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**UT/2021/000023**
Hearing Venue: **Royal Courts of Justice,**
**Rolls Building, Fetter Lane, London**
Heard on: 10 May 2022
Judgment Date: 4 August 2022

**Upper Tribunal**
**(Tax and Chancery Chamber)**

**Before**

**MRS JUSTICE FALK**
**JUDGE THOMAS SCOTT**

**Between**

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

**Appellants**

**and**

**DOLPHIN DRILLING LIMITED**

**Respondent**

**Representation:**

For the Appellants: Christopher McNall, Counsel, instructed by the General Counsel and Solicitor to HM Revenue and Customs

For the Respondent: Nicola Shaw QC, instructed by Ernst & Young LLP

DECISION

## Introduction

1. This is an appeal by the Commissioners for Her Majesty's Revenue & Customs ("**HMRC**") against a decision of the First-Tier Tribunal ("**FTT**") (Judge Jeanette Zaman and Mr Duncan McBride) released on 16 November 2020 (the "**Decision**").

2. Dolphin Drilling Limited ("**DDL**") provided vessels by way of bareboat charter to operators in the oil and gas industry. DDL chartered a vessel called the Borgsten Dolphin (the "**Borgsten**") from an associated entity, Borgsten Dolphin Pte Ltd ("**BDPL**"), to fulfil a contract with the operator Total E&P (UK) Limited ("**Total**") in connection with drilling activities at the Dunbar oil platform (the "**Dunbar**"). The Borgsten had initially been a semi-submersible drilling rig but was converted into a tender support vessel ("**TSV**") to meet Total's requirements. The contract negotiated between DDL and Total is referred to in the Decision, and below, as the "**Total Contract**".

3. HMRC concluded that the deductions claimed by DDL in computing its profits for corporation tax purposes in respect of amounts paid for the hire of the Borgsten should be restricted. This was on the basis that the Borgsten was a "relevant asset" within the meaning of Part 8ZA of the Corporation Tax Act 2010 ("**CTA 2010**"), set out below. HMRC issued the following closure notices:

   (1) on 15 January 2018 HMRC amended DDL's tax return for the year ended 31 December 2014 so as to increase its taxable profits by $21,909,895, giving rise to an additional liability to corporation tax of £3,034,129. The quantum of the amendment was subsequently increased to £4,039,309.26; and

   (2) on 21 October 2019 HMRC amended DDL's tax return for the year ended 31 December 2015 so as to increase its taxable profits by $20,340,976, giving rise to an additional liability to corporation tax of £2,691,385.73.

4. DDL appealed to the FTT against the closure notices on the basis that the Borgsten was not a "relevant asset". The FTT allowed DDL's appeal.

5. HMRC now appeal with the permission of the FTT on two grounds, having been refused permission to appeal on two further grounds by both the FTT and this Tribunal. HMRC contend that the FTT (i) applied an incorrect legal test in interpreting the relevant legislation; and (ii) took an incorrect approach when interpreting the Total Contract.

## The statutory regime

6. Part 8ZA of CTA 2010 was inserted by the Finance Act 2014, with effect from 1 April 2014. Part 8ZA applies to "oil contractor activities". The legislation operates by ring-fencing the profits from those activities and restricting the deduction of payments under leases of "relevant assets" in computing those ring fence profits. This is known as the "hire cap".

7. The legislation set out below is that in force for the periods under appeal and so far as relevant to this appeal.

8. "**Oil contractor activities**" are defined in section 356L CTA 2010. In broad terms they cover the provision, operation or use by contractors of a "relevant asset" in connection with exploration or exploitation activities within the UK territorial sea or Continental Shelf.

9. Section 356LA, the key provision in this appeal, defines the term "**relevant asset**". It relevantly provides as follows:

> **356LA "Relevant asset"**
>
> (1) In this Part "relevant asset" means an asset within subsection (2) in respect of which conditions A and B are met.
>
> (2) An asset is within this subsection if it is a structure that—
>
> (a) can be moved from place to place (whether or not under its own power) without major dismantling or modification, and
>
> (b) can be used to—
>
> (i) drill for the purposes of searching for, or extracting, oil, or
>
> (ii) provide accommodation for individuals who work on or from another structure used in a relevant offshore area for, or in connection with, exploration or exploitation activities ("offshore workers").
>
> (3) But an asset is not within subsection (2)(b)(ii) if it is reasonable to suppose that its use to provide accommodation for offshore workers is unlikely to be more than incidental to another use, or other uses, to which the asset is likely to be put.
>
> (4) In subsection (2)—
>
> "oil" means any substance capable of being won under the authority of a licence granted under Part 1 of the Petroleum Act 1998 or the Petroleum (Production) Act (Northern Ireland) 1964;
>
> "structure" includes a ship or other vessel.
>
> (5) Condition A is that the asset, or any part of the asset, is leased (whether by the contractor or not) from an associated person other than the contractor.
>
> (6) Condition B is that the asset is of the requisite value.
>
> (7) The asset is of the "requisite value" if its market value is £2,000,000 or more.

10. Section 356N of the CTA 2010 relevantly provides as follows:

> **356N Restriction on hire etc of relevant assets to be brought into account**
>
> (1) This section applies if the contractor makes, or is to make, one or more payments under a lease of—
>
> (a) a relevant asset, or
>
> (b) part of a relevant asset.
>
> (2) The total amount that may be brought into account in respect of the payments for the purposes of calculating the contractor's ring fence profits in an accounting period is limited to the hire cap.

11. The "hire cap" is defined by reference to a formula, the details of which are not material in this appeal.

12. The dispute turns on whether for the relevant periods the Borgsten falls outside the definition of "relevant asset" on the grounds that it is within section 356LA(3), because it is reasonable to suppose that its use to provide accommodation for offshore workers "is unlikely to be more than incidental to another use, or other uses, to which the asset is likely to be put".

## Factual background

13. References to numbered paragraphs in parentheses, [xx], unless stated otherwise, are references to paragraphs in the Decision.

14. As explained at paragraphs [23] and [24], a TSV is designed to provide essential operational support services known as tender assisted drilling ("**TAD**") services to a minimum facility platform, without which the platform's drilling operations cannot be performed. Minimum facility drilling platforms have a drilling derrick and drill floor with other operational functionality, but they lack significant facilities which are essential for active drilling operations. For those missing facilities they rely on the support of TAD services. A TSV cannot drill in its own right and can only support drilling activities by another vessel or platform. The TSV is moored alongside the minimum facility platform and is connected via a gangway and an assortment of hoses. When connected, the TSV and the platform would effectively be an integrated unit during the drilling campaign.

15. In June 2011, DDL received an invitation to tender ("**ITT**") from Total for what was described as the Dunbar Drilling Package Reinstatement Services and TSV Drilling Services, with a view to Total recommencing drilling activities at the Dunbar in 2012. The ITT stated that the Dunbar was designed originally "as tender assist", so that Total required the use of a TSV to become fully operational for drilling. At the time of receiving the ITT, the Dolphin group (of which DDL was a majority-owned indirect subsidiary) did not have a suitable vessel to deliver the requirements described in the ITT, but it did have the Borgsten drilling rig available. After carrying out a commercial appraisal of the costs of converting the Borgsten into a TSV, DDL tendered for the TSV Drilling Services. (See paragraphs [29] and [30].)

