

THE SPECIAL COMMISSIONERS

**SC/3041/2005
SC/3042/2005**

NEWS DATACOM LIMITED

Appellant

- and -

**J M ATKINSON
(HM Inspector of Taxes)**

Respondent

NEWS DATA SECURITY PRODUCTS LIMITED

Appellant

- and -

**J M ATKINSON
(HM Inspector of Taxes)**

Respondent

**Special Commissioners: ADRIAN SHIPWRIGHT
EDWARD SADLER**

Sitting in public in London on 27 February 2006 – 3 March 2006 and 6 March 2006

**David Waksman QC and Conrad McDonnell, Counsel, for the Appellant instructed by
Allen & Overy**

**Timothy Brennan QC and Akash Nawbatt, Counsel, for the Respondent instructed by
the Acting Solicitor for HM Revenue and Customs**

DECISION

Introduction

1. This decision is concerned with two issues directed to be heard as first issues in two appeals (one concerning NDL and the other NDSP) directed to be heard together. It is a decision in principle and not a final decision.

2. The two first or preliminary issues are set out below. They are:

(1) the Residence Issue; and

(2) the Section 178 Limitation Issue.

3. These are important as they are relevant to the charge on NDSP, whether a group could have existed between NDSP and NDL, whether a degrouping charge could arise and, if so, whether that assessment was made in time.

Summary of Decision

4. In short form we find and decide that:

(1) NDSP was resident outside, and not in, the UK at all relevant times; and

(2) The assessment in respect of section 178 TCGA was made in time as section 178 (10) TCGA is not exhaustive and does not oust section 34 TMA.

The reasons for this are set out in the rest of this decision.

Abbreviations

5. The main abbreviations used in this decision are as follows:

The Board	the Board of Directors of NDSP
BSkyB	British Satellite Broadcasting Ltd - BSkyB Limited from December 1990
Mr Clinger	Michael Clinger, a shareholder and director of NDSP
The Executive Committee	the executive committee of NDSP
Gemplus	Gemplus Card International SA
Hughes Direct	a satellite TV station in the USA
The Hughes Contract	the contract negotiated between NDSP and Hughes Direct

IDG	International Development Group NV, the vehicle through which Mr Clinger held his shares in NDSP
The Judgment	the judgment of Lindsay J. in <i>News International plc v Michael Clinger</i> Ch 1996 N No 4257
The Minority	the minority shareholders in NDSP as a group
NCHL	News Cayman Holdings Limited
NDL	New Datacom Limited
NDSP	News Data Security Products Limited
The News Group	the group of companies and interests which TNCL headed
NGL	News Gem Limited
NI	News International plc, the main UK News Group company
NPL	News Publishers Limited
NRL	News Datacom Research Limited
The Office of the Chairman	the group of individuals based in New York described in paragraph 39
The Override Agreement	the agreement between the News Group and its bankers which, <i>inter alia</i> , placed restrictions on the transfer of assets within the News Group
The Residence Issue	the question “Whether NDSP was resident in the United Kingdom when it disposed of its business to NDL on 8 July 1992?”
The Section 178 Limitation Issue	the question “Whether section 178(10) TCGA 1992 has the effect that notwithstanding the ordinary time limit for assessment in section 34 TMA 1970, the time limit for an assessment to Corporation Tax chargeable on NDL in consequence of section 178 TCGA 1992 expired on 9 July 1998 (that is, six years after NDL ceased to be a member of the group) so that the assessment under appeal (made on 15 April 1999) is out of time?”

Sky	Sky Satellite Television
TA	Income and Corporation Taxes Act 1988
TCGA	Taxation and Chargeable Gains Act 1992
TMA	Taxes Management Act 1970
TNCL	The News Corporation Limited
UK	the United Kingdom
The Watershed	the change in the ownership and status of NDSP completed on 1 July 1992 whereby NDSP ceased to have minority shareholders and became a wholly-owned subsidiary of the News Group

The Issues

6. The two issues directed to be tried as first issues were:

“(1) The Residence Issue

Whether NDSP was resident in the UK when it disposed of its business to NDL on 8 July 1992? and

(2) The Section 178 Limitation Issue

Whether section 178(10) TCGA 1992 has the effect that notwithstanding the ordinary time limit for assessments in section 34 TMA 1970, the time limit for an assessment to corporation tax chargeable on NDL in consequence of section 178 TCGA 1992 expired on 9 July 1998 (that is, six years after NDL ceased to be a member of the group) so that the assessment under appeal (made on 15 April 1999) is out of time?”

7. The relevance of these two issues is that if NDSP were UK resident at the relevant time (namely, when it disposed of its business) then NDSP and NDL would at that time form a chargeable gains group. An exit or degrouping charge would then arise on the transfer of the shares in NDL to NI by NDSP, being the occasion when NDL left the group (see paragraph 15 below). The issue would then arise whether the assessment on NDL in respect of the degrouping charge was made in time.

8. If NDSP were non-resident in the UK at the relevant time there would be no chargeable gains group and a charge to UK corporation tax could only arise if it carried on a trade in the UK through a branch or agency (which is not a matter for decision on the two issues before us).

Assessment and Procedural Matters

9. The transactions which took place in July 1992 described below gave rise to two assessments.

10. The first assessment was made on NDSP, London branch, in May 1998. This was on the basis that NDSP was not resident in the UK. This assessment is not the subject of this decision which relates only to the first issues.

11. The second assessment was made in April 1999 on NDL on the basis that NDL had left the NDSP group (having acquired the NDSP business) so that a charge arose under section 178 TCGA. This was on the basis that NDSP was resident in the UK at the time it transferred its business to NDL (and hence was in a chargeable gains tax group with NDL at that time, it being a requirement of such a group that the relevant companies are UK resident). It is common ground that at all material times NDL was UK resident. This assessment is not directly the subject of this decision which relates only to the first issues (but since the assessment, if it is to succeed, requires both that it is made in time and that NDSP should be UK resident at the relevant time, our decisions on the first issues bear directly upon the validity of the assessment).

12. Appeals were entered in time against both of these assessments by the appropriate Appellants.

13. Because the assessments appeared to be inconsistent as to the residence of NDSP it was directed that the appeals be heard together and that the Residence Issue be heard as the first issue and the Section 178 Limitation Issue as a further first issue. It is only with these issues that this decision is concerned.

The Law and Authorities

14. A company is within the charge to UK corporation tax if it is resident in the UK or carrying on a trade in the UK through a branch or agency (now permanent establishment) subject to any applicable Double Tax Agreement (see sections 8 and 11 TA).

15. The transfer of assets between members of a UK group does not (and did not in 1992) give rise to a charge to corporation tax on chargeable gains at the time of the intra group transfer. A "clawback" charge arose on the recipient company if it left the group within six years of the intra group transfer. The authority for this for companies leaving the group for the period in question is section 178 TCGA. It provided, so far as is relevant, as follows:

“178. Company ceasing to be member of group: pre-appointed day cases

(1) If a company ("the chargeable company") ceases to be a member of a group of companies, this section shall have effect as respects any asset which the chargeable company acquired from another company which was at the time of acquisition a member of that group of companies, but only if the time of acquisition fell within the period of 6 years ending with the time when the company ceases to be a member of the group; and references in this section to a company ceasing to be a member of a group of companies do not apply to cases where a company ceases to be a member of a group in consequence of another member of the group ceasing to exist...

(3) If, when the chargeable company ceases to be a member of the group, the chargeable company, or an associated company also leaving the group, owns, otherwise than as trading stock—

(a) the asset, or

(b) property to which a chargeable gain has been carried forward from the asset on a replacement of business assets,

the chargeable company shall be treated for all the purposes of this Act as if immediately after its acquisition of the asset it had sold, and immediately reacquired, the asset at market value at that time...

(10) Notwithstanding any limitation on the time for making assessments, an assessment to corporation tax chargeable in consequence of this section may be made at any time within 6 years from the time when the chargeable company ceased to be a member of the group, and where under this section the chargeable company is to be treated as having disposed of, and reacquired, an asset, all such recomputations of liability in respect of other disposals, and all such adjustments of tax, whether by way of assessment or by way of discharge or repayment of tax, as may be required in consequence of the provisions of this section shall be carried out...

16. For there to be a group of companies for these purposes the conditions in section 170 TCGA need to be fulfilled. Here, as at the relevant time NDSPs held more than 75% of the shares of NDL, then if NDSP were UK resident there would be such a group of companies at that time. As mentioned, it is common ground that NDL was UK resident at all material times.

17. Section 34 TMA is headed “Ordinary time limit of six years”. It provides:

“(1) Subject to the following provisions of this Act, and to any other provisions of the Taxes Acts allowing a longer period in any particular class of case, an assessment to tax may be made at any time not later than six years after the end of the chargeable period to which the assessment relates.

(2) An objection to the making of any assessment on the ground that the time limit for making it has expired shall only be made on an appeal against the assessment”.

The Authorities

18. We were provided with bundles of authorities by each side. These contained (inter alia) copies of the reports of the following cases:

Cesena Sulphur Co Ltd v Nicholson (1876) 1 TC 88

De Beers Consolidated Mines Ltd v Howe [1906] AC 455

Unit Construction Co v Bullock [1960] AC 351

Esquire Nominees Ltd v Commissioner of Taxation (1971) 129 CLR 177

In re Little Olympian Each Ways Ltd [1995] 1 WLR 560

Wood v Holden [2005] EWHC 547 (Ch)

Wood v Holden [2006] EWCA Civ 26

The Evidence

19. We were provided with 5 main files of documents and a number of files of other relevant materials. These documents were in agreed bundles clearly paginated and helpfully arranged. We express our gratitude for this.

