Case Ref: SC/CIV/03/21

IN THE SUPREME COURT
OF THE FALKLAND ISLANDS

Courts and Tribunal Service
Stanley
Falkland Islands

Date: 31 January 2022

Before:

THE HONOURABLE JAMES LEWIS QC
(CHIEF JUSTICE OF THE FALKLAND ISLANDS)

- -

THIS JUDGEMENT HAS BEEN REDACTED IN COMPLIANCE WITH SECTION 202 TAXES ORDINANCE 1997

BETWEEN:

A LIMITED

Appellant

And

COMMISSIONER OF TAXATION

Respondent

Julian Ghosh QC and Laura Ruxandu for the Appellant

Laura Poots for the Respondent

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THE CHIEF JUSTICE:

I. INTRODUCTION AND BACKGROUND

1. This is an appeal against a determination of the Tax Appeal Tribunal ("TAT") dated 20 August 2021 ("the Determination"). The appeal concerns the tax liability of the Appellant for two periods which covered 5 February 2015 to 29 February 2016.

2. In the Falkland Islands there is a regime under the Taxation Ordinance 1997 ("TO") whereby petroleum extraction activities are 'ring-fenced' for tax purposes. If the activities in question are ring-fenced then a higher charge to profits is applied and leasing cost expenses are capped at annual maximum 7.5% of the original cost of the leased vessel. The question that arises on this appeal is whether the Appellant is within those ring-fenced provisions or is the Appellant within the ordinary corporation tax regime.

3. The Appellant is a member of a corporate group ("the A Group"), the parent company of which is B Limited. The Appellant and its parent were incorporated in the United Kingdom.

4. In 2015, C Limited ("C") and D Ltd ("D") were undertaking an exploration programme in the Falkland Islands for oil, utilizing the 5th/6th generation, harsh environment, *F* mobile offshore drilling unit.

5. C and D started a tender process that commenced in August 2014 inviting tenders for two Platform Supply Vessels ('PSVs') and an Emergency Response and Rescue Vehicle ('ERRV'). The provision of the vessels was for the support of the exploration programme undertaken by C and D using the *F* mobile offshore drilling unit.

6. A Group tendered for and were offered the contract for the ERRV by letter dated the 3rd October 2014. A Ltd, the Appellant, was incorporated on the 5th December 2014.

7. The Appellant entered into a tripartite time charter party with C and D on 9 December 2015 for the period it took to drill 6 wells. Both the tender invitation and the Time Charter Party contract required the ERRV to comply with the ERRV Guidelines.

8. During the relevant period, C and D were undertaking exploration programmes for oil, offshore the Falkland Islands. The Appellant's ERRV used to support these exploration programmes was the *Fastnet A* which it leased from another member of the A Group, E Limited. The Charter price was USD 25,500 per day. The leasing cost was USD 12,000 per day.

9. The *Fastnet A*'s primary purpose was to provide emergency response and rescue services. The services of A were only required in case of an emergency, events which all parties hoped would not occur. During the Time Charter Party, there were no incidents.

10. The services provided by the Appellant to C and D were to:

    1) rescue persons from the water and provide medical aid;
    2) act as a place of safety in accordance with the Offshore Installations (Prevention of Fire Explosion Emergency Response Regulations) 1995 SI 1995No 743 (PFEER);
    3) provide on scene coordination as required;

4) participate fully in executing the Installation collision avoidance strategy;
5) act as reserve radio station;
6) try to divert objects which were drifting towards the platform and alert other vessels if they were sailing in the direction of the rig;
7) try to disperse oil spills, or try to clean it using the vessels oil gathering equipment; and
8) in one instance the carriage of cargo.

11. It is common ground that the Appellant is within the scope of Falkland Islands' corporation tax. The issue that arises is the extent to which the leasing costs for the *Fastnet A* are deductible in calculating the Appellant's profits.

II. PROCEDURAL HISTORY

12. The Appellant filed its tax return for 2015 in September 2016 and for 2016 in August 2017. Both assessments were filed with deduction of the full leasing costs for the *Fastnet A* payable to its sister company under the lease agreement.

13. On 20 October 2020, the Respondent issued Tax Assessments, which cover the period to 31 December 2015 and the period to 29 February 2016 respectively, increasing the Appellant's taxable profits to £775,445 for 2015 (disallowing part of the deduction of the leasing costs: £543,743), and to £464,163 for 2016 (disallowing part of the deduction of the leasing costs: £337,713.

14. The Appellant appealed these tax assessments to the TAT who held a full evidential hearing pursuant to Schedule 3 to the TO.

15. On 20 August 2021 the TAT dismissed the appeal and on 17 September 2021 the Appellant appealed the Determination to the Supreme Court.

16. The grounds of appeal made by the Appellant concern the three issues before the TAT. Those issues were:

> "Issue 1", the connection issue: whether A undertook activities "in connection with" the search for petroleum within the meaning of ss. 150(1) and 140 TO 1997;
>
> "Issue 2", the contractor issue: whether A was a "contractor" for another person carrying on ring-fenced activities within the meaning of TO 1997 s. 150(11);

"Issue 3", the discrimination issue: whether, if A is wrong in relation to Issues 1 or 2 above, the Falkland Islands legislation in respect of ring-fenced trades (including TO 1997 ss. 140, 150, 152A, 152B and following) is discriminatory contrary to Article 25 of the DTA.

