



[2015] UKUT 0513 (TT)
Appeal number: UT/2013/0022

VALUE ADDED TAX—input tax- MTIC appeal-whether First-tier Tribunal made errors of law in concluding that taxpayer neither knew or should have known that its transactions were connected to fraud-yes-appeal allowed and case remitted for reconsideration to differently constituted tribunal

**UPPER TRIBUNAL
TAX AND CHANCERY CHAMBER**

**THE COMMISSIONERS FOR HER MAJESTY'S Appellant
REVENUE & CUSTOMS**

- and -

**CCA DISTRIBUTION LIMITED Respondent
(in administration)**

**TRIBUNAL: Mr Justice Morgan
Judge Timothy Herrington**

Sitting in public at the Rolls Building, Fetter Lane London EC4A 1NL on 29 and 30 June and 1 July 2015

Jeremy Benson QC, Christopher Kerr and Ben Hayhurst instructed by the General Counsel and Solicitor to HM Revenue and Customs, for the Appellant

James Pickup QC and Simon Taylor, instructed by Smith & Williamson LLP for the Respondent

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DECISION

Introduction

5 1. This is an appeal against a decision of the First-tier Tribunal (Judge Malachy
Cornwell-Kelly and Mr John Agboola ACCA) (“the F-tT”) released on 22 April 2013
 (“the Decision”). The F-tT allowed an appeal by the respondent, CCA Distribution
 Limited (“CCA”), against decisions of the appellant (“HMRC”) to deny CCA the
10 right to deduct input tax in excess of £9.8 million in relation to purchases of mobile
 phones made in three VAT periods, namely 04/06, 05/06 and 06/06.

2. HMRC denied CCA its claimed right to deduct input tax in relation to 39 purchase
 transactions effected by CCA in those VAT periods. In each of those deals CCA
 purchased the goods from one of three UK companies and exported the goods to one
 of a number of EU companies. The grounds on which HMRC refused the credit of
15 input tax were that it was satisfied that the transactions concerned formed part of an
 overall scheme to defraud the revenue and that there were features of those
 transactions and conduct on the part of CCA which demonstrated that CCA knew or
 should have known that this was the case. It will be apparent from this short
 introduction that this was what is commonly known as an MTIC appeal. We will not
20 set out in this decision a full description of what is typically involved in this type of
 case but we will assume that the reader is familiar with the concept, and the
 conventional terms used, in such appeals.

3. CCA accepted the allegation of connection with fraud but disputed HMRC’s
 finding that it knew or should have known that the transactions in question were so
25 connected. The F-tT were split on this issue. Judge Cornwell-Kelly (“the Judge”)
 exercised his casting vote in favour of allowing CCA’s appeal pursuant to article 8 of
 the First-tier Tribunal and Upper Tribunal (Composition of Tribunal) Order 2008. Mr
 Agboola (“the Member”) would have dismissed the appeal. Much of the Decision is
 taken up with findings which both members of the F-tT were prepared to make. The
30 Judge then set out the reasoning on which he alone relied and this was followed by the
 reasoning relied upon by the Member in support of his conclusion that there was a
 fraudulent scheme going on and CCA was a willing participant in the scheme.

4. It is helpful as further background to note that in respect of each of the 39
 transactions with which this appeal is concerned CCA acquired the goods from what
35 is known as a “contra-trader”. This is a term coined by HMRC to describe a
 fraudulent trader which (a) acquires goods from a UK trader as a participant in a chain
 of transactions which includes a defaulting trader (known as the “dirty chain”) and
 exports them to an EU trader claiming a credit for input tax (“the dirty input tax”) on
 the purchase and (b) in a chain which includes no defaulter (known as the “clean
40 chain”), imports goods from an EU trader and sells them to another UK trader and
 then offsets the dirty input tax against the clean output tax he is liable to pay HMRC
 in respect of the sale to the second UK trader. The purpose of this is to attempt to turn
 the dirty input tax into clean input tax in the hands of the second UK trader (who
 himself exports the goods to an EU trader) and to distance the second UK trader from

the default in the dirty chain so that he could not know of his connection to the default. It also means that it is more difficult for HMRC to discover the connection.

5 5. In respect of the 39 transactions referred to above, CCA is in the position of the second UK trader in that it acquired the goods concerned from what it accepted was a fraudulent contra-trader before exporting them. It was therefore at risk of being denied credit for input tax on its purchases if HMRC were to discover the role of the fraudulent contra-trader and were to establish that CCA knew or should have known of the connection to fraud in the dirty chain. CCA also featured as a “buffer” in a further 117 transactions where it was positioned in a dirty chain between another UK trader from whom it acquired goods which were sold to two of the three contra traders it dealt with in the clean chains. HMRC did not seek to deny CCA credit for input tax in relation to these deals, but as we shall see, these transactions are relevant to the fraudulent scheme as a whole. HMRC’s position is that the identity of CCA’s customer and supplier was crucial to the scheme and to the circulation of money through pre-ordained movements.

20 6. HMRC contends that CCA was not a free agent but had agreed to buy from a supplier in the scheme and to sell to a customer in the scheme to ensure that the funds continued to circulate and it would not have been rational for the organisers of the fraud to have used a conduit for the goods and money that was in ignorance of the scheme. This contention was in essence accepted by the Member in his statement of dissent. On the other hand, CCA points to the fact that it needs to look to HMRC for repayment of its input tax and risks its own capital pending HMRC’s scrutiny of its claim for credit. CCA is thus fully exposed in the way the contra-trader, who does not need to seek a repayment from HMRC, is not exposed. CCA’s alternative to HMRC’s contention is that it was an innocent trader unwittingly caught up in the scheme. The Judge found that HMRC had not made out its case on the question of knowledge or means of knowledge as a consequence of which, through the exercise of the Judge’s casting vote, the appeal was allowed. The question for us is whether the F-tT made errors of law in the course of coming to its conclusions.

30 **The F-tT’s Decision**

The legal framework

35 7. The F-tT correctly set out the legal framework for its decision and it referred in detail to the principal cases which were relevant. In particular, it identified and set out the legal principles that govern the circumstances in which the right to claim credit for input tax can be denied. We need not summarise everything which was stated by the F-tT in this respect as it will suffice to refer to the two main authorities which are relevant. At [7], the F-tT referred to the findings of the European Court of Justice in *Axel Kittel v Belgium; Belgium v Recolta Recycling Sprl* [2006] ECR1-6161 as analysed by Moses LJ in his judgment in the Court of Appeal in *Mobilx Limited (in administration) v HMRC & Ors.* [2010] EWCA Civ 517 where Moses LJ said at [41] and [42] :

5 “[41] In *Kittel* after §55 the [European] Court developed its established principles in relation to fraudulent evasion. It extended the principle, that the objective criteria are not met where tax is evaded, beyond evasion by the taxable person himself to the position of those who knew or should have known that by their purchase they were taking part in a transaction connected with fraudulent evasion of VAT:-

10 "56. *In the same way*, a taxable person who knew or should have known that, by his purchase, he was taking part in a transaction connected with fraudulent evasion of VAT must, for the purposes of the Sixth Directive, be regarded as a participant in that fraud, irrespective of whether or not he profited by the resale of the goods.