20. We heard evidence from:

(1) Dr Dov Zev Rubin, Technical Marketing and Sales Manager of NRL at the relevant times;

(2) Morris Zelkha, Tax Adviser and a partner in Arthur Andersen at the relevant times; and

(3) Arthur Michael Siskind, Group General Counsel of TNCL.

21. Witness statements were provided for each of them. They were all called by the Appellants, gave oral evidence and were cross examined. No witnesses were called by HMRC.

Findings of Fact

Introductory

22. From the documents and the evidence we make the following findings of fact. We start first by considering the various entities and persons involved and making findings of fact in respect of them and then proceed to consider NDSP's business, the Board of NDSP and the Executive Committee of the Board; Mr Price and Others – control and usurpation; the Watershed; Mr Clinger's activities; the Hughes Contract; buying out the Minorities; the transactions in question (that is, the transfer by NDSP of its business and assets to NDL and the subsequent disposal of the NDL shares), the Override Agreement; and a summary of our findings.

Dramatic Personae

i. NDSP

23. News Data Security Products Limited ("NDSP") is a Hong Kong incorporated company. It was originally called Bungo Limited. It changed its name to NDSP on 23 March 1988.

24. At 30 June 1989 NDSP had an authorised share capital of US \$10,000 divided into 10,000 shares of US \$1 each. All of this share capital had been issued and was held as follows.

<u>Shareholder</u>	<u>Number</u>	<u>%</u>	<u>Issue Price (US \$)</u>
NPL	6000	60	600 per share
Yeda Research & Development Co ¹	1000	10	1 per share

¹ the commercial arm of the Weizman Institute of Science

Professor Shamir	1000	10	1 per share
International Development Group NV	2000	20	1 per share

25. NPL's holding was transferred to NCHL in June 1991. Professor Shamir's shares were transferred to BDB Nominees Limited as trustee for him in about February 1990.

26. NDSP was set up as a joint-venture to pursue the commercial applications of the Fiat-Shamir algorithm (mathematical codes or ciphers). The Minority (together holding 40% of the Share Capital of NDSP) was based in Israel. They had the real technical expertise in this area. Much of NDSP's work was carried on in Israel. The News Group, through NPL, was the majority Shareholder (holding 60% of the Share Capital of NDSP) and it contributed the finance to the joint venture.

27. NDSP's governance was controlled by its Articles of Association and its Shareholders' Agreement dated 16 February 1988. The Shareholders' Agreement was amended on 9 October 1990.

28. The effect of the Articles of Association (Article 69) and the Shareholders' Agreement (Clause 3) was that NPL had the right to appoint four directors and the Minority had the right to appoint in aggregate four directors. Each of the 10% shareholders had the right to appoint one director and the 20% shareholder had the right to appoint two. The largest shareholder, NPL, was given the right under the Shareholders' Agreement (Clause 4.4) to appoint the Chairman of the Board. The Chairman was to have a casting vote. A table of the directors for the period from January 1988 to date is set out at paragraph 55.

29. The Shareholders' Agreement provided (inter alia) that NDSP would not enter into certain specified categories of transactions without the prior written consent of all the shareholders in NDSP. The specified matters (as extended by the amendment of 9 October 1990) included:

- a. the grant or assignment of licences and sub licences of the encryption technology including for new customers of NDSP;
- b. the disposal of the whole or a substantial part of NDSP's undertaking;
and
- c. entry into transactions other than at arm's length or based on pricing policies agreed by all the directors

30. This effectively meant that the consent of the Minority was required for any major step to be taken by NDSP. There were also special provisions as to the transfer of shares: in brief, a shareholder wishing to dispose of his shares was required first to offer those shares to the remaining shareholders, under conventional pre-emption provisions. The Shareholders' Agreement rights also made removal of a director such as Mr Clinger virtually impossible.

ii NPL

31. News Publishers Limited ("NPL") was incorporated in Bermuda and resident in the UK. It was a company within the News Group. It was owned as to 48% of the issued share capital by NI and as to the other 52% by companies outside the UK within the News Group. NPL held 60% of the shares in NDSP till June 1991 when they were transferred to NCHL.

iii NI

32. News International plc ("NI") was a company incorporated in England which held directly or indirectly virtually all of the News Group's UK assets. These were substantial and included The Times, The Sunday Times and The Sun newspapers as well as the News Group interests in Sky Television (BSkyB from December 1990). It was a 98% plus subsidiary of Newscorp Investments Limited which was itself a subsidiary of TNCL.

iv NCHL

33. News Cayman Holdings Limited ("NCHL") was a company incorporated and resident in the Cayman Islands. It became the owner of 60% of NDSP when the shares held by NPL were transferred to NCHL in June 1991. It was part of the News Group as an indirect subsidiary of TNCL managed from New York.

v NRL

34. News Datacom Research Limited ("NRL") was a company incorporated in Israel. It was the 100% subsidiary of NDSP. It was run as one economic group with NDSP. It carried out most of the research and development work required for NDSP's business.

vi NDL

35. News Datacom Limited ("NDL") was a company incorporated in England. It was acquired by NDSP on 7 July 1992 and transferred to NI on 9 July 1992. It was common ground that NDL was UK resident at all relevant times.

vii NGL

36. News Gem Smartcard International Limited ("NGL") was a Hong Kong incorporated and resident company registered in Scotland as an overseas company. Originally it was a joint venture between NDSP and Gemplus. Gemplus sold its shareholding in NGL to NI in June 1991. After 9 July 1992 NGL was a wholly-owned subsidiary of NDL.

viii Gemplus

37. Gemplus Card International SA ("Gemplus") was a French company (independent of News Group) manufacturing smartcards. It was a 50% shareholder in NGL till June 1991.

ix News Group and TNCL

38. News Group is the well-known worldwide group of companies owned by The News Corporation Limited ("TNCL"). It has interests principally in the newspaper, television, publishing and films sectors. TNCL was incorporated in Australia. Mr

Rupert Murdoch has a shareholding interest in and was the Chairman and Chief Executive Officer ("CEO") of TNCL at all relevant times. At all relevant times the global headquarters of News Group, from which operations were conducted, were in New York City, New York, USA.

x The Office of the Chairman

39. The Office of the Chairman was the highest level of management of the News Group of companies. The Office of the Chairman was based in New York where Mr Murdoch was based. At the times in question its members were:

- a. Keith Rupert Murdoch, Chairman and CEO;
- b. Arthur Michael Siskind, Group General Counsel of News Group
- c. August ("Gus") Fischer, Chief Operating Officer of News Group
- d. David Devoe, Chief Financial Officer of News Group

xi Hughes Direct and DirecTV

40. DirecTV was the brand name used by a US satellite television company (independent of News Group), Hughes Direct, which was a customer of NDSP/NDL from 1992.

xii The Hughes Contract

41. The contract between NDSP and Hughes Direct the negotiation of which was the business activity which occupied much of NDSP during late 1991 and early 1992 and which is discussed at paragraphs 68 and following.

xiii Mr Clinger and International Development Group NV

42. Mr Clinger was a 20% shareholder in NDSP. He held his shares through International Development Group NV ("IDG"), a company incorporated in the Netherlands Antilles. Under the Shareholders' Agreement IDG had the right to appoint two directors to the Board of NDSP. IDG appointed Mr Clinger and Mr P H Baris (an Israeli lawyer) as directors of NDSP from 19 January 1988 to 1 July 1992.

43. On the evidence of Mr Rubin, which we accept, Mr Clinger was the person who ran the NDSP business – all those involved in developing and exploiting the encryption product (which was work largely undertaken in Israel) looked to him for their direction, and no significant decisions were taken without his agreement. As it later became apparent, Mr Clinger abused and exploited his position (and his uniquely extensive knowledge of NDSP's business affairs) by defrauding the company, as described below. Mr Clinger lived and worked principally in Israel. Between July 1991 and July 1992 he visited the UK on NDSP matters on four occasions only, each visit of one or two days' duration.

xiv Tom Price

44. Tom Price was an accountant working for the News Group. He was based in the UK. He was appointed a director of NDSP by NPL from 17 July 1990. He retired as a director of NDSP on 22 August 1997. He was the Chief Executive Officer of

NDSP and of NDL from July 1990 until March 1993. He was a director of NGL from July 1990 to March 1993.

xv Steve Brown

45. Steven ("Steve") Brown was the UK-based Financial Controller of NI. He was seconded to the project for News Group to buy out the Minority from December 1991. He was a director and Chief Financial Officer of NDL from 2 January 1992. He was not a director of NDSP at any relevant times. He carried out some work in relation to the Hughes Contract, but was not directly involved in its negotiation.

xvi Stephen Barraclough

46. Stephen Barraclough was an accountant. He was the UK-based Financial Director of NI. He was not a director of NDSP at any relevant times. He was a director of NDL. The News Group provided the principal funding for NDSP, and Mr Barraclough had responsibility within News Group for providing and supervising that funding.

xvii Gus Fischer

47. August ("Gus") Fischer was Chief Operating Officer of TNCL. He was a member of the Office of the Chairman (which was in New York) from February 1991. He was also the Managing Director of NI from February 1991. He was appointed a director of NDSP by NPL from 20 February 1990 and Chairman from May 1990 and continued as a director beyond 1992 (seemingly till 22 August 1997). During the relevant period he divided his working time between London and New York (and from January 1992 he was predominantly in New York).

xviii Peter Stehrenberger

48. Peter Stehrenberger was a UK-based executive director of NI. He was a director of NDSP (appointed by NDL) from 24 April 1989 until 1 September 1990. He was an alternate director for Tom Price from 1 July 1992. He was a director of NGL from June 1991 until 1995 and of NDL from January 1992 till July 1992.