17. In the grounds of appeal the Appellant stated that in respect of Issue 1, the TAT erred in law in concluding that the Appellant undertook activities "in connection with" the search for petroleum because:

    1) it held there was no link between the words "in connection with" appearing in the United Kingdom and Falkland Islands Double Taxation Agreement ("DTA") and the same words in the domestic legislation;
    2) it made no findings of fact as to how the activities undertaken by the Appellant were connected with the "search for petroleum";
    3) its reasoning that the Appellant fulfilled the legal requirements of Regulation 17 is misconceived;
    4) it ignored the evidence which showed the Appellant provided the same services to the United Kingdom government;

18. In respect of Issue 2 Appellant stated that the TAT erred in its interpretation of s.150(11) of the TO in concluding the Appellant was a contractor undertaking activities for the purpose of C and D. The TAT erred in:

    1) placing too much emphasis on the word 'contractor' in contractual documents instead of the interpretation from the statute;
    2) it misrepresented the Appellant's argument; namely, the Appellants submission was that one needs to be a contractor assigned part of the ring-fenced trade; and
    3) it failed to provide reasoning for its interpretation of section 150(11) of the TO.

19. The Appellant had an alternative argument that arose if Issues 1 and 2 were rejected; namely that the legislation was indirectly discriminatory contrary to Article 25 of the Double Taxation Treaty ("DTA") between the United Kingdom and the Falkland Islands. The complaint was that the TAT did not decide this issue despite holding Issues 1 and 2 against the Appellant.

20. It can be seen that part of the grounds of appeal put forward by the Appellant are not issues of law in that there is a complaint - [17.4)] is about evidence (not on rationality grounds), which is in any case wrong as the TAT did consider this point at paragraph [84] of the Determination. The complaints at [17.2)] and [18.3)] are an adequacy of reasons

challenge, although Mr Ghosh specifically resiled from saying his challenge was a 'reasons' challenge.

21. It is to be emphasised that an appeal pursuant to Schedule 3 paragraph 4 of the TO is not a re-hearing of the appeal before the TAT. It is a second appeal on a point of law. In relation to the TAT, there is no doubt that tribunal exercises an appellate jurisdiction. As Simon Bryan CJ (as he then was) said in *Commissioner of Taxation v A* SC/CIV/18/16*:*

> "There is no express provision in the Tax Ordinance which articulates the Tribunal's powers or the function of the Tribunal. However it is common ground between the parties, as is clearly right, that it is an appellate jurisdiction. The function of the Tribunal is therefore supervisory, that is to say, the Tribunal could not simply substitute its own views for those of the Commissioner as to the merits as to how the discretion under section 200 of the Taxes Ordinance should be exercised – see *GB Housley Limited v The Commissioners for Her Majesty's Revenue and Customs* [2016] EWCA Civ 1299 and the judgment of Gloster LJ, in particular at paragraph 69 thereof."

III. THE RELEVANT LEGISLATION

22. So far as relevant to the period in dispute the TO reads:

Section 140:

> Petroleum extraction activities means any activities carried on in connection with –
>
> (a) searching for petroleum
>
> (b) extracting petroleum
>
> (c) transporting petroleum
>
> (d) effecting initial treatment or initial storage of petroleum
>
> (e) decommissioning or abandoning plant or machinery previously used or designed to be used in connection with an activity within paragraphs (a) to (d). [Emphasis added]

Section 150:

> (1) where a person carries on as part of a trade-
>
> (a) any petroleum extraction activities;
>
> (b) any of the following activities, namely, the acquisition, enjoyment or exploitation of petroleum rights; or
>
> (c) activities of both those descriptions,
>
> Those activities shall be treated for the purposes of this Ordinance as a separate trade, distinct from all other activities carried on by him as part of the trade.
>
> …

(11) A reference in this Act to a ring fence trade includes a reference to anything undertaken by one person (C) as a contractor for another person (P) who carries on a ring fence trade for the purposes of this Chapter, if and in so far as C's activities are undertaken for the purposes of P's ring fence trade.

Section 152A (repealed):

(1) Leasing costs incurred by a company shall not be allowable under section 97 as a deduction against the company's ring fence income except to the extent permitted by subsection (2) below, but subject to subsections (3) (4) and (5) below and section 155.

…

(5) Leasing costs paid by a company in respect of plant or machinery leased from a connected person shall not be allowable under section 97

Section 152B:

(1) Section 152C applies to a company which carries on a ring fence trade if –

(a) the company makes or is to make one or more payments under a lease of a relevant asset, or part of a relevant asset, for the purposes of its ring fence trade; and

(b) any of the following applies –

(i) the lessor is an associated person of a contractor;

(ii) the lessor is a person who is connected with the company, or was connected with the company when the lease was imposed;

(iii) the Commissioner notifies the company that the Commissioner considers that the lease is made in connection with arrangements with a main purpose of securing a tax advantage.

(2) For the purposes of subsection (1), a person is a contractor if the person carries out any of the following activities for the company –

(a) exploration or exploitation activities in, or in connection with, providing, operating or using a relevant asset in a relevant offshore service;

(b) any other activity in, or in connection with, providing a relevant offshore service.

…

(6) In this section –

…

"exploration or exploitation activities" does not include petroleum extraction activities or activities consisting of the acquisition, enjoyment or exploitation of petroleum rights;

"provide a relevant offshore service" means provide, operate or use a relevant asset in, or in connection with, carrying on exploration or exploitation activities in controlled waters;

"relevant asset" has the meaning given to it in section 152E;

152C:

(1) The total amount that may be brought into account in respect of the payments for the purposes of calculating the company's ring fence income in an accounting period is limited to the hire cap.

(2) The "hire cap" is an amount equal to the relevant percentage of TC for the accounting period, subject to subsection (3).

