the Convention on the International Maritime Satellite Organization (INMARSAT) (the "Convention"). The Convention was entered into on 3 September 1976 and came into force on 16 July 1979. Its purpose was to "make provision for the space segment necessary for improving maritime communications". By the Convention, IMSO was to operate on a sound economic and financial basis and would, accordingly, charge for the use of the navigation system it established. IMSO was headquartered in the UK, was a body corporate for UK tax purposes and so, in principle, would be subject to UK corporation tax. However, by the Inmarsat (Immunities and Privileges) Order 1980, IMSO was exempt from taxes on income and gains ([8] to [10]).

5. The Satellites comprised three second generation "I-2 Satellites" and three third generation "I-3 Satellites" and were commissioned, and launched, in the course of IMSO's trade of operating a telecommunications satellite system ([10]).

6. The same basic contractual structure governed the construction, ownership and lease of all six Satellites (although as we will explain, the order in which the various

contracts were concluded differed as between the I-2 Satellites and the I-3 Satellites). That contractual structure can be summarised as follows:

> (1) IMSO entered into agreements (the "Construction Contracts") with a satellite construction company (British Aerospace Plc in the case of the I-2 Satellites and General Electric Technical Services Company Inc in the case of the I-3 Satellites) for the construction and sale of the Satellites.
>
> (2) However, IMSO never took delivery of the Satellites pursuant to those contracts. Instead financial lessors ("Lessors") (NSM in the case of the I-2 Satellites and Abbey in the case of the I-3 Satellites) obtained, by means of novation, the benefit and burden of relevant aspects of the Construction Contracts so that the Lessors obtained the right to delivery of the Satellites and the obligation to pay for them.
>
> (3) The Lessors agreed to lease the Satellites to Inmarsat in return for periodic rental payments (the "Leases"). The intentional ignition of any first stage engine of the launch vehicle would trigger the commencement of the term of the Leases.
>
> (4) The Satellites were entirely useless for their intended purposes until they were launched into orbit ([66]). Accordingly, IMSO entered into contracts for the launch of the Satellites with various parties. IMSO paid the launch costs under those contracts.

7. Initially, it was thought that IMSO would own the I-2 Satellites itself and, accordingly, that no Lessor would be involved with those Satellites. Accordingly, thinking that it would at all times be the owner of the Satellites, IMSO followed the natural course of first entering into Construction Contracts for the I-2 Satellites and, having done so, entering into launch contracts for those Satellites (see [15] to [17]).

8. It is reasonable to infer that at some point after it entered into its final launch contract for the I-2 Satellites, on 31 March 1988, IMSO realised that its chosen structure would be inefficient from a tax perspective. IMSO, as a tax-exempt body, could not benefit from the significant capital allowances that capital expenditure on the Satellites would attract. By contrast, if that capital expenditure was incurred by Lessors, who were subject to tax, the Lessors could set capital allowances on the Satellites against their other tax liabilities or those of their respective groups with the tax benefit of those capital allowances shared with IMSO in the form of reduced lease rental payments. Accordingly, the decision was taken to novate the Construction Contracts to the Lessors, which would enable the Lessors to claim capital allowances on the costs of acquiring the I-2 Satellites and to enter into the Leases. The result of this change of course was that, at the time the Lessors became party to the arrangements relating to the I-2 Satellites, IMSO was already party to launch contracts.

9. By the time the I-3 Satellites came to be commissioned, IMSO was aware from the beginning that Lessors needed to be involved. Accordingly, while it still entered into Construction Contracts and novated them in favour of the Lessors, the launch contracts were not entered into until after the agreements for lease were entered into.

10. IMSO paid the majority of the launch costs after it became party to the Leases but before the Satellites had been launched so as to trigger the commencement of the terms of the Leases.

11. All six Satellites were constructed and launched well before Inmarsat had any involvement with these arrangements. The I-2 Satellites were launched on various dates between October 1990 and December 1991 with IMSO paying the significant launch costs at or around this time. The I-3 Satellites were launched on various dates in 1996, again with IMSO paying the launch costs before Inmarsat became involved.

12. The Lessors were entitled to claim, and did claim, capital allowances on the price they paid to acquire the Satellites under the novated Construction Contracts. However, since the Lessors did not pay the launch costs which were instead paid by IMSO, the Lessors could not claim any allowances in respect of those launch costs, even if those costs could in principle qualify for allowances.

13. In 1999, Inmarsat acquired the business and assets of IMSO's trade in return for the issue of shares. We refer to this as the "Succession" because it was common ground that Inmarsat succeeded to IMSO's trade for the purposes of s78 of the Capital Allowances Act 1990 ("CAA1990"). As part of the Succession, Inmarsat obtained, by means of contracts of novation, both the benefit and burden of contracts to which IMSO was party including the Leases and other contracts to which IMSO was party in relation to the Satellites. However, since, by 1999 all the launch costs had been paid, Inmarsat became subject to no contractual obligation to pay those launch costs.

Relevant statutory provisions

14. In order to put the parties' respective contentions into context, we start with the relevant statutory provisions. All of the legislation set out below is as it was in force at the time of the Succession.

Entitlement to plant and machinery allowances

15. The basic entitlement to capital allowances on plant and machinery is conferred by s24 of the Capital Allowances Act 1990[1] which provides as follows:

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

[1]Inmarsat referred us to legislation on "first year allowances" contained in s22 of CAA1990. However, since even on Inmarsat's case, it could not have obtained any entitlement to first year allowances, and since the relevant requirements of s22 overlap with those of s24, we consider that the issues raised in this appeal as to how relevant aspects of the capital allowances code fit together are best explored by reference to s24. Accordingly, we do not set out the requirements of s22.

(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.

(2) …, for any chargeable period for which a person within subsection (1) above has qualifying expenditure which exceeds any disposal value to be brought into account in accordance with subsection (6) below, there shall be made to him-

(a) unless the period is the chargeable period related to the permanent discontinuance of the trade, an allowance ("a writing-down allowance") equal to-

(i) 25 per cent of the excess, or

(ii)….

(b) if the period is the chargeable period related to the permanent discontinuance of the trade, an allowance ("a balancing allowance") equal to the whole of the excess.

….

(5) For any chargeable period for which a person's qualifying expenditure is less than the disposal value which he is to bring into account, there shall be made on him a charge ("a balancing charge"), and the amount on which the charge is made shall be an amount equal to the difference.

(6) The disposal value to be brought into account by a person for any chargeable period is the disposal value of all machinery and plant-

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

(b) which belongs to him at some time in the chargeable period or its basis period, and

(c) in respect of which, in the chargeable period or its basis period, one of the following occurs, namely-

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

….

(v) the trade is permanently discontinued (or is treated by virtue of any provision of the Tax Acts as permanently discontinued);

and that is the first such event to occur;

16. We will address the parties' detailed submissions on these and other provisions later in this decision. However, for the time being, we note the following salient features of s24:

(1) In order for capital allowances to be available, both requirements set out in s24(1)(a) and s24(1)(b) must be satisfied. To comply with s24(1)(a), a person must incur capital expenditure "on the provision of plant and

machinery" (we add the emphasis because the scope of the word "provision" was at the heart of some of the issues before us). To comply with s24(1)(b), the plant and machinery in question must "belong" to that person as a result of incurring the expenditure.

(2) Capital allowances on plant and machinery have been available since at least the time of the Income Tax Act 1952. However, a requirement for the plant and machinery to "belong" to the relevant person has not always appeared in the same statutory provision as that stating that expenditure on the "provision" of plant and machinery benefited from allowances.a. Accordingly, some authorities on the meaning of the word "provision" to which we were referred, including *Commissioners of Inland Revenue v Barclay, Curle & Co Ltd* 45 TC 221 considered sections of a statute that referred to the "provision" of plant and machinery without also referring to a "belonging" condition.

(3) Section 24(6) requires "disposal values" to be brought into account on the occurrence of the events specified in s24(6)(c) including either (i) the plant and machinery ceasing to belong to the person who claimed allowances and (ii) the trade in which it is used being permanently discontinued. Those "disposal values" generally operate as a downward adjustment to the amount of allowances available since, by s24(2) capital allowances are available on the excess of any qualifying expenditure over disposal values to be brought into account.