NDSP's Business

49. NDSP was set up to exploit the Fiat-Shamir algorithm. This included its use as a method of encryption which allowed TV broadcasts to be scrambled and descrambled. This permitted programmes to be broadcast generally but viewed only by those who had subscribed to do so.

50. From 5 February 1990 BSkyB was available to paying subscribers. It used a system invented by NDSP and its subsidiary NRL, known as "Videocrypt", each subscriber's decoder box using a numeric key to descramble the image. The descrambling key was provided by a "smartcard". This is a plastic card about the size of a credit card containing a microchip which could be programmed to allow only the channels for which the subscriber had paid to be descrambled. The key was changed regularly and encrypted to prevent unauthorised viewing. The Fiat-Shamir algorithm was at the heart of the encryption.

51. The Videocrypt system was based on smartcards. These credit card size plastic cards each containing a microchip were the first of their kind. Elements of the system had been developed jointly with Thomson Consumer Electronics SA, a French manufacturer of television and other consumer electronics products. NDSP's secure encryption and smartcard technology combined with Thomson's method of broadcast scrambling created a viable secure system limiting access to particular satellite television channels to those who had subscribed to them.

52. Smartcards need to be assembled. NGL was established as a joint venture between NDSP and Gemplus to produce and assemble smartcards suitable for use with the Videocrypt system. Each card was assembled by NGL from components including a microchip, a micro module into which the microchip was inserted and the plastic card for the micro module. Gemplus supplied the components and the machinery for assembling cards. NGL then programmed cards with NDSP's security codes.

53. NGL supplied BskyB which was the main customer. The actual sales were made by NGL. Where Videocrypt was used by a broadcaster, NDSP through NRL in Israel would provide certain consulting and technical services to the broadcaster. NDSP received royalties from NGL for the use of certain technology in the smartcard. NDSP also received royalties from decoder manufacturers. NDSP's business consisted mainly of its interest in NGL and collecting royalty income. It also carried out research and development principally in Israel.

The Board of NDSP

54. The board of directors of NDSP ("the Board") consisted of eight directors until the Watershed (save for the period from 31 January 1992, when one of the News Group directors retired and was not replaced – this was at the time when negotiations were in progress for News Group to buy out the Minority). Four directors were appointed by NPL/NCHL and four were appointed by the Minority (as described above). The quorum for a meeting of the board was four until July 1992.

55. The Appellant produced a useful table of directorships which we accept and set out below. From January 1990 until the Watershed the directors appointed by the Minority were Messrs Clinger, Shamir, Schlachet and Baris.

1. January 1988 – December 1990

Name	Director from	Director until	Residence
D Martin	18 January 1988	10 January 1990	Israel
IT Kohlberg	19 January 1988	1 January 1989	Israel
PW Smith	16 February 1988	24 April 1989	Australia
CC Chang	16 February 1988	31 July 1989	Australia
B Hundertmark	16 February 1988	18 May 1990	Australia
PW Stehrenberger	24 April 1989	1 September 1990	UK
RH Searby	16 February 1988	31 January 1992	Australia
A Shamir	18 January 1988	1 July 1992	Israel
M Clinger	19 January 1988	1 July 1992	France/Switzerland/Israel
D Schlachet	1 January 1989	1 July 1992	Israel
PH Baris	30 January 1990	1 July 1992	Israel
LJ Holloway	1 August 1989	18 December 1992	Hong Kong
AA Fischer	20 February 1990	22 August 1997	UK/USA
TG Price	17 July 1990	22 August 1997	UK

2. January 1991 – December 1991

Name	Director from	Director until	Residence
RH Searby	16 February 1988	31 January 1992	Australia
A Shamir	18 January 1988	1 July 1992	Israel
M Clinger	19 January 1988	1 July 1992	France/Switzerland/Israel
D Schlachet	1 January 1989	1 July 1992	Israel
PH Baris	30 January 1990	1 July 1992	Israel
LJ Holloway	1 August 1989	18 December 1992	Hong Kong
AA Fisher	20 February 1990	22 August 1997	UK/USA
TG Price	17 July 1990	22 August 1997	UK

3. January 1992 – Completion of buy-out on 1 July 1992

Name	Director from	Director until	Residence
RH Searby	16 February 1988	31 January 1992	Australia
A Shamir	18 January 1988	1 July 1992	Israel
M Clinger	19 January 1988	1 July 1992	France/Switzerland/Israel
D Schlachet	1 January 1989	1 July 1992	Israel
PH Baris	30 January 1990	1 July 1992	Israel
LJ Holloway	1 August 1989	18 December 1992	Hong Kong
AA Fisher	20 February 1990	22 August 1997	UK/USA
TG Price	17 July 1990	22 August 1997	UK

4. Completion of buy-out on 1 July 1992 to date

Name	Director from	Director until	Residence
LJ Holloway	1 August 1989	18 December 1992	Hong Kong
AA Fischer	20 February 1990	22 August 1997	UK/USA
TG Price	17 July 1990	22 August 1997	UK
AM Siskind	1 July 1992	12 January 2005	USA
DF Devoe	1 July 1992	Existing director	USA
JA Leist	1 July 1992	Existing director	USA

56. After the Watershed (that is, following completion on 1 July 1992 of the purchase by News Group of all the minority shareholdings), the quorum for meetings of the Board was brought into line with the general position within the of the News Group and reduced to two as part of the administrative matters dealt with at the Board meeting on 1 July 1992.

57. In the period up to but not including 1 July 1992 no meeting of the Board took place in the UK. The dates and locations of the meetings of the Board during that period were as follows:

Number	Date	Location
1	16 February 1988	Zurich
2	3 January 1988	Zurich
3	26 April 1988	Hong Kong
4	9 August 1988	Istanbul
5	5 September 1988	Hong Kong
6	20 November 1988	Munich
7	20 March 1989	Hong Kong
8	6 June 1989	Zurich
9	13 November 1989	Rome
10	18 January 1990	Hong Kong
11	20 February 1990	Rome
12	17 September 1990	Zurich
13	13 March 1991	Zurich

58. It is clear from the minutes of these board meetings that the directors discussed and decided upon major matters of policy relating to NDSP and its business at these meetings – they were not a mere formality.

59. There were no more Board meetings till 1 July 1992. However, there was evidence that it was considered to continue to exist and be of effect. For example, two reports were submitted on 7 June 1991 to the Board for a meeting to be held later that month, although in the event the meeting did not take place. It should be noted that during the period from September 1991 until July 1992 NDSP and its shareholders were closely concerned with two major matters: the negotiation of the buyout of the Minority and the negotiation of the Hughes Contract (the two matters were related, in that the success of the Hughes Contract impacted directly upon the value of the NDSP shares, and hence the price which the Minority would receive on selling out their interest to News Group). In the course of these negotiations the directors met periodically, albeit outside the context of formal board meetings. We find that the Board did continue to exist and be of effect from March 1991 till 1 July 1992. The position of the Board as a constitutional organ was not usurped at any time. We find this as a primary fact. It certainly existed and met to full effect in July 1992.

60. The meeting on 1 July 1992 was held in the office of Messrs Farrer & Co, solicitors, in London. Farrers acted for News Group on the buyout of the Minority, and this meeting followed the completion on that date of the purchase of the Minority shareholdings by NHCL. Those in attendance were Mr Stehrenberger and Mr Richards.

61. Mr Stehrenberger was the alternate for Mr Fischer and Mr Price. Mr Richards was the alternate for Mr Searby and Mr Holloway. The directors appointed by the Minority had resigned earlier that day upon completion of the purchase of the Minority shareholdings.

62. The business of the meeting consisted of registering the share transfers in relation to the Minority shareholdings purchased by NHCL and bringing the quorum for Board meetings into line with News Group policy by reducing it to two.

63. We find as a primary fact that this meeting was concerned only with ministerial matters and matters of good housekeeping. The meeting was not concerned with policy, strategic, or management matters relating to the conduct of the business of NDSP. It did not reflect a manifestation of the controlling brain or where the business of the company was really carried on. It was not an exercise of central management and control. It was the tidying up operation following the buyout of the Minority, conducted by alternate directors. It is the case that the reduction in the quorum of directors was a significant matter, since the subsequent Board meetings later in July which authorised the key transactions (see paragraph 104 and following below) were conducted on the basis of that reduced quorum, but nevertheless, in the context of an action which was a consequence of the company coming fully into the News Group and conforming its governance arrangements to group policy, undertaken by alternate directors who can reasonably be regarded as acting under instruction, this action in itself cannot be seen as the exercise of central management and control.

64. Despite Mr Brennan QC's seductive efforts to persuade us otherwise we find that whilst Mr Price and others from the UK may have been trying to exert authority they singularly failed to do so. We find as a primary fact that Mr Price and others did not exercise any central management and control from the UK in the sense of manifesting the whole or a part of the controlling brain of NDSP, or being where NDSP actually carried on business or where it abided (see paragraphs 96 and following).