***152D**:*

(1) Subject to subsection (2), the percentage appropriate for a relevant asset is 7.5%.

152E:

(1) Subject to subsections (4) and (5), in sections 152B, 152C and 152D, "relevant asset" means an asset which is of the requisite value.

(2) A reference to an asset in subsection (1) is a reference to an asset (including a ship or other vessel) that − (a) can be moved from place to place (whether or not under its own power) without major dismantling or modification; (b) can be used in connection with a ring fence trade; and (c) is or will be provided, operated or used in controlled waters for 30 days or more in aggregate within a continuous 12 month period. (3) An asset is of the requisite value if its market value is £2,000,000 or more. …"

23. The Offshore Installations (Prevention of Fire and Explosion and Emergency Response) Order 1998, Regulation 17 of the FI Regulations provides:

"Arrangements for recovery and rescue

The duty holder shall ensure that effective arrangements are made, which shall include such arrangements with suitable persons beyond the installation, for-

(a) recovery of persons following their evacuation or escape from the installation; and

(b) rescue of persons near the installation; and

(c) taking such persons to a place of safety,

and for the purposes of this regulation arrangements shall be regarded as being effective if they good prospect of those persons being recovered, rescued, and taken to a place of safety."

24. The UK-Falklands Double Taxation Agreement.

Article 21:

"(1) The provisions of this Paragraph shall apply notwithstanding any other provision of this Arrangement.

(2) In this Paragraph the term "offshore activities" means activities which are carried on offshore in a territory in connection with the exploration or exploitation of the seabed and subsoil and their natural resources situated in that territory.

…

(5) Profits derived by an enterprise of a territory from the operation, in connection with offshore activities in the other territory, of ships or aircraft, may be taxed in that other territory."

Article 25:

"(1) The taxation on a permanent establishment which an enterprise of a territory has in the other territory shall not be less favourably levied in that other territory than the taxation levied on enterprises of that other territory carrying on the same activities."

IV. THE DECISION OF THE TAT

25. In a comprehensive Determination the TAT set out the core facts, reviewed the relevant legislation and case law, set out the evidence before them, identified the Appellant's and Respondent's arguments, and made a decision. The TAT said:

> Issue 1
>
> <u>The Appellant's Arguments</u>
>
> 91. The first issue is whether or not the Appellant's activities were carried on in connection with searching for petroleum to bring the Appellant within the ring-fence. The Appellant argues that they are not. A did not search for petroleum under s140(a) and this is the only petroleum extraction type activity undertaken. In paragraph 62 of Mr Ghosh's skeleton argument it says, 'A's activities have only been in connection with the rescue and recovery of C and D personnel. This connection between A's services and the rescue and recovery of individuals displaces any connection with searching for petroleum etc'.
>
> 92. The activity of rescuing the personnel is connected to someone falling in the water. The dispersal of oil is connected to an oil spillage. These emergency events displace the connection to petroleum activities just as in the Barclays case the connection to being a pensioner is displaced by the quiz. You may be invited to the quiz because you are a pensioner but you win because you answer the questions correctly.
>
> 93. With reference to the case law, the Barclays case allows a broad interpretation of 'in connection with', but within the context of the legislative scheme, and considering all the facts of the particular circumstances of a case to assist with the interpretation. None of the other cases we were referred to detracts from that. The Tribunal notes that case law from the UK is of assistance in interpreting Falkland Islands' legislation but not binding.
>
> 94. The Tribunal were told that the services are connected to a contingent event that no one wants to happen which is an emergency taking place. In no sense did A contribute to searching for oil.
>
> 95. Mr Ghosh says that even the Financial Secretary does not include a rescue vessel in his report (HBp643) when he refers to who would be caught or not within the words 'in connection with' in paragraph 6.9. The Tribunal have considered this but, looking at paragraph 6.9, are of the view the Financial Secretary was referring to those who are potentially taxable under s2.1 and not under the amended s140.
>
> 96. Mr Ghosh suggests that the Tribunal should be careful not to let the Commissioner remove the Tribunals jurisdiction as he suggests in paragraph 6.11.

97. We are asked to consider Article 21 of the DTA. Mr Ghosh in his opening submissions led the Tribunal through the UK –Falkland island DTA1997 (Authorities Bundle p178) making it clear that A as a UK company was subject to Falkland Island tax because of Article 21(5). A are connected to offshore activities through C and D. They themselves do not undertake offshore activities. It was then suggested in closing submissions that the basis of taxation under the DTA was under Article 22(2) and Article 21(5) was not required, with the need to establish a connection, albeit under a different structure to that in the TO1997. Mr Ghosh suggests that is correct as the UK and the Falkland Islands would have an eye for each other's tax legislation.

98. We can say now that the Tribunals view is that the DTA and the TO 1997 are separate in their purposes. One is to decide if a UK company is subject to Falkland Islands tax as Mr Ghosh has said, and the other is to decide if and how much tax might be due subject to Falkland Islands law, drafted for this jurisdiction and its own domestic requirements and passed by this legislature. Whether FI and UK have an eye for each other's legislation is not a matter that the Tribunal need consider.

99. Finally, a time was spent during the hearing on the matter of the legal and regulatory requirements for the support C and D looked for and what they actually sought in the Invitation to Tender. The companies had to satisfy Regulation 17 of the Offshore Installations (Prevention of Fire and Explosion and Emergency Response) Order 1998. They did so comprehensively in the Invitation to Tender which reflected the Guidance, their own companies' policies and the needs of any operative working in harsh conditions. That was their choice.