15 57. That is because in such a situation the taxable person aids the perpetrators of the fraud and becomes their accomplice.

15 58. In addition, such an interpretation, by making it more difficult to carry out fraudulent transactions, is apt to prevent them."

20 59. *Therefore*, it is for the referring court to refuse entitlement to the right to deduct where it is ascertained, having regard to objective factors, that the taxable person *knew or should have known* that, by his purchase, he was participating in a transaction connected with fraudulent evasion of VAT, and to do so even where the transaction in question meets the objective criteria which form the basis of the concepts of 'supply of goods effected by a taxable person acting as such' and 'economic activity'. [emphasis added]"

25 The words I have emphasised "in the same way" and "therefore" link those paragraphs to the earlier paragraphs between 53-55. They demonstrate the basis for the development of the Court's approach. It extended the category of participants who fall outwith the objective criteria to those who knew or should have known of the connection between their purchase and fraudulent evasion. *Kittel* did represent a development of the law because it enlarged the category of participants to those who themselves had no intention of committing fraud but who, by virtue of the fact that they knew or should have known that the transaction was connected with fraud, were to be treated as participants. Once such traders were treated as participants their transactions did not meet the objective criteria determining the scope of the right to deduct.

35 [42] By the concluding words of §59 the Court must be taken to mean that even where the *transaction in question* would otherwise meet the objective criteria which the Court identified, it will not do so in a case where a person is to be regarded, by reason of his state of knowledge, as a participant."

40 8. The F-tT also referred to [52], [59] and [60] of *Mobilx* where Moses LJ dealt with the meaning of "should have known", as follows:

45 “[52] If a taxpayer has the means at his disposal of knowing that by his purchase he is participating in a transaction connected with fraudulent evasion of VAT he loses his right to deduct, not as a penalty for negligence, but because the objective criteria for the scope of that right are not met. It profits nothing to contend that, in domestic law, complicity in fraud denotes a more culpable state of mind than carelessness, in the light of the principle in *Kittel*. A trader who fails to deploy means of knowledge available to him does not satisfy the objective criteria which must be met before his right to deduct arises.

...

5 [59] The test in *Kittel* is simple and should not be over-refined. It embraces not only those who know of the connection but those who “should have known”. Thus it includes those who should have known from the circumstances which surround their transactions that they were connected to fraudulent evasion. If a trader should have known that the only reasonable explanation for the transaction in which he was involved was that it was connected with fraud and if it turns out that the transaction was connected with fraudulent evasion of VAT then he should have known of that fact. He may properly be regarded as a participant for the reasons explained in *Kittel*.
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15 [60] The true principle to be derived from *Kittel* does not extend to circumstances in which a taxable person should have known that by his purchase it was more likely than not that his transaction was connected with fraudulent evasion. But a trader may be regarded as a participant where he should have known that the only reasonable explanation for the circumstances in which his purchase took place was that it was a transaction connected with such fraudulent evasion.”

Findings of Fact

20 9. The Ft-T made extensive findings of fact at [28] to [240] of the Decision. We should emphasise that these are expressed in the Decision as findings of both members of the Tribunal. We summarise those findings which are relevant to the grounds of appeal in this case at paragraphs 10 to 26 below. References to numbered paragraphs in parentheses, as [xx], are references to paragraphs in the Decision.

25 10. Ashley Trees (“Mr Trees”) was the guiding mind of CCA and its primary witness of fact in the appeal: [2]. Mr Trees started his own business manufacturing new computers from older technology subsequently also dealing in computers in the grey market: [33]. He later diversified into mobile phones and in due course this trading was conducted through a separate company, CCA, which he controlled. The involvement of CCA was primarily to assist Mr Vincent D’Rozario, (“Mr D’Rozario”) the HMRC officer responsible for the business’s VAT compliance, who was only interested in looking at records relating to mobile phone trading: [35] to [38].
30

35 11. CCA’s business was subject to close scrutiny by HMRC on a monthly basis and its input tax claims were subject to full or extended verification from time to time due to it trading, as Mr D’Rozario put it, in “MTIC goods”. CCA was effectively self-financed with Mr Trees mortgaging his house and another property to raise finance: [40] to [42].

40 12. On UK to UK deals, CCA routinely made a fixed mark up of £1 per item. Profit margins for export deals were higher and subject to negotiation. Mr Trees was content with making this amount on each unit supplied. A supplier would typically offer stock to CCA who then sought a buyer for it. It did not usually hold stock itself which remained with the freight forwarder. The supplier was not paid until the goods had been sold and payment received from the customer; purchase and sale documents for

the transactions which are the subject of this appeal all bore the same date: [43] to [46] and [72].

13. Mr D'Rozario encouraged CCA to carry out more extensive due diligence checks on suppliers from November 2004 which it duly did: [54] to [55].

5 14. Mrs Ryan, CCA's bookkeeper, supplied HMRC with 'deal packs' for each transaction consisting of the sales invoice, the sales purchase order, the purchase invoice, the purchase order and all the payment details. Mrs Ryan's work included trying to reconcile payments made by CCA with the relevant invoices. The task was difficult because payments were often not matched neatly to purchases or sales and in that case she sought to annotate allocations to the invoices accordingly. Mr D'Rozario, having done spot checks with the bank statements, considered these annotations generally to be accurate and that CCA's payments had been received or paid in full. Mr Trees made his own allocation of payments to transactions which often differed from Mrs Ryan's and that was the one he relied on when making payments: [60] to [61].

15 15. An unannounced visit by HMRC officers at CCA's premises took place on 1 June 2006. One of the contra-traders with whom CCA dealt, Future Communications, was raided simultaneously. A substantial number of CCA's records were taken, some of which have not been returned and it seemed likely that they were lost. Mr Trees has not been interviewed, prosecuted or called as a witness in the subsequent prosecution of Future Communications or any other prosecution: [65] to [70] and [197].