16. On 10 November 2011, under a Letter of Award, DDL was awarded the contract to supply TAD services to the Dunbar. The Total Contract was signed on 1 February 2012, with an effective date of 10 November 2011. The base rate fee payable was set at $202,000 per day, assuming a start date in 2012. There was scope for a price increase after 1 August 2012 based on an industry formula. As the hire did not start until 1 February 2013, the base rate at commencement of the Total Contract had increased according to that formula to $203,433 per day. (See paragraphs [33] and [35].)

17. Between the dates of the Letter of Award and signing of the Total Contract, DDL agreed to undertake a five-year class renewal survey for the vessel, at a cost of around $30 million. The Total Contract provided that Total would make a payment of $25 million towards this cost. This would be undertaken in parallel to the project to convert the Borgsten to a TSV. (See paragraph [34].)

18. After the Total Contract had been signed, various "Change Orders" were entered into by the parties (paragraph [36]), which we discuss below.

19. Substantial works were required in order to convert the Borgsten into a TSV. These included removal of derrick drilling equipment; removal of subsea equipment; installation of a gangway for personnel transfer and mud lines, water lines and compressed air; upgrade of the mud system; upgrade of seawater and freshwater capacity; relocation of the lifeboats and upgrade of the fire-fighting system: paragraph [39].

20. It was agreed that the original accommodation on the Borgsten would be retained. The DDL employees and sub-contractors who would be working on the Borgsten ("**DDL Personnel**") would be around 55 individuals. There was expected to be around 47 surplus berths on board: paragraph [40].

21. On 21 December 2011 Total requested that DDL prepare a study to detail the cost and schedule impacts of increasing the accommodation on the Borgsten from 102 to 120 persons, with a report to be prepared by 20 January 2012. Total wanted to increase the number of berths available to it from 40, being the number referred to in the ITT documentation, to 65: paragraph [114].

22. On 7 March 2012 DDL wrote to Total in connection with the proposal to increase the capacity of the living quarters on board the TSV from 102 to 120 berths or "People on Board" ("**POBs**"). The letter refers to the increase having been discussed between the parties. DDL proposed that the works be undertaken during the scheduled yard visit in 2012, in parallel with other TSV modifications. The price was to be $6,700,800, i.e. £4,188,000. The letter describes the main elements of the work as:

> (1) new 20 bed accommodation block on two levels,
>
> (2) extend mess room and upgrade gallery for higher POB,
>
> (3) create improved alternative non-smoking lounge facilities,
>
> (4) install new 2x60 man lifeboats and associated upgraded davits,
>
> (5) provide life rafts, and
>
> (6) obtain DNV approvals.

(See paragraph [116].)

23. The relevant Change Order was dated 1 May 2012, stating that the value of the Change Order was £4,188,000 and that Total agreed to pay DDL for the cost: paragraph [118].

24. In 2015, poor market conditions and low oil and gas prices resulted in Total requesting a reduction in the base rate from $203,433 to $164,000 per day with effect from 1 October 2015. Thereafter, continued difficulties in the oil market led to Total triggering its early termination rights, and the Total Contract came to an end in October 2016. Following the termination of the Total Contract, and in the absence of any alternative need for a TSV in the UK continental shelf or elsewhere, the Borgsten was scrapped in 2017. (See paragraphs [47]-[49].)

**The FTT's decision**

25. In view of HMRC's grounds of appeal it is necessary to summarise the Decision in some detail.

*Evidence*

26. In addition to documentary evidence, the FTT heard oral evidence from three witnesses for DDL. These were Mr Brandvold, a director of DDL; Mr Mitchell, another director of DDL, whose role involved marketing vessels and negotiating their terms of use by third parties, and who was part of the team which conducted negotiations for the use of the Borgsten by Total, and Mr Thain, a DDL employee who was rig manager of the Borgsten with overall responsibility for the safety and operation of the vessel. The FTT found all three witnesses to be credible. It accepted their evidence, subject to the caveats that their statements that accommodation was incidental to the Borgsten's main purpose related to the legal question for the FTT to determine, and that answers given by Mr Thain as to numbers of personnel on board the Borgsten and the Dunbar were honest estimates: paragraph [17].

27. There was no witness or documentary evidence from Total.

*Findings of fact*

28. The FTT made detailed findings of fact, some of which we have summarised above. Further findings included the following:

> (1) There were only two minimum facility drilling platforms in the UK continental shelf designed to require TAD services from semi-submersible TSVs, one of which was the Dunbar: paragraph [25].
>
> (2) TAD services include the uninterrupted supply of a compound known as "mud" used in drilling activities, together with water, compressed air and cement; warehousing and storage; workshop and lab space; office and conferencing facilities; "blow out" protection to seal the platform well in case of a catastrophic event; a heliport; and living space: paragraph [26].
>
> (3) At the time of the ITT, there was expected to be a pre-drilling phase of 120 days with an operational period of a further 1095 days: paragraph [31].
>
> (4) The Borgsten had two decks, each approximately the size of the Wembley football pitch. The significant majority of the space on board was used for the provision of TAD services. At the time of the ITT the Borgsten had capacity to accommodate 102 personnel on board. There would be around 55 DDL Personnel on board the Borgsten, meaning there would be around 47 surplus berths. (See paragraphs [38] and [40].)
>
> (5) Substantial works were required to convert the Borgsten into a TSV. The original accommodation was to be retained: paragraph [39].
>
> (6) During drilling, there would be personnel working on the platform and/or the TSV. "Everyone requires accommodation—this may be on either the platform or the TSV": paragraph [41].

29. The FTT made the following findings at [42] to [46] (references to the Operator are to Total):

> 42. Whilst the crew of the Borgsten, the DDL Personnel, were expected to be accommodated on the Borgsten, the Operator would be expected to decide where to accommodate other personnel - both the Operator's personnel working on the Borgsten and those working on the platform. The Dunbar could accommodate 60 personnel.
>
> 43. This flexibility only existed during drilling operations, as this was the only period during which the TSV was alongside and connected to the platform. Once drilling ceased and the platform only carried out production activities (which the Dunbar was capable of doing without support from another vessel) then all those working on the platform needed to be accommodated on the Dunbar.
>
> 44. The commencement date under the Total Contract was 1 February 2013 and the Borgsten moved into position alongside the Dunbar in February 2013. Although originally expected to last 120 days, the pre-drilling phase was extended until 3 April 2015 as the upgrade works on the Dunbar took longer than anticipated to complete.
>
> 45. The Borgsten was operational and fully crewed throughout the pre-drilling phase. Once the Borgsten was in position, it was connected to the Dunbar and kept in a constant state of readiness. Its functions included:
>
> (1) running the mud systems on a closed loop,
>
> (2) supplying water and compressed air, and
>
> (3) providing warehousing, heliport, welding and machine shop, deck storage, cranes, wharf, office and accommodation facilities.

> 46. There was little difference between the day-to-day activities on board the Borgsten during the pre-drilling phase and the fully operational phase. The main differences were:
>
> (1) the Borgsten crew who would have seen the most change in their daily duties were the drilling team (responsible for the mudding system) and the roughneck team (responsible for general labour);
>
> (2) the mud system - this was running water on a closed loop during the pre-drilling phase and then, once drilling operations commenced, started producing mud and flowing it to and from the Dunbar; and
>
> (3) the type of personnel engaged by Total and its third party contractors and their roles.

*The FTT's approach*

30. It was common ground before the FTT that:

> (1) Unless the Borgsten was within the exception[1] in section 356LA(3) it would be a "relevant asset", on the basis that (at the relevant time) it could be used to provide accommodation for offshore workers, and
>
> (2) During the relevant accounting periods the Borgsten could not be used to drill for the purpose of searching for or extracting oil, within section 356LA(2)(b)(i).