The Respondent's Arguments

100. Miss Poots, for the Respondent, took no point on A falling under Article 21(5) DTA and this then having an impact on the interpretation of 'in connection with' under s140 TO1997 and further said that Article 21 should not be considered before domestic legislation. It is clearly the case that the Falkland Islands, under Article 21- have taxing rights over the Appellant from its activities with C and D. We have addressed our view on this already.

101. Regarding the interpretation of 'in connection with' in s 140, Miss Poots says 'in connection with' should be interpreted with the facts of this case and in statutory context. With reference to the Barclays pensioners case Miss Poots reminded the Tribunal that LJ Arden had said that it is rare for one connexion to be displaced with another, with the example of the pensioners receiving quiz prize money in mind, and did not agree that there was a similarity to the quiz example and A's position. As activities flow from those of C and D. They do not provide only search and rescue capability, services for other activities shows the strength of the connection, not just search and rescue but the monitoring for debris, and the oil spill management and the high alert in moments of greater possible dangers, abseiling scaffolders and helicopter landings. Miss Poots advised us to look at the facts of this case and not generalisations. We were reminded of the use of language in the tender, time charter and Tripartite agreement, that the word support was used, reference to time in terms of 'wells firm'. A was engaged by C and D to supply support services for the drilling campaign. There was no other connection that displaced that.

102. Miss Poots suggests that if you only wanted petroleum based activities you could have left out 'in connection with' in our legislation. Her view is that you can rely on the words in the statute.

103. C and D had to satisfy Regulation 17, which broadly says you have to have a rescue service. They decided to go beyond the limit of s17 and get a 24/7 high level service from the potential contractor, as set out in their tender document. This is the service provided on which the decision as to in connection with is based. Not something speculative without evidence.

Decision on Issue 1

104. The Tribunal agree with the Respondent. The words 'in connection with' on a broad interpretation in the context of our legislative scheme and taking into account the facts of this case, do bring the Appellant within the ring-fence. The activities described by Mr M in his statement are not only search and rescue, but include monitoring the area around the installation, warning vessels of the installation and vice versa, monitoring for debris, moving cargo if needed, and indeed moving cargo on one occasion. The monitoring was intensified for the movement of helicopters and when persons were working on the installation such as scaffolders.

105. A fulfilled the legal requirements of Regulation 17 and the obligations they had taken on under the Time Charter informed by the Invitation to tender, which informed the terms under which they carried out the support services they provided to the Respondent.

106. It is possible that C and D could have used a lower level of service to fulfil their obligations under Regulation 17. This Tribunal is not concerned with what might have been used but what was actually used.

Issue 2

<u>The Appellant's Argument</u>

107. The Appellant argues that A is not a contractor as required under s150(11) and therefore does not fall within the ring-fence. The key points in s150(11) are the need to have something undertaken by a person as a contractor for someone else, and it has to be for the purposes of that someone else's ring-fenced trade.

108. C and D clearly carry out a ring-fenced trade. The Appellant says that in this case the customers, The Appellant and C and D are unconnected, the revenue paid to the Appellant was for search and rescue and not linked to searching for oil. A contractor is someone who provides services to another entity, in the entities use of their business. A is an unconnected customer of C and D, and as such are not a contractor as termed in s150(11).

109. The success of the Appellant's activity is not dependent on C and D's success.

110. The Appellant has not artificially taken away something that C or D do.

111. If s150(11) were to be interpreted as suggested by the Respondent it would be limitless and anyone who had a contract with C and D would fall under the ring fence. That is not what was intended.

<u>The Respondent's Argument</u>

112.The Respondent says that s150(11) is clear in its meaning and not limitless, because the ring-fence boundary prescribes who will come into s150(11), and the words 'if and in so far as' also limit the link to an oil related activity. The section is drafted to ensure the ring-fence is applied only to a contractor's income so derived, recognising other sources of income.

113. The section does not limit a contractor to one who is connected to the recipient of the services. The ordinary meaning of contractor does not require the connection suggested.

114. The Appellant's activities are linked to the activities of C and D in their search for oil because of the services they provided.

115. The success or otherwise of C and D does not affect s150(11).

Decision on Issue 2

116. The Tribunal agrees with the Respondent. We have already decided that the Appellant is within the ring-fence under s150 and s140. We consider the same services provided by A in making the connection between the Appellant and C and D, as we did for Issue 1. Under s150(11) we consider that the Appellant's activities were 'for the purposes' of C and D's ring-fence trade.

117. It is the Tribunal's view that the word 'contractor' has an ordinary meaning that is not artificially restricted in its use in the TO1997 by the need to find a connection as suggested by the Appellant .

Issue 3

118. It is the Tribunals view that because of the decisions we have made in Issue 1 and 2 there is no requirement for us to give any view on whether the TO1997 is discriminatory.

V. SUBMISSIONS OF THE PARTIES BEFORE THIS COURT

26. In many ways the submissions by the Appellant have been a repetition of the arguments before the TAT but with the gloss of arguing the TAT misdirected itself as to the true construction of the legislative provisions, failed to give adequate reasons, failed to identify relevant facts and misunderstood the original arguments. It will be necessary for me to identify how these arguments have been recast and developed in this appeal. I will do so under the discussion section below.

VI. DISCUSSION

A. Appeal to this court

27. The appeal to this Court is pursuant to Schedule 3 paragraph 4 of the Taxes Ordinance which provides:

> "(2) The Appellant and the Commissioner may appeal against the determination of the Tribunal to the Supreme Court on a point of law.
>
> (3) An appeal under this paragraph shall be lodged by the Appellant or the Commissioner in triplicate with the Registrar of the Supreme Court within twenty-eight days of the receipt by the Appellant or the Commissioner (as the case may be) of the notice of the Tribunal's determination; and the notice of appeal shall-
>
> (a) specify the points of law in question;

(b) the reasons for alleging that in relation to that point of law, that the Tribunal was in error.