The Executive Committee

65. An executive committee of the Board of NDSP was in existence from late 1989. The setting up of committees of the Board was permitted by the Articles of Association (Article 90). The precise timing of its creation and the extent of its authority and, indeed its membership is not as clear as one could wish from the evidence and documents. However, we find that there was an Executive Committee, however constituted, and it was concerned with day-to-day operational matters. We have seen no evidence showing that the Executive Committee exercised all or part of

the controlling brain of NDSP. The evidence that was presented to us was to the contrary. A table of meetings is set out below. In considering the role of the Executive Committee (and in particular whether, as Mr Brennan argued, it, rather than the Board, exercised central management and control of NDSP) it is important to take account of the nature of the interests in NDSP: as mentioned, the different shareholders had specific rights carefully regulated by the Articles of Association and the Shareholders' Agreement, including their respective rights to appoint directors. No doubt at times the Minority acted together, but they were not required to do so. An individual shareholder's best interests were served by ensuring that his appointed director was active as a member of the Board. In the absence of any specific evidence to the contrary (and we had no such evidence) it is reasonable to infer that the shareholders did not in effect weaken their position by allowing the Executive Committee to exercise those rights and to control those matters which properly were within the scope of the Board's powers and responsibilities.

66. The meetings of the Executive Committee were as follows:

Number	Date	Location
1	12 December 1989	London
2	18 March 1990	London
3	11 July 1990	London
4	15 August 1990	London
5	7 November 1990	Hong Kong
6	12 February 1991	London
7	18 June 1991	Maidenhead
8	9 August 1991	Maidenhead
9	9 January 1992	Israel

Mr Clinger's Activities

67. These were the subject of litigation (a six-week trial) and a careful judgment of Lindsay J. in *News International plc v Michael Clinger* CH 1996 N No 4257 to which reference should be made. As was said in the agreed statement of facts:

"It emerged much later that from around mid- 1990, Mr Clinger had been defrauding NDSP and had been manipulating its dealings accordingly. In particular, he procured that NDSP (and subsequently NPL) purchased blank smartcards at an inflated price. A part of that price would indirectly pass back to Mr Clinger, through agency and other agreements with companies with which Mr Clinger was connected or other secret arrangements."

When News Group discovered the fraud, NI, NDSP, NDL, NCHL and NPL made a claim against Mr Clinger in the High Court, and after lengthy litigation including a six-week trial, they obtained judgement against Mr Clinger for £28 m. Judgement was given by Lindsay J. on 17 November 1998. The judge described Mr Clinger as

"a skilful liar on whose evidence no reliance can be put" (paragraph 149 of the Judgement).

The Hughes Contract

68. This was a major contract affecting NDSP and the News Group. It was negotiated in late 1991 and early 1992, and, in terms of business activity was by far and away the most significant matter undertaken by NDSP during that period. It also had wider significance for the News Group, and for the individual shareholders comprising the Minority, as mentioned below. It therefore attracted attention at the highest level on the part of all the shareholders. The significance of the Hughes Contract in this appeal is that it was negotiated and concluded during the period when the Board did not meet. HMRC argued that key matters relating to the Hughes Contract were decided by Mr Price (at that time the UK-based CEO of NDSP), claiming that as evidence that the business of NDSP was being managed and controlled in the UK; the Appellant argues that the key matters were decided by the Minority shareholders (either individually, as they were engaged in the negotiations, or through Mr Clinger) and by the Office of the Chairman for the News Group – and in any event, were not decided within the UK.

69. The evidence of Mr Siskind (which we accept) was that the Hughes Contract "... was of interest to News Corporation at the highest level and was one in which Mr Murdoch took a very personal interest in being sure that it was done right" This accords with Dr Rubin's evidence.

70. The reason for this high level interest was that the Hughes Contract had a material effect on the viability of NDSP and successor companies. It made NDSP a more viable supplier and thereby ensured the health of BSkyB. It also gave News Group another outlet for selling their products into the marketplace.

71. Mr Siskind also told us (which we accept) that his operational role in the Hughes Contract "... was in my capacity as being directed by Mr Murdoch and [TNCL] to ensure it was acceptable to us".

72. To this end he arranged for the New York law firm in which he was formerly a partner to represent NDSP in connection with the contract. He, together with his colleague David Devoe in the Office of the Chairman at News Group reviewed the drafts and signed off the Hughes Contract as acceptable to TNCL in accordance with Mr Murdoch's direction to ensure that it was acceptable to TNCL.

73. The Hughes Contract was mainly negotiated in California, where Hughes was based. Dr Rubin, Leo Krieger (a senior business manager at NDSP) and technical staff (including Professor Shamir, one of the Minority shareholders) went out to California from Israel. Day-to-day negotiations were conducted there principally by Dr Rubin and Mr Krieger on NDSP's behalf.

74. Dr Rubin gave evidence that Mr Clinger "was very intimately involved". He could not enter the United States himself as he was "a fugitive from US justice".

However, Dr Rubin and Mr Krieger had many discussions with him by phone. These were almost daily and centred on determining the strategy to be adopted in the course of the Hughes negotiations. These negotiations were critical to the Minority as they went to the value of NDSP at the time when the Minority were negotiating the sale of their interests to News Group. We accept this evidence.

75. Dr Rubin said he reported to Mr Clinger on the Hughes negotiations, and looked to him for direction. He said that he kept Mr Price informed out of courtesy – he relayed information to him, but did not seek direction or permission from him. In his view Mr Price was not experienced in the technical matters which were a key part of the negotiations, nor was he sufficiently close to the commercial basis of the negotiations – certainly he did not have the technical and commercial expertise of Mr Clinger. We accept this evidence.

76. According to Dr Rubin, Mr Price got himself involved in the negotiations in the USA. As Dr Rubin graphically described it Mr Price was "pulling an Alexander Haig": he was trying to claim he was in charge when in reality all the key decisions were taken by others, and he came in to sign the contract as NDSP's CEO when its negotiation had been completed by others.

77. Dr Rubin gave evidence that senior News Group directors in New York also had input into the Hughes negotiations. He said that he and Leo Krieger had conference calls with Mr Siskind and other members of the office of the Chairman. We were told documents had been faxed to New York from California. These were discussed in the telephone conference calls.

78. We accept both Mr Siskind's and Dr Rubin's evidence as to the Hughes Contract. Given the passage of time (some 15 years) we do not find it at all surprising that no surviving documents have been found which record the involvement of the relevant individuals. Further, since the negotiations were in California and the senior News Group directors concerned were in New York, and Mr Clinger was in Israel, it is entirely likely that matters were resolved by telephone conference calls and faxed documents.

79. It is the case that Mr Price signed the Hughes Contract on behalf of NDSP, but we find that there is no significance to be attached to this – at least, not in the context of who was controlling NDSP in relation to the Hughes Contract, or where that control was being exercised. In any event, were the signing of the contract itself material to this question, the evidence is that Mr Price signed the contract outside the UK in the USA. We find as a fact that the negotiations were not controlled in any significant sense from the UK.

80. There is evidence that in relation to the Hughes Contract and its negotiation, Steve Brown (and perhaps others under his supervision) may have prepared costings and other financial modelling in the UK, but none of that amounted to more than providing financial and related information to be used by those carrying out the negotiations and taking the eventual decisions as to the terms of the Hughes Contract.

Such action did not amount to the exercise of central management or control of NDSP or its business in any sense.

81. In summary we find as facts on the Hughes Contract:

- (a) it was negotiated by Dr Rubin and Mr Krieger in California;
- (b) Mr Clinger in Israel was intimately involved, and Dr Rubin and Mr Krieger took direction from him;
- (c) senior directors at the highest level in News Group in New York at the request of Mr Murdoch were heavily involved and the Hughes Contract would not have been entered into by NDSP had it not met with their approval;
- (d) Mr Price signed the Hughes Contract on behalf of NDSP, and did so in the USA and therefore outside the UK. Despite any aspirations he may have had to take a more prominent part in the negotiations, in reality he did not materially influence those negotiations, nor, ultimately, were his views taken into account on the key issues: the decisions were taken elsewhere;
- (e) the negotiations and conclusion of the Hughes Contract were not run or controlled from or determined in the UK in any significant sense: they were run and controlled from and determined in Israel and the US (New York and California). Accordingly, in so far as the Hughes Contract speaks to the issue of where the central control and management of NDSP was exercised during the period of its negotiation, it is evident that such control and management was not exercised in the UK.

Buying out the Minority

82. The Minority were all based in Israel. Much of NDSP's vital activities were carried out in Israel. Until the Watershed, NDSP was not under the News Group's control, and, as mentioned, Board representation was divided equally between News Group on the one hand and the Minority on the other. The Minority knew much more of what was happening in NDSP than the News Group. They – and in particular Mr Clinger - seem to have been heavily involved in the running of NDSP's business. This is illustrated by the News Group taking the unusual step of carrying out a full legal and accounting due diligence exercise on a company in which it owned 60% of the share capital when it came to purchase the Minority's shareholding.

83. News Group became aware in 1990 that Mr Clinger was causing friction between NDSP and NGL and between those two companies and its principal customer BSkyB. It was only later (after News Group had purchased the Minority shareholdings) that News Group learnt that Mr Clinger had been defrauding NDSP on a massive scale since 1990 (see paragraph 67 and following above and the Judgement).

84. Mr Clinger, through IDV, was a 20% shareholder in NDSP. He had detailed knowledge of the business. Many of the key staff in Israel were loyal to him. The Shareholders' Agreement gave him a right to appoint two directors. Accordingly Mr

Clinger's co-operation was required if his appointee directors (which included himself) were to be removed.