31. The FTT identified that the question for determination was therefore whether, in respect of each accounting period under appeal, the Borgsten was excluded from falling within section 356LA(2)(b)(ii) because "it is reasonable to suppose that its use to provide accommodation for offshore workers is unlikely to be more than incidental to another use, or uses, to which [it] is likely to be put": section 356LA(3).

32. The FTT reminded itself that it was for DDL to establish, on the balance of probabilities, that the Borgsten fell within the exception: [52].

33. The FTT noted that the use which needed to be assessed was use to provide accommodation for "offshore workers" as defined in section 356LA(2)(b)(ii), not use as accommodation generally. In particular, none of the DDL Personnel was an offshore worker: paragraph [53].

34. Ms Shaw and Mr McNall also represented DDL and HMRC respectively before the FTT. Ms Shaw submitted that "incidental" meant minor or subordinate to other uses. Mr McNall emphasised that because the burden was on DDL to advance evidence to prove the exception applied, "these are facts within the knowledge of DDL": paragraph [55]. He argued that the evidence which was relevant was "who was sleeping on the Borgsten and where those individuals were working". He submitted that the use of accommodation on the Borgsten could not be incidental because of various factors.

35. The FTT then assessed in detail the following areas in considering the issue before it:

> (1) Accommodation on different categories of offshore vessels, and the capacity of the Borgsten to provide accommodation.

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[1] Ms Shaw submitted, by reference to the legislative history of the provisions, that section 356LA(3) is not an "exception" but simply part of the definition of "relevant asset". While accepting that that argument has some force, we refer to it in this decision as the exception for the sake of convenience, but without any implication that it must, as an exception, be narrowly construed.

(2) The arrangements with Total.

(3) The actual use of the accommodation on the Borgsten by personnel (whether employees or sub-contractors) provided by Total ("**Total Personnel**"), including evidence as to whether the individuals concerned were "offshore workers", and any other uses to which the vessel was likely to be put.

(4) The approach to be taken to the interpretation of the statutory provisions in the light of HMRC's technical notes and relevant Parliamentary debates.

(5) The terms of the exception, and its application to the facts found.

36. We now summarise the FTT's findings in relation to these five areas.

*Accommodation on different categories of offshore vessels, and the capacity of the Borgsten to provide accommodation: paragraphs [59] to [66].*

37. The FTT referred to vessels whose sole purpose was to provide accommodation units (with a heliport and crane), known as "flotels". The FTT accepted DDL's evidence as to the differences between accommodation vessels and TSVs, and agreed that the Total Contract did not fit the description of a contract for the provision of accommodation by the hire of an accommodation vessel: paragraph [62(2)]. The FTT accepted the evidence of DDL's witnesses that all offshore vessels will have berths for the crew that live and work on the vessels, and that almost all support vessels can be expected to have surplus berths: paragraph [63]. Ultimately, the FTT did not find a comparison between accommodation vessels and TSVs to be particularly helpful in construing the application of the exception: paragraph [66].

*The arrangements with Total: paragraphs [67] to [126].*

38. In this section of the Decision, the FTT considered at length the arrangements between DDL and Total, by reference both to the documents and the evidence of DDL's witnesses. It noted that it was evident from the face of the ITT that accommodation was one aspect of the services which a successful tenderer was expected to provide, while recording Ms Shaw's submission that some accommodation was always a necessity for a TSV.

39. The FTT considered the terms of a pro forma contract which accompanied the ITT, described as a specimen contract for TSV Drilling Services. This provided at paragraph 2.14 that the TSV must provide living accommodation and associated safety equipment for 100-120 persons, and that Total required accommodation for 40 Total "company personnel". The section on remuneration included a separate item for "Accommodation Rate (Flotel Mode)", a label described by Ms Shaw as "wholly inapt". The FTT's conclusions in relation to the specimen contract were as follows:

> 81. It was clear that Total expected and required that the TSV providing the TSV Drilling Services would have surplus accommodation that could be used for Total Personnel.
>
> 82. We accept Ms Shaw's submissions that there is very little detail in this specimen contract in relation to such accommodation - it is "tacked on" - and that all labels and descriptions in this version are those of Total. There was no evidence before us from Total as to why the terms "flotel mode" or "accommodation rate" had been used…

40. At paragraphs [83]-[93] the FTT then considered the tender submitted by DDL. The tender set out DDL's proposals on remuneration in the form required by the ITT. For the "TSV daily rate (drilling mode)" the rate was $210,000 per day, described as "Base Rate T", and for the "TSV accommodation rate (flotel mode)" the rate was stated as 100% of Base Rate T. The price pitched for both the drilling and pre-drilling phases was thus the same. In the item relating to "food and

accommodation" the price pitched was a unit price of $80 per person for full board and accommodation, which DDL said was intended to cover the marginal cost. Mr McNall submitted that the evidence demonstrated that Total's request for accommodation was "important or vital". Against that, the evidence from DDL's witnesses was that "Total's request for accommodation was not considered by DDL to be of any significance". Their evidence was that the average number of berths on a TSV vessel was 150, so any TSV vessel would have had sufficient accommodation to meet Total's requirements. Moreover, Total's request for up to 40 berths was within the Borgsten's original capacity of 102 berths. The primary focus of the contract negotiations with Total, they said, was on the provision of TAD services, not the provision of accommodation to Total Personnel, and the value of the contract to DDL attached predominantly to the TAD services.

41. The FTT's conclusions in relation to the tender and DDL's evidence regarding it were as follows:

> 93. We accept this evidence and reach the following conclusions in relation to the tender submitted by DDL:
>
> (1) DDL was keen to ensure that Total was aware of its expertise in providing support vessels in the North Sea, including providing accommodation. However, this was against the backdrop that at the time of submission of the tender the Borgsten was not a support vessel but was a drilling rig in its own right. There was clearly a message that needed to be "sold" to an Operator about experience in providing support to a platform.
>
> (2) The proposed pricing (with the daily rate proposed to be the same throughout the contract period) supports the proposition that DDL did not draw a distinction between different phases of the period, particularly in the context that the timing of the move from one phase to another was not within its control. It proposed a daily price for the provision of the services.
>
> (3) The difference between the proposed daily rate of $210,000 and the unit price for food and accommodation of $80 is striking, particularly given that when being asked to make available 40 berths per day the maximum charge was going to be limited ($96,000 per month if all were fully occupied throughout).
>
> (4) DDL did not seek to make any changes to the terminology used by Total for the different phases of the contract. In tendering for a high value commercial contract such as that in issue, we recognise that there is often a commercial incentive to avoid requiring what might be seen as unnecessary, or "nice to have", changes, and instead to focus only on matters which have commercial value. That is not a complete answer to the reason for not changing the labels used by Total - looking at the 138 changes which were proposed in the Contractual Qualifications Table, some of the changes requested were "for clarity", including a proposed deletion of what was presumably considered to be some unnecessary blurb in the preamble itself to the contract, and a request that "undertakes and warrants" be changed to "agrees". DDL was therefore prepared to propose changes which did not go to value or liability. We accept the evidence of both Mr Brandvold and Mr Mitchell that they just had not focused on the language at the time, it was not important to them, and the main focus was to propose that the same rate would apply throughout the hire period. The label used just did not matter.