(4) On determination of an appeal under this paragraph the Supreme Court may- "(a) correct any immaterial informality or error in the determination of the Tribunal which it is satisfied can be made without injustice to the parties; (b) quash or vary the determination of the Tribunal in such manner as it considers appropriate; and (c) make any other order it considers appropriate in the circumstances of the case (including, without prejudice to the generality of the foregoing, an order as to the costs of the appeal to the Supreme Court."

28. An appeal to this court on a point of law is not a re-hearing. There must be a discernable error of law in the determination of the tribunal. As Laws LJ said at paragraph 21 in *One of Her Majesty's Inspectors of Health and Safety v Rotary Yorkshire Limited [2015]* EWCA Civ 696 a point of law means either a material legal error, a misconstruction of a relevant statutory provision, a finding of fact not rationally supportable on the evidence or a procedural error leading to unfairness. This court is not entitled to substitute its own conclusion unless there was no other rational or legal conclusion the TAT could have come to.

B. The correct approach

29. In so far as this appeal turns on statutory construction, the principles should not be contentious. The Court's duty is to establish the legislative intention. The legislative intention relates to the legal meaning of the enactment. The intention of the legislature is an objective concept as explained by Lord Nicholls in *R v Secretary of State ex parte Spath Holme Ltd 2 AC 349, at 396.*

30. The starting point in determining the legislative intention is the text itself. The context and mischief are obviously relevant and important aids to construction but as Lord Neuberger said in *Williams v Central Bank of Nigeria* [2014] UKSC 10 at [72]:

> " .. When interpreting a statute, the court's function is to determine the meaning of the words used in the statute. The fact that context and mischief are factors which must be taken into account does not mean that, when performing its interpretive role, the court can take a free-wheeling view of the intention of Parliament looking at all admissible material, and treating the wording of the statute as merely one item. Context and mischief do not represent a licence to judges to ignore the plain meaning of the words that Parliament has used. As Lord Reid said in *Black-Clawson International Ltd v Papierwerke Waldhof-Aschaffenburg AG [1975] AC 591* , 613, "We often say that we are looking for the intention of Parliament, but that is not quite accurate. We are seeking the meaning of the words which Parliament used".

31. The interpretive criteria are aids to construing the legislative text. Sales J. (as he then was) said in *Bogdanic v Secretary of State* [2014] EWHC 2872 at [48]:

> "The overarching requirement is that a court should give effect to the intention of the legislator, as objectively determined having regard to all relevant indicators and aids to construction."

32. Context as an aid to construction includes consideration of the enactment as a whole, and its social and legislative history, but is subject to the general rules as to the admissibility of external aids to construction.

1. *The purpose of Part VI of the TO*

33. Part VI of the TO was enacted to apply special rules to ring-fenced trades and related activities. It consists of four chapters including a definitions section. It was clearly enacted to impose a special tax regime on oil exploitation and extraction in and around the Falkland Islands' waters.

34. The submission by Mr Ghosh QC that the hire cap was imposed to prevent transfer pricing is only partially correct. The overall regime in Part VI was to benefit the Falkland Islands from a different tax rate where oil exploration, extraction and transportation was involved. In short it was meant to encompass the oil industry arising out of the mineral resources on the seabed. The hire cap was to ensure that excessive expenses were not claimed, and as Mr Ghosh QC submits, in part to prevent transfer pricing to related entities taxable elsewhere. However, the categorisation of a ring-fenced trade was clearly not aimed at transfer pricing, and that is the definition with which we are grappling.

35. The submission by Mr Ghosh QC that the Appellant's profits have no connection at all to the success or otherwise of any oil related activity is neither accurate or to the point. Safety and rescue services are integral to the operation of the oil rig. The definition of ring-fenced trade in section 140 is:

> 'ring-fence trade" means a trade consisting of any of the activities referred to in section 150(1) (whether or not the trade is a separate trade by virtue of that provision).

36. The words in parenthesis indicate that the legislature intended to catch separate trades that were an integral part of any oil exploration or exploitation activities. No legislative

intention can be derived that integral support services such as safety and rescue services should be excluded from the ring-fenced activities.

2. *Legislative history*

37. The legislature amended section 140 of the TO in 2015. Previously it had read:

> ' "petroleum extraction activities" means any activities of a person –
> (a) in searching for petroleum or causing such searching to be carried out for him; or..'

After amendment in 2015 it reads:

> ' "petroleum extraction activities" means <u>any activities carried on in connection with</u> searching for petroleum…

38. The words 'in connection with' which have been added, in either a declaratory or amending sense, are clearly intended to ensure that "petroleum extraction activities" are given a wide meaning, otherwise the additional words would be otiose.

3. *The textual context*

39. The words 'in connection with' are not capable of a precise legal definition. They are not causative but require that the activities are 'having to do with' searching for petroleum. A link is necessary and the purpose, mischief and context of the legislative scheme will inform the court as to the extent of the link required by section 140 of the TO.