16. As well as the 39 transactions which are the subject of this appeal, between April and June 2006 CCA conducted 112 transactions involving sales to Future Communications, and five involving sales to Infinity Holdings, both subsequently identified by HMRC as fraudulent contra-traders, making a profit in virtually all cases of £1 per unit. Mr Trees's explanation of this pattern was that he had "dealt with Future for a long time and there was no need to negotiate with Future." The same was true of Infinity Holdings. Mr Trees could offer no explanation as to why at the same time as dealing with CCA the three suppliers he dealt with were at the same time trading with CCA's European customers: [71] to [73].

17. There was very little documentation dealing with contractual terms such as the passing of title, distribution of risk or terms of payment or detailed specifications regarding the goods supplied, although invoices from suppliers provided that title remained with the supplier until payment had been made. Mr Trees gave no thought to the question as to how this squared with CCA selling the goods and receiving payment from its customer before it paid its supplier: [75] to [83].

18. CCA had originally banked with Royal Bank of Scotland which closed CCA's accounts in 2005 when it indicated that it did not wish to provide banking facilities for companies operating in CCA's sector. Thereafter, CCA's primary bankers were First Curacao International Bank ("FCIB"). Although the F-tT's findings on the banking evidence are expressed to be those of both members of the tribunal, in view of the divergent position of the two members in their conclusions on the significance of this

evidence we are more inclined to regard the key findings set out at [102] to [116], on which the Judge appears to have based his conclusions at [397] to [399], as reflecting the findings of the Judge alone.

5 19. The F-tT made some general findings on the banking evidence at [102] to [104], as follows :

10 “102 the banking evidence consisted of extracts from FCIB material which the relevant officer, Mr Peter Birchfield, had examined in the context of another case but which incidentally showed monies flowing through CCA’s account. Mr Birchfield had traced the movements of monies through CCA’s FCIB account in relation to six transactions; three of these six, were ‘buffer’ deals and three were ‘broker’ deals i.e. exports from the United Kingdom. Evidence was also produced about the flows of money through the accounts of Future Communications and Infinity Holdings which Mr Birchfield had had occasion to examine earlier.

15 103 It was not claimed that any of these figures related to the transactions under appeal, but the purpose of their being put in evidence was to assert that transactions in which CCA had been involved at the time of the appeal were contrived and uncommercial – and that therefore it was probable that those actually under appeal were likewise contrived and uncommercial. According to this thesis, the evidence shows actual knowledge of fraud by CCA, because it was
20 accepted by the witnesses that CCA could not otherwise have been aware of the transactions above and below its own, or at least been aware that they were steps in a linked fraudulent undertaking; Mr Birchfield indeed specifically agreed that in 2005, when CCA’s account was opened, FCIB was to the public perception a “highly reputable offshore bank offering up to the minute state of the art e-banking facilities”.

25 104 In regard to the previously compiled evidence regarding the transactions of Future Communications and Infinity Holdings, the Crown’s case is that the analysis shows that, where CCA appears in it, it was paying and receiving monies in the context of money flows which were either circular, or contrived, or both. It suffices to say that, while the analyses show a
30 *prima facie* case indicating that further investigation might call in doubt the commerciality of the transactions, we have no specific evidence in regard to any of them or the circumstances in which any of them took place, and our assessment of that section of the FCIB material is that it does not get near to establishing on the balance of probabilities that CCA knew or should have known that its trading in those cases was connected to fraud. Accordingly, we focus in this
35 evidence on the six cases Mr Birchfield put forward as indicative of CCA’s trading in the period of this appeal.”

40 20. The F-tT then, at [105] to [116], looked in detail at the six transactions referred to in the last sentence of [104] by reference to the relevant invoices and the annotations made by Mrs Ryan on them and concludes in relation to each in effect that although there is “limited evidence” of circularity of funds the money movements shown by the banking evidence have not been effectively reconciled with the invoices.

21. At [133], the F-tT made the following finding regarding the pattern of CCA’s trading in respect of the 39 deals which are the subject of this appeal:

45 “133 In all 39 deals under appeal, the quantity of goods available from a single supplier always matched exactly the quantity that CCA’s customer wished to purchase. The deal

documents were almost always raised in the space of a day. There was never a need for CCA to buy from multiple sources in order to satisfy the demand, or to split a purchase from a supplier between several customers. In 24 deals, the same pattern applied throughout the known supply chain from the EU supplier to CCA's EU customer."

5 22. At [135] to [141], the F-tT found that CCA did carry out some due diligence on its trading partners, including credit checks to which it did not attach much importance as it did not grant credit, and that more was done than appeared from the evidence before it, it becoming apparent during the course of the hearing of the appeal that there was historical material that had not been adduced, a matter to which we return when
10 considering the grounds of appeal.

23. At [185] to [199], there is a discussion by the F-tT of certain matters under the heading: "The evidence of Mr Trees' knowledge". The F-tT stated that HMRC's case was that Mr Trees was a knowing partner in the enterprise to defraud HMRC in relation to VAT. The F-tT also stated that the case against CCA was based on
15 inference from the circumstances of trading patterns and money payments. The F-tT recorded that Mr Trees denied actual knowledge that a fraud was taking place. Despite the heading to these paragraphs in the Decision, they do not purport to summarise the entirety of the evidence relied upon by HMRC in support of its allegation as to Mr Trees' knowledge of the underlying fraud.

20 24. The F-tT recorded in some detail the evidence it received from two experts, Mr John Fletcher of KPMG for HMRC and Mr Nigel Attenborough of NERA Consulting for CCA, on the operation of what is known as the "grey market" in mobile phones. Before considering the expert evidence the F-tT made the following finding, at [200] :

25 "As is typical in cases such as this, CCA was what is known as a grey market trader, that is to say that it was buying and selling for the most part outside the manufacturers' authorised distribution systems, which are supported by a contractual network designed to maintain distinct sales territories and the wholesale and retail prices within them. Effectively, the grey market operates to circumvent these restrictions and to maximise the immediacy and sufficiency of supply to the markets, but because it is unregulated
30 by the main industry players the conditions in it at any one time are more difficult to establish and, by the same token, are more open to manipulation by organised crime; and the grey market is in general viewed with disfavour by original equipment manufacturers."

25. The F-tT made the following finding at [206] on the state of the grey market in
35 2006:

40 "Both experts agreed that in 2006 there was a significant, vibrant, legitimate and honest grey market in the wholesale distribution of mobile phone handsets. This market was global, including not only the U.K. but also Europe, India, Asia and Africa, though not generally north or south America; between 2002 and 2006 there had been an explosion in the demand for mobile phone handsets worldwide and for traders in the grey market there were substantial profits to be made. Mr Attenborough and Mr Fletcher identified four areas of opportunity for the grey market afforded by failures in the operation of the official distribution systems, or 'white market'. These areas are: arbitrage, box-breaking, volume shortages and volume surpluses."