85. The commercial difficulty for the News Group was that NDSP was vital to the success of News Group's interests in BSKyB, but, for so long as the current shareholding and management interests subsisted in NDSP, they could not control NDSP and were compelled to accept Mr Clinger's dominant position in the company, especially for so long as he had the support of the other Minority shareholders and their appointee directors. News Group considered ways in which to resolve these difficulties. As Mr Siskind put it "the game plan... was for News to gain and keep control of the News Datacom operation. It was decided that it would be in News' best interest to acquire one hundred percent ownership of NDSP and consequently for it to become its subsidiary company".

86. Mr Siskind had been asked after March 1, 1991 by Mr Murdoch to become involved in both the BSKyB operation and the NDSP/NRL operations on behalf of News Group. He identified the problem as one of relationships and in particular the dominance of Mr Clinger and his readiness to act on his own accord without reference back to the News Group.

87. The buyout of the Minority took time to achieve. Negotiations began in September 1991 and were not completed until May 1992.

88. Various positions were taken by various parties in the course of these negotiations, and at times relations between the parties were strained. On one occasion the Minority complained that News Group were concealing information about the way NDSP was being run, an incident to which HMRC attached some importance. Mr Siskind was emphatic that he did not accept that that was the case at all. We saw no evidence to support the contention that the Minority were kept in the dark about the way NDSP was being run at that time, or that News Group had in some way taken over control of NDSP during that period. Such evidence as there is suggests strongly the contrary, as, for example, the involvement of all parties in the Hughes Contract, as described above. The letter of complaint from the Minority can in all the circumstances reasonably be seen as a tactical position taken for the purpose of negotiating and obtaining the highest price for the Minority.

89. Mr Siskind also gave evidence that there was a great deal of interest in the buyout coming from the Office of the Chairman, and that Mr Murdoch himself took a considerable interest. At the time the BSKyB business was losing approximately £12 million per week. News Group could not risk matters further by having a continuing unsatisfactory relationship with NDSP where they felt they were not kept informed and had no real control over its management, and were increasingly concerned about the activities of Mr Clinger. They were also concerned about the poor personal relationships between Mr Clinger and Mr Sam Chisholm who had come in to run the merged British Sky Broadcasting business.

90. The process leading to the buyout of the Minority was at all times under the oversight of Mr Siskind, the Group General Counsel for News Group and under the overall direction of the Office of the Chairman in New York.

91. The first meeting took place between News Group and the Minority on 12 September 1991 in London. Mr Siskind and Mr Fischer attended on by half of the News Group. News Group made an initial offer to buy out the Minority on 27 September 1991. A revised offer was made in early November 1991 at a meeting in Israel. One of the terms of this offer was that Mr Clinger was to cease his executive activities. Yeda (the commercial arm of the Weizman Institute) and Professor Shamir agreed to the buyout in principle on 7 November 1991. These were shareholder matters and did not relate to the central management and control of NDSP.

92. On 8 November 1991 Mr Clinger agreed to give up his executive role as NDSP. However, he remained as a director of NDSP, NGL and NRL until 1 July 1992 and in practice retained considerable influence in NDSP and NRL (as evidenced by his role in the Hughes Contract). The continuing Chief Executive Officer of NRL, Leo Krieger, had been appointed upon Mr Clinger's recommendation, and he and Mr Clinger enjoyed a close relationship. He continued in office until April 1992.

93. Mr Clinger also continued to influence Meir Matatyahu who was instrumental in the smartcard orders placed by NDSP. As the Judgement shows Mr Clinger was able to benefit from these orders.

94. The negotiations of the final price and other details was protracted. It is for this reason that Mr Clinger remained director until July 1992.

95. As part of the buyout process, and prior to entering into the contract to buy the Minority shares, News Group instructed Farrers and Arthur Andersen to carry out a full due diligence investigation of the affairs of NDSP and NRL and to report back on that investigation to News Group. They reported back in December 1991. Such an investigation is commonly undertaken in the situation where the purchaser has no knowledge, or limited knowledge, of the business, financial and legal affairs of the company it is purchasing or investing into. That News Group should think it necessary to carry out such an investigation into NDSP and NRL is in our view compelling evidence that neither the News Group nor its appointee directors on the board of NDSP had control of the affairs of those companies, since if they had been so in control, they would have been in possession of all the information which the due diligence investigation was designed to reveal.

Mr Price and other News Group personnel – control and usurpation

96. We heard evidence about the role and functions of Mr Price and other News Group executives involved with NDSP, in some cases as directors and in others as key executives responsible for News Group's investment in NDSP. In broad terms the Revenue contended that the role of these executives indicated that they had positions of control in the business and management of the company; the Appellant contended that the reality was somewhat different in that the business of the company was run in Israel by Mr Clinger and his associates.

97. Mr Price held the title of Chief Executive Officer of NDSP, a position to which he was appointed in about July 1990. However, as Mr Siskind said "he had the title but really was not running the business per se". His function, according to Mr Siskind, was more administrative than operational. Mr Siskind's view is reinforced by Dr Rubin's evidence: Dr Rubin had sympathy for the position Mr Price found himself in – nominally the chief executive, but in reality without the knowledge or expertise or presence in Israel to keep up with the real running of the business by Mr Clinger and the technical experts in Israel. In practice Mr Price found himself constantly asking for information (and many of his requests were simply ignored), or dealing with minor matters, such as the company logo. His role in the negotiation of the key Hughes Contract was peripheral, notwithstanding his efforts to take a more prominent position (see paragraph 76 and following).

98. The subsequent litigation by News Group against Mr Clinger throws light on the true nature of the role of Mr Price and his relationship with Mr Clinger. We were told that the judge considered that Mr Clinger ran rings round Mr Price. Mr Clinger was able to perpetuate a substantial fraud on the Company without Mr Price being aware of it. This corroborates Mr Siskind's statement that "the problem [was] that much of the business was being run out of Israel under Michael Clinger".

99. We find as a fact that Mr Price did not on his own or with others exercise operational control over NDSP let alone central management and control of NDSP. We also find as a primary fact that Mr Price either alone or with others did not usurp the functions of Board at any relevant time.

100. Steve Brown worked on the Hughes Contract, providing some of the financial and costings information and analysis. As he was the Financial Controller of NI this is hardly surprising, and it demonstrates the close interest which the News Group took in that Contract, as Mr Siskind testified. Mr Brown should be seen as part of the team, but neither in relation to the Hughes Contract, nor, so far as we could see from the evidence presented to us, in relation to other business of NDSP, was he the controlling mind of NDSP. He was not a director of NDSP. He did not on his own or with others usurp the board of NDSP. We find this as a fact.

101. Gus Fischer was part of the Office of the Chairman. In that capacity he represented the interests of the News Group on the board of NDSP from February 1990. There was absolutely no evidence of Mr Fischer usurping the board of NDSP either on his own or with others. We find this as a fact.

102. Neither Mr Stehrenberg are nor Mr Barraclough were directors of NDSP. There was no evidence of either or both of them alone or with others seeking to usurp the board of NDSP. We find this is a fact.

The Watershed -- 1 July 1992

103. The completion on 1 July 1992 of the acquisition of the Minority's shares was an important day in NDSP's history. It then became fully under the control of and a wholly-owned member of the News Group. This was important in terms of the News Group's knowledge of NDSP's affairs and its integration into the News Group. We consider this was a watershed in NDSP's history as it became a full part of the News Group. It was also the start of a new accounting period.

The Transactions In Question

Introduction

104. The transactions which gave rise to the assessments took place on three consecutive days in July 1992, early in NDSP's accounting period which commenced on 1 July 1992.

105. According to the evidence of Mr Siskind, the genesis of these transactions was that the Office of the Chairman had decided in principle that once News Group had acquired 100% control of NDSP, the business of NDSP would then be transferred to a new UK company. A UK company was proposed because NDSP's trading subsidiary NGL was already based in the UK, and NDSP and NGL's principal customer BSKyB were also in the UK.

106. There was concern to avoid triggering a tax charge in Australia on the News Group parent company under the Australian controlled foreign company provisions. Mr Zelkha, on the advice of the News Group's accountants in Australia, considered that there was a risk of such a tax charge in relation to the continuing business of NDSP if NDSP were to become a UK resident company. It was considered this would not be the case if instead the business were carried on by a new UK company to which NDSP would transfer the business.

107. It was originally proposed to transfer NDSP's business immediately to NDL following the buy out of the Minority on 1 July 1992. As will appear, this plan was thwarted after other concerns, arising from the Override Agreement, were raised (see paragraph 116 and following).

7 July 1992

108. On 7 July 1992 NDSP acquired the whole share capital of NDL (at that time two ordinary shares of one pound each) from NI for £2. NDL thus became a 100% subsidiary of NDSP.

8 July 1992

109. On 8 July 1992 NDSP transferred its assets to NDL. NDSP transferred its hundred percent shareholding in NRL to NDL in consideration of:

- (1) the issue of 98 ordinary shares of one pound each in NDL; and
- (2) a loan note for US \$138, 612.

110. On the same day NDSP transferred its business and remaining assets to NDL in consideration of three loan notes for a total of US \$43,085,010 issued by NDL and the assumption of NDSP's liabilities by NDL. NRL thus became a subsidiary of NDL and NDL became the owner of all the business assets of NDSP. NDSP now owned 100 shares in NDL (two shares and 98 shares issued as consideration). This was the whole of the issued share capital of NDL.