42. The FTT then turned at paragraphs [94]-[102] to the class renewal survey for the Borgsten. DDL agreed that this survey would be conducted during the conversion project, even though it would not otherwise be due for another three years. DDL thought that this was probably critical to being awarded the contract with Total, as conducting the survey only after the three years would have disrupted drilling operations. The FTT considered that the acceleration of the survey was important to Total as it wanted continuity of drilling operations. It did not accept Mr McNall's submission that it showed

the importance to Total of having the accommodation on the Borgsten available throughout the drilling period. Indeed, it concluded that the accommodation on the Borgsten would not have been needed at all for any Total personnel in a period when drilling was suspended because the Borgsten needed to return to the yard: paragraph [99].

43. The FTT considered the Letter of Award to DDL from Total, which prompted an announcement by Dolphin's parent company to the Norwegian Stock Exchange (paragraphs [103]-[110]). Ms Shaw noted that the announcement referred to the provision of tender support services (not accommodation) and that the stated estimated contract value did not include the $80 per berth charge. Mr McNall emphasised a reference in an internal email preceding the draft announcement to "1215 days i.e. 1095 days TSV support preceded by 120 days accommodation/commissioning support". The FTT agreed with Mr McNall that the reference to accommodation in the internal email was "an indicator of how DDL regarded the contract". It noted, however, that it was "just one indicator", and that in any event it referred to both accommodation and the TAD services: paragraph [110].

44. Following the execution of the Total Contract (which largely followed the specimen contract attached to the ITT), there were various Change Order instructions from Total to DDL. These were requests from Total for DDL to submit a price for specified additional works, together with any amendments to the Total Contract which DDL believed were necessary to take account of the proposed change. These requests were a matter for negotiation between the parties. If the price and contract changes were agreed, the parties would sign a Change Order. As already mentioned, Total asked DDL to prepare a study about increasing the accommodation on the Borgsten, wanting to increase the number of berths available to it from 40 to 65. Mr Mitchell explained that this was to maximise Total's opportunities to increase the capacity of the crew in the hope that upgrades to the Dunbar would take less time, so that drilling operations could begin more quickly. Mr Mitchell also said that "it was made very clear by Total's project manager to DDL that it was important that this additional request for accommodation should not delay the Borgsten being deployed": paragraph [115].

45. The FTT considered that the cost of the additional works to increase the accommodation was "not insignificant, either viewed in isolation or in comparison to the cost of the conversion project": paragraph [122]. However, monitoring the works would not have involved significant additional management time for DDL: paragraph [124]. Having noted at paragraph [125] that the relevant Change Order was agreed after the contract was signed and could not be forced on DDL, the FTT's primary conclusion as to the relevance of the Change Order to the issue in the appeal was as follows:

> 126. Whilst we agree that no distinction was drawn in the initial request from Total or in the Change Order between whether the berths would be used by Total Personnel working on the Borgsten or those working on the Dunbar, we regard the fact that the request was made at all as telling, as is the explanation given – the plan was to increase the number of personnel working on the upgrades to the Dunbar so that drilling operations could commence more quickly. This is the first occasion on which the evidence addresses the question of who the accommodation being made available to Total Personnel was to be used by – the additional 25 berths (ie the increase from 40 to 65) were requested so that more Total Personnel working on the Dunbar could be accommodated, ie offshore workers.

*Extent of actual use to provide accommodation for offshore workers, and other uses: paragraphs [127] to [154]*

46. As regards the use of the accommodation, the FTT stated as follows:

> 127. It was not in dispute (and we find as facts) that:

(1) All personnel working onboard the Borgsten and the Dunbar needed to be accommodated on one of those vessels throughout the time those vessels were in the field. Personnel and/or supplies were brought to the Borgsten by helicopter most week days (usually twice a day). This was how the crews were changed over after their period on board, typically of around two weeks. Some individuals were occasionally flown in and out on the same day (eg management visits), or stayed on board just one or two nights. There were no routine helicopters on Saturdays or Sundays.

(2) The DDL Personnel were working on the Borgsten, not the Dunbar.

(3) The Borgsten had 102 berths when it operated as a drilling rig, and DDL had intended to retain this number upon its conversion to a TSV.

(4) Total initially required 40 berths to be available on the Borgsten for Total Personnel. This required no additional works on the Borgsten. Total later requested that the number of berths be increased from 102 to 120 and that 65 be made available to Total Personnel. This work was done during the conversion programme, and the cost was borne by Total.

(5) The Borgsten thus had 120 berths; this was also the maximum number of individuals who could be on board the vessel at any one time (irrespective of sleeping capacity) as this was the lifeboat capacity of the vessel.

(6) The Dunbar had 60 berths.

128. There was considerable evidence before us as to the extent of the actual use of the surplus accommodation on the Borgsten by Total Personnel, ie the extent to which they used the 65 berths which were made available to them.

47. Ms Shaw submitted to the FTT that because the exception looked to the use which it was reasonable to suppose, it was not concerned with actual use, whereas Mr McNall submitted that actual use was relevant and should be considered. The FTT dealt with this issue in its consideration and conclusions, but considered it appropriate for the FTT as the fact-finding tribunal to consider evidence of actual use and make findings in respect thereto.

48. The FTT considered in detail all the evidence presented to it, and made various findings of fact. It noted that the documentary evidence, which it was satisfied gave a fair reflection of the overall picture, did not record whether the individuals comprised in Total Personnel who were accommodated on the Borgsten at various times were or were not "offshore workers". It considered in this regard and accepted the unchallenged evidence of Mr Thain. The FTT considered that "this evidence supports the fact that the large majority of Total Personnel sleeping on the Borgsten were working on the Dunbar – in the pre-drilling phase this was 53-54 of the average 58 Total Personnel and in the drilling phase, this was 49-50 of the average 59 Total Personnel sleeping on the Borgsten were working on the Dunbar": paragraph [143]. The FTT also accepted, as estimates, Mr Thain's beliefs that (1) the maximum number of personnel permitted on the Dunbar at any one time was 85-89 (being the lifeboat capacity), (2) during the pre-drilling phase there would have been on average around 80 personnel working on the Dunbar, and (3) during the drilling campaign this would have reduced to 60-70 personnel.

49. The FTT correctly observed that use of the Borgsten for accommodation for offshore workers could only be incidental if there was "another use, or other uses" to which the vessel was likely to be put. It referred to such other uses as a "Permitted Use", and we adopt that term below: paragraph [148]. The FTT concluded that there were two Permitted Uses to which it was reasonable to suppose the Borgsten would be likely to be put, being the provision of TAD services to the Dunbar and the provision of accommodation to personnel working on the Borgsten rather than the Dunbar. As to

whether any distinction should be drawn in relation to Permitted Use between the pre-drilling and drilling phases, the FTT referred at paragraph [151] to additional Permitted Uses of the Borgsten in the pre-drilling phase, which was much longer than the parties had anticipated, but as already mentioned had found at paragraph [46] that there was little difference in day-to-day operations between the phases.