40. In another tax case the words 'in connection with' were construed. In *Barclays Bank Plc, Trustees of the Barclays Bank Pension Fund v Commissioners for Her Majesty's Revenue and Customs* [2007] EWCA Civ 442, Arden LJ said at [18]:

> 18. The primary question in this case is the proper meaning of the words "in connection with past service" in section 612(1) of ICTA . The expression "in connection with" could describe a range of links. In *Coventry Waste Ltd v Russell [1999] 1 WLR 2093* at 2103, Lord Hope held that in this situation the court must look closely at the surrounding words and the context of the legislative scheme:
>
> "The majority in the Court of Appeal held that it was a sufficient answer to the Appellant's argument to construe the words "in connection with" as meaning "having to do with". This explanation of the meaning of the phrase was given by McFarlane J in Re Nanaimo Community Hotel Limited [1944] 4 D.L.R. 638 . It was adopted by Somervell L.J. in *Johnson v. Johnson [1952] P. 47* , 50–51. It may be that in some contexts the substitution of the words "having to do with" will solve the entire problem which is created by the use

> of the words "in connection with." But I am not, with respect, satisfied that it does so in this case, and Mr. Holgate did not rely on this solution to the difficulty. As he said, the phrase is a protean one which tends to draw its meaning from the words which surround it. In this case it is the surrounding words, when taken together with the words used in the 1991 Amending Order and its wider context, which provide the best guide to a sensible solution of the problem which has been created by the ambiguity."

41. There are unquestionably links between the provision of an ERRV used to support a deep sea mobile drilling unit ("MODU") and in the search for petroleum. If C or D were not searching for petroleum then the Appellant would not have provided its services to them. The question is whether the links that exist are those intended by the legislature such to make the activities 'in connection with' the activity of searching for petroleum.

42. By way of example the provision of food supplies to the crew on the MODU would not fall within the legislative intention, but the supply of crew for the MODU itself, if such supply was chargeable to tax in the Falklands Islands, would be sufficiently linked.

C. Issue 1 - were the activities of the Appellant a ring-fenced trade?

1. *The DTA*

43. It is common ground that the Falkland Islands have taxing rights over the activities of the Appellant. However, the route by which each party gets there is different.

44. The Appellant says that Article 21(5) of the DTA creates the taxing rights, while the Respondent says Article 21(3) in conjunction with Article 7 (permanent establishment) creates the taxing rights.

45. It is of note that both Article 21(3) and (5) depend on the definition of 'offshore activities. However, Article 21(5) is one further removed in that it depends upon activities of ships or aircraft 'in connection with' 'offshore activities'; and *'offshore activities'* is itself defined by Article 21(2) as '*activities which are carried on offshore in a territory in connection with the exploration or exploitation of the seabed'*.

46. As I understand the Appellant's submission, this means by virtue of Article 21(5) you can be taxed on activities which are not offshore activities themselves. It is this point that the Appellant puts forward as showing that the phrase has a more narrow meaning, otherwise its repetition would be otiose. Because of Article 3(2) the domestic meaning of section 140 TO

takes its context from this and in oral argument Mr Ghosh QC put this as a cross check on the meaning of the words in both the Ordinance and the Treaty; that the words should bear the same meaning in both instruments.

47. Mr Ghosh QC then submitted that the DTA therefore is an aid to construction of the words 'in connection with' in section 140 of the TO and that the TAT erroneously did not use the DTA as such an aid. Ms Poots submits that the DTA does not assist in the interpretation of the phrase. She argues that Article 3(2) DTA requires terms to be interpreted by reference to domestic law. In other words, the meanings of terms used in the TO 1997 inform the interpretation of terms used in the DTA, not the other way round. Finally, she submits that the phrase is not a defined term.

48. Resourceful as the argument of Mr Ghosh QC is, I do not think it carries weight. The phrase 'in connection with' is not a defined term in the DTA. The phrase is a preposition. The purpose of the phrase in Article 21(5) which says that taxing rights may apply, is to widen the taxing rights past deemed permanent establishments; it was not to create a definition of the phrase 'in connection with'. In my judgment it is of little or no assistance in determining the true construction of the same preposition used in a different context in the TO. The TAT committed no error of law in not using it as an aid to construction of the phrase in question.

2. *Application of the facts*

49. The facts were essentially not in dispute before the TAT. It is not a valid criticism to say the TAT did not find facts. The TAT recited the facts, which were uncontentious, and upon those facts made their determination.

50. The TAT stated, at [18], that all three of the two PSVs and the one ERRV were in support of the petroleum exploration program. Moreover, it was a common ground and not a disputed fact that C and D's activities during the time charter was oil exploration. The Tribunal went on to say:

> [60] The invitation to tender (HB p331) was brokered by Stewart Offshore services. It says in its opening sequence that the brokers on behalf of C and D are exclusively inviting B to tender for the provision of two PSVs and one ERRV to support the forthcoming exploration programme utilising the 5th/6th generation, harsh environment MODU *'F'* offshore Falklands in the South Atlantic.

[61] The charter period is for '6 Six wells firm', and this refers to the time that it takes to drill 6 wells.

[62] The vessel specification says that the vessels are required to work to the UK Oil and Gas Emergency Response and Rescue Vessel Management Guidelines Issue 5 April 2013 and comply with UK Oil and Gas ERRV Survey Guidelines Issue 6 2013, referred to as the ERRV Guidelines.

[63] The ERRV Guidelines are found at HBp504. They are produced by the UK Oil and Gas Industry Association Ltd trading as Oil and Gas. The ERRV Guidelines refer to other guidelines, legislation and standards.

[64] Clause 1.2 of the ERRV Guidelines state that the legal requirements for off shore emergency response for offshore installations is to be found in The Offshore Installations (Prevention of Fire, Explosion and Emergency Response Regulations 1995 (SI 1995 No 743) (PFEER). Regulation 17 says;

The duty holder shall ensure that effective arrangements are made, which include such arrangements with suitable persons beyond the Installation, for;

(1) recovery of persons following their evacuation or escape from the Installation and

(2) rescue of persons near the Installation and

(3) taking such persons to a place of safety.