9 July 1992

111. NDSP transferred the hundred shares in NDL to NI for a consideration of £100. NDL thus ceased to be a subsidiary of NDSP.

112. The reason for the transactions being structured in this way was to comply with the Override Agreement (that is, to enable the reorganisation to proceed in a manner which did not require prior consent of the News Group's lending banks): see paragraph 116 and following below.

The Board Meetings to carry out the Transactions in Question

113. The four directors of NDSP appointed by the Minority resigned on 1 July 1992. With effect from 1 July 1992 NCHL appointed three new directors in their place. They joined the then current News Group-appointed directors, Messrs Fischer, Price and Holloway. The three new directors were Arthur Siskind, David Devoe and Jeffrey Leist. Mr Siskind and Mr Devoe were senior executive directors of TNCL and members of the Office of the Chairman. Mr Leist worked with Mr Devoe. He was not a director of TNCL but was a director of several News Group subsidiaries. These three directors were all US residents and for work purposes were based at TNCL's global headquarters in New York.

114. The NDSP board meetings of 7, 8 and 9 July 1992 were chaired by Mr Siskind at TNCL's office in New York. Due notice of the meetings was sent to all directors, but those attending 8 and 9 July 1991 meetings were Mr Siskind, Mr Devoe, and Mr Leist, that is, the newly-appointed directors. Mr Siskind and Mr Leist attended the 7 July 1992 meeting. Following the reduction in the number of directors comprising a quorum for board meetings (from four to two - at the board meeting of 1 July 1992: see paragraph 62 above), two directors was sufficient to a valid meeting of the board. Mr Devoe was at that time attending for conference in Sun Valley, Idaho. He participated by telephone. Mr Leist was at home in Bedford, New York where he then lived. He participated by telephone. The articles of NDSP adopted on 16 February 1988 provided that a director "in telephonic communication" with a board meeting was to be counted towards the quorum.

115. None of those present or treated as present at these board meetings was within the UK and all were outside the UK. We find as a fact that these three meetings took place outside the UK and not in the UK. We also find as a fact that they were in exercise the central management and control.

The Override Agreement

116. The Override Agreement was a complex refinancing agreement made between various News Group companies with their bankers in 1991. The Override Agreement remained in force until 1993.

117. The Override Agreement contained extensive provisions affecting the operation and structuring of the News Group. Relevant to the transactions with which this appeal is concerned were the so-called "standstill provisions", which prohibited News Group companies from entering into certain types of transaction or incurring major expenditure without the banks' prior approval.

118. NDSP was not a party to the Override Agreement. However, transactions undertaken by NDSP were potentially within the scope of the Override Agreement.

119. Compliance with the Override Agreement was one of Mr Siskind's responsibilities. The immediate transfer of NDSP's business to NDL was postponed pending consideration of the impact of the Override Agreement. There was a deal of communication between Mr Siskind, Mr Zelkha and Australian advisers in early 1992.

120. On 2 July 1992 Mr Siskind informed Mr Zelkha that the proposed asset sale transaction (that is, the sale by NDSP of its business and assets to NDL as then planned) could not proceed as it was not permitted by the Override Agreement without the prior approval of the banks, which the News Group did not want to seek. Mr Zelkha then proposed the revised transaction (the key difference was for NDSP first to acquire the shares of NDL, so that the sale of the NDSP business was then a transaction between parent and subsidiary) which Mr Siskind approved in principle on 2 July 1992 on the basis that the revised transaction would not fall foul of the Override Agreement. The revised transaction was then considered in detail by the professional advisors in the UK, the US and Australia over the period 2 July to 5 July 1992. The revised transaction was designed to achieve the same end result in a manner compliant with the Override Agreement. This was essentially what was implemented.

121. Mr Siskind approved this revised transaction in its detail on 6 July 1992.

Summary of Findings of Facts as to the NDSP Board and Executive Committee

122. In summary, we have found the following facts in relation to the Board and the Executive Committee:

- a. The functions of the Board as a constitutional organ of NDSP were not usurped at any relevant time.
- b. None of the meetings of the Board took place in the UK except the 1 July 1992 meeting at Farrers' offices in London.
- c. The meeting on 1 July 1992 at Farrer's was not an exercise of central management and control but a mere matter of tidying up and good housekeeping consequent upon the completion of the Minority buy-out

and to put in place the News Group general policy as to quorums for board meetings.

- d. The Executive Committee's functions were limited to operational matters. It never exercised central management and control of NDSP. It was not the controlling brain of NDSP, it was not the body through which NDSP really or actually did business and it was not the situs of where NDSP kept house or really did abide.
- e. In so far as there were external influences they came not from the UK but from New York and/or Jerusalem.
- f. Mr Price's and others' attempts to influence matters did not amount to the exercise of central management and control. At most they were involved in administrative and day-to-day matters.
- g. There was a real change in NDSP's history on 1 July 1992 which amounted to a watershed.

Finding of NDSP's Non-UK Residence

123. Accordingly we find that NDSP was resident outside and not in the UK at all material times whether one takes a narrow view of the relevant period (1 July to 9 July 1992), for which the Appellant primarily contends, or a wider view (from 1988 to July 1992), for which the Revenue primarily contend. The reasons for this are set out below. Despite Mr Brennan's request that we should "avoid a fudge", we do not consider it would be helpful, nor is it required as a matter of law, to find where outside the UK NDSP was resident. Following the approach adopted by Lord Radcliffe in *Unit Construction* (at 368), we find that NDSP was not resident in the UK, which is what is needed to determine whether there was a deemed disposal giving rise to a charge to UK tax under section 178 (3) TCGA.

The Submissions of the Parties

The Appellants' Submissions

(a) The Residence Issue

124. In essence, the Appellants' submissions on the Residence Issue were:

- a. the period to consider was 2 to 9 July 1992;
- b. there had been no usurpation of the functions of the constitutional organs of NDSP in that period or if relevant before;
- c. the Board met (other than for merely ministerial matters) during the relevant period only outside the UK;
- d. following *Wood v Holden* in the Court of Appeal the situs of central management and control which determines residence (in the absence – as here - of usurpation) is the place where the Board meets;

- e. the Board did not meet in the UK during the relevant period (other than for merely ministerial matters) and so NDSP could not be and was not resident in the UK.

125. On the matter of what constituted central management and control Mr Waksman QC submitted that the Board constitutes the organ of central management and control unless there has been a usurpation. The situs of such management and control is where the Board meets.

126. In more detail the submissions were as follows:

- (1) The test for corporate residence is central management and control. There is no separate test of “real” or effective decision.
- (2) In a normally constituted company those who exercise its central management and control are its Board of Directors.
- (3) The central management and control by the Board is exercised where the Board meets.
- (4) Unless it can be said that the Board has in fact been usurped so that some third party (including a parent company) is taking the decision then:
 - (a) the fact that there is not much involved in the Board’s acts amounting to management or control is irrelevant;
 - (b) it is irrelevant that the Board was acting on clear professional advice and was influenced by that advice;
 - (c) it is irrelevant that the Board did exactly what the other persons connected with the transactions expected them to do;
 - (d) it is equally irrelevant that the Company was set up only for the transaction in question even as part of a predetermined and complex scheme of tax avoidance;
 - (e) it is also irrelevant that in making its decision the Board was ill-informed or ill-advised.

(b) The Appellants' Submissions on the Section 178 Limitation Point

127. In essence, the Appellants submitted (on the assumption, which was not admitted, that NDSP was UK resident) that section 178 (10) TCGA was the sole and exclusive time limitation on the making of assessments under section 178 TCGA. It ousted section 34 TMA. Accordingly, the assessment on NDL made on 15 April 1999 was out of time as it was made more than six years after NDL was deemed to have made the disposal (i.e. 8 July 1992) and when NDL left the NDSP group (i.e. 9 July 1992).

128. In more expanded form, the submissions were as follows:

- a. By section 178 (3) TCGA there was a charge to corporation tax when a company left a group in circumstances such as those under consideration.
- b. Section 178 (10) TCGA provides:

“Notwithstanding any limitation on the time for making assessments, an assessment to corporation tax chargeable in consequence of this section may be made at any time within 6 years from the time when the chargeable company ceased to be a member of the group...”. This is exhaustive.
- c. The general rule in section 34 TMA provides that an assessment may be made six years from the end of the accounting period in which the chargeable event occurs. This is ousted by section 178 (10) TCGA which is exclusive.
- d. The effect of this is that section 178 (10) TCGA should be read as having the effect that an assessment under section 178 may only be made within six years of the company leaving the group.
- e. This is supported by comparison with sections 101, 137, 169 and 190 TCGA.
- f. Certainty is the underlying rationale for section 178(10) TCGA ousting section 34 TMA.

HMRC's Submissions

(a) The Residence Issue

129. Mr Brennan QC submitted that the test of corporate residence is the *De Beers* test. This required the questions to be asked where is the real business of the company carried on and where does central management and control actually abide?

130. These questions were to be answered in all cases by reference to the course of business and trading.

131. The test of central management and control is not to be treated as a test which depends solely on the location where the directors meet. The search is for the principal seat of business – it is there where the central management and control actually abides (see the *Calcutta Jute* case at page 96). This carries with it connotations of continuity because of the use of phrases such as "actually abides", "carries on business", "keeping house". It is not sufficient, therefore, to look simply at the period during July 1992 when the relevant transactions were carried out: instead it is necessary to consider the overall pattern of conduct established over a period of time – residence does not change on every occasion where there is short-term change in the location of board meetings.

