[2015] UKUT 0219 (TCC)

Appeal against Lower Tribunal to strike out evidence served by HMRC as to the conviction of other companies and parties of participating in a Missing Trader Fraud – Burden of proof and weight to be given to such evidence – allegation of bad faith whether it imports allegation of dishonesty.

FTC/111/2013

IN THE UPPER TRIBUNAL
(TAX AND CHANCERY CHAMBER)

BETWEEN

THE COMMISSIONERS FOR HER MAJESTY'S REVENUE AND CUSTOMS

Appellants

-and-

INFINITY DISTRIBUTION LIMITED (IN ADMINISTRATION)

Respondents

Tribunal:

The Honourable Mr Justice Peter Smith
Sitting in public in London on 17th February 2015

Representation:
Jeremy Benson QC and Lucy Wilson-Barnes instructed by HMRC for the Appellants
Ian Bridge and Nataly Papandreou instructed by Morgan Rose for the Respondents

DECISION

I dismiss the Appellant's appeal.

REASONS

Introduction

1. This is an appeal dated 26th September 2013 by Her Majesty's Revenue and Customs ("HMRC") against part of the decision of Tribunal Judge Porter dated 1st November 2012 and in particular paragraphs 7, 8 and 10 where the learned Judge struck out evidence which HMRC were seeking to introduce namely a witness statement of a Mr Wafer, paragraph 94 of a witness statement of Miss Holder and various paragraphs set out in her witness statement as identified in paragraph 10 of the Decision.

2. Judge Porter gave brief reasons on 27th December 2012.

3. Permission to appeal was given by a direction dated 27th August 2013 and the appeal was made on 26th September 2013.

Background

4. The present appeal by the Respondents is in respect of a number of appeals by Infinity Distribution Ltd (In administration) ("Infinity"). Those appeals relate to a decision made by HMRC that 6 invoices were invalid in that they failed to satisfy the requirements of regulation 14 (1) VAT Regulations 1995.

5. The invoices relate on their face to Sony Ericsson P990 phones and Samsung Serene phones. HMRC contend that the invoices do not contain a description ***sufficiently*** to identify the goods or ***"for each description the quantity of the goods".*** The main plank of HMC's case is their contention that the phones in question had not actually been manufactured when the goods were ostensibly bought and sold. If the transactions are genuine Infinity has a claim for repayment of VAT in excess of £11m. However HMRC's contention is that because the evidence they have is that the phones did not exist the invoices did not contain a description as required by regulation 14 above mentioned.

6. However that is somewhat disingenuous. The case in reality is one of fraud. Thus one starts with HMRC's contention that no phones existed. Second in paragraph 38 of their statement of case they set out evidence which showed the alleged freight forwarder did not have business premises, had been arrested and interviewed by the Dutch Fiscal Authorities Dutch Fiscal Authorities remain in respect of admitting to fabricated evidence of the rival of non existent goods and that others did not genuinely insist having a Lawyers Bureau for an office (Easy Trading Communications SL) a mailbox (Sopex BV). This leads HMRC to contend in paragraph 39 of their case:

> ***"Accordingly, the commissioners do not consider the appellants acting in good faith and/or they took every reasonable measure to ensure that their supply did not lead to their participation in tax evasion, in accordance with the ECJ decision in Teleos Plc and others v the Commissioners of Customs and Excise."***

7. Despite the contention in paragraph 39 that Infinity did not act in good faith, HMRC contended before the learned Judge and before me that they were ***not*** alleging that Infinity were guilty of fraud. This, in my view, is an impossible

stance. It is well established that an allegation of lack of good faith is tantamount to an allegation of fraud see for example ***Medforth v Blake [1999] 3WLR 922*** at page 937 where Sir Richard Scott VC (who gave the majority judgment in the Court of Appeal) said:

> ***"I do not think that the concept of good faith should be diluted by treating it as capable of being breached by conduct but is not dishonest or otherwise tainted by bad faith. It is sometimes said that recklessness is equivalent to intent. Shutting ones eyes deliberately to the consequence of what one is doing may make it possible to deny an intention to bring out those consequences. There apart, however, the concepts of negligence, on the one hand, and fraud and bad faith on the other, ought, in my view, to be kept strictly apart. Equity has not always done so. The equitable doctoring of "fraud on a power" has little, if anything, to do with fraud. Lord Herschell in Kennedy v Dee Trafford [1987] AC 188 gave an explanation of a lack of good faith that would have allowed conduct that was grossly negligent to have qualified notwithstanding that the consequence of the conduct was not intended. In my judgment, the breach of the duty of good faith should, in this area as in all other areas, require some dishonesty or improper motive, some element of bad faith can be established" (emphasis added).***

8. Thus in my view it is improper for HMRC on the one hand to allege that Infinity is not fraudulent but on the other hand to allege it is not acting in good faith.

HOW THIS CAME ABOUT

9. These cases involve what are undoubtedly MTC fraud ("Missing Trader Frauds"). The stance of HMRC however, is ambiguous. Although as I have said they allege that initially it is lacking in good faith but it is not fraudulent the appeal relates to evidence which does not have any direct relevance to Infinity. That evidence shows there was indeed an MTC fraud it this case but what it does ***not*** do is implicate Infinity.

THE EVIDENCE

10. Mr Wafer by his witness statement of 14 July 2011 gave evidence as to the results of "***Operation Inertia***" that investigation resulted in the criminal prosecution of individuals trading in Future Communications UK (Ltd) ("Future") and Unique Distributions Limited. Future was one of the suppliers to Infinity. His evidence (according to the decision of the learned judge below) reveals no more than that various officers were charged with cheating HMRC and were found guilty. The statement provides no evidence of any connection with a transaction as subject to the appeal.

11. As the learned judge therefore observed in paragraph 9 of his reasons, Mr Wafer's statement does no more than establish some but not all of the owners and workers for future were involved in fraudulent activities. As he rightly observed by implication HMRC are suggesting that Infinity could not have acted in good faith and could not have taken reasonable measures when dealing with such a company. There is as he observed a considerable difference in failing to act in good faith and taking reasonable measures and suggesting that Infinity knew or ought to have known that Future was fraudulent. However, HMRC do not allege that Infinity are fraudulent. The learned Judge (point 7) struck out Mr Wafer's witness statement as it was ***"highly prejudicial"*** to Infinity's case.

12. I cannot with respect to the Judge see that that is a basis for striking out evidence in a civil case. However, it seems to me that the evidence is not relevant to the appeal unless HMRC are alleging fraud or alternatively that

Infinity knew or ought to have known there was a fraud. As the statements of case currently stand. HMRC does neither.

13. In respect of Ms Holden's witness statement the learned Judge struck out large amounts of the evidence because they implied fraud on the part of Infinity but he said in his judgment (paragraph 10) (point 8) that if HMRC wished to rely on fraud as they would in an MTC case they should plead it. He referred to the well known observations of Millett LJ in ***Armitgage v Nurse CH 241*** at 254-7:

> ***"The general principle is well known. Fraud must be distinctly alleged and distinctly proved…."***

14. He further referred to the well known observations of Buckley LJ in ***Bellmont Finance Corporation Limited v Williams Furniture Limited [1979]*** 250,268:

> ***"An allegation of dishonesty must be pleaded clearly and with particularity."***

HMRC'S STANCE

15. In paragraph 8 of their skeleton for the purposes of the appeal HMRC repeat their contention that Infinity did not act in good faith "***and/or took every reasonable measure to ensure that its supplies did not lead to the participation in tax evasion"***. This as I have shown is a bare assertion in paragraph 39 of their statement of case. No particulars are provided by HMRC. The reason for that is tactical. It is also based on the proposition (in paragraph 10 of their skeleton argument) that the burden of proof in both the invalid invoice appeals and in the 0 rate of goods appeal is on Infinity. All of this is said to flow from the ECJ decision in ***Regina (Teleos Plc and others) v Customs and Excise [2008] QB 600***. That decision established that for a

challenge to a supplier seeking repayment of VAT for example it is not possible where a supplier acts in good faith and submitting evidence establishing at first sight his right to meet relevant exemption unless evidence was found to be false or that there was evidence that the supplier being involved in the tax evasion or he had failed to take every reasonable measure in his power to ensure that the intra-community supply would not lead to his participating in such tax evasion.