26. The F-tT recorded the differing views of the experts as to the size of the legitimate grey market in 2006, the prevalence of fraud in the market, the way that intermediaries operated in the market, the opportunities for intermediaries in the four areas identified referred to at [206] of the Decision and the extent to which CCA were trading in unreasonably high volumes of phones or their trading was otherwise not authentic: [207] to [230]. The F-tT came to no conclusions at this stage on the conflicting views of the experts expressed before it.

Submissions

27. The F-tT recorded in detail the submissions of CCA at [241] to [306] and those of HMRC at [307] to [356]. We refer to these later when dealing with the specific grounds of appeal but observe at this point that the F-tT recorded in considerable detail, at [296] to [301], CCA's submissions in relation to the banking evidence to the effect that (a) the movement of money revealed certain patterns but was not circular and the flow was ongoing and (b) that there were significant factual limitations in HMRC's analysis, both as to the attempt to link the payments in and the payments out and the integrity of the money movements themselves. By way of contrast, when recording HMRC's submissions, there was only one brief reference to the banking evidence; at [319] the F-tT referred to the banking evidence as being one of the factors relied on by HMRC as showing CCA knew or should have known of the connection to fraud.

28. We also observe that although, earlier in the Decision, at [188], the F-tT recorded that the case against Mr Trees and CCA was one of dishonesty and actual knowledge of fraud (but not necessarily all of the details of the fraud), the F-tT was also aware that HMRC's alternative case was that CCA should have known that the deals were connected with the fraudulent evasion of VAT. The F-tT recorded, at [354], HMRC's submission that, taking into account all the circumstances, the only reasonable explanation was that the deals were connected with fraud before setting out the following twenty matters which HMRC submitted that a reasonably prudent businessman in the position of Mr Trees should have questioned:

- i. Why it was being presented with the opportunity to make such profits, and to trade in such volumes of goods, in a model which was apparently risk free, and relatively effortless, with little experience or history of trading in mobile phones, no contacts and minimal investment and infrastructure, in contrast to the labour intensive business of its associated company, the profits and turnover of which were very small by comparison?
- ii. Why it did not need to advertise the stock?
- iii. Why its suppliers and customers were apparently content to shoulder all the risk in terms of the timings of the payments, and the shipping of the goods: its suppliers were happy to release the goods without payment despite CCA having a poor credit rating, but customers were happy to pay for the goods up front before they had even been shipped?

- iv. Why Future Communications, in particular, was content to release the goods to CCA without payment, but was quite happy to pay up front when being supplied with the goods by CCA?
- 5 v. Why the four EU customers were content, apparently without question, to pay in sterling, thus shouldering the risk of any currency fluctuation?
- 10 vi. Why its suppliers and its customers, with some of whom it had only started to deal, were never apparently concerned about the description of important contractual terms, or commercially important information (such as whether the goods might need to be adapted for the destination market) in the deal documents?
- 15 vii. Why it was receiving such offers of stock for which it was able to find customers on so many occasions over such a period of time, and why it was not being cut out of the supply chains, despite the fact that it was adding no value to the goods?
- 20 viii. Why such volumes of goods, manufactured to meet an end retail demand, were apparently repeatedly passing through the UK, despite the fact that the ultimate demand was elsewhere?
- 25 ix. Why it was able to match the available supply with demand so precisely on so many occasions; CCA apparently never needed to buy from multiple sources to satisfy an order, or to split a purchase between several customers, and the deal documentation was always raised during the course of one day?
- 30 x. Why its supplier and customers, all relatively newly established businesses, were able legitimately to source and purchase millions of pounds worth of goods, and why there was so little financial information, or adverse information, about these entities?
- 35 xi. Why so many of the counterparties did not provide documents required by CCA's own due diligence process, and why the descriptions of the business activities of some of the counterparties in the documentation which was available was at odds with the wholesale trading of mobile phones?
- 40 xii. Why all four of its EU customers wanted the goods delivered to the same warehouse in Belgium?
- 45 xiii. Why none of the goods were ever returned, and why there were never any reports of damaged, missing, or misdescribed stock?
- xiv. Why in 115 out of 117 of the buffer deals, its customer was always willing to pay a price, and/or its supplier always charged a price which allowed it to make a mark up of precisely £1, and why there was no need to negotiate with Infinity Holdings and Future Communications with regard to the price?

- xv. Why all of its suppliers and customers were using the same offshore bank in the Dutch Antilles?
- 5 xvi. Why Infinity Holdings gave the names of both Future Communications and Soul Communications as referees, potentially promoting its competitors, and also the names of both of the freight forwarders involved in all the broker deals, A1 Distribution and Aquarius?
- 10 xvii. Why Soul Communications was trading from premises apparently next door to Future Communications?
- xviii. Why both Infinity Holdings, based in Leicester, and Soul Communications, based in London, were using the same freight forwarder, Aquarius?
- 15 xix. Why on every occasion when the appellant was able to find a buyer in the EU (39 deals) its supplier was Infinity Holdings, Future Communications or Soul Communications, and why on every occasion when it sold goods in the UK (117 deals), its customer was Infinity Holdings or Future Communications but its supplier was one of eight other traders? (In April 2006 for example its supplier in all 14 of the broker deals was Infinity Holdings; however, in all 70 of the buffer deals, Infinity Holdings did not supply the goods once, and they were all sold to Future Communications.)
- 20
- 25 xx. Why it had been raided by officers on 1 June, and whether CCA's suppliers and customers had also been raided, or whether they knew anything about it?

Conclusions

30 29. We deal in detail later with the F-tT's conclusions when considering the specific grounds of appeal. We can summarise those that are relevant to this appeal as follows.

30. The conclusions common to both members of the tribunal were :

35 (1) Although the F-tT was critical of the fact that certain evidence regarding due diligence and details of payments made was not produced (to which we refer at paragraph 22 above) it declined to draw an adverse inference from that fact, finding that there was nothing beyond speculation to suggest that the failure has been "a deliberate ploy" to conceal matters which would harm its case: [363] to [369]; and

40 (2) The F-tT derived little assistance from the expert evidence on how the legitimate trade in the grey market operated and although it found that many of the practices and patterns of trade required explanation it concluded that it could not regard any of these features as inevitably pointing to uncommercial trading or as clear indicators of bad faith, the

only first hand evidence of the way this market worked being that of Mr Trees: [376] to [382].