*Approach to statutory construction: paragraphs [155] to [166]*

50. The FTT considered a technical note published by HMRC on 1 April 2014 on offshore bareboat chartering in the UK oil and gas industry, which included draft legislation, explanatory notes and a tax information and impact note (the "**TIEN**"). The TIEN referred to the announcement by the Government in its 2013 Autumn Statement that it would introduce legislative changes to ensure that more of the profits made by offshore contractors in the UK were subject to UK tax. The introduction to the TIEN stated that, following informal consultation, the draft legislation had been changed so that "the measure [the hire cap] will now only apply to drilling rigs and accommodation vessels". The draft legislation did not at that stage include section 365LA(3), the provision with which this appeal is concerned. The TIEN stated as follows:

> Legislation will be introduced during the passage of Finance Bill 2014 to cap the amount of lease payment allowed as a tax deduction for companies providing drilling rigs and accommodation vessels under bareboat charter (or similar) arrangement, where this arises as part of a composite service…

51. When the new clauses, including section 365LA(3), were being read in Parliament on 2 July 2014, David Gauke (then the Exchequer Secretary) stated as follows:

> The UK is not currently receiving a fair amount of tax from companies that provide drilling rigs and accommodation vessels to the oil and gas industry. Many of those companies own their assets in lower tax jurisdictions overseas. Those assets are then leased to associated entities operating on the UK continental shelf through specialised leasing arrangements…, giving rise to a large deductible leasing expense in the UK… This measure will cap the amount the UK base contractor can claim as a deductible expense for those leasing payments.

52. During the debate, Mr Gauke referred to consultation within the industry, and stated:

> As a result of the evidence received, the scope of the measure has been limited to drilling rigs and accommodation vessels and we have increased the deduction cap.

53. The FTT was not persuaded that the legislation was sufficiently ambiguous or obscure to permit it to consider the statements made in Parliament, particularly since the exception in section 356LA(3) was not expressly mentioned: paragraphs [161] and [162].

54. Mr McNall also referred the FTT to HMRC's Oil Taxation Manual, which gave examples (at OT50010) of what HMRC considered to be the normal meaning of the incidental provision of accommodation. The FTT concluded that "given its status as guidance, we did not consider that these examples assisted with our application of the exception to the facts as we have found them": paragraph [166].

*Consideration and Conclusions: paragraphs [167] to [176]*

55. The FTT considered that while the language of the exception did not focus on an assessment of actual use, actual usage could be relevant to assessing the reasonableness of what was supposed to be likely or unlikely in terms of use.

56. As to the meaning of "incidental", the FTT said this:

> 170. Both parties noted that there is no definition of "incidental" or "more than incidental" for this purpose, and thus this word, or this phrase, must bear their ordinary meaning. Something is incidental to another matter if it is subordinate, or secondary, to it. We bear in mind throughout that the legislation does not specifically require that this other use is the main (or a main) or primary use.

57. The FTT then began its conclusions as follows:

> 171. Having considered all of the evidence before us, we have reached the view that there is a significant amount of evidence supporting a conclusion that it is reasonable to suppose that the use of the Borgsten to provide accommodation to Total Personnel generally (ie irrespective of whether they were offshore workers on the Dunbar or working on the Borgsten) was unlikely to be more than incidental to the Permitted Uses:
>
> (1) The ITT and the Total Contract focus on the provision by the Borgsten of TSV Drilling Services or TAD services to the Dunbar and the technical specifications which would be required of the Borgsten. The requirements relating to accommodation needing to be made available for Total Personnel (up to 40 berths at that stage) are brief, with minimal detail in relation thereto.
>
> (2) At the time of submitting the tender, DDL did not give any significant thought to the use of the accommodation on the Borgsten by Total Personnel, as the Borgsten had surplus capacity in excess of the number of berths that Total was requesting. As Mr Mitchell put it, the accommodation was just there. This was typical and to be expected of any TSV.
>
> (3) Having required that 40 berths be available for Total Personnel, there is no mention in the ITT or the Total Contract of how much use Total would make of the accommodation available to it or who Total would seek to have accommodated on the Borgsten. There was no commitment by Total to use any of these berths (and if it had not done so there would have been no charge of the $80 unit price). Total had access to office space and a conference room on the Borgsten, thus illustrating that some Total Personnel would be working (at least some of the time) on the Borgsten.
>
> (4) In practical terms, making available the surplus accommodation to Total Personnel was immaterial to DDL. Accommodation needed to be available to, and used by, the DDL Personnel. As such, DDL needed to make arrangements to deal with matters such as catering and laundry, and provide a gym and lounges. Ensuring that this covered a larger amount of usage made minimal difference.
>
> (5) The basis on which DDL agreed to increase the accommodation on board the Borgsten from 102 to 120 berths was that Total would bear the cost of the works and this did not delay the conversion (and thus the commencement date under the Total Contract). The additional works involved could be completed as part of the much bigger programme of works to convert the drilling rig into a TSV.
>
> (6) After the conversion into a TSV and the increase in the accommodation, most of the deck space on the Borgsten was related to its use to provide TAD services to the Dunbar. Mr Thain's evidence was that less than 10% was used for accommodation (which we take to refer to the cabins) but we do note that there was, in addition, space taken by related facilities including, eg, lounges, galley, mess and the gym.
>
> (7) By the time Part 8ZA came into effect on 1 April 2014, the Borgsten had been alongside the Dunbar for more than one year, and had been ready to support the commencement of drilling for just under a year. The drilling reinstatement programme was behind schedule. However, the day-to-day activities on board the Borgsten were largely the same in both the pre-drilling and drilling phases.

58. The FTT considered in detail the monetary "value" of the Total Contract, and the amounts spent by Total to accommodate Total Personnel on the Borgsten. It stated as follows, at [172(3)] onwards:

> (3)…The overwhelming weight of the evidence before us was that the focus was on the TAD services to be provided from the Borgsten (even to the extent that the tender included a breakdown of the crew that would be provided by DDL and their pay rates). Thus whilst the value of the Total Contract was in the daily rate, this rate itself included an amount for the accommodation-related services (albeit that we concluded this was a very small amount).
>
> (4) Looking at the amounts of money involved, DDL were charging Total $136,640 (for March 2013), $151,680 for September 2014, per month for accommodating Total Personnel on the Borgsten. The numbers do not draw a distinction between the proportion of this which related to offshore workers. Also, as a result of the agreement to increase the number of berths on the Borgsten, Total met the cost of $6,700,800. These are clearly large sums of money. However, we do not look at these amounts in isolation. Total paid DDL a daily rate of $203,433 - on a 30-day month basis, this was $6,102,990 per month. Similarly, in the Letter of Award Total agreed that it would be responsible for costs of $20,470,000 (envisaged to relate to the pre-ordering of items such as the gangway) even before a contract for the TSV Drilling Services was agreed, and paid $25 million towards the costs of the class renewal survey.
>
> (5) There were large sums of money being spent under the Total Contract, and in readiness for it, albeit that even the $25 million paid towards the class renewal survey was less than 10% of what DDL calculated to be the value of the contract. The monthly costs being borne by Total to accommodate its personnel on the Borgsten, some of whom were working on the Borgsten and were not offshore workers, were very small, even taking account of the fact that some of the daily rate related to the availability of accommodation facilities.
>
> 173. Nevertheless, when assessing what it is reasonable to suppose for the purpose of applying s356LA(3), it was clear that Total expected and required that the TSV providing the TSV Drilling Services would have surplus accommodation that could be used for Total Personnel. We note in particular:
>
> (1) All support vessels are expected to have surplus accommodation (ie over and above that which is required for its own crew) which can be used by the Operator. In putting out the ITT and stating in it that Total required the use of 40 berths, Total was wanting to have access to some of that accommodation, as it would typically expect to be able to do.
>
> (2) Having initially not focused on this request for accommodation at the time of submission of the tender (as the Borgsten had surplus in excess of that which was required by Total), there is then a pattern showing that DDL paid more attention to this use of accommodation - this can be seen from the correspondence relating to the drafting of the stock exchange announcement where Mr Mitchell referred to "accommodation/commissioning support", and then the fact of Total's request for additional berths (which necessitated the Change Order as the numbers requested exceeded those which already existed as surplus).
>
> (3) Total wanted to have more berths available for Total Personnel and was prepared to pay for them, albeit not at the expense of delaying the completion of the conversion of the Borgsten into a TSV. At this time, it was apparent that some of the accommodation was sought by Total for Total Personnel who would be offshore workers, as Total wanted to increase the number of personnel working on the upgrades to the Dunbar so that drilling operations could commence more quickly.