17. The amount of disposal value to be brought into account is fixed by s26 of CAA1990 as follows:

> **26 The disposal value**
>
> (1) Subject to subsection (2) below, for the purposes of section 24 the disposal value of any machinery or plant depends upon the event by reason of which it falls to be taken into account and—
>
> (a) unless paragraph (b) below applies, if that event is the sale of the machinery or plant, equals the net proceeds to the person in question of the sale…,
>
> (b) if that event is the sale of the machinery or plant at a price lower than that which it would have fetched if sold in the open market, and otherwise than in circumstances such that—
>
> (i) the buyer's expenditure on the acquisition of the machinery or plant can be taken into account in making allowances to him under this Part or under Part VII and the buyer is not a dual resident investing company which is connected with the seller within the terms of section 839 of the principal Act, or
>
> (ii) there is a charge to tax under Schedule E,
>
> equals the price which the machinery or plant would have fetched if sold in the open market,
>
> …

> (e) if that event is the permanent discontinuance of the trade before the occurrence of an event within paragraph (a), (b), (c) or (d) above, is the same as the disposal value specified for the last-mentioned event,
>
> …
>
> and
>
> (f) in the case of any other event, equals the price which the machinery or plant would have fetched if sold in the open market at the time of the event.

18. At this stage, we will simply highlight the following salient features of s26:

> (1) The concept of a "disposal value" is of no direct relevance to a person who acquires plant and machinery and who wishes to claim capital allowances on that machinery. Rather, the concept is relevant to someone who is already claiming allowances on machinery as a disposal value operates to reduce the amount of allowances that can be obtained.
>
> (2) The amount of disposal value to be brought into account will depend on the precise disposal event. So, for example, where a person sells plant and machinery for market value, the disposal value is, by s26(1)(a), the "net proceeds of sale". If a sale is at below market value, the disposal value can be calculated by reference to market value instead, pursuant to s26(1)(b).
>
> (3) A "permanent discontinuance" of a trade is a disposal event even though it will not, of itself, result in a cash receipt for the owner of the plant and machinery in question. If the permanent discontinuance is followed by a sale of the plant and machinery then, by s26(1)(e), the disposal value is calculated by reference to the appropriate disposal value for the sale. However, if the trade is permanently discontinued without any subsequent sale of the plant and machinery, it is possible for s26(1)(f) to produce a disposal value calculated by reference to the market value of the plant and machinery at the time of the discontinuance.

19. As will be seen from s24(1)(b), the general position is that a person is entitled to capital allowances only where, as a result of incurring the expenditure, the plant and machinery "belongs" to that person (the "belonging condition"). Section 61 of CAA1990 modifies that position in relation to lessees under leases by deeming the belonging condition to be satisfied where it would not otherwise be.

> **61 Machinery and plant on lease**
>
> …
>
> (4) Where—
>
> (a) a lessee incurs capital expenditure on the provision for the purposes of a trade carried on by him of machinery or plant which he is required to provide under the terms of the lease, and

> (b) the machinery or plant is not so installed or otherwise fixed in or to a building or any other description of land as to become, in law, part of that building or other land,
>
> then, if the machinery or plant would not otherwise belong to him, the machinery or plant shall be treated for the purposes of this Part as belonging to him for so long as it continues to be used for the purposes of the trade; but, as from the determination of the lease, section 24(6) shall have effect as if the capital expenditure on providing the machinery or plant had been incurred by the lessor and not by the lessee.

20. Relevant definitions are provided by s61(8) which provides as follows:

> (8) In this section "lease" includes an agreement for lease where the term to be covered by the lease has begun, and any tenancy, but does not include a mortgage, and "lessee" and other cognate expressions shall be construed accordingly.

21. Section 61(4), therefore, is a "deeming provision". It applies when, among other conditions, a lessee is required to "provide" plant and machinery under the terms of a lease and there are obvious parallels between the use of the word "provide" and the word "provision" that appears in s24(1)(a). Where s61(4) applies, that plant and machinery is treated as belonging to that person where it would not otherwise do so. However, it is not stated expressly whether or not the machinery or plant can also belong to any other person. Nor is it stated expressly why persons in the lessee's position are deserving of a special treatment, a point to which we will return when considering how s61(4) should be purposively construed.

Successions

22. A "succession" to a trade involves one person ceasing to carry that trade on, and another starting it, usually following a transfer of that trade. Without special rules, the ordinary provisions of s24 and s26 of CAA1990 would apply: the transferor would be required to bring into account a disposal value in relation to any plant and machinery it transfers and the transferee would obtain allowances, by operation of s24 of CAA 1990, on the price paid to acquire that plant and machinery. For the transferor, since the trade is discontinued, s24(2) or s24(5) would provide for a balancing allowance or balancing charge to be made. Sections 77 and 78 modify that position.

23. First, where the transferor and transferee are connected persons, s77 permits them to make an election that plant and machinery is treated as transferring for a price that secures that neither a balancing allowance nor balancing charge is made on the transferor. Making such an election effectively makes the transfer tax neutral for capital allowances purposes: with the transferee stepping into the historic capital allowances position of the transferor.

24. Section 78 of CAA1990 applies where no election is made under 77:

> **78 Succession to trades where no election made under section 77**
>
> (1) Where a person succeeds to any trade which until that time was carried on by another person and, by virtue of section 113 or 337(1) of

> [Income and Corporation Taxes Act 1988] (changes in persons carrying on a trade, and special rules for corporation tax), the trade is to be treated as discontinued, any property which, immediately before the succession takes place, was either in use or provided and available for use for the purposes of the discontinued trade and, without being sold, is, immediately after the succession takes place, either in use or provided and available for use for the purposes of the new trade shall, for the purposes of this Part be treated as if—
>
> > (a) it had been sold to the successor when the succession takes place, and
> >
> > (b) the net proceeds of the sale had been the price which that property would have fetched if sold in the open market;
>
> but no first-year allowance shall be made by virtue of this subsection.
>
> (2) …

25. Section 78 is also a "deeming provision". On its face, it states that, where the necessary conditions for its application are satisfied, plant and machinery that was not "sold" is to be treated as "sold". Moreover, it deems the "net proceeds" of that sale to be of a particular amount. Section 78 does not expressly state that the plant and machinery in question is to be treated as belonging to the successor and whether the section has this effect is one of the points at issue in this appeal.

The parties' competing analyses

26. Inmarsat relies on the following chain of reasoning in support of its contention that it was entitled to capital allowances in its corporation tax returns from 1999 onwards in respect of the costs of launch of the Satellites:

> (1) By paying the launch costs, IMSO incurred capital expenditure "on the provision of" the Satellites. The Leases required IMSO to pay those launch costs. Accordingly, the provisions of s61(4) of CAA1990 were engaged with the result that by s61(4) of CAA1990, the Satellites were deemed to belong to IMSO. That "belonging" was not exclusive: the Satellites also belonged to the Lessors who had also incurred capital expenditure on their provision. Accordingly, the effect of s61(4) was to treat the Satellites as owned jointly by IMSO and the Lessors in proportion to their capital expenditure.
>
> (2) On 15 April 1999, when Inmarsat succeeded to IMSO's trade, the provisions of s78(1) of CAA1990 were engaged. Section 78 of CAA1990 provided for all assets of IMSO's trade, including its deemed co-ownership interest in the Satellites, to be treated as sold to Inmarsat for their then market value. That meant the requirements of s24 of CAA1990 were met and Inmarsat was entitled to capital allowances by reference to the market value consideration deemed to have been incurred.
>
> (3) The market value consideration that Inmarsat was treated as incurring should reflect the fact that IMSO owned only a partial interest in the Satellites by the operation of s61(4). If, following the application of s61(4),

IMSO obtained an interest of X% in the Satellites, the consideration that Inmarsat was deemed to give should similarly be X% of the market value of the Satellites as at 15 April 1999 and that figure would determine Inmarsat's entitlement to capital allowances.