[65] This legislation is United Kingdom legislation. Falkland Islands' legislation is in the same terms with the same numbered Regulation 17 (p59, authorities bundle).

[66] The invitation to tender included the providing of two PSVs platform supply vessels. The scope of the PSVs role was described as including as follows;

"to give adhoc emergency rescue cover for the ERRV, but this should not be interpreted to mean that the vessel is a fully certified ERRV but is equipped to provide limited standby duties"

[67] A did not take up the tender for the PSVs. Mr M told us that one of the two PSVs chartered by C and D had emergency response and rescue capabilities, though these were more limited than the capabilities of the ERRV.

[68] The Invitation to Tender provided more detail as to scope of the work to be carried out by Premier and Noble, referring to a multi well drilling campaign and an exploration and appraisal drilling campaign.

[69] The Invitation to tender contained detailed diagrams and specifications of the wells to be drilled as well as the health and safety obligations imposed on the Drilling Unit The DTA Owner and the Contractor. The word 'contractor' was used throughout.

51. It is clear that the TAT were referring in this passage at paragraph [50] above to the relevant links between the activities of the Appellant and the search for petroleum. C and D needed, or in fact employed whether needed or not, the PSVs and the ERRV to support their oil exploration.

52. The facts show that the provision of the ERRV was an integral part of the Management Safety System of C and D (see section 3 of the invitation to tender). Moreover, the

invitation to tender itself foresaw the activities of the Appellant as part of the ring-fenced trade as Appendix 8 to the invitation to tender indicated as such. The TAT relied upon Regulation 17.

53. The complaint that the TAT did not sufficiently identify the facts or links that brought the Appellant's activities into the requirement of 'in connection with' is misplaced. Read as a whole it is clear the determination shows the TAT identified a number of connections between the Appellant's activities and the search for petroleum. They found expressly in paragraph [104] of the Determination that the linked activities were:

    1) search and rescue;
    2) monitoring the area around the installation;
    3) warning vessels of the installation;
    4) monitoring for debris;
    5) moving cargo if needed;
    6) intensified monitoring when the installation used helicopters or workers outside the installation; and
    7) fulfilling the legal requirements of Regulation 17 on behalf of Premier and Noble.

54. Given the width of the words 'in connection with' and that the TAT was referred to the relevant law which they took into account, the only error of law the Appellant can argue on this appeal is that none of the activities of the Appellant set out above are capable as a matter of law as being in 'in connection with' petroleum exploration within the true meaning of the section. Importantly the TAT found that the Appellant's support fulfilled the Regulation 17 obligations of C and D. The contrary argument that one of the PSVs also had some limited rescue facilities does not detract from that finding.

55. Providing off-shore support activities including statutorily required support activities to C and D's oil drilling rig is in my view legally capable of being activities 'in connection with' searching for petroleum.

56. One only has to ask the theoretical question of whether C and D could have explored for oil in the designated areas without the type and nature of the activities supplied by the Appellant. Given the duty imposed by Regulation 17 on C and D, and the fact that C and D employed the Appellant to provide ERRV services, the answer to that question seems

to me plainly 'no'. If the Appellant had not provided the ERRV activities then someone else (or they themselves) would have had to have provided them in order for C and D to have prospected for oil. ERRV activities are it seems to me a necessary part of oil prospecting by any responsible company. The evidence does not support the submission that one of the PSVs could have done as such, albeit it could provide some limited temporary activities.

57. It follows the TAT did not misdirect themselves in law and came to a legally sound conclusion.

58. It follows I see no reason to interfere with the decision of the TAT that the Appellant's activities in providing support activities including statutorily required support activities to C and D's exploration was a ring-fenced trade. While the line must be drawn somewhere as to whether the links that exist are sufficient to be those intended by the legislature, where the off-shore activities are part and parcel of the overall running of the off-shore oil drilling rig operation, they will be part of the ring-fenced trade. The words "in connection with" the legislator enacted in section 140 TO were intended to encompass such part and parcel activities as provision of ERRV.

D. Issue 2 - Section 150(11)

59. Issue 2 and the construction of section 150(11) does not strictly arise given my findings on section 150(1). However, it was fully and persuasively argued before me by Ms Ruxandu on behalf of the Appellant. The TAT made a finding of fact at paragraph [116] of the Determination "*Under s150(11) we consider that the Appellant's activities were 'for the purposes' of C and D's ring-fence trade."*

60. The Appellant submits that A is not a contractor within the true meaning of 'contractor' within section 150(11). They argue that Section 150(11) assimilates sub-contractors to those who undertake "oil related activities" as principals. Reliance is made on the word 'for' limiting the context to those contractors who themselves carry out a ring fenced trade.

61. The Respondent, as the TAT held, submits that contractor is to be given its ordinary meaning and the words 'if and in so far as' within the section limit the link to an oil related activity.

62. In my judgment the meaning and intent of the subsection is clear. There is no ambiguity. The legislative intent was to make liable to taxation under the ring-fenced rules any sub-contractor of the entity carrying on a ring fenced trade as long as what the sub-contractor does is limited to the purposes of the entity's ring fenced trade.