31. At [387], the F-tT stated:

5 “For the reasons already given, we have not found this an easy case to determine and it would be fair to describe it as a borderline case, some evidence pointing in one direction and other evidence in another. In spite of careful efforts to reach a common view, the members of the tribunal remain divided on the issues outlined in the following paragraphs. In the event, the judge has exercised his casting vote in favour of the appellant
10 pursuant to article 8 of the First-tier Tribunal and Upper Tribunal (Composition of Tribunal) Order 2008. Paragraphs 388 to 411 which follow record the views of the tribunal judge, while those at paragraphs 412 to 421 are those of the second Member.”

32. The conclusions of the Judge were:

15 (1) Mr Trees was a “tense but truthful witness.” He did not speculate about possible trading patterns but “just got on with buying and selling when the opportunity was there” and was “a businessman who was essentially pragmatic” who never queried a situation “because, whatever its explanation, it offered an opportunity for him”: [388] to [390];

20 (2) It was “inherently improbable” where CCA was being closely and constantly monitored by HMRC and had instructed external advisers to carry out checks on its trading partners that Mr Trees was at the same time consciously collaborating in an organised fraud: [391];

25 (3) “Nor can it be irrelevant” that the criminal investigation, referred to at paragraph 15 above, paid no attention to Mr Trees: [392];

(4) Therefore it had not been established on the balance of probabilities that CCA was a knowing participant in a fraud on HMRC: [393];

30 (5) The twenty matters set out at paragraph 28 above might on Mr Attenborough’s evidence be consistent with the peculiarities of a specialised wholesale market, especially during the boom years of the economy: [394];

(6) Therefore there was no adequate basis on which to support the conclusion that a *bona fide* trader, taking reasonable precautions and being of normal prudence, should have realised that his transactions *were* connected to fraud: [395]; and

35 (7) HMRC’s banking analysis was inconclusive, capable of more than one explanation and established, in so far as CCA’s involvement is concerned, no more than a *prima facie* case requiring further investigation. HMRC accepted that it was possible for an innocent trader to be caught up in a very large scheme and the banking evidence did not demonstrate that CCA was not free to choose
40 their trading partners, who first made contact with CCA and not the other way round: [397] to [399].

33. The conclusions of the Member were:

5 (1) The charts produced by HMRC as to the money flows clearly demonstrated that there was a fraudulent scheme going on. The order, timing, how the money split and re-amalgamated must have been more than mere coincidence. The flow would not have been possible if CCA did not play its part in it: [413] to [415];

10 (2) It did not appear credible that the trusting relationship described by Mr. Trees was only one way in that when the traders were in the status of a supplier they trusted CCA but when their status changed to customers of CCA – CCA did not trust them and must receive payment before goods were released: [417];

15 (3) It was far-fetched (simply not credible) that at no point was there a single human error – stock was never short or wrong item sent or received, there were no damaged items or misdescribed items – everything went to plan and smoothly each and every time. This could not be the case in the real business world: [418];

(4) The business process had no business risk whatsoever and was too good to be true: [419];

20 (5) One could infer from the insurance situation that Mr Trees knew that there was no business risk and the insurance cover was only to legitimise CCA’s non-commercial activities: [420]; and

25 (6) CCA was a willing participant in a fraudulent scheme and could not have been a free agent in the selection of its customers and suppliers: [421].

The grounds of Appeal

34. In its application to the F-tT for permission to appeal, HMRC put forward eight grounds of appeal. The F-tT gave permission to appeal on Grounds 3 and 5 and refused permission on the remaining grounds. The application for permission to appeal on the remaining grounds was renewed before the Upper Tribunal. That application was refused by the Upper Tribunal on the papers but was reconsidered at an oral hearing following which permission was granted on Grounds 2 and 8 but refused again on grounds 1, 4, 6 and 7. Thus it is only Grounds 2, 3, 5 and 8 which fall to be considered on this appeal.

35. In order to establish what is involved in Grounds 2, 3, 5 and 8, we need to refer to some of the documents which led to permission being granted in relation to these grounds. HMRC first served an application to the F-tT for permission to appeal to the Upper Tribunal. That referred to eight matters under the heading: “the grounds of appeal”. HMRC’s case in relation to each matter was described under a separate heading as “Ground 1”, “Ground 2” etc. In this decision, we will refer only to Grounds 2, 3, 5 and 8.

36. Ground 2 was headed: “the adverse inference”. There were several paragraphs and sub-paragraphs under this heading. The first paragraph, paragraph 11, refers to one error of law but then in three sub-paragraphs of paragraph 11, it was stated that the F-tT had “further erred”. This was followed by paragraphs 12 and 13, still under the heading Ground 2, which appeared to be more in the nature of submissions rather than an identification of an error of law or a ground of appeal. There was a similar pattern in respect of Grounds 3, 5 and 8.

37. The difficulty with grounds of appeal presented in this way arises when one seeks to define the ground of appeal. When doing so, it is necessary to investigate whether each paragraph or sub-paragraph, presented under a heading which refers to a ground of appeal, is intended to refer to a separate ground of appeal or whether it is only intended to be a submission supporting a ground of appeal identified somewhere else. When the F-tT, and later, the Upper Tribunal gave permission to appeal in this case, those tribunals did so by referring to “Ground 2” or “Ground 3” etc. However, we consider that the material presented under such a heading contained more than one separate ground and it is far from clear that either the F-tT or the Upper Tribunal considered the full extent of the matters raised under each heading.

38. There is a further difficulty when, somewhere within the material presented under the heading for one ground of appeal, there is a contention which is identical to, or similar to, a contention which appears under another ground of appeal and the relevant tribunal granted permission in relation to one ground of appeal but refused permission in relation to another ground of appeal. In the present case, there is material deployed under Grounds 1, 4, 6 and 7 (in relation to which permission to appeal was refused) which overlaps with material deployed under Grounds 2, 3, 5 and 8 (in relation to which permission to appeal was granted). We consider that it is quite possible in this case that the grant of permission to appeal in relation to Grounds 2, 3, 5 and 8 as drafted by HMRC has produced the result that HMRC has been allowed to argue points on appeal which the relevant tribunal probably thought it was preventing, by refusing permission in relation to Grounds 1, 4, 6 and 7. In the event, CCA did not rely on a point of this kind in order to argue that HMRC was not entitled to rely on any material presented under Grounds 2, 3, 5 and 8 but the point could arise in a future case.

39. When the F-tT granted HMRC permission to appeal on Grounds 3 and 5 and refused permission to appeal on the six other grounds, it gave a written decision setting out its reasons. In that decision it commented on grounds 3 and 5 in a way which we will refer to again when we consider those grounds.