> (4) The delays to the works on board the Dunbar meant that there was an extended period before drilling commenced. However, we note that these delays were unexpected and the evidence from Mr Thain addressed the activities on board the Borgsten during this period.
>
> (5) The POB Logs show the actual use by Total Personnel of the accommodation on the Borgsten. They did use the additional accommodation which had been requested and paid for. A large majority of Total Personnel sleeping on the Borgsten were working on the Dunbar – this was the case in both the pre-drilling and drilling phases.
>
> (6) Total was paying between $96,080 and $163,920 every month to DDL for Total Personnel to be accommodated on the Borgsten.

59. The FTT then referred to various matters which it did not consider to be particularly relevant to the analysis, and concluded as follows:

> 175. The assessment of whether the Borgsten is within s356LA(3) for the accounting periods in issue does not require us simply to weigh these lists of factors against each other. We recognise that, taken together, the factors listed at [173] above demonstrate that the use of the Borgsten to provide accommodation to offshore workers could reasonably be supposed to be of some importance. We have therefore had to consider whether this precludes the use from being no more than incidental. We have concluded that it does not – incidental does not need to be confined to uses which are trivial; it can capture uses which, whilst being desirable, sought-after or even important are nevertheless, when viewed in context, secondary to (or less important than) another use or uses.
>
> 176. Having considered all of the evidence before us, we are satisfied that, on the balance of probabilities, it is reasonable to suppose that the use of the Borgsten to provide accommodation for Total Personnel working on the Dunbar was unlikely to be more than incidental to the use of the Borgsten to provide TAD services to the Dunbar and/or to accommodate DDL Personnel (who were working on the Borgsten). Accordingly we have concluded that the terms of the exception in s356LA(3) are satisfied such that the Borgsten was not within s356LA(2)(b)(ii) for the accounting periods in issue. DDL's appeal is allowed.

## Grounds of Appeal

60. HMRC were refused permission to appeal on certain grounds but granted permission to appeal on the two grounds described below.

*Ground 1: The FTT applied an incorrect legal test in interpreting the meaning of "incidental".*

61. HMRC contend that the FTT wrongly directed itself as to the meaning of "incidental" and, having done so, reached an incorrect conclusion at paragraph [175]. In particular, given that the FTT recognised at paragraph [175] that "the use of the Borgsten to provide accommodation to offshore workers could reasonably be supposed to be of some importance", it was not then open to the FTT as a matter of law to conclude that such use was unlikely to be more than incidental.

*Ground 2: The FTT took an incorrect approach to interpretation of the Total Contract.*

62. HMRC contend that the FTT erred in interpreting the Total Contract, in particular by giving weight to what DDL's witnesses of fact said about it and not regarding the Total Contract as determining the issue. We consider HMRC's specific criticisms in our discussion of Ground 2 below.

**Ground 1: the meaning of "incidental to" in section 356LA(3)**

*Discussion*

63. HMRC's grounds of appeal set out their argument under Ground 1 as follows:

> An important use cannot, either as a matter of law or of language, be a (no more than) incidental use within the proper meaning and effect of the legislation…The treatment of a use (here, accommodation) which is important as nonetheless still no more than incidental is suggestive that the Tribunal has, wrongly, imported a main or principal purpose or use test into the legislation…The natural and ordinary meaning of 'incidental' is 'minor', 'inessential' or 'not crucial'.

64. In his skeleton argument and oral submissions, Mr McNall's primary argument was that a use which was "important" could not be incidental, though in response to questioning he appeared to lean towards the alternative formulation that a use which was "essential" could not be incidental. We therefore consider HMRC's appeal under Ground 1 on each basis.

65. We remind ourselves that the terms of the exception from the hire cap are as follows:

> …an asset is not [a relevant asset] if it is reasonable to suppose that its use to provide accommodation for offshore workers is unlikely to be more than incidental to another use, or other uses, to which the asset is likely to be put.

66. As with any statutory language, these words must be interpreted purposively, and that construction applied to the facts, viewed realistically[2].

67. The purpose of the provisions introduced by the Finance Act 2014 was to impose a ring-fence cap on tax deductions for payments under certain types of lease of certain types of asset. The assets brought within the cap are (broadly) moveable assets which "can be used" for drilling or for accommodation of offshore workers: section 356LA(2). As discussed above, the exception contained in section 356LA(3) was introduced only following industry consultation. We consider it self-evident that the purpose of the exception was to limit the types of "accommodation" assets caught by the cap, by carving out assets which "can be used" for accommodation of offshore workers but where such use is expected to be incidental to a Permitted Use. The test is objective ("reasonable to suppose") and it applies by reference to the relationship between two assessments of likely use, namely the Permitted Use/s to which the asset is/are likely to be put and its likely use as accommodation for offshore workers. The test is then whether it is reasonable to suppose that the latter is unlikely to be more than incidental to the former.

68. The FTT agreed with the parties that there was no definition of "incidental" or "more than incidental" for the purpose of the exception, and that these words should bear their ordinary meaning: paragraph [170]. We agree. The issue in this appeal is therefore whether the FTT then erred in deciding what that ordinary meaning was.

69. Neither party referred us to any dictionary definitions, and we consider that this is a case where such definitions would be of limited assistance. The issue is whether in relation to this particular statutory provision one type of likely use can reasonably be supposed to be incidental to another, and dictionary definitions of "incidental" do not really help us to resolve that question.

[2] This was the widely-adopted formulation suggested by Ribeiro PJ in *Collector of Stamp Revenue v Arrowtown Assets Ltd* [2003] HKCFA 46 at [35].

70. The decision in *Robson v Dixon* [1972] 1 WLR 1493 concerned the meaning of "merely incidental to" and is therefore of some relevance. In that case, the taxpayer was a commercial pilot based at Schiphol Airport, Amsterdam who had a home in England and commuted between it and Schiphol when his flying duties permitted. His duties were to fly scheduled flights which always originated from Schiphol. In the relevant period, only about 5% of his take-offs and landings were from or in the UK. He was assessed to tax on the basis that he was UK resident. He appealed on the ground that he was not UK resident because, under the exemption in section 11 Finance Act 1956, his landings and take-offs in the UK were "merely incidental to the performance of the other duties outside the United Kingdom". Sir John Pennycuick V-C held that there were no clearly defined "other duties" outside the UK; rather, all of the relevant activities were "precisely co-ordinate", so one could not be said to be merely incidental to the other. He stated as follows, at page 1498:

> The expression "merely incidental to" is a striking one, and effect must be given to the natural meaning of those words. The words "merely incidental to" are upon their ordinary use apt to denote an activity (here the performance of duties) which does not serve any independent purpose but is carried out in order to further some other purpose.

71. In rejecting an argument put forward by Mr Robson, Sir John Pennycuick implicitly characterised the test of "merely incidental to" as one which was qualitative not quantitative (at page 1499):

> Again, I think it is impossible to construe subsection (3) in the way in which it was sought to construe it in the taxpayer's contentions in the case stated, as indicating merely relatively short periods of employment in the United Kingdom in relation to the period of employment outside the United Kingdom. It would have been quite simple for the section so to provide; and it may well be that if the condition were imported only by the expression "in substance," that would be the result. But the second requirement is expressed in quite different terms and cannot, I think, be treated as referring merely to what has been described as a quantitative, in contradistinction to a qualitative, basis.