16. In so concluding there are a number of parts of the opinion of the advocate general and the Judgment which are relevant. First in paragraph 77 of his Opinion the Advocate General said this:

> ***"77 It would, on the other hand, be excessive to go so far as to hold the supplier liable for criminal conduct of his business partner, against which he cannot protect himself. (The idea, that in levying of VAT, a careful and honest taxable person should not have to assume liability for the fraudulent conduct of theirs, is expressed in a series of decisions on carousel frauds; see in particular the Federation of Technological Industries case [2006] ECR I-419, para 33; Optigen Ltd v Customs and Excise Comrs (Joined Cases C-354, 355 and 484/03) [2006] Ch 218, paras 52 et seq, and Kittel case [2006] ECR I-6161, paras 45 et seq. Those cases are, however, not entirely comparable with the present set of circumstances, since those cases concerned several transactions which could be distinguished from each other, whereas in this case all that was supposed to take place was one intra-Community supply, albeit one in the implementation of which several persons were involved.) It would, for example, be of no help to the supplier in this case to require security in the amount of the VAT from the acquirer until proof of the transportation of the goods to another member state, as recommended in Commissioners' Notice 703. That is because the presentation of the consignment note, which so far as the supplier can determine contains no discernible false information, appears to provide just that proof. The supplier would thus be obliged to release the security on receiving the consignment note, even if – as it later turns out – transport across the frontier has not in reality taken place."***

17. He affirmed this opinion in paragraph 86:

> ***"86 The answer to the third question should therefore be; if the supplier, acting in good faith, presents objective proofs that the goods supplied to him have left the state of origin and the authorities of that state thereupon exempt the supply from tax in accordance with article 28c (A) (a) of the Sixth Directive, payment of the tax cannot be retrospectively demanded from the supplier in the circumstances of the main dispute in this case if it turns out that the proofs presented contained false information but the supplier neither knew nor could have known anything of it. That does, however, apply only where the supplier has done everything in his power to ensure the proper application of the provisions on VAT."***

18. The judgment of the ECJ followed this:

> ***"65 Moreover, according to the Court's settled case-law, which is applicable to the main proceedings by way of analogy, it would not be contrary to Community law to require the supplier to take every step which could reasonably be required of him to satisfy himself that the transaction which he is effecting does not result in his participation in tax evasion (see, as regards 'carousel' type fraud, Federation of Technological Industries and Others, paragraph 33, and Kittel and Recolta Recycling, paragraph 51). "***
>
> ***66 Accordingly, the fact that the supplier acted in good faith, that he took every reasonable measure in his power and that his participation in fraud is excluded are important points in deciding whether that supplier can be obliged to account for the VAT after the event.***
>
> ***67 By contrast, as the Commission observes, once the supplier has fulfilled his obligations relating to evidence of an intra-Community supply, where the contractual obligation to dispatch or transport the goods out of the Member State of supply has not been satisfied by the purchaser, it is the latter who should be held liable for the VAT in that Member State.***
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> ***68 The reply to the third question referred must therefore be that the first subparagraph of Article 28c(A)(a) of the Sixth Directive is to be interpreted as precluding the competent authorities of the Member State of supply from requiring a supplier, who acted in good faith and submitted evidence establishing, at first sight, his right to the exemption of an intra-Community supply of goods, subsequently to account for VAT on those goods where that evidence is found to be false, without, however, the supplier's involvement in the tax***

> ***evasion being established, provided that the supplier took every reasonable measure in his power to ensure that the intra-Community supply he was effecting did not lead to his participation in such evasion."***

19. Next I should refer to the decision of Arnold J in ***N2J Limited the Commissioner for Her Majesty's Commissioner and Customs [2009] EWHC 1596 (Ch).*** This case also addressed the question of the provision or non provision of mobile phones under a transaction.