40. Having obtained permission to appeal from the F-tT in relation to Grounds 3 and 5, HMRC served a document which amounted to a notice of appeal in relation to Grounds 3 and 5 and also an application to the Upper Tribunal for permission to appeal in relation to the other six grounds. In the notice of appeal in relation to Ground 3, HMRC contended that the error of the F-tT was “further demonstrated” by something which the F-tT had stated when it granted permission to appeal on Ground 3. Further, under Ground 5, the notice of appeal again referred to a statement made by the F-tT when it granted permission to appeal in relation to Ground 5. CCA did not

5 argue that this additional material in relation to Grounds 3 and 5 could not be relied upon by HMRC. The application to the Upper Tribunal for permission in relation to Grounds 2 and 8 repeated the matters put forward in the application to the F-tT for permission in relation to Grounds 2 and 8 and the Upper Tribunal gave permission in relation to Grounds 2 and 8.

10 41. We will now attempt to summarise the grounds of appeal which we consider HMRC has been permitted to argue. For this purpose, we will take Grounds 3 and 5 from HMRC's notice of appeal to the Upper Tribunal and Grounds 2 and 8 from the application to the Upper Tribunal for permission to appeal. We were, of course, provided by both parties with lengthy skeleton arguments for the hearing of this appeal. It may be that the way in which the alleged errors in the decision of the F-tT and/or the alleged grounds of appeal are described in HMRC's skeleton, and answered in CCA's skeleton, differs from what appears from the notice of appeal and the application for permission. Nonetheless, we consider that the definition of the permitted grounds of appeal must be derived from these documents and not from the skeleton arguments. However, if there is uncertainty as to the grounds put forward in the notice of appeal and the application for permission and those grounds have been interpreted by HMRC in a particular way, without objection from CCA, we will take that into account.

20 42. The grounds on which permission has been granted are, in summary, as follows:

Ground 2

25 (1) The F-tT applied the wrong test in deciding not to draw an adverse inference from CCA's failure to adduce evidence in respect of the matters referred to at paragraphs 22 and 30 above in that it asked itself if the failure was "a deliberate ploy to conceal matters".

(2) It also erred in taking account of the fact that the burden of proof was upon HMRC.

30 (3) It also took into account irrelevant factors in deciding the issue and it failed to address HMRC's arguments that CCA's evidence on the issue was not credible.

Ground 3

The F-tT erred in law in taking into account an irrelevant consideration relating to connected criminal proceedings against one of CCA's suppliers, Future Communications.

35 *Ground 5*

The Ft-T misapplied the test in *Kittel* in that:

(1) It considered a more onerous test than that prescribed by law;

(2) It applied the burden and standard of proof to individual pieces of evidence as opposed to considering the totality of the evidence;

- (3) It adopted an overly sceptical approach to circumstantial evidence;
- (4) It paid insufficient regard to the “should have known” limb of the test;
- (5) It misinterpreted the case advanced by HMRC as being a case of dishonesty and, in particular, it was wrongly influenced by the opinion of the officers of HMRC as to the nature of the fraud; and
- (6) It considered it relevant that the criminal investigation had paid no attention to Mr Trees.

Ground 8

The Judge erred in law in his approach to the banking evidence in that:

- (1) His conclusions were inconsistent with the evidence to the extent that they were not conclusions which a reasonable tribunal could have reached;
- (2) He wrongly disregarded relevant evidence;
- (3) He failed to take into account the detailed submissions made on behalf of HMRC;
- (4) His conclusions were based on errors of fact; and
- (5) He took account of irrelevant matters;
- (6) He failed to give an adequate explanation or reasons for dismissing the banking evidence.

Grounds of appeal: further comments

43. Having regard to what happened in this case as regards the drafting of the grounds of appeal and the applications for permission to appeal, we consider that it would be helpful if we made some further comments which might be useful in other cases. We begin by referring to the relevant tribunal rules.

44. Both the Tribunal Procedure (First-Tier Tribunal)(Tax Chamber) Rules 2009 (“the 2009 Rules”) and the Tribunal Procedure (Upper Tribunal) Rules 2008 (“the 2008 Rules”) contain provisions which are relevant in this context. Rule 39 of the 2009 Rules deals with applications to the F-tT for permission to appeal to the Upper Tribunal against a decision of the F-tT. Rule 39(5) (b) of the 2009 Rules provides that such an application must identify the alleged error or errors in the decision. Rule 40(5) of the 2009 Rules provides that the F-tT may give permission on part only of the decision or on limited grounds. Rule 23 of the 2008 Rules provides for an appellant to serve a notice of appeal where the F-tT has given permission to appeal to the Upper Tribunal. Rule 23(2) (b) of the 2008 Rules, cross-referring to rule 21(4) (e) of the 2008 Rules, requires the notice of appeal to state the grounds on which the appellant relies. Where the F-tT has not given permission to appeal to the Upper Tribunal and the appellant applies to the Upper Tribunal for permission to appeal, then under Rule 21(4) (e) of the 2008 Rules, the application for permission to appeal must state the grounds on which the appellant relies. Where the Upper Tribunal grants permission on an application to it, it is not then necessary for there to be a notice of appeal to the Upper Tribunal.

45. The effect of these rules is therefore as follows:

(1) in a case where the F-tT has given permission to appeal to the Upper Tribunal, the Upper Tribunal should have available to it the application to the F-tT, setting out the alleged error or errors in the decision of the F-tT, and a notice of appeal to the Upper Tribunal setting out the relevant grounds of appeal;

(2) in a case where the Upper Tribunal has given permission to appeal, the Upper Tribunal should have an application for permission to appeal setting out the relevant grounds of appeal.

46. In the light of the difficulties we have encountered in the present case, we would invite the President of the Tax and Chancery Chamber to consider whether it would be beneficial to make a Practice Statement emphasising certain matters. We make the following suggestions as to the guidance which might usefully be given in such a Practice Statement:

(1) an appellant should comply with the rules as regards the identification of alleged errors in the decision the subject of the intended appeal and as regards the expression of a ground of appeal;

(2) the alleged error of law should be succinctly and clearly identified;

(3) the ground of appeal should be succinctly and clearly expressed;

(4) if an appellant wishes to appeal on the ground that the decision is inadequately reasoned, that ground of appeal should be clearly stated in the application for permission to appeal so that the F-tT can consider whether it is appropriate to review the decision and to give further reasons;

(5) submissions in support of the ground of appeal should be clearly distinct from the ground of appeal itself;

(6) when a tribunal gives permission to appeal, it should ensure that the ground of appeal on which permission is granted is succinctly and clearly expressed; this is particularly important where the relevant tribunal grants permission on some grounds of appeal and refuses it on other grounds of appeal.