132. The location of directors meetings could have been but was not chosen as the test for corporate residence (see Lord Radcliffe in *Unit Construction* [1960] AC 351 at 365).

133. The Court of Appeal decision in *Wood v Holden* does not change the test. The House of Lords decisions applying the test of "central management and control" are not to be read as qualified in any way by the decision in *Wood v Holden*. The critical question in that case was whether the relevant company had become UK resident. It was held not to become UK resident by reason of falling in with the wishes of Mr Wood as expressed through his advisers. The court held that the decision to buy the relevant shares was made in the Netherlands because the directors met there and so decided.

134. The factual position was radically different in *Wood v Holden*. In the case of NDSP the board did not meet between March 1991 and July 1992, it did at the relevant times in *Wood v Holden*.

135. HMRC submitted that central management and control actually abided with Messrs Price and Brown (the accountants) under the supervision of Messrs Fischer, Barraclough and Stehrenberger who were based in the UK. It did not lie with the Office of the Chairman, Michael Clinger, the other Minority-appointed directors, or the appointed directors who were based in the USA.

136. Mr Brennan QC went further in oral argument. In effect, he was suggesting that the Board was suspended and that the accountants, Messrs Price and Brown had usurped the function of the Board along with Messrs Fisher, Barraclough and Stehrenberg.

137. Mr Brennan also submitted that the 1 July 1992 meeting in London was not merely ministerial in character. The change reducing the quorum of directors was central to the management and control of any company's business as it determines who can carry out management and control.

138. There was no Watershed on or after 1 July 1992. The purchase of NDL, a shell company, for £2 on 7 July 1992 was a routine matter and it is irrelevant that it was decided on by newly appointed US directors.

139. It is for the Appellants to establish that NDSP was resident outside the UK and not in the UK. If they do not do that then NDSP would be dual resident (see *Swedish Central Railway Company* at 372-373 (Lord Cave), *Union Corporation* at 266-268 and *Unit Construction* at 367-368 (Lord Radcliffe)). As the Appellants have failed to show that NDSP was not resident in the UK and/or that it was not dual resident then it inevitably follows that NDSP was resident in the UK on 8 July 1992.

(b) The Section 178 Limitation Issue

140. In essence, HMRC's argument on this point is that the section should be read and given effect as drafted. There is no justification for reading the word "may" in subsection 178 (10) TCGA as meaning "may only", nor is there any justification for

reading the provision as if "notwithstanding any limitation" read "notwithstanding any provision for longer limitation".

141. Mr Brennan QC also contended that the Appellants' construction has the effect that the time for assessing the grouping gain can expire earlier than the time for making ordinary assessment to corporation tax. No reason is offered why such a result should follow.

Discussion

Introduction

142. There are two issues for us to decide, namely:

- (1) the Residence Issue; and
- (2) the Section 178 Limitation Issue.

We consider the Residence Issue first.

The Residence Issue

The Questions to Consider

143. The residence issue requires us to consider three questions. These are:

- a. What is the correct test to apply in deciding the residence of NDSP?
- b. What is the evidential burden of showing this and on whom this is fall?
- c. What is the result of applying the correct test in evidential burden to the facts we have found?

What is the Test for Corporate Residence for NDSP?

144. The generally accepted test for corporate residence for the purposes under consideration where a company is incorporated outside the UK is that the company is resident at the situs of the central management and control of the company in question (see eg what Lord Loreburn LC said in the *De Beers* case quoted below)

145. We also have the assistance of the recent Court of Appeal decision in *Wood v Holden*. We were told by Mr Brennan QC (who appeared for HMRC in that case, as well as in this case) that HMRC were seeking leave from the House of Lords to appeal to the House of Lords. We have borne that in mind in reaching our decision and the making our findings of fact. We were informed later that the House of Lords had refused leave to appeal in *Wood v Holden*.

146. As Chadwick LJ said at paragraph 27 in *Wood v Holden*:

“In my view the judge was correct in his analysis of the law. In seeking to determine where "central management and control" of a company

incorporated outside the United Kingdom lies, it is essential to recognise the distinction between cases where management and control of the company is exercised through its own constitutional organs (the board of directors or the general meeting) and cases where the functions of those constitutional organs are "usurped" - in the sense that management and control is exercised independently of, or without regard to, those constitutional organs. And, in cases which fall within the former class, it is essential to recognise the distinction (in concept, at least) between the role of an "outsider" in proposing, advising and influencing the decisions which the constitutional organs take in fulfilling their functions and the role of an outsider who dictates the decisions which are to be taken. In that context an "outsider" is a person who is not, himself, a participant in the formal process (a board meeting or a general meeting) through which the relevant constitutional organ fulfils its function.

147. This reveals two categories to consider. The first category is where management and control of the company is exercised by its own constitutional organs. The second category concerns where the functions of those constitutional organs are "usurped".

148. We have already found as a primary fact that there was no usurpation of the Board so the second category is not in point. We would note again that if there were any vacuum during the relevant period it was filled from abroad (USA and/or Israel) and not from the UK. Those providing influence and advice and/or dictating what should happen were not in the UK, but outside.

149. Management and control was considered by Park J. at paragraph [21]. He said:

“The 'common law' of corporate residence

[21] The basic test which the cases have evolved is the 'central management and control' test. The test seems to have originated in the Court of Exchequer in 1876: *Calcutta Jute Mills Co Ltd v Nicholson* 1 TC 83, and *Cesena Sulphur Co Ltd v Nicholson* 1 TC 88. It was adopted some thirty years later by the House of Lords in what is generally regarded as the seminal authority on the matter: *De Beers Consolidated Mines Ltd v Howe* [1906] AC 455. Lord Loreburn said at page 458:

"... the principle that a company resides for purposes of income tax where its real business is carried on. ... I regard that as the true rule, and the real business is carried on where the central control and management actually abides."

In all the three cases which I have mentioned the underlying trading operations were to a considerable extent carried on overseas (for example, in *De Beers*, diamond mining in South Africa), but because the central control and management of the business operations was carried on in the United Kingdom, the companies were held to be resident in the United Kingdom. In all normal cases the central control and management is identified with the control which a company's board of directors has over

its business and affairs, so that the principle almost always followed is that a company is resident in the jurisdiction where its board of directors meets.

[22] In the previous sentence I have said 'almost always' because it is possible for a company to be resident in one territory even if it does not hold directors' meetings there. The authority always cited for that proposition is the House of Lords decision in *Unit Construction Co Ltd v Bullock* [1960] AC 455. A United Kingdom parent company owned several subsidiaries which were incorporated in jurisdictions in East Africa and carried on trading activities there. The managing director of the parent company formed the view that 'the situation of the African subsidiaries was becoming so serious that it was unwise to allow them to be managed in Africa any longer, and that their management must be taken over by the directors of [the parent company] in London.' The board of directors of the parent company 'decided that ... they were forced to take over management and control'. (See paragraph 5 of the Case Stated at 38 TC 716.) Thereafter the representative of the parent company in East Africa effectively usurped the functions of the local boards, which still existed but stood aside, and controlled the subsidiaries in accordance with the requirements of the parent. Much of that may have been irregular, or even unconstitutional, but it was what happened. It was held that the African subsidiaries had become resident in the United Kingdom..."

150. He continued at paragraph [25]:

“There is a difference between, on the one hand, exercising management and control and, on the other hand, being able to influence those who exercise management and control. There is another difference, highlighted by *Unit Construction v Bullock*, between, on the one hand, usurping the power of a local board to take decisions concerning the company and, on the other hand, ensuring that the local board knows what the parent company desires the decisions to be. It is also necessary to keep in mind that, while the cases which I have referred to so far all involved the residence of companies with active continuing businesses, it is possible (and is common in modern international finance and commerce) for a company to be established which may have limited functions to perform, sometimes being functions which do not require the company to remain in existence for long. Such companies are sometimes referred to as vehicle companies or SPVs (special purpose vehicles). 'Vehicle' has a belittling sound to it, but such companies exist. They can and do fulfil important functions within international groups, and they are principals, not mere nominees or agents, in whatever roles they are established to undertake. They usually have board meetings in the jurisdictions in which they are believed to be resident, but the meetings may not be frequent or lengthy. The reason why not is that in many cases the things which such companies do, though important, tend not to involve much positive outward activity. So the companies do not need frequent and lengthy board meetings..."

The four cases which I have described in the foregoing sub-paragraphs involve different sets of facts, and are obviously not identical. However, they do have some common features which, in my opinion, are relevant to the present case. They all involved persons based in one jurisdiction (commonly a high tax jurisdiction) causing companies to be established in other jurisdictions (commonly low or no tax jurisdictions). In all the cases the companies so established were intended to fulfil particular purposes which were ancillary to the activities of the persons who caused them to be established. In all the cases the local managements did not take initiatives, but responded to proposals (described in some passages in the judgments as instructions) which were presented to them. In all the cases they did implement the proposals, and it is obvious that, when the foreign companies had been established, the confident expectation was that they would implement the proposals. In general, although large amounts of money may have been involved, the functions which the companies were established to fulfil did not involve much regular activity, so there was no great need for frequent exercises of central management and control. It is worth stating that, except for *Unit Construction v Bullock*, Mr Brennan did not refer me to any case which might give a different impression of the law from the four cases which I have described. Further, in all four of them *Unit Construction v Bullock* was expressly distinguished. The essential ground of distinction was that, whereas in *Unit Construction v Bullock* the parent company itself exercised central control and management of the African subsidiaries, effectively by-passing the local boards altogether, in the four cases the parent companies or their equivalents, while telling the local boards what they wished them to do, left it to the local boards to do it.”