20. The Tribunal found that the appellants had not taken every reasonable measure in its power to ensure the transactions were not connected with the fraud as is clear in paragraph 13 of the judgment ***N2J***'s appeal was on the basis that the Tribunal had lost sight of the fact and coming to the conclusion that it had not taken every reasonable precaution because there was no evidence of a fraud and fraud had not been suggested by the HMRC: its case was that it failed to provide valid commercial evidence that the goods had been sent for transported.

21. Further ***N2J*** contended that the Tribunal decision was wrong in law because the trader had submitted the correct documentation which unless there was something on the face which was obviously illegitimate or necessitated further enquiry was entitled to be conclusive.

22. Arnold J rejected the submissions as being inconsistent with paragraph 66 and 68 of ***Teleos*** (see paragraph 21 of his Judgment). I agree with that observation. The ***Teleos*** case shows that it is a matter of proof and that the documents can be undermined if there is evidence to show that the trader in question either participated in the fraud or failed to make reasonable enquiries as to whether or not he was involved in the fraudulent transaction.

23. Arnold J referred to the Judgment of Floyd J ***Mobilex Limited v HMRC [2009] EWHC 133*** where he said as follows:

> ***"16 Complete absence of evidence, or the evidence being to the contrary effect, are two of the grounds on which it may be said that a tribunal was not entitled to reach a conclusion of fact. It is also well settled that a tribunal is not entitled to find serious allegations established against a party who calls relevant witnesses unless those allegations are clearly formulated and put in cross-examination. As Briggs J said in HMRC v Dempster [2008] EWHC 63 (Ch) (unreported)***
>
> ***"it is a cardinal principle of litigation that if serious allegations, in particular allegations of dishonesty are to be made against a party who is called as a witness they must be both fairly and squarely pleaded, and fairly and squarely put to that witness in cross-examination."***

CONCLUSIONS

24. I draw the following conclusions from the Authorities:

1) The presentation of documentation which appears on its face to be correct raises a prime facie piece of evidence that the trader in question is entitled to relief sought and that the documents are genuine.

2) Those documents are not conclusive and can be challenged if it can be shown that the trader either participates in the fraud or failed to take reasonable care to avoid being involved in the fraud.

3) In accordance with established principles if it is going to be alleged that there was wrongdoing or failure to take reasonable care the burden is on the party which alleges that. That party in question is HMRC and it is not for the trader to prove that he was not fraudulent nor that he had taken reasonable precautions to avoid being involved in a fraud.

25. It remains a fundamental tenet of jurisprudence both at the European Court level and in this jurisdiction that allegations of wrong doing have to be made against the person in question and they must be put both fairly and squarely.

26. This merely reflects law at the ECJ level and the national level as set out above. This is a fundamental tenet that allegations of wrongdoing are put. Nothing in the above decisions as far as I can see alters that fundamental tenet and requires in effect Infinity to prove that it is bona fide and to prove that it did not know of the fraud.

EVIDENCE

27. It is therefore the burden on HMRC to establish those breaches as is all evidential burdens. Whilst the legal burden might remain with HMRC, the evidential burden can of course shift depending on what matters HMRC deploys in favour of its case.

28. It is a matter for HMRC as to how it wishes to prove the allegations. Evidence can take many forms. Undoubtedly the best case is that of direct evidence which can be the subject matter of cross-examination to establish the truth of the consequence. Less satisfactory of course is hearsay evidence which is untested. Assertions by officers (see for example in other context my observations in ***Farepak***) is not evidence at all. Neither is a conviction in another court effecting other parties to which Infinity and/or its officers has not been a party. The fact of conviction counts for nothing in this case. Of course the underlying evidence might be relevant and HMRC can deploy that evidence in any way it wishes. Of course the weaker the evidence the less likely that HMRC will be able to establish the allegations that it has made.

29. The principle of inadmissibility of prior convictions (especially when the person against whom it is thought to deploy was not the subject matter of that conviction nor a party) is well established see ***Phipson*** "On Evidence" paragraphs 43-78 and in particular ***Hollington v Hewthorn Co Ltd [1943] KB587***. It appears that the evidence in the previous action might be relevant but it needs to be assessed and reproven see ***Land Securities Plc v Westminster City Council [1993] 4 All ER 124.*** What is crystal clear however is that the conviction of itself cannot simply be deployed as a means of proving matters referred to therein against Infinity.