Appeal on point of law only

47. The only appeal which can be brought in this case is an appeal on a point of law arising from the decision of the F-tT: see Tribunals, Courts and Enforcement Act 2007, section 11(1). There cannot be an appeal on a pure question of fact which is decided by the F-tT. However, a tribunal may arrive at a finding of fact in a way which discloses an error of law. So much is clear from *Edwards v Bairstow* [1956] AC 14 in which Lord Simonds referred to making a finding, without any evidence or upon a view of the facts which could not be supported, as involving an error of law: see at page 29. In the same case, Lord Radcliffe, at page 36, regarded cases where there was no evidence to support a finding or where the evidence contradicted the

finding or where the only reasonable conclusion contradicted the finding, as cases involving errors of law.

48. In relation to an appeal which is said to involve a point of law of the kind identified in *Edwards v Bairstow*, we were reminded of what was said by Evans LJ in *Georgiou v Customs and Excise Commissioners* [1996] STC 463 at 476, as follows:

10 “It is right, in my judgment, to strike two cautionary notes at this stage. There is a well-recognised need for caution in permitting challenges to findings of fact on the ground that they raise this kind of question of law. That is well seen in arbitration cases and in many others. It is all too easy for a so-called question of law to become no more than a disguised attack on findings of fact which must be accepted by the courts. As this case demonstrates, it is all too easy for the appeals procedure to the High Court to be misused in this way. Secondly, the nature of the factual inquiry which an appellate court can and does undertake in a proper case is essentially different from the decision-making process which is undertaken by the tribunal of fact. The question is not, has the party upon whom rests the burden of proof established on the balance of probabilities the facts upon which he relies, but, was there evidence before the tribunal which was sufficient to support the finding which it made? In other words, was the finding one which the tribunal was entitled to make? Clearly, if there was no evidence, or the evidence was to the contrary effect, the tribunal was not so entitled.”

20 49. The F-tT was obliged to give reasons for its Decision by virtue of rule 35 of the 2009 Rules. The F-tT did not purport to provide a summary only of its findings of fact and its reasons within rule 35(3) (a) so this case came within rule 35(3) (b) requiring reasons for the Decision. The common law test as to the adequacy of reasons for a judicial decision, as expounded in *Flannery v Halifax Estate Agencies Ltd* [2000] 1 WLR 377 and *English v Emery Reimbold & Strick Ltd* [2002] 1 WLR 2409, applies to the requirement to give reasons under rule 35 also. Reasons which do not satisfy this standard of adequacy involve an error of law which can be the subject of an appeal under section 11 of the Tribunals, Courts & Enforcement Act 2007. Later in this decision, we will consider in more detail the relevant test as to the adequacy of reasons for a judicial decision.

Ground 2

50. We have earlier summarised Ground 2 as:

35 “(1) The F-tT applied the wrong test in deciding not to draw an adverse inference from CCA’s failure to adduce evidence in respect of the matters referred to at paragraphs 22 and 30 above in that it asked itself if the failure was “a deliberate ploy to conceal matters”.

(2) It also erred in taking account of the fact that the burden of proof was upon HMRC.

(3) It also took into account irrelevant factors in deciding the issue and it failed to address HMRC’s arguments that CCA’s evidence on the issue was not credible.”

40 51. The evidence which existed but which was not produced was said to be relevant to the extent of the due diligence carried out by CCA in relation to its trading partners. Evidence as to due diligence was said to be relevant to the question as to whether Mr

Trees knew, or should have known, that the CCA transactions were connected with fraud. At an early point in its Decision, the F-tT had reminded itself of what was said by Moses LJ in *Mobilx* at [75], as follows:

5 “[75] The ultimate question is not whether the trader exercised due diligence but rather whether he should have known that the only reasonable explanation for the circumstances in which his transaction took place was that it was connected to fraudulent evasion of VAT.”

10 52. Nonetheless, the exercise of due diligence or the lack of due diligence can potentially be relevant. If the trader has not carried out due diligence in relation to a transaction, that might assist HMRC in showing that the trader knew or should have known that the transaction was connected with fraud. Conversely, if due diligence has been exercised by the trader, that fact might not be conclusive as to whether the trader did not know or should not have known that a transaction was connected with fraud;

15 the due diligence might have been done as window dressing and there might be other evidence which established that the trader knew or should have known that the transaction was connected with fraud.

20 53. In any event, in this case, there was extensive evidence and cross-examination as to the extent of the due diligence carried out by CCA. CCA called Mr Trees to deal with that subject. The F-tT held that Mr Trees was the guiding mind in control of CCA; see at [2].

25 54. In the course of the evidence, HMRC investigated with Mr Trees why CCA was not calling a Mrs Ryan and a Mr Gordon to give evidence. HMRC also examined the position in relation to a database said to exist on a computer owned by CCA, which database was not produced. Similarly, HMRC examined the position in relation to documents which Mr Trees said were in the custody of Ashton Law, solicitors who had formerly acted for CCA.

30 55. There are copious references to Mrs Ryan in the Decision. The F-tT found that she was a bookkeeper employed by CCA and that she had had a good working relationship with the officers of HMRC when they carried out inspections of CCA’s records. Mrs Ryan had provided the officers with “deal packs” in relation to certain transactions. She sought to reconcile payments made by CCA with relevant invoices. The evidence was that Mr Trees’ allocation of payments to transactions differed from those of Mrs Ryan but details of his allocation were on his computer which was not in

35 evidence. At one point in his evidence, at [81], when pressed as to why he did not find a particular matter surprising, Mr Trees relied on the fact that Mrs Ryan had not said anything to him about it. Mrs Ryan was not involved in giving instructions to the bank, FCIB. The F-tT recorded CCA’s submissions as to why Mrs Ryan had not been called which submission included the contention that it was unlikely that she would

40 have been able to add anything to that which was revealed by the documents.

56. The F-tT referred to Mr Gordon in a number of places in the Decision. Mr Gordon was the company secretary of CCA and an officer of HMRC spoke to him at an early

stage during the checks being carried out by officers of HMRC. When Mr Trees gave evidence describing the due diligence which was carried out, he said that Mr Gordon took over the due diligence work in 2006. The F-tT recorded CCA's submissions as to why Mr Gordon had not been called which submission included the contention that it was unlikely that he would have been able to add anything to that which was revealed by the documents.

57. The F-tT referred to Mr Trees' computer which had not been produced and the database or spreadsheet which was said to be stored on that computer. The F-tT made findings as to the general nature of the information which Mr Trees said was stored in the database; the F-tT held that there was a significant amount of information stored in this way. The F-tT recorded HMRC's submissions that Mr Trees' evidence on this subject was unsatisfactory.