63. There is little difference between 'for the purposes of C's ring fence trade' in section 150(11) and the words 'in connection with [a ring-fenced activity]' in section 150(1). If what the sub-contractor does is not 'in connection with' a ring-fenced activity it is difficult to see how it could nevertheless be 'for the purposes of' C's ring-fenced trade. It follows in practice whether activities are within section 150(1) or 150(11) will stand or fall together. The legislative intent was not to permit a sub-contracted or otherwise contracted entity to avoid ring-fenced taxation on a ring-fenced activity; equally it was not to make a sub-contractor or otherwise contracted entity liable for its activities which were not ring-fenced activities.

64. I reject the Appellant's submission that it is not a contractor within the meaning of the word 'contractor' in section 150(11) or that section 150(11) assimilates sub-contractors to those who undertake "oil related activities" as principals. The word contractor in the statute should be given, as the TAT gave it, its ordinary and commonplace meaning. The specified reference to the meaning of contractor in section 152B(2) cannot be imported into section 150(11). The definition of contractor in section 152B(2) is limited to contractor within section 152B(1). If it were of general application it would be included in a general definition section and not be expressed in terms that it only applies to section 152B(1). The specific definition of 'contractor' was required in section 152B because of section 152B(1)(b)(i). The draftsman of that section was dealing with associated and connected persons. It was necessary to specifically defined 'contractor' in that subsection rather than leave it to its general meaning.

65. The contractual documents show that the Appellant was indeed a contractor or sub-contractor, and that the rescue services that C and D required had been contracted out to the Appellant by C and D. It follows, although I accept the submission of the Appellant

that in order for the activities of the Appellant to be within section 150(11) those activities it carried out must themselves essentially be ring-fenced activities within of section 150(1), there is no need for the assignment to the contractor of 'part of the ring-fence trade' of the principal. Accordingly, the Appellant also falls within section 150(11).

E. Issue 3 - Indirect Discrimination

66. I agree with the submissions of Mr Ghosh QC that only if the Appellant fails on Issues 1 and 2, does Issue 3 become engaged. The TAT were wrong not to have determined Issue 3 once they had rejected the Appellant's case on issues 1 and 2. It follows, as I have upheld the TAT on Issues 1 and 2, I need to determine Issue 3.

67. The submission of Mr Ghosh QC is that Part VI is indirectly discriminatory because it affects companies outside the Falkland Islands more than companies in the Falkland Islands.

68. Article 25(1) is set out above at paragraph [24]. The starting point is that the face of the legislation applies equally to (a) companies incorporated and/or resident in the Falkland Islands and (b) United Kingdom companies with a permanent establishment in the Falkland Islands. Mr Ghosh QC is therefore driven to argue that the discrimination is indirect.

69. No actual evidence was adduced before the TAT or this court that foreign permanent establishments are treated differently. Mr Ghosh QC submitted that the practical reality is that all lessors will be overseas lessors and that the Head of Tax for the Falkland Islands had recognized that fact in the consultation which took place in relation to section 152A and its replacement by section 152B in 2019. He relied on *Hervis Sport* Case C-385/12 where the Court of Justice of the European Union held that a Hungarian legislative provision which applied a higher rate of tax mainly to groups of companies registered outside Hungary was indirectly discriminatory.

70. Ms Poots says that for a company to be brought within the hire cap it must be both carrying on a ring-fence trade; and that the company makes payments under a lease to a connected company or associated contractor. She points out that not all companies within the ring-fence will make lease payments to connected companies in respect of relevant assets. For

those that do, the rules apply in the same way to a Falkland Islands permanent establishment and a Falkland Islands company. Importantly she says even if the lessor will generally be outside the Falkland Islands that does not indicate discrimination against the entity within the scope of Falkland Islands tax, i.e. the lessee of the asset. A cross-border leasing transaction carried out by a Falkland Islands Company acting as lessee is treated in the same way as the same transaction carried out by a Falkland Islands permanent establishment.

71. I was referred to *Vogel* on Double Tax Conventions; and Double Taxation Conventions by Philip Baker QC. It is clear that Article 25(1) is in the same terms as Article 24(3) of the Model Convention on double taxation agreements. The author of *Vogel* cautions that Article 24 should not be unduly extended to cover 'indirect ' discrimination and at page 425 says:

> "The purpose of this provision [Article 24(3)] is to end all discrimination in the treatment of permanent establishments as compared with resident enterprises belonging to the same sector of activities,…"

72. It is difficult to see how there is any discrimination here. Part VI of the TO accords the same rights to resident enterprises as permanent establishments to deduct trading expenses from taxable profits. The fact is that in a very small jurisdiction such as the Falkland Islands it will often always be in practice a foreign company offering leasing. That is not in itself enough to make the taxation indirectly discriminatory.

73. I note *Hervis Sport* was concerned with EU law and not a double taxation agreement and the TFEU itself contains non-discrimination provision in Article 18 which is based upon nationality discrimination. As the authors of *Vogel* observe Article 24(3) of the Model Treaty is based not on nationality but the actual situs of the enterprise. It follows, I agree with Ms Poots that you cannot simply read across from *Hervis Sport* in this case.

74. In my judgment the fact that the treatment of foreign companies is not discriminatory compared to the domestic situation is a very powerful factor. No evidence was adduced before the TAT or this court that the provisions are in practice discriminatory. A provision arising from a regime in such a small jurisdiction will inevitable in practice apply to foreign companies. That does not make it *ipso facto* indirectly discriminatory. As is shown

in this case an operator can register a domestic company in the Falkland Islands. It follows I reject the submission that the provisions are indirectly discriminatory.

VII. CONCLUSIONS

75. For the reasons given above the TAT did not make an error of law or an unsustainable determination in relation to Grounds 1 and 2. While the TAT failed to determine the Article 25(1) Issue that submission has been determined by this court against the Appellant. It follows the appeal is dismissed.