30. Nothing in the decision of ***Revenue and Customs Commissioners v Atlantic Electronics [2013] EWCA Civ 651*** affects the analysis above which related to a note from a prosecution case against somebody else.

31. As Ryder LJ said in the leading Judgment the decision to allow the prosecution note in that case is a balancing exercise following extensive submissions as to the word of the prosecution note and or the reasonable objections of Infinity. In paragraph 39 he reminded everybody of the status of the prosecution note:-

> ***"the asserted prejudice to the company relates to a misapprehension of the state of the document which is not evidence of the truth of its content, merely evidence as to what was said in opening about the background of the offences and accordingly the nature and extent of the dishonest activities of Morganrise in respect of the convictions. The prejudice to the Revenue in not being able to rely on the note of the prosecution opening is clear once the purpose of the admission of that material is analysed i.e. the dishonest and knowing participation of Morganrise as a contrary trader. Morganrise was not a party to the appeal in question in that case."***

32. Arden LJ (paragraph 72 and 73) confirmed that one has to look at the purpose of the conviction and the prosecution opening. The purpose was to show dishonesty on the part of the person convicted but she affirmed that of course the opening was not evidence which is capable of proving those transactions in law and ***"if its weight were challenged HMRC would have to adduce more probative evidence"*** (paragraph 73). Further she reinforced that some parts of the opening were not relevant because they concerned other irrelevant transactions.

33. In paragraph 84 she affirmed ***"the conviction of Mr Ahmed would be a matter of public record but it carries no weight on its own. Thus if HMRC's application is rejected it inevitably follows that HMRC will be prejudiced by its exclusion…."***

34. It is by no means clear in the present appeal upon what basis HMRC wishes to adduce this material. I have already averted to the erroneous stance on burden of proof and the contention that whilst they consider that Infinity did not act in good faith and did not take every reasonable measure to ensure their supply did not lead participation in tax evasion. They provided no particulars and they have not addressed the relevance of the material sought to be included in relation to the case ***against Infinity***.

35. It follows therefore in my view that save in respect of the prejudice point the learned Judge's Decision was entirely correct and was within the reasonable parameters that the Judge could have come to. That to my mind is the end of the appeal and I will dismiss the appeal.

36. The Decision of the learned judge was not in my opinion so unreasonable that it could not have been fairly made (***Bairstow v Edwards) [1956] AC 14***. He was perfectly entitled to conclude at that stage that the admission of the material was challengeable because it was not admissible as Infinity.

FURTHER MATTERS

37. The matter cannot be left in the present unsatisfactory state. In my view because of the reasons I have given in this ruling HMRC are required to set out the basis of its case against Infinity. Thus they should provide full particulars of every fact or matter relied upon for the allegation that Infinity did not act in good faith. If they are going to allege fraud they must give full particulars of fraud to the like extent. I have already observed that in my view an allegation of bad faith is tantamount to an allegation of fraud on established authority. Further they must give full particulars of every fact or matter relied upon for the allegation that they did not take every reasonable measure to ensure that their supply did not lead to their participation in tax evasion.

38. It is only when those particulars are provided that Infinity can know the case against it. I will hear further submissions on that from the time point of view but my tentative view would be that HMRC should be given 56 days to provide that information. If they are not going to give Infinity all the information it can apply to have paragraph 39 struck out.

39. I will remit the matter to the Lower Tribunal for reconsideration if HMRC wish. By that I mean that merely because I have dismissed the appeal will not prevent HMRC seeking to produce some or all of the matters that have been disallowed if it can establish that it is relevant to the case against Infinity.

That exercise has not been done at the moment but I do not preclude a fresh application on that basis to consider whether or not some or all of the material ought to be received. If it is to be received then as the ***Atlantic*** case above shows the ***purpose*** of the admission of the material must be clearly identified. If for example it is to be used solely to set the scene and to show that the non party was guilty of illegal conduct that is one thing; if it is sought to be used as evidence against Infinity that is entirely different and difficult matter for the reasons set out above.

Mr Justice Peter Smith

Released 2 May 2015

Amended 11 May 2015