151. This was approved by the Court of Appeal at paragraphs [24] and [27]

“[24] The judge's reference, in that paragraph, to "the common law of corporate residence" is to the *De Beers* test of "central management and control". The judge had set out that test at paragraph [21] of his judgment. At paragraphs [22] and [23] he had considered the subsequent decision of the House of Lords in *Unit Construction Co Ltd v Bullock (Inspector of Taxes)* [1960] AC 351 – which he described as "a very important case, but . . . a highly exceptional case in terms of the result". As he explained:

"[22] . . . the representative of the parent company in East Africa effectively usurped the functions of the local boards, which still existed but stood aside, and controlled the subsidiaries in accordance with the requirements of the parent. Much of that may have been irregular, or even unconstitutional, but it was what happened. It was held that the African subsidiaries had become resident in the United Kingdom.

[23] . . . It was not a case where the local boards still exercised central management and control, but did so under guidance and influence from the parent company in the United Kingdom. It was a case in which the

local boards stood aside altogether, and the parent company effectively usurped what in theory were the functions of the local boards..."

[27] In my view the judge was correct in his analysis of the law. In seeking to determine where "central management and control" of a company incorporated outside the United Kingdom lies, it is essential to recognise the distinction between cases where management and control of the company is exercised through its own constitutional organs (the board of directors or the general meeting) and cases where the functions of those constitutional organs are "usurped" - in the sense that management and control is exercised independently of, or without regard to, those constitutional organs. And, in cases which fall within the former class, it is essential to recognise the distinction (in concept, at least) between the role of an "outsider" in proposing, advising and influencing the decisions which the constitutional organs take in fulfilling their functions and the role of an outsider who dictates the decisions which are to be taken. In that context an "outsider" is a person who is not, himself, a participant in the formal process (a board meeting or a general meeting) through which the relevant constitutional organ fulfils its function.

152. It is also important to note is that the degree of activities not consider to be part of the test. Chadwick LJ said (at paragraphs [35] and [36]):

"For my part I find the judge's analysis compelling. At paragraphs [64] and [65] he said this:

"[64] . . . The making of the board resolutions and the signing and execution of documents which the Commissioners say were the only acts of management and control of Eulalia all took place in the Netherlands. A company is resident where its central management and control are situated. How, therefore, can Eulalia have been resident in the United Kingdom? How can it have been resident anywhere other than the Netherlands?

[64] . . . What [the Commissioners] seem really to be saying is that, although the only acts of control and management took place outside the United Kingdom, there was not much involved in them. But the test of a company's residence is still the central control and management test: it is not the law that that test is superseded by some different test if the business of a company is such that not a great deal is required for central control and management of its business to be carried out."

[36] The judge went on, at paragraph [66] to say this:

"[66] . . . If directors of an overseas company sign documents mindlessly, without even thinking what the documents are, I accept that it would be difficult to say that the national jurisdiction in which the directors do that is the jurisdiction of residence of the company. But if they apply their

minds to whether or not to sign the documents, the authorities . . . indicate that it is a very different matter. . . ."

In addressing the question whether ABN AMRO had taken "effective decisions" the judge pointed out, at paragraph [68] of his judgment, that the two decisions "which matter are the decision in July 1996 that Eulalia should purchase the 49% holding in Holdings and the decisions in October 1996 that Eulalia should sell the holding". He had rejected (at paragraph [67]) the suggestion that, if ABN AMRO did take those decisions, "because they were not informed decisions they . . . did not count".

153. If the test is held to be wider and the question of where the company really does business in a broader sense than we do not consider this assist HMRC as we would conclude applying that test that apart from that an operational level the place where NDSP did real business and kept house was not in the UK but outside the UK at all relevant times.

The Evidential Burden Question

154. Chadwick LJ noted at paragraph [31] that at paragraph [63] of his judgment in *Wood v Holden* the judge said this:

"[63] . . . in so far as the Commissioners decided this appeal against Mr and Mrs Wood on grounds relating to the burden of proof (and the opening part of paragraph SC145 suggests that those were the critical grounds for the decision), I consider that they were in error."

Chadwick LJ continued:

"He could not have been intending to suggest, in that paragraph, that the Special Commissioners had been wrong in principle to approach the matter on the basis that it was for Mr and Mrs Wood to show that the adjustments to their self-assessments had been wrongly made. Rather, I think, he was stating his conclusion that the Special Commissioners had been wrong in failing to appreciate that the evidential burden had passed to the Revenue in the present case."

155. Accordingly, we have proceeded on the basis that it is for the Appellants to show that the assessments had been wrongly made. We also accept that the evidential burden can shift to HMRC. However, we do not reach our decision purely on grounds relating to the burden of proof in the *Wood v Holden* sense. Rather we reach a positive decision that NDSP was not resident in and was resident outside the UK, not that there is a failure to discharge the evidential burden that this is the case. We consider the evidential burden discharged having had the benefit of seeing the witnesses.

156. Mr Waksman QC for the appellants asked us to record that at paragraph 90 of his skeleton he reserved the right to argue should this case go further that the entire burden of proof is on HMRC. Accordingly, we record this reservation.

Application to the Facts

157. On the basis that the test is as set out by the Court of Appeal in *Wood v Holden* we find:

- a. there was no usurpation of the Board's functions;
- b. management and control in the sense of the exercise of the controlling brain of NDSP through its appropriate constitutional organs, here the Board, was exercised outside and not in the UK as all the Board meetings doing so were outside the UK and not in the UK.
- c. The Board Meeting of 1 July 1992 (which took place in London) was of a purely ministerial or housekeeping nature and is to be disregarded for these purposes as not being an exercise of central management and control.

158. Accordingly we find that on that basis that NDSP was resident outside and not in the UK at all relevant times. For the avoidance of doubt (but without prejudice to the generality of the foregoing) we find this for the periods:

- a. 2 July 1992 – 9 July 1992
- b. 30 March 1992 – 9 July 1992
- c. 30 June 1991 – 9 July 1992

159. If the test is a wider test and the question is where does the company really do business other than in a day-to-day operational sense then we still find that the situs of the management and control of NDSP, in the sense of where does the company keep house and really do business, is outside the UK. We make this finding for each of the periods:

- a. 2 July 1992 – 9 July 1992
- b. 30 March 1992 – 9 July 1992
- c. 30 June 1991 – 9 July 1992

Conclusion on the Residence Issue

160. In applying both the Court of Appeal test in *Wood v Holden* and the wider test argued for by HMRC we find on the facts that NDSP was resident outside and not in the UK at all relevant times.

161. Accordingly the answer to the question “Whether NDSP was resident in the UK when it disposed of its business to NDL on 8 July 1992?” is that it was not resident in the UK.

The Section 178 Limitation Issue

162. We consider that section 178 (10) TCGA is not exhaustive and does not oust the general rule in section 34 TMA. The reasons for this are as follows.

- a. Section 178 (10) TCGA does not say that it is exhaustive and ousts section 34 TMA.
- b. The subsection says that an assessment may be made any time within six years of the company leaving the group. It does not say "may only" be made within six years of the company leaving the group.
- c. Section 178 (3) TCGA charges the company leaving the group as if it had disposed of the asset it acquired intragroup immediately after it received the assets.
- d. The effect of section 178 (10) TCGA is to give an extension to the period in which an assessment can be made in many cases. If the recipient left the group 5 years after the intragroup transfer of the relevant assets section 34 TMA will give a year in which to make the assessment. Subsection (10) extends the period to six years from the date of leaving the group. There would seem to be clear policy reasons why Parliament should intend this to be the case. There is no policy reason why s178 (10) should be restrictive of the general rule.
- e. The other provisions of the TCGA prayed in aid are cases allowing collection of tax not paid by a taxpayer from another party so that the limitation is inherent in the grant of the power to collect. The effect of section 178 TCGA is not to allow collection of tax as a secondary liability but is to impose a primary liability on the company leaving the group. A charge to tax is imposed on the company leaving the group by subsection (3) as a primary and not a secondary liability. The contrast between subsections (3) and (9) of section 178 TCGA shows this clearly.

Conclusion on the section 178 Limitation Issue

163. Accordingly, we answer the question “Whether section 178(10) TCGA 1992 has the effect that notwithstanding the ordinary time limit for assessments in section 34 TMA 1970, the time limit for an assessment to Corporation Tax chargeable on NDL in consequence of section 178 TCGA 1992 expired on 9 July 1998 (that is, six years after NDL ceased to be a member of the group) so that the assessment under appeal (made on 15 April 1999) is out of time?” No, the assessment was made in time and not out of time.

Conclusions on the First or Preliminary Issues

164. We conclude and find that:

- a. NDSP was resident outside and not in the UK as all relevant times; and
- b. the assessment in respect of section 178 TCGA was made in time as section 178 (10) TCGA is not exhaustive and does not oust section 34 TMA.

165. We would remind the parties that the Direction of [] 2005 requires that

“Within 28 days of the release of the decision(s) concerning the Residence Issue and/or the Section 178 Limitation Issue the Parties shall jointly apply to the Tribunal for further directions in relation to the NDL Appeal and the NDSP Appeal setting out agreed draft directions if possible and if no such draft is agreed their respective drafts.”

ADRIAN SHIPWRIGHT

EDWARD SADLER

**SPECIAL COMMISSIONERS
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