72. There are important differences between *Robson v Dixon* and this appeal. Whether something is "incidental" is not the same as whether it is "merely incidental". Additionally, in *Robson* there was, in effect, nothing to which the UK activities could ever be incidental, because all the relevant activities were found to be "precisely co-ordinate".

73. Notwithstanding those differences, we agree that the question of whether one thing is incidental to another is a qualitative rather than a quantitative test. However, it is possible to contemplate situations in which the sheer quantity of one thing relative to another might call into question whether the former could be properly described as incidental to the latter.

74. Sir John Pennycuick considered that the words "merely incidental to" when applied to an activity were apt to denote an activity which "does not serve any independent purpose but is carried out in order to further some other purpose". With respect, we would exercise caution in assuming that this formulation can necessarily be read across to the words "incidental to" when applied to a use which it is reasonable to suppose. However, we agree that the test does incorporate a relational or relative element, in the sense that use for accommodation must be incidental to some other use.

75. We consider that the FTT did not make an error of law in stating (at paragraph [170]) that something is incidental to another matter if it is subordinate, or secondary, to it. The critical element in our opinion is the element of subordination. This is not the same as merely identifying anticipated

uses and ranking them in terms of importance[3], and, as the FTT recognised (again at paragraph [170]), is not the same as a test of main or primary use.

76. It follows from this that we consider that the FTT was right to state (at paragraph [175]) that their conclusion that "the use of the Borgsten to provide accommodation to offshore workers could reasonably be supposed to be of some importance" did not preclude a finding that such use was nevertheless incidental to Permitted Uses. The fact that a use is desirable, sought-after or important (by whatever measure) may on its face suggest that it is unlikely to be incidental; but whether it is incidental depends on all the facts and whether such use is (or in this case can reasonably be supposed to be) subordinate or secondary to another use.

77. We therefore reject HMRC's argument that the FTT erred in law in deciding that a use which is important may nevertheless be incidental to another use.

78. While we do not rely on it in reaching our decision, we consider that this conclusion is reinforced by the legislative history of the exception. The FTT found that in practice a TSV will have some accommodation available, meaning that it "can be used" for accommodation and would therefore fall within the definition of "relevant asset" as originally drafted. However, a TSV is not an accommodation vessel (such as a flotel), which is designed and used primarily for accommodation, and the target of the hire cap was stated to be drilling rigs and accommodation vessels. The intention of the exception was to remove from the cap assets whose use as accommodation was incidental to another (permitted) use. If the drafter had intended the exception to apply only where the use as accommodation was not important, that test could have been chosen, or (more conventionally) a test based on significance or materiality would have been adopted.

79. HMRC also submit that the use of accommodation for offshore workers on the Borgsten was essential, and that the FTT erred in concluding that a use which was essential could nevertheless be incidental.

80. The appeal on this basis effectively rests on two propositions:

> (1) the FTT found that use of the Borgsten for accommodation for offshore workers was essential; and
>
> (2) the FTT decided that notwithstanding this such use was still incidental to Permitted Uses.

81. Having considered the Decision in its entirety, we do not consider that either proposition is made out.

82. The FTT at no point found as a fact that the use of the Borgsten for such accommodation was essential, either to Total or to DDL, or in the round[4]. Mr McNall asserted in his skeleton argument that such use was "crucial and/or essential", because "the operations on the Dunbar could not realistically have gone ahead without the accommodation on the Vessel" and "had the Borgsten not

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[3] At paragraph [175] the FTT stated that uses which were "secondary to (or less important than)" another use could still be incidental. While this may simply be loose wording, we do not consider that merely ranking the relative importance of uses is the correct approach.

[4] Although HMRC did not refer us to it, we observe that at paragraphs [81] and [173] the FTT stated that Total "expected and required" that the TSV would have surplus accommodation that could be used for Total Personnel. Seen in context, we consider that "required" in this phrase is simply indicating that that is what Total asked for, and not describing a finding that such accommodation was essential.

provided the accommodation which it did to those working on the Dunbar, then the personnel which Total needed for the operations on the Dunbar could not have been accommodated overnight (even on the Dunbar) and therefore would have had to be flown by helicopter to and from the mainland every day (a round-trip of up to 4 hours)".

83. However, there was no finding by the FTT to this effect. Additionally, the need for accommodation does not mean that that accommodation must necessarily be provided, or provided in full, by the Borgsten. An accommodation vessel could also have provided some accommodation. That is speculation, but so is the assertion that only accommodation on the Borgsten could have met Total's needs.

84. We do not consider that the Change Order demonstrates that the accommodation element was "essential" to Total. The FTT's findings at paragraphs [113] to [126] are consistently to the effect that Total wanted the additional accommodation in order to begin drilling more quickly, rather than it being essential in itself. This is reflected in its conclusion at paragraph [173(3)] that Total wanted more berths and was prepared to pay for them "albeit not at the expense of delaying the completion of the conversion of the Borgsten into a TSV". In other words, Total wanted more accommodation because that would allow work to proceed faster, but not if that meant imperilling the timetable for the Borgsten becoming available.

85. At no point did the FTT state that while the use as accommodation for offshore workers was essential it was nevertheless incidental.

86. We therefore reject the premises on which HMRC's alternative argument is based. As a result, we do not need to decide whether a supposed use which was found as a fact to be essential could nevertheless be incidental within the terms of the exception. It is appropriate for that question to be left for an appeal in which there has been such a finding.

87. Stepping back, we consider that the FTT was justified in approaching the question before it as it did and taking into account the evidence which it did in making its careful and detailed findings of fact. Mr McNall submitted that the question of whether the exception applied was "binary and not multi-factorial". However, that is a false dichotomy. The question is indeed binary in that if the exception does not apply the vessel is a relevant asset and the hire cap applies; there is no apportionment involved. But like several binary tax questions, such as the existence of a trade, the evaluation calls for a multi-factorial assessment.

88. We initially had some concern at the weight which the FTT appeared to attach to the subjective views of the DDL witnesses. However, we do not consider that such evidence can be said to have been irrelevant, and no such submission was made to the FTT. If nothing else, it is important to keep in mind that the hire cap applies to payments under the lease contract between DDL and its affiliate, so that it is not solely the Total Contract which falls to be taken into account in considering anticipated use. In any event, as with any multi-factorial assessment, the weight to be attached to particular facts is a matter for the fact-finding tribunal, unless it has misdirected itself, which we have concluded in this case it did not.

89. Mr McNall made the further criticism of the FTT that they attached no weight to the examples in the OTO Manual put forward by HMRC. We have no hesitation in rejecting that criticism. The FTT was justified in taking the approach which it took to examples (none of which related specifically to the point in this appeal) of HMRC's view of the legislation.

**Ground 1:Conclusion**

90. The appeal on this ground is dismissed.

**Ground 2: Incorrect approach to the interpretation of the Total Contract**

*Discussion*

91. HMRC say that the FTT made three errors of law, namely:

> (1) In determining whether the exception applies, the Total Contract "has primacy", and the FTT should have confined its consideration to what that contract said about use of the Borgsten for accommodation. The FTT should not have taken into account what the parties said or thought about the contract, and (contrary to HMRC's approach before the FTT, see paragraph [130]) should not have taken into account actual use. The Total Contract and preceding documents explicitly provided for accommodation.
>
> (2) In interpreting the Total Contract, the FTT departed from the general rule that in the construction of written contracts the intention of the parties is to be ascertained objectively, only from the words in the contract, and parol evidence, such as the evidence of DDL's witnesses, is inadmissible.
>
> (3) At [98], the FTT appears to have accepted without any evidence, and gone on to find, that Total would have considered acceleration of the class renewal survey to be important as part of its desire for more accommodation on the Borgsten.