27. HMRC raise the following arguments in disagreeing with Inmarsat's approach:

(1) Section 78 is a computational provision. It is engaged when there is a succession, not involving a sale, that results in a transferor ceasing to own machinery and a transferee becoming the owner of it. Where s78 applies, it fixes the transfer value that should apply as between those two parties for the purposes of the capital allowances regime. Therefore, Inmarsat's assertion that s78 resulted in Inmarsat becoming a deemed owner of the Satellites involves a misreading of that provision. The correct reading is that s78 applies only to determine the nature of a transfer that has actually taken place and the value to be ascribed to that transfer. The questions raised by s78 did not arise when Inmarsat acquired IMSO's trade since, at that stage, there was no accompanying actual transfer of ownership of the Satellites which remained at all material times in the ownership of the Lessor.

(2) In any event, Inmarsat's analysis of s78 assumes that at the time of the Succession s61(4) of CAA1990 deemed IMSO to own the Satellites as a consequence of paying the launch costs. Section 61(4) does not have this effect for the following broad reasons:

(a) The launch costs that IMSO paid, while constituting "capital expenditure", were not "on the provision … of machinery and plant".

(b) IMSO was not "required to provide" any plant and machinery under the terms of the Leases for the purposes of s61(4). That was for two broad reasons. First, the Leases of the I-3 Satellites imposed no obligation on IMSO to incur launch costs at all, though HMRC accept that the leases of the I-2 Satellites did. In any event, an obligation to procure launch services was not enough to constitute a requirement to "provide" the Satellites. Second, there is a "chronological flow" to s61(4), when read together with the definitions provision in s61(8) which means that expenditure only counts for the purposes of s61(4) if it is incurred after the lease is in existence. Here the lease terms of both the I-2 Satellites and the I-3 Satellites did not commence until after the launch costs had been incurred which meant that IMSO's expenditure on launch costs was incapable of engaging s61(4).

(c) Inmarsat's succession to IMSO's trade on 15 April 1999 involved a novation of the Leases. That novation constituted a "determination" of the original Leases for the purposes of s61(4), thereby engaging the "tailpiece" to that provision.

28. The way in which both parties put their cases has evolved somewhat since the FTT proceedings. However, in broad terms, both before us and the FTT, there were three issues between the parties, all of which the FTT determined in favour of HMRC:

> (1) Issue 1 - Whether s78 of CAA1990 applied to deem IMSO to sell the Satellites to Inmarsat and, if so, with what effect.
>
> (2) Issue 2 - Whether IMSO incurred the launch costs "on the provision of … plant" for the purposes of s61(4).
>
> (3) Issue 3 - Whether the other requirements of s61(4) of CAA1990 were satisfied so as to deem the Satellites to belong to IMSO as at 15 April 1999. That can be broken down into the following sub-issues:
>
> > (a) Issue 3(a) – whether there was any "requirement" of the Leases for IMSO to "provide" the Satellites.
> >
> > (b) Issue 3(b) – whether the fact that IMSO incurred launch costs before the terms of the Leases commenced failed to satisfy the "chronological flow" of s61(4).
> >
> > (c) Issue 3(c) – whether the "tailpiece" of s61(4) applied and, if so, with what consequence.

29. In order to obtain any capital allowances on the Satellites, Inmarsat needs to succeed on all of Issues 1, 2, 3(a) and 3(b)[2]. If it does succeed on those issues, questions of valuation arise. Both parties are agreed that those questions should, if necessary, be revisited if the determination of these issues means that Inmarsat is entitled to some capital allowances.

The Decision of the FTT

30. At [55] to [61] of the Decision the FTT, in deciding Issue 1 in favour of HMRC, decided that, there is an "implicit assumption" in s78 of CAA1990 to the effect that:

> … the provisions only apply where the assets in question actually belong (or, potentially, are deemed by some other provision to belong) to the successor after the succession.

31. Accordingly, in the FTT's judgment, whether or not s61(4) of CAA1990 deemed the Satellites to "belong" to the predecessor (IMSO), s78 did not apply to the Satellites because they did not belong to Inmarsat after that succession. That was enough for it to determine the application in HMRC's favour but having heard full argument, the FTT went on to consider Issues 2 and 3.

32. The FTT's conclusions on Issue 2 are set out at [63] to [67]. It considered the judgment of the House of Lords in *Barclay, Curle & Co Limited v Commissioners of Inland Revenue* 45 TC 221 in which it was held that certain costs of installation of plant could be treated as capital expenditure on the "provision" of plant for the purposes of a

[2] As we will explain, we do not consider that Issue 3(c) involves any separate point of disagreement between the parties.

trade. However, while acknowledging that the Satellites were entirely useless for their intended purpose until they had been launched into orbit, the FTT concluded that the launch costs at issue in these proceedings were not incurred on the "provision" of the Satellites for the purposes of s61(4) saying, at [66]:

> 66. I acknowledge Mr Prosser's argument that the Satellites were entirely useless for their intended purpose until they had been launched into orbit, however the question before me is whether IMSO incurred capital expenditure (in the form of the launch costs) "on the provision for the purposes of a trade carried on by [it] of machinery or plant…". Here I agree essentially with Mr Gibbon's argument. Any "provision of plant" must have at its heart the plant itself; simply moving someone else's plant from A to B (even if B is the place at which it is to operate in your trade, and however complex and expensive the process of movement may be) cannot in my view amount to the "provision" of that plant.

33. The FTT's analysis of Issue 3(a) was complicated by the fact that the terms of the leases of the I-2 Satellites were significantly different from those contained in the leases of the I-3 Satellites.

34. As regards the leases of the I-2 Satellites, Clause 6 of the Agreement to Acquire and Lease dated 28 September 1988, made between IMSO as lessee and NSM as lessor, required IMSO to use all reasonable endeavours to put the I-2 Satellites into a geosynchronous orbit. The FTT concluded, at [104], that that imposed a requirement, under the terms of the lease, for IMSO to incur the launch costs. However, the FTT concluded that this was not sufficient to amount to a requirement to "provide" the I-2 Satellites.

35. There was no similar express obligation present in the leases of the I-3 Satellites. At [101] to [104], the FTT rejected the following arguments that Inmarsat had raised to the effect that the necessary "requirement" for the purposes of s61(4) could be found in all or any of the following:

> (1) an obligation, imposed on IMSO pursuant to Clause 7.03 of the Master Lease Agreement dated 20 December 1991 to "satisfy all Pertinent Laws". One such requirement was for IMSO to operate on a sound economic and financial basis and IMSO would be in breach of this rule if it failed to launch the Satellites.
>
> (2) the requirement "as a practical matter" that the satellites be launched; or
>
> (3) a term to be implied into the various contracts.

36. For those reasons, the FTT decided Issue 3(a) in favour of HMRC.

37. At [111], the FTT dealt with Issue 3(b) saying:

> 111. S 61(4) starts by referring to a "lessee" incurring capital expenditure on the provision of machinery or plant, and it must be machinery or plant "which he is required to provide under the terms of the lease". It seems to me that there is a natural chronological flow about

> this provision, which necessarily implies that the lease must be in existence before the capital expenditure is incurred. This view is reinforced by the fact that the draftsman has felt it necessary, in s 61(8), to extend the provision so as to apply where there is an agreement for lease (but only where the agreed term of the lease has already begun), rather than an immediately effective lease. If Mr Prosser's argument were correct, this provision would effectively be unnecessary.

38. At [118], the FTT decided Issue 3(c), holding that the novations of the Leases that were effected when Inmarsat succeeded to IMSO's trade involved "determinations" of those Leases so as to engage the tailpiece to s61(4) saying:

> 117. … This is highly technical legislation and the draftsman would have been well aware of the legal effects of a novation. The effect of the novations was therefore to cause the "determination" of the leases; it follows that the effect of the tailpiece (if it were to apply) would be to effectively transfer the benefit of the capital expenditure from IMSO as lessee to the various lessors and this, it seems to me, is predicated on the assumption that the property actually belongs to the lessors (the deemed belonging in the earlier part of s 61(4) having been brought to an end as a result of the succession). To the extent the tailpiece applies, therefore, I consider it to be inconsistent with an essential implied pre-requisite of s 78(1) applying for the benefit of Inmarsat – namely that the Satellites should have belonged to it after the succession on 15 April 1999 (see [59] above).

