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3rd REPORT
([2004] UKHL 51)
on appeal from: [2002] EWCA Civ 1853

APPELLATE COMMITTEE

Barclays Mercantile Business Finance Limited (Respondents)

v.

Mawson (Her Majesty's Inspector of Taxes (Appellant)

REPORT

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3rd REPORT

from the Appellate Committee

25 NOVEMBER 2004

Barclays Mercantile Business Finance Limited (Respondents)
v.
Mawson (Her Majesty's Inspector of Taxes) (Appellant)

ORDERED TO REPORT

The Committee (Lord Nicholls of Birkenhead, Lord Steyn, Lord Hoffmann, Lord Hope of Craighead and Lord Walker of Gestingthorpe) have met and considered the cause *Barclays Mercantile Business Finance Limited (Respondents) v. Mawson (Her Majesty's Inspector of Taxes) (Appellant)*. We have heard counsel on behalf of the appellants and respondents.

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

Capital allowances

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

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

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

> "(1) Subject to the provisions of this Part, where—
>
> (a) a person carrying on a trade has incurred capital expenditure on the provision of machinery or plant wholly and exclusively for the purposes of the trade, and
>
> (b) in consequence of his incurring that expenditure, the machinery or plant belongs or has belonged to him,
>
> allowances and charges shall be made to and on him in accordance with the following provisions of this section."

BMBF

5. BMBF is a member of the Barclays group which carries on the trade of finance leasing or providing "asset based finance". It is the UK market leader in this field. The essence of its business is to provide capital for the purchase of an asset for use by its customer in return for a series of periodic payments secured upon the asset itself. The transaction normally takes the form of a

purchase of the asset by BMBF, either from a third party or (by way of "sale and lease back") from the customer himself, followed by the grant to the customer of a lease at a rent calculated to secure BMBF an appropriate return. BMBF has the security of being owner of the asset and entitled in the event of default to sell it and recover the sums outstanding.

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

The pipeline

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

The sale and lease back

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

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

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

11. At the same time BMBF, BGE and BGE (UK) entered into an Assumption Agreement by which BGE (UK) assumed direct liability to BMBF to pay the rent due under the head lease. BMBF agreed to accept these payments in discharge of BGE's liability and BGE agreed to treat them as discharging BGE(UK)'s liability under the sublease. The only complication arose from the absence of any provision for adjustment of the rent under the sublease. Park J described what he understood would be the position if the rent under the headlease was adjusted ([2002] STC 1068, 1089-90, para 18):

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

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

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

The scheme

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

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

they were not security arrangements. They neutralised the effect of the transaction in providing finance to BGE and took it outside the scope of section 24(1).

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

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

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

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

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

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

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

The decisions of the special commissioners and the judge

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

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

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

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

21. The special commissioners summed up their views on the effect of the transactions:

> "The only benefit which BGE obtained from the very complicated arrangements choreographed by BZW were amounts B and C paid to it under the terms of the deposit agreement. Payments of amount A returned eventually to BMBF and from BMBF to the bank. BGE was to benefit to an extent of £8.1m net and the Irish government was to receive £1.8m in stamp duty. Those payments would be financed entirely by United Kingdom taxpayers by means of the hoped for capital allowances. Without the capital allowances BGE would receive nothing, for the amounts of the rents would increase to take account of the non-availability of capital allowances.
>
> Looking at the matter in the round, we accept Mr Goy's primary submission that the payment of money by BMBF, even if it is said to have involved BMBF incurring expenditure, cannot be said to have been expenditure on the pipeline.
>
> The payment by BMBF to BGE achieved no commercial purpose. Commercially driven finance leasing is designed to provide working capital to the lessee. But BGE could not get its hands on the money. It parted with a valuable asset allegedly for £91,292,000 but received no immediate benefit from the transaction. [BMBF] provided no finance to BGE simply because the amounts had to be deposited as part of the arrangements with Deepstream to be repaid only in accordance with the deposit agreement with Deepstream…
>
> In our judgment the purpose of the expenditure by BMBF on 31 December 1993 was not the acquisition of the pipeline but the obtaining of capital allowances which would result in ultimately a profit to BGE and fees payable to BMBF and BZW. The transaction had no commercial reality."

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

> "But in the transaction involved in the present case no up-front finance was provided. BGE already owned the pipeline and had paid for it with a loan from a syndicate of banks. After the transaction BGE was still able to use the pipeline

> as before, though by then it did so by virtue of the lease, sublease and transportation agreement, and it still owed to the banks the money which it had borrowed. Nor was the £91m available to BGE for it to use in any other way to finance transactions or activities of its business."

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

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

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

The Court of Appeal

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

The Ramsay *principle.*

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

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

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

own separate tax consequences, whatever might be the terms of the statute. As Lord Steyn said, it was:

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

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

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

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

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

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

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

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

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

33. The simplicity of this question, however difficult it might be to answer on the facts of a particular case, shows that the *Ramsay* case did not introduce a new doctrine operating within the special field of revenue statutes. On the contrary, as Lord Steyn observed in *McGuckian* [1997] 1 WLR 991, 999 it rescued tax law from being "some island of literal interpretation" and brought it within generally applicable principles.

34. Unfortunately, the novelty for tax lawyers of this exposure to ordinary principles of statutory construction produced a tendency to regard *Ramsay* as establishing a new jurisprudence governed by special rules of its own. This tendency has been encouraged by two features characteristic of tax law, although by no means exclusively so. The first is that tax is generally

imposed by reference to economic activities or transactions which exist, as Lord Wilberforce said, "in the real world". The second is that a good deal of intellectual effort is devoted to structuring transactions in a form which will have the same or nearly the same economic effect as a taxable transaction but which it is hoped will fall outside the terms of the taxing statute. It is characteristic of these composite transactions that they will include elements which have been inserted without any business or commercial purpose but are intended to have the effect of removing the transaction from the scope of the charge.

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

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

> "[T]he driving principle in the *Ramsay* line of cases continues to involve a general rule of statutory construction and an unblinkered approach to the analysis of the facts. The ultimate question is whether the relevant statutory provisions, construed purposively, were intended to apply to the transaction, viewed realistically."

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

38. *MacNiven* shows the need to focus carefully upon the particular statutory provision and to identify its requirements before one can decide whether circular payments or elements inserted for the purpose of tax avoidance should be disregarded or treated as irrelevant for the purposes of the statute. In the speech of Lord Hoffmann in *MacNiven* it was said that if a statute laid down requirements by reference to some commercial concept such as gain or loss, it would usually

follow that elements inserted into a composite transaction without any commercial purpose could be disregarded, whereas if the requirements of the statute were purely by reference to its legal nature (in *MacNiven*, the discharge of a debt) then an act having that legal effect would suffice, whatever its commercial purpose may have been. This is not an unreasonable generalisation, indeed perhaps something of a truism, but we do not think that it was intended to provide a substitute for a close analysis of what the statute means. It certainly does not justify the assumption that an answer can be obtained by classifying all concepts *a priori* as either "commercial" or "legal". That would be the very negation of purposive construction: see Ribeiro PJ in *Arrowtown* at paras 37 and 39 and the perceptive judgment of the special commissioners (Theodore Wallace and Julian Ghosh) in *Campbell v Inland Revenue Commissioners* [2004] STC (SCD) 396.

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

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

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

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

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

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