92. We consider each of these submissions in turn.

93. As regards all three alleged errors, Mr McNall's skeleton argument rests on a confusion between subsections (2) and (3) of section 356LA. It asserts that the question of whether an asset "can be used" to provide accommodation for offshore workers (1) looks solely to potential use and treats actual use as irrelevant, and (2) is "provided for, circumscribed by, and identifiable only with reference to the Total Contract".

94. We would regard this as too sweeping a generalisation, but in any event it is nothing to the point. The question of whether the Borgsten "can be used" to provide such accommodation is relevant to whether it fell within the definition of "relevant asset " in subsection (2). It was and is common ground that it did. The only dispute was and is whether the exception to that definition in subsection (3) applied. That turns on the likely uses which could reasonably be expected for the vessel. The relevant question is therefore not that supposed by HMRC's skeleton argument, but rather whether the FTT erred in any of the ways suggested in making the assessment required by subsection (3). That is sufficient for us to dismiss the appeal under Ground 2 as framed by HMRC. We have, however, considered the three alleged errors from the perspective of the issue that was in fact before the FTT, namely the applicability of the exception.

95. The first suggested error is that in reaching its decision the FTT took into account matters other than the written terms of the Total Contract. We have no hesitation in rejecting that argument. A determination by the FTT of whether the exception applied required it to determine the uses of the vessel which it was reasonable to suppose were likely to arise. As we have stated in relation to Ground 1, that exercise involved a multi-factorial assessment, in which the Total Contract would clearly have been important but in relation to which it was not only legitimate, but in our view correct, for the FTT to take into account and weigh all the relevant evidence before it. This included evidence as to the contractual negotiations between the parties and the actual use of the vessel. Both are relevant because they may well shed light on what was likely to occur. The weight to be given to the various findings

of fact made by the FTT on those issues was a matter for the FTT, given our decision that it did not misdirect itself and its conclusion was one which was available to it.

96. This conclusion is reinforced when one takes into account the manner in which the hire cap operates. Under section 356N, the cap applies by reference to payments under the lease of a relevant asset, being in this case the payments made by DDL to BDPL. So, it applies for any accounting period in which such a payment is made. It is therefore unlikely that the drafter can have intended that the status of the asset should fall to be determined for all future accounting periods by the terms of the contract for use of the asset (in this case the Total Contract) at the point when it was executed.

97. The second suggested error is that the FTT failed to apply conventional principles of construction in relation to the Total Contract, by admitting and giving any weight to the oral evidence of the DDL witnesses. It is said that "none of that evidence was admissible in interpreting the contract or (insofar as different) in assessing the relative importance of different parts of the Total Contract in the mind of one of the contracting parties, i.e. the taxpayer."

98. We reject this argument. It is an over-simplification to say that it is a rule of contractual construction that matters outside a written contract can never be taken into account. We were not taken to it, but a useful recent summary of the uncontroversial principles of contractual construction is contained in *ABC Electrification Limited v Network Rail Infrastructure Limited* [2020] EWCA Civ 1645 at [18] and [19]. These principles include that contracts must be construed in the factual context known to the parties at the time of execution. In any event, while the FTT did indeed take into account the evidence of the DDL witnesses as to various issues in relation to the Total Contract and the accommodation Change Order, including the importance placed by the parties on the accommodation, they did not do so in interpreting the Total Contract. They did so in considering the likely uses of the Borgsten which it was reasonable to suppose. It is in fact apparent from the Decision that there was no material dispute as to the meaning of any of the terms of the Total Contract.

99. We suspect that HMRC's real objection is that in HMRC's view the FTT gave more weight than it should have to the evidence of DDL and less weight than it should have to references to accommodation in the Total Contact. That is on examination a challenge to the FTT's findings based on the principles in *Edwards v Bairstow*[5], notwithstanding that Mr McNall said that he made no such challenge. The Upper Tribunal recently summarised the position in relation to such a challenge in *HMRC v Anna Cook* [2021] UKUT 0015 (TCC) as follows, at [18] to [19]:

> 18. An appeal to this tribunal lies only on a point of law: section 11(1) of the Tribunals, Courts and Enforcement Act 2007 ("TCEA 2007"). While there cannot be an appeal on a pure question of fact which is decided by the FTT, the FTT may arrive at a finding of fact in a way which discloses an error of law. That is clear from *Edwards v Bairstow* [1956] AC 14. In that case, Viscount Simonds referred to making a finding without any evidence or upon a view of the facts which could not be reasonably entertained, and Lord Radcliffe described as errors of law cases where there was no evidence to support a finding, or where the evidence contradicted the finding or where the only reasonable conclusion contradicted the finding. Lord Diplock has described this ground of challenge as "irrationality".
>
> 19…In considering [such challenges], we have borne in mind the caveats helpfully summarised in *Ingenious Games LLP & Others v HMRC* [2019] UKUT 226 (TCC), at [54]-[69]. The bar to establishing an error of law based on challenges to findings of fact is deliberately set high, and that is particularly so where the FTT is called on to make a

[5] [1956] AC 14.

multi-factorial assessment. As stated by Evans LJ in *Georgiou v Customs and Excise Commissioners* [1996] STC 463, at 476:

> … for a question of law to arise in the circumstances, the appellant must first identify the finding which is challenged; secondly, show that it is significant in relation to the conclusion; thirdly, identify the evidence, if any, which was relevant to that finding; and fourthly, show that that finding, on the basis of that evidence, was one which the tribunal was not entitled to make. What is not permitted, in my view, is a roving selection of evidence coupled with a general assertion that the tribunal's conclusion was against the weight of the evidence and was therefore wrong. A failure to appreciate what is the correct approach accounts for much of the time and expense that was occasioned by this appeal to the High Court.

100. To the extent that this is HMRC's real complaint, we regard it as an example of what Evans LJ described as a roving selection of the evidence before the FTT coupled with an assertion that the FTT's conclusion was against the weight of that evidence. That is insufficient to demonstrate that the FTT erred in law. We note in this context that the FTT found, and took into account, that the focus of the Total Contract was the TSV function, with "minimal detail" being included in respect of accommodation (paragraph [171(1)], above).

101. It is not clear whether the third alleged error is merely intended as an example of the first two alleged errors. If it is, we reject it for the reasons given above. Insofar as it is an independent argument, it is again an *Edwards v Bairstow* challenge, and in fact does not reflect paragraph [98], which concludes that the acceleration was important because Total wanted continuity of drilling operations. It was HMRC's case that the increased accommodation was part of this, but the FTT rejected that argument because if drilling operations ceased (the Borgsten having to return onshore to carry out the survey) then Total would have no need for additional accommodation. The FTT set out the evidence on which it based that conclusion at paragraphs [94] and [95], and we consider it clear that their conclusion discloses no error of law.

**Ground 2: Conclusion**

102. HMRC's appeal under Ground 2 is dismissed.

**Disposition**

103. HMRC's appeal is dismissed.

**Signed on Original**

**MRS JUSTICE FALK**
**JUDGE THOMAS SCOTT**

**RELEASE DATE: 4 August 2022**