Authorities on the interpretation of "deeming" provisions

39. Both parties agree that both s61(4) and s78 of CAA1990 are examples of "deeming provisions". While they do not agree on the scope and effect of those provisions, they both agree that the provisions treat particular circumstances as existing even if those circumstances do not exist in reality. For example, s78 treats a particular transaction as a "sale", even if it might not otherwise answer to that definition. Section 61 treats plant and machinery as "belonging" to a person, even where that might not otherwise be the case.

40. We did not understand the parties to differ materially on the correct approach to the construction of such deeming provisions. However, since Mr Gibbon devoted a good part of his oral submissions to an analysis of authorities in this area because he expressed disagreement with aspects of Inmarsat's approach, we will set out some conclusions of our own on how deeming provisions should be approached.

41. In *Szoma v Secretary of State for Work and Pensions* [2006] 1 AC 564, Lord Brown of Eaton-under-Heywood endorsed the following statement of principle set out in the then current 4th edition of Bennion on Statutory Interpretation:

> The intention of a deeming provision, in laying down a hypothesis, is that the hypothesis shall be carried as far as necessary to achieve the legislative purpose, but no further.

42. The difficulty that arises in this and in other cases is how to determine how far the hypothesis should be taken in any particular case. The modern approach is to focus on

a purposive construction of the statute, as exemplified by the following statement of Peter Gibson J (sitting as a judge of the Court of Appeal) in *Marshall (Inspector of Taxes) v Kerr* [1993] STC 360 at 366, which was approved by the Supreme Court in *HMRC v DCC Holdings (UK) Limited* [2010] UKSC 58:

> For my part, I take the correct approach in construing a deeming provision to be to give the words used their ordinary and natural meaning, consistent so far as possible with the policy of the Act and the purposes of the provisions so far as such policy and purposes can be ascertained; but if such construction would lead to injustice or absurdity, the application of the statutory fiction should be limited to the extent needed to avoid such injustice or absurdity, unless such application would clearly be within the purposes of the fiction. I further bear in mind that, because one must treat as real that which is only deemed to be so, one must treat as real the consequences and incidents inevitably flowing from or accompanying that deemed state of affairs, unless prohibited from doing so.

43. Obviously, the wording of the particular deeming provision under consideration will be central to an understanding of its "policy and purposes". However, it is also permissible in appropriate cases to draw on an understanding of the wider scheme of the Act of which it forms part. For example, in *HMRC v DV3 RS Limited Partnership v HMRC* [2013] EWCA Civ 907 the Court of Appeal rejected the taxpayer's argument on the scope of a deeming provision because it would have the consequence that, in the case under consideration, stamp duty land tax (SDLT) would "revert to being a tax on documents" whereas, in the judgment of the Court of Appeal, "the whole point of SDLT was to get away from a tax on documents and to replace it with a tax on land transactions".

44. Moreover, in deciding the scope of a deeming provision, it is important to bear in mind the obvious difficulties that Parliament has in prescribing the full extent of that deeming. As Neuberger J, as he then was, said in *Jenks v Dickinson (Inspector of Taxes)* [1997] STC 853 at 878:

> …[By] its very nature, a deeming provision involves artificial assumptions. It will frequently be difficult or unrealistic to expect the legislature to be able satisfactorily to [prescribe] the precise limit to the circumstances in which, or the extent to which, the artificial assumptions are to be made.

45. Finally in this regard, a deeming provision necessarily involves a statutory hypothesis that is at odds with the "real world". However, this does not mean that, when a deeming provision is engaged, the "real world" is irrelevant as the deeming provision must be applied to real world facts and circumstances. As Schiemann LJ observed in *Hoare v National Trust* (1998) 77 P&CR 366 in the context of the statutory "rating hypothesis" that applied in order to determine the rateable value of a non-domestic heriditament:

> The statutory hypothesis is only a mechanism for enabling one to arrive at a value for a particular hereditament for rating purposes. It does not entitle the valuer to depart from the real world further than the

> hypothesis compels. The Tribunal rightly accepted that in some respects it has to stay in the real world. It looked at the hereditament as it was; it took the actual assets of the actual tenant… into account.

46. We did not understand the general principles set out above to be in dispute between the parties. More controversial was the submission, contained in the skeleton argument of Mr Prosser on behalf of Inmarsat, to the effect that it may be necessary to apply a fiction set out in a deeming provision "further than … is necessary in order to give effect to the legislative purpose". That submission prompted Mr Gibbon to argue that there could never be any justification for applying a statutory fiction further than is "necessary".

47. We consider the difference between the parties was more apparent than real, however. We understood Mr Prosser to be saying no more than that the ultimate task is one of purposive construction. Giving effect to that statutory purpose might result in the fiction being taken further than might, at first sight, appear justified by the words used. But one is still bound only to go as far as is necessary, and no further.

Issue 1 - Discussion

48. The parties agree that the following preconditions to the application of s78 of CAA1990 were met:

(1) Inmarsat succeeded to a trade which IMSO had previously carried on;

(2) that trade was, by virtue of s337 of ICTA, treated as discontinued; and

(3) immediately before the Succession, the Satellites were in use for the purposes of IMSO's trade and immediately after the Succession, they were in use for the purposes of Inmarsat's trade.

49. Therefore, the parties' dispute on this Issue relates to the effect that s78 has on capital allowances associated with the Satellites. Inmarsat's central argument is that, since s78 deems the Satellites to have been "sold" to Inmarsat, it necessarily follows from that deeming that they "belong" to it, so that Inmarsat can obtain allowances under s24 of CAA1990.

50. The obvious objection to Inmarsat's argument is that s78 says nothing express about whether the successor satisfies the "belonging" requirement. Moreover, in deeming the transaction to be a "sale" and in specifying the "net proceeds" of that sale, s78 appears to be focusing on the disposal event to be brought in for the predecessor, rather than the tax treatment of the successor. However, Inmarsat argues that any such initial impression is dispelled by an appropriately close reading of s78, having regard both to its overall purpose and the scheme of the capital allowances legislation. It makes the following arguments in support of its approach:

(1) Read closely, s78 is not concerned with the capital allowances of the predecessor <u>at all</u>. Section 78 applies only where the predecessor discontinues a trade. That discontinuance itself triggers a disposal event under s24(6)(c)(v) of CAA1990. The disposal value to be brought into account on the occurrence of that discontinuance is the market value of the

relevant plant and machinery (see s26(1)(f) of CAA1990). That is precisely the result specified by s78. Accordingly, since s78 has nothing new to say about the position of the predecessor, it must follow that it is concerned only with the position of the successor, with its purpose being to put the successor into the predecessor's shoes in respect of property that continues to be used in the trade.

(2) The closing words of s78(1), "but no first-year allowances shall be made by virtue of this subsection" demonstrate that capital allowances are intended to be available "by virtue of" s78(1), albeit that this treatment does not extend to first-year allowances which are given to encourage expenditure on plant and machinery newly brought into use in the trade.

(3) The deeming in s78(1) is that the plant and machinery "shall, for the purposes of this Part, be treated as if it had been sold to the successor". The inevitable and intended corollary of this is that it should "belong" to the successor.

(4) There is no policy reason why Parliament would have intended that only plant and machinery that "belongs" to the successor should be treated as sold to that successor. Section 78 concerns a situation where a predecessor is required to bring into account a disposal value equal to the market value of plant and machinery, and the plant and machinery continues to be used for the purpose of the trade (albeit carried on by the successor rather than the predecessor). In those circumstances, it makes perfect sense that allowances should continue to be available to the successor.

51. We do not accept Inmarsat's first argument summarised at paragraph 50(1). We are prepared to accept that, in certain circumstances, the treatment of the predecessor prescribed by s78(1) might be produced by a combination of s24 and s26 even if it were not separately spelled out in s78. But even if s78 does duplicate the effect of other provisions, it does not follow that s78 has nothing to say about the tax position of the predecessor. Section 78 provides an "at a glance" summary of important aspects of the predecessor's treatment for capital allowances purposes by using phrases that resonate for the purposes of determining the predecessor's disposal value. By treating the transaction as a "sale", and fixing the "net proceeds", the provisions of s26(1)(a) of CAA1990 are engaged so as to determine the amount of disposal value to be brought into account by the predecessor. Accordingly, s78 resolves any doubt that might otherwise have existed as to the predecessor's tax position by spelling out (i) the nature of the disposal event relevant to the predecessor, (ii) the time at which that disposal event takes place and (iii) the disposal value to be brought into account.

52. We do not consider that the closing words of s78(1), which form the basis of Inmarsat's second argument, set out at paragraph 50(2), shed any significant light on the issue. Parliament was clearly concerned to ensure that a successor to a trade would not obtain first-year allowances on plant and machinery that it acquired as part of that succession. However, that concern would arise equally on HMRC's interpretation of s78(1) under which the provision is engaged only in relation to assets that belong to a predecessor before a succession and to a successor afterwards. We therefore consider that the closing words of s78(1) are entirely consistent with Parliament having a purpose

of denying the successor entitlement to first year allowances which it might otherwise have obtained as a result of obtaining actual ownership of the assets in question.

53. We will take Inmarsat's arguments set out at paragraph 50(3) and paragraph 50(4) above together. We agree with Inmarsat that deeming property to be "sold" to a person is capable of carrying with it a deeming that the property is to "belong" to that person. However, we do not consider that to be an "inevitable" consequence. The relevant question is whether, having due regard to the purpose of s78, and the statutory scheme of which it forms part, Parliament intended the deeming provision to extend as far as treating Inmarsat to be the owner of the Satellites, even though it did not actually own them.

54. In this regard, we consider that HMRC are correct to emphasise the point that, if s78(1) were intended to establish a deemed "belonging" of plant and machinery, in the absence of a real "belonging", it might have been expected to deal with further matters such as when the deemed belonging comes to an end and what is to happen when it does. Yet s78 does not address such points. That is in contrast with other provisions that deem machinery to belong to someone other than the real owner. For example, the tailpiece to s61(4) prescribes what is to happen when the relevant lease is terminated. The "contributions" code in s154 and s155 of CAA1990 treats a person who contributes to another's capital expenditure on plant and machinery as having an entitlement to allowances and as satisfying the "belonging" condition. That code stipulates, in s155(3) what is to happen on a transfer of the contributor's trade.

55. Inmarsat argues that it is not necessary for s78 to deal with the future since the ordinary provisions set out in s24 and s26 of CAA1990 can apply to the deemed belonging established by s78. We do not accept that submission. To take an obvious example, suppose that after the Succession, Inmarsat had sold its entire business for market value in cash. The scheme of the legislation would suggest that Inmarsat should not be entitled to continue to claim capital allowances on the Satellites. But it is not straightforward to derive that result from the provisions of s24 and s26. Even the conclusion that there is a disposal event under s24(c)(i) of CAA1990 on the grounds that the Satellites "ceased to belong" to Inmarsat would not be entirely secure as Inmarsat's ownership would only be deemed to exist for tax purposes and it is not obvious how Inmarsat's sale of its "actual" assets would necessarily bring to an end its ownership of deemed assets. Moreover, there would be difficulties in fixing the amount of disposal value to be brought into account. Logic suggests that the disposal value should be calculated by reference to deemed market value (since Inmarsat, not having actually sold the Satellites, could not attribute any part of the actual purchase price received to the Satellites). But if the "real" sale was at market value, Inmarsat's disposal value would be fixed by s26(1)(a) by reference to proceeds that it actually receives. If none of the actual proceeds are referable to the Satellites, it is not obvious to see how the legislation could produce a sensible disposal value in relation to the Satellites.

56. We quite acknowledge Inmarsat's submission that it might have made sense in policy terms for s78 to provide that, if IMSO had been entitled to allowances under s61(4) in relation to assets deemed to belong to it, Inmarsat would step into its shoes following the Succession. But the question is not whether such a result would have

made sense in policy terms; rather the issue is whether that is the result for which Parliament has legislated. Given the points we have made above, we do not consider that Parliament has legislated for such an outcome. Rather, we prefer HMRC's interpretation of s78 to the effect that the section has no application in relation to a successor such as Inmarsat unless it becomes the actual owner of the relevant asset with s78 fixing, in such a case, the amount of expenditure on which the successor can claim plant and machinery allowances.

57. Having reached that conclusion, we do not need to address other points of detail arising in relation to Issue 1 namely, if s78(1) did deem the Satellites to belong to Inmarsat:

> (1) whether s78(1) deemed Inmarsat to incur expenditure on the Satellites' provision, wholly and exclusively for the purposes of its trade (without which the requirements of s24(1)(a) of CAA 1990 would not be satisfied); or
>
> (2) whether s78(1) deemed the Satellites to "continue to belong" to Inmarsat.

58. As regards the first issue, we will say only that the fact that s78(1) is silent as to whether a successor is deemed to have incurred expenditure wholly and exclusively for the purposes of its trade reinforces us in our conclusion that the section is concerned with a situation where a successor becomes the actual owner of an asset. That enables the "purpose" of the successor's expenditure to be ascertained by reference to the successor's purpose in acquiring an actual asset. As regards the second issue, we tend to agree with Inmarsat that there is no requirement, in order for allowances to be claimed that an asset should "continue" to belong to a person. Rather, as Inmarsat observes, allowances are available, by virtue of s24(1)(b) of CAA1990 in a situation where machinery or plant "belongs or has belonged" to a person. If the asset ceases to belong, then a disposal event occurs, but that is not the same as saying that the plant or machinery never qualified for allowances.

59. Nor, given our conclusion on Issue 1 is it strictly necessary for us to consider Issues 2 and 3 since, as we have noted above, Inmarsat's failure on Issue 1 means that its appeal as a whole must fail. However, since we heard full argument on all issues, we will go on to express our conclusions on these other issues, although our reasoning is more abbreviated than it would be if the appeal hinged on their outcome.

Issues 2 and 3 – "Purposive construction"

60. Issues 2 and 3 both focus on the correct construction, and application, of s61(4) of CAA1990. Both parties were rightly agreed that s61(4) should, like all statutory provisions, be construed having due regard to its purpose. However, while both parties sought to provide examples of situations in which s61(4) might apply, neither party was able to provide any satisfactory explanation of the underlying overall policy behind it.

61. In a narrow sense, of course, the purpose of s61(4) can be understood as treating a person as the owner of an asset, if particular conditions are satisfied, where that person

is required to provide that asset under the terms of a lease. But that is simply to recite the words of the statutory provision. It does not explain why persons who are required to provide an asset under the terms of a lease should enjoy the privilege of being treated as owning that asset for capital allowances purposes. It does not explain whether Parliament had in mind, when enacting the earliest predecessor of s61(4), a particular kind of situation as deserving of special treatment.

62. It follows that we have been unable, in determining this appeal, to derive as much assistance from submissions on the policy or purpose of s61(4) as we might have hoped. That is not to criticise the parties or their representatives. The original version of s61(4) must have been enacted many decades ago and we are sure that much time and effort has been spent on both sides going back through old legislation with a view to divining its purpose. Later in this decision, we will explain how the absence of a clearly articulated purpose or policy behind s61(4) has affected our decision on specific points of construction that were in issue.

63. That said, there was some measure of agreement between the parties on the construction of s61(4). Both parties agree that, given the inclusive definition of "lease" in s61(8), the "lease" in question could be a lease of chattels, or a lease of real estate although HMRC contend that the definition in s61(8) with its references to land law concepts is more concerned with leases of land.

Issue 2 - Discussion

64. For the purposes of Issue 2 it was common ground that the launch costs that IMSO incurred represented capital expenditure and, when the Satellites were operating and in use, they were "plant" in relation to IMSO's trade. Issue 2, therefore, is concerned with the question whether IMSO incurred the launch costs on "the provision for the purposes of a trade … of machinery or plant" within the meaning of that phrase in s61(4) of CAA1990.

65. We were not referred to any authority in which this phrase has been considered in the context of s61(4). However, there are authorities on the meaning of similar phrasing that appears in predecessor legislation to that contained in s24 of CAA1990.

66. We have already referred to the judgment of the House of Lords in *Barclay-Curle.* In that case, the taxpayer carried on a trade of shipbuilding and repairs. For the purposes of that trade, the taxpayer (i) excavated a large quantity of earth and rock, (ii) lined the resulting hole with concrete and (iii) installed a dock gate and pumps to form a dry dock. The House of Lords held, by a majority of 3 to 2, that the dry dock was "plant". That meant that the taxpayer was entitled to capital allowances on expenditure incurred on the "provision of" the dry dock under the provisions of s279 of the Income Tax Act 1952 which at the time governed entitlement to allowances and the question arose whether this extended to the costs of "making room" for that dry dock.

67. At 239I to 240B, Lord Reid said:

> So the question is whether, if the dock is plant, the cost of making room for it is expenditure on the provision of plant for the purposes of the trade of the dock owner. In my view, this can include more than the cost of the plant itself, because plant cannot be said to have been provided for the purposes of a trade until it is installed: until then it is of no use for the purposes of the trade. This plant, the dock, could not even be made until the necessary excavating had been done. All the Commissioners say in refusing this part of the claim is that this expenditure was too remote from the provision of the dry dock. There, I think they misdirected themselves. If the cost of the provision of plant can include more than the cost of the plant itself, I do not see how expenditure which must be incurred before the plant can be provided can be too remote.

68. Lord Guest said, at 245G:

> The Commissioners upheld the contention of the Crown … that the expenditure was "too remote" from the provision of the dry dock. In my view they were wrong in excluding this expenditure. The excavation was a necessary preliminary to the construction of the dry dock and in my view was covered by the provision of plant under s279. "Provision" must cover something more than the actual supply. In this case it includes the excavation of the hole in which the concrete is laid.

69. Lord Donovan also agreed that the expenditure on excavation was "on the provision of … plant". Lord Upjohn and Lord Hodson expressed no view on the matter since they were in the minority who did not consider that the dry dock was "plant" at all.

70. In *Ben-Odeco Ltd v Powlson* [1978] 1 WLR 1093, the House of Lords held by a majority of 4 to 1 that financing costs that the taxpayer paid under loans taken out to fund the acquisition of an oil rig did not amount to capital expenditure on the provision of plant and machinery for the purposes of s41 of the Finance Act 1971.

71. In the course of argument, their Lordships were taken to provisions of Canadian statute law under which allowances were available on the "capital cost to the taxpayer of property" and it had been held that this extended to financing costs. Lord Wilberforce (in the majority), however, concluded that the Canadian and UK statutes had a different scope saying at 1097H:

> The expression "capital cost to the taxpayer" makes it easier to include within deductible expenditure costs which the particular taxpayer incurs, whereas the UK words, more objectively, focus on expenditure directly related to the plant. The one draws a line round the taxpayer and the plant; the other confines the limiting curve to the plant itself.

72. At 1098B to E, Lord Wilberforce expanded on the scope of the UK statute. He observed that it would be undesirable for a taxpayer who finances an acquisition of plant and machinery out of its own resources to obtain a different measure of allowances from a taxpayer who borrows money. Accordingly, an interpretation of the statute that introduces a large element of subjectivity by reference to a taxpayer's individual circumstances was to be avoided. He said:

> The words "expenditure on the provision of" do not appear to me to be designed for this purpose. They focus attention on the plant and the expenditure on the plant – not limiting it necessarily to the bare purchase price, but including such items as transport and installation, in any event not extending to expenditure more remote in purpose.

73. Lord Russell, also in the majority, phrased the test as follows, at 1106G:

> In my view the question to be asked is, what is the effect of particular capital expenditure? Is it the provision of finance to the taxpayer or the provision of plant to the taxpayer? In my opinion the effect of the expenditure was the provision of finance and not the provision of plant. I would add that I do not seek to confine qualifying capital expenditure to the price paid to the supplier of the plant. I should have thought, for example, that if the cost of transport from the supplier to the place of user is directly borne by the taxpayer it would be expenditure on the provision of plant for the purposes of the taxpayer's trade.

74. Pausing there, if IMSO had been the owner, rather than merely a lessee of the Satellites, we do not consider that there could be much doubt that the launch costs it incurred would have been "expenditure on the provision of" the Satellites given the FTT's finding that the Satellites were of no use whatsoever until they were launched into orbit.

75. HMRC, however, argue that the fact that the Satellites did not belong to IMSO makes all the difference. In their submission, since IMSO did not incur the "core" expenditure of "providing" the asset (namely the costs of acquisition), the launch costs that it did pay were simply "ancillary" or "freestanding" expenditure. HMRC supported the FTT's conclusion that, without ownership of the Satellites, IMSO had simply paid to move "someone else's plant from A to B" and that this could not involve expenditure being incurred on the "provision" of the Satellites.

76. In effect that argument involves an assertion that IMSO's status as a person who did not own the Satellites converted expenditure that would, if incurred by an owner, have been on the "provision" of those Satellites into expenditure that was not on provision. That involves a focus on IMSO rather than on the nature of the expenditure, contrary to Lord Wilberforce's approach as set out in *Ben-Odeco*.

77. In his oral submissions, Mr Gibbon rightly noted that the word "provision" should not be read in isolation as s61(4) is concerned with whether expenditure is incurred "on the provision for the purposes of a trade … of machinery or plant". He argued that the focus should, accordingly, be on the specific plant and machinery. However, we do not consider that this wider context alters the conclusion we have expressed at paragraph 76 above. Lord Russell in *Ben-Odeco* held that the focus should be on the effect of particular capital expenditure and not on the particular attributes or circumstances of the person incurring the expenditure. If the launch costs would have had the necessary effect if incurred by an owner of the Satellites, we see no reason why, in the context of authorities on statutory predecessors to s24, it should be deprived of that effect when incurred by someone other than an owner.

78. Mr Gibbon also argued that in order to amount to expenditure on the provision of plant and machinery, there must be some sort of nexus between the incurring of expenditure and the plant and machinery "belonging" to that person. We do not, however, consider that approach to be supported by authorities. The decision of the House of Lords in *Barclay-Curle* was given in the context of statutory provisions that contained no belonging requirement. We do not, therefore, consider that the House of Lords had any concept of "belonging" in mind when they determined that expenditure on the installation of plant and machinery was expenditure on the "provision" of that plant and machinery.

79. Therefore, our interpretation of the authorities on predecessors to s24 of CAA1990 is that the launch costs would involve expenditure on the provision of the Satellites for the purposes of those provisions. We acknowledge that under the CAA1990 regime, with its "belonging" requirement, a person who incurred what HMRC refer to as "free-standing" expenditure on the costs of transporting plant and machinery which it does not own would not be entitled to capital allowances under s24. However, that is because such a person would not be able to satisfy the requirements of s24(1)(b), rather than because the expenditure is not on the provision of plant and machinery. That difficulty does not trouble Inmarsat in this case because, as Mr Prosser observed, if s61(4) applies, then the Satellites would be deemed to belong to IMSO.

80. Thus far we have confined our attention to the concept of capital expenditure on the provision of plant and machinery as it has been analysed for the purposes of statutory predecessors to s24 of CAA1990. HMRC's submissions also focused on what they considered would be the unworkable and absurd effects if s61(4) specifically was capable of applying to someone like IMSO who incurred free-standing launch costs. Mr Gibbon's skeleton argument stated that while HMRC maintained the position that "provide" and "provision" have the same meaning in s61(4) as in s24, nonetheless "there are nuances depending on context". It seems to us that HMRC must be arguing for some different interpretation of "provide" and "provision" in the context of s61(4), if only because the difficulties that they highlighted were not argued to arise in relation to s24.

81. HMRC's first argument was that absurd consequences would arise if IMSO's free-standing expenditure on launch costs triggered an application of s61(4). Section 61(4) could not be applying to deem the plant and machinery to belong both to IMSO and to the Lessors because, as HMRC put it in their skeleton argument, on Inmarsat's approach:

> …there are two persons treated as full owners of a single asset and able to claim allowances on it.

82. We do not accept that submission. Inmarsat's interpretation would not entitle IMSO (had it been subject to corporation tax) to claim capital allowances on the price that the Lessors paid to acquire the Satellites. IMSO had not incurred that expenditure and so could never claim capital allowances on it, even if the Satellites were deemed to belong to IMSO. Similarly, even though the Satellites actually belonged to the Lessors, they could not claim capital allowances on the launch costs, since they had not actually incurred them.

83. In a similar vein, HMRC submitted that s61(4) did not operate to create ownership of a part or share in the plant and machinery. It either deemed the plant and machinery to belong (exclusively) to the lessee, or it did not. In other places, such as the contributions code set out in s154 and s155 of CAA1990, where the capital allowances code deals with real or deemed division of an asset, it did so expressly. Outside those situations, the capital allowances code identifies a single owner. HMRC argue that since s61(4) contains no mechanism to ascertain the comparative extent of each person's ownership of the relevant plant, that was a strong indication that it did not envisage any deemed division of ownership of the kind for which Inmarsat argues.

84. If the parties had been able to provide some analysis of the purpose or policy behind s61(4), that would have put us in a better position to assess the force of this submission. However, in the absence of such an analysis, we consider that there are difficulties with this submission:

(1) As we have noted, no "division of ownership" is needed to make s61(4) workable, at least insofar as the obtaining of allowances prior to a disposal event is concerned. It is quite straightforward to interpret s61(4) as enabling a lessee to claim allowances on the expenditure it has incurred on the "provision" of the asset (with the assistance of a deemed satisfaction of the belonging condition) and for the lessor, if it is also the actual owner of the asset, to claim allowances on any expenditure it has incurred on provision.

(2) We agree with HMRC that matters become much more complicated on a disposal of the asset. If there is a sale of the asset, for example and both lessor and lessee have been claiming allowances on the expenditure that they have respectively incurred, s61(4) contains no mechanism spelling out the effect of that sale. In such a case, the lessor being the "real owner" would no doubt receive the "real" disposal proceeds, but s61(4) leaves unanswered the question whether the lessor would need to bring into account the entirety of the resulting disposal value, or whether some of the disposal proceeds should be treated as received by the lessee, so as to result in the lessee bringing into account a disposal value as well. Still less does the legislation contain any mechanism for apportioning the disposal values.

(3) We acknowledge that, conceptually, this lacuna in the legislation might indicate that Parliament did not intend s61(4) to result in a "division of ownership". But the force of that point is significantly diminished by the fact that a similar lacuna exists in the "contributions code" contained in s154 and s155 CAA1990 which quite clearly is intended to result in a division of deemed ownership[3]. HMRC and Inmarsat put forward different analyses of how the lacuna might be resolved in the context of s154 and s155 by reference to the situation where a contributor, C, contributes 50 to a recipient, R, who acquires plant and machinery for 100 with the plant and

[3] Section 154 deals with a situation where one person (a contributor) makes a contribution to expenditure incurred by another (the recipient). Section 154(2) treats the asset in question as belonging both to the contributor for as long as it is owned by the recipient. It therefore explicitly envisages a case where two distinct persons are treated as the owner of an asset.

machinery subsequently being sold for 50, or C subsequently ceasing to trade. We do not need to determine which party's analysis of these various situations was correct. The fact that neither s154 nor s155 offered any guidance as to how relatively straightforward situations as this should be analysed suggests to us that the capital allowances code contains at least one other instance where the consequences of deemed co-ownership are not fully spelled out. It follows that we attach little weight to HMRC's argument to the effect that the presence of this lacuna in s61(4) indicates that Parliament cannot have intended it to result in deemed co-ownership of an asset.

(4) Moreover, once it is accepted that s61(4) applies to leases of chattels, it is difficult to think of a real-world situation where s61(4) would wish to treat the lessee's ownership as being exclusive. Of course, if the lessee incurred all of the expenditure on provision of the asset, it might make sense for the lessee alone to be treated as the owner. But it is difficult to see how such a situation could ever come within s61(4) since it is not obvious why a person who has provided all of the expenditure on the asset would then agree to lease it from another.

85. Accordingly, HMRC's arguments as to the presence of anomalies have not persuaded us that the term "capital expenditure … on the provision … of machinery or plant" in s61(4) of CAA1990 should be construed any differently from similar phrasing in statutory predecessors to s24. Given our conclusions on the effect of that wording in predecessors to s24, we determine Issue 2 against HMRC.

Issue 3(a) – Discussion

86. Issue 3(a) involves two distinct questions:

(1) First, in relation to the I-3 Satellites, whether IMSO was "required" under the terms of the relevant Leases to procure the launch of the Satellites. (HMRC do not challenge the FTT's conclusion that there was such a "requirement" in relation to the I-2 Satellites).

(2) Second whether any "requirement" to procure the launch of the Satellites was sufficient to amount to a "requirement to provide" the Satellites for the purposes of s61(4).

Whether IMSO was required to procure launch of the I-3 Satellites

87. Clause 7.03 of the Master Lease Agreement between the applicable Lessor and IMSO relating to the I-3 Satellites provided that IMSO:

> …shall satisfy the requirements of all Pertinent Laws.

88. "Pertinent Laws" were defined in Clause 1 as including "Applicable Laws" which, in turn included the Convention. Article 5.3 of the Convention provided as follows:

> The Organization [i.e. IMSO] shall operate on a sound economic and financial basis having regard to accepted commercial principles.

89. Inmarsat makes the following arguments in support of its contention that it was, for the purposes of s61(4), required to launch Satellites under the terms of the Leases of the I-3 Satellites:

> (1) IMSO owed a contractual duty to the relevant Lessor to operate on a sound economic and financial basis having regard to accepted commercial principles.
>
> (2) IMSO would have been in breach of that contractual obligation if, having entered into launch contracts that obliged it to pay significant sums for the launch of the I-3 Satellites, it had decided not to launch them. Inmarsat acknowledges that it only became party to the Leases after it entered into the launch contracts. But it argues there is no reason why s61(4) should take a snapshot of IMSO's obligations under the Lease only at the very moment that Lease was signed.

90. HMRC's first objection is that Clause 7.03 of the Master Lease Agreement is a generalised obligation, which imposes no requirement to launch any particular satellites. If this submission had been supported by a clear examination of the purpose and policy behind s61(4) affording a beneficial treatment to persons "required" to provide plant and machinery under the terms of a lease, we might, depending on that purposes and policy, have concluded that a general obligation such as Clause 7.03 was insufficient. However, in the absence of any such analysis of purpose and policy, we simply have the words of s61(4) to guide us. If, as Inmarsat submits, IMSO would have been in breach of the Master Lease Agreement if it had not launched the Satellites, we consider that, as a matter of ordinary English, it could be said to be "required" to launch the Satellites, whether Clause 7.03 is expressed in general or specific terms.

91. HMRC relied on the decision of the Court of Appeal in *Ennstone v Stanger* [2002] 1 WLR 3059 in support of their argument that a generalised "requirement" was not enough. The case concerned whether, for the purposes of Article 4(2) of the Rome Convention on the Law Applicable to Contractual Obligations (1980), contractual performance was to be effected "under the terms of contract" in Scotland or in England. The court concluded that, even though the parties may have anticipated that performance would be effected in Scotland, that was not sufficient for performance to be effected in Scotland "under the terms of the contract" in the absence of an express or implied term requiring performance in Scotland.

92. We regard this authority as being of little assistance to the determination of Issue 3(a). Although there is some similarity between the wording of s61(4) and Article 4(2) of the Rome Convention, with both provisions focusing on whether something is required "under the terms of" a contract or lease, the two provisions are markedly different. Moreover, in this case, Inmarsat is not arguing simply that the parties merely "anticipated" that the Satellites would be launched. Rather, it says that, if they had not been launched, IMSO would have been in breach of a contractual obligation.

93. We accept Inmarsat's submission that, if the I-3 Satellites had not been launched, IMSO would have been in breach of its obligations under the applicable Lease for the following reasons:

(1) The focus of s61(4) is on whether IMSO was "required to provide [the Satellites] under the terms of the Lease". We see no reason why any contractual obligation to procure launch of the Satellites should be discounted simply because it was not in existence at the very moment the Leases were signed[4]. Put another way, if there is a "requirement", s61(4) makes no stipulation as to the point in time at which that requirement must come into existence.

(2) HMRC object that Inmarsat have not pointed to any "requirement" to launch the I-3 Satellites themselves, as distinct from obligations in relation to satellites generally. They also argue that there were circumstances in which IMSO could properly have decided not to proceed with the launch of the Satellites as it is possible for businesses operating on a sound economic and financial basis to write off expenditure that they have already incurred. But that is to ignore the reality of what actually happened. Perhaps in the early days of the launch contracts, something might have happened that would have entitled, or required, IMSO to abandon those contracts and either replace them with different contracts, or decide to launch no I-3 Satellites at all. However, the I-3 Satellites were ultimately launched under those contracts, so a point must have come at which it would have made no commercial sense for IMSO to decide not to launch. At that point, whenever it came, IMSO would have been in breach of Clause 7.03 if it had not launched the I-3 Satellites.

(3) Next HMRC argue that IMSO was under an obligation to comply with the Convention anyway. We do not consider that this makes any difference: s61(4) simply asks whether a particular "requirement" is present under the terms of the applicable lease. Once such a requirement is found, s61(4) contains no suggestion that it is not to count if it also forms part of other obligations, whether contractual, statutory or otherwise.

(4) We are reassured in the above analysis by considerations of commercial common sense. The Leases clearly envisaged that both IMSO and the Lessors would enjoy commercial benefits from the provision of the I-3 Satellites. Yet if those Satellites were never launched IMSO would not be able to derive revenue from them and so would not be able to use that revenue to pay the Lessors their rent. In those circumstances, it would be surprising indeed if IMSO could, without breaching its contract with the Lessors, decide not to launch the I-3 Satellites at all.

94. Having reached that conclusion, we do not need to address the other ways in which Inmarsat argued that the necessary "requirement" could be deduced.

[4] As Issue 3(b) we consider the separate issue of whether it matters that IMSO incurred expenditure on launch costs before the term of the relevant Leases began.

Was the requirement "to provide plant and machinery"?

95. HMRC argue that, even if there was a "requirement", it was only a requirement to procure launch services; not a requirement on IMSO to "provide" plant and machinery as required by s61(4).

96. Our conclusion on Issue 1 means that expenditure incurred on launching the Satellites was expenditure on the "provision" of those Satellites. It follows that the requirement imposed on IMSO to launch the Satellites was a requirement to "provide" those Satellites.

97. We do not consider that it makes any difference that IMSO paid third parties to launch the Satellites as opposed to launching them itself. The House of Lords in *Ben-Odeco* noted that expenditure on transporting or installing plant was an example of expenditure on the "provision" of that plant. Their Lordships did not limit that conclusion to situations where the trader itself transports the plant and we see no reason why such a limitation should be imposed for the purposes of s61(4)(a) of CAA1990.

98. Accordingly, had it been necessary to determine Issue 3(a), we would have determined that issue in favour of Inmarsat.

Issue 3(b) - Discussion

99. It was common ground that IMSO incurred the expenditure on launch costs relating to both the I-2 Satellites and the I-3 Satellites after it became party to Leases of those Satellites but before the term of those Leases commenced following the Satellites' successful launch into geosynchronous orbit. HMRC that this brought IMSO's expenditure on launch costs outside the scope of s61(4) for two broad reasons[5]:

> (1) Section 61(4) requires that the relevant taxpayer must be a "lessee" when the expenditure is incurred. That condition cannot be satisfied if the relevant lease has not commenced at that point.
>
> (2) The way that agreements for lease are dealt with in s61(8) emphasises this requirement. The definition of "lease", includes an agreement for lease, but only "where the term to be covered by the lease has begun". That brings within the scope of s61(4) expenditure that would have been "under" the lease but for a delay in the lease's execution and emphasises the temporal requirement imposed by s61(4).

100. These arguments found favour with the FTT, but we respectfully disagree with the FTT's conclusion. In our judgment, the focus in s61(4)(a) is on whether the necessary requirement "under the terms of the lease" is present. The section does not make any express provision as to when that requirement must be honoured. As we have noted, it is not at all clear why Parliament wished to make special provision for persons required to provide plant and machinery under the terms of the lease. However, having done so

[5] We have, in our discussion of Issue 3(a), already addressed HMRC's related argument that any contractual "requirement" to provide the plant and machinery must be present at commencement of the lease in order to count for the purposes of s61(4).

it is not obvious why Parliament would have wished persons who incur expenditure before their lease has begun to be in a different position from persons who incur their expenditure afterwards.

101. We also agree with the interpretation of s61(8) that Inmarsat put forward. Parliament recognises that leases are often preceded by agreements for lease (particularly in the context of real estate transactions). Accordingly, an agreement for lease can be a source of a "requirement" to provide plant and machinery as well as the lease itself. However if, a requirement is imposed in an agreement for lease but for whatever reason, no lease is ever granted, Parliament did not wish the obligation in the agreement for lease to count. That is achieved by providing that an agreement for lease is only within the scope of s61(8) where it culminates in the grant of an actual lease. Accordingly, in using the phrase "where the term covered by the lease has begun", s61(8) is not emphasising the presence of any "temporal flow". Rather, the word "where" should be understood as meaning "in a situation where".

102. We determine Issue 3(b) in favour of Inmarsat.

Issue 3(c) – Discussion

103. The Succession involved the Leases being novated which, as a matter of law involved the Leases between the Lessors and IMSO being terminated in consideration of the creation of new Leases, between the Lessors and Inmarsat. That, argue HMRC, resulted in a "determination" of the original Leases between IMSO and the Lessors so as to engage the tailpiece to s61(4). Inmarsat denies that the novation of the Leases involved their "determination" since the Leases continued in force, albeit as between different parties.

104. Given our conclusions on the other Issues, we do not consider that Issue 3(c) needs to be determined. In their skeleton argument, HMRC acknowledged that the tailpiece to s61(4) could not have any bearing on whether the Satellites were deemed to belong to IMSO immediately before the Succession. Accordingly, HMRC do not seek to argue that the tailpiece caused IMSO to fail a "belonging" condition immediately before the Succession so as to prevent s78 from applying. We consider that HMRC were correct not to pursue such an argument, not least because the tailpiece says nothing at all about who plant and machinery "belongs" to; rather, it focuses on who is treated as incurring capital expenditure.

105. Therefore, it seems to us that ultimately the reliance that HMRC placed on the tailpiece to s61(4) was limited. In essence, HMRC were arguing that the tailpiece shows that, in s61(4), Parliament considered carefully what was to happen following an occasion of deemed ownership and concluded that this deemed ownership should not, as Mr Gibbon put it in his oral submissions, result in allowances "rolling forward indefinitely". Therefore, argue HMRC, if Parliament had intended s78 to result in deemed satisfaction of a belonging condition it would have given similar detailed consideration to the question of when such deemed belonging was to come to an end. The absence of any such consideration points, in HMRC's submission, to a conclusion

that s78 was not, after all, intended to result in the belonging requirement being treated as satisfied.

106. We have already considered arguments to similar effect in our conclusion on Issue 1. Accordingly, given the way in which HMRC seek to rely on the tailpiece to s61(4), we do not consider that we need to decide the question of whether the novation of the Leases was a "determination" for the purposes of that tailpiece and we will not do so.

Disposition

107. The FTT was correct to determine Issue 1 in favour of HMRC. For that reason, while we respectfully disagree with the FTT's determination of Issues 2, 3(a) and 3(b), that does not alter the outcome. Inmarsat's appeal is dismissed.

Signed on original

MR JUSTICE ADAM JOHNSON
JUDGE JONATHAN RICHARDS

RELEASE DATE: 23 March 2021