58. Mr Trees gave evidence that CCA had instructed solicitors, Ashton Law, in relation to this dispute with HMRC. Ashton Law had later entered a process of insolvency and they ceased to act for CCA. Before that happened, CCA had provided documents to Ashton Law and those documents had not been returned to CCA. It was possible that those documents included documents which were relevant as to the extent of CCA's due diligence. Mr Trees had not mentioned this matter in his witness statement but volunteered this information when cross-examined. The F-tT recorded CCA's submissions based on Mr Trees' evidence as to Ashton Law. The F-tT recorded HMRC's submissions that Mr Trees' evidence on this subject was unsatisfactory.

59. Mr Trees also gave evidence, which was apparently accepted by the F-tT, about documents which were removed by HMRC during the raid on CCA's premises on 1 June 2006. The evidence was that HMRC was invited to, and did, take away substantial quantities of documents. Those documents included documents relevant to the question of the extent of the due diligence carried out by CCA. It was said that HMRC had then lost some of those documents. HMRC had kept the originals of the documents which they took away but did not lose. HMRC did not return those originals to CCA at any time but did provide copies.

60. At [135] – [175] the F-tT made detailed findings, based on the documents available to it, as to the extent of the due diligence carried out by CCA.

61. It appears from what was said in the written closing submissions for CCA that the F-tT invited submissions from the parties as to the correct approach in law in relation to a party's failure to adduce relevant evidence which was available to that party. HMRC's written closing submissions contained a section dealing with "missing documents". In this section, HMRC referred to Mr Trees' computer and the documents allegedly with Ashton Law. It submitted that the F-tT should draw an adverse inference as to the credibility of Mr Trees and should also reject the suggestion that significant documentation was missing. CCA's closing submissions drew attention to the decisions of the Court of Appeal in *Wisniewski v Central Manchester Health Authority* [1998] PIQR 324 and *Jaffray v Society of Lloyd's*

[2002] EWCA Civ 1101 and the F-tT referred to those two cases at an early point in its Decision.

62. At [363] – [369], the F-tT approached the matter as follows:

“Missing evidence

5 363 It is clear that some material of relevance was not before the tribunal – in particular, evidence regarding CCA's historical due diligence and evidence concerning the details of payments made, and how they and the receipts were allocated to individual deals. The sources from which this material would have come were putatively: Mrs Pat Ryan, Mr Wesley Gordon, Ashton Law and Mr Ashley Trees's
10 computer. The two witnesses were not called and had not refused to give evidence; no production order for the papers apparently with Ashton Law had been sought; Mr Trees had not interrogated his computer for the relevant data.

15 364 It was submitted by Mr Pickup QC that the proper course would be for the tribunal to draw an adverse inference from the absence of this material only if it is satisfied that there has been a deliberate attempt to conceal relevant and damaging evidence from it. Mr Kerr submitted that the explanations for the failure to provide this evidence were opportunistic and lacking credibility, and he invited the tribunal to draw an adverse
20 inference.

25 365 Whether the evidence would be damaging or advantageous to CCA, we cannot of course determine without having seen it, but it is plain that all of it could have been provided if CCA had wished. Mrs Ryan is said to be elderly, but beyond this general assertion there is no evidence of her ill-health and it is very unlikely that she would not have been able to corroborate or otherwise, at least in general terms, the important
30 evidence given by Mr Trees about the different approach she and he adopted to recording payments and receipts. In regard to the papers held by Ashton Law and the material on Mr Trees's computer, we can see no reason for them not having been produced, with the aid of a production order if necessary, especially bearing in mind the ample time there has been for preparation. Mr Gordon could have been summoned and the contents of Mr Trees's computer could have been put in evidence.

35 366 All this evidence would, it is said, have assisted the appellant, and the tribunal would not have been asked to rely on Mr Trees's possibly self-serving assertions alone. That said, it must be remembered in this context that the burden of proof lies on HMRC to justify the withholding of what is *prima facie* the taxpayer's entitlement, and that the department is armed with wide powers of search and inspection of documents which were exercised, but it seems only by the criminal investigators. The material in
40 question could have been obtained by HMRC, or the lack of it demonstrated, in the lengthy civil review of the case; it is probable, moreover, that the criminal investigators' handling of the records seized on 1 June 2006 has contributed to the situation.

45 367 Although we are critical of CCA's failure to produce, or seek to have produced, the evidence we are discussing there is nothing beyond speculation to suggest that the failure has been a deliberate ploy to conceal matters which would harm its case; indeed if it were to be shown that relevant material had deliberately been held back the conduct involved would be very serious, and might indeed also reflect on the appellant's professional representatives. In the event, we do not have the evidence on

which to reach such a conclusion, and we do not therefore draw an adverse inference from the absence of the material in question.

5 368 We have before commented upon the objection taken by Mr Kerr [counsel for HMRC] that Mr Trees's claims to have shown or given Mr D'Rozario evidence of the due diligence he had undertaken, and which was now not available, were not put to Mr D'Rozario as a witness. It is said therefore that no finding adverse to HMRC should be made with regard to its evidence about due diligence documentation or IMEI numbers.

10 369 While there is clearly force in these procedural objections in principle, it is evident that little practical difference would have resulted from the exercise of explicitly putting matters to the witness, since it was made quite clear by Mr D'Rozario that as far as he was concerned all the relevant detail was recorded in his meticulously kept logs and that there was nothing else relevant. The precise extent of the due diligence is in
15 any event not one on which, having regard to authority, the appeal turns or which has in fact been determinative in reaching our decision.”

63. In support of this ground of appeal, HMRC argued:

20 (1) the F-tT applied a test which posed the question whether CCA's failure to adduce the evidence in question was a deliberate ploy to conceal matters;

25 (2) this test was contrary to the two authorities cited to the F-tT by CCA, namely, *Wisniewski v Central Manchester Health Authority* [1998] PIQR 324 and *Jaffray v Society of Lloyd's* [2002] EWCA Civ 1101; in addition, HMRC cited *Commissioners for Her Majesty's Revenue and Customs v Sunico A/S* [2013] EWHC 941 (Ch);

(3) the F-tT held that there was no reason for CCA's failure to adduce the evidence;

30 (4) it was wrong to take into account the fact that the burden of proof lay on HMRC;

(5) it was wrong to take account of irrelevant matters, such as, the statement that the criminal investigation had contributed to the situation and the statement that the material could have been obtained by HMRC or the lack of it demonstrated by HMRC;

35 (6) the F-tT did not address HMRC's argument that Mr Trees' evidence about the missing material was not credible.

64. CCA's submissions included the following:

(1) had the missing material been provided, it could only have assisted CCA;

40 (2) the F-tT gave reasons why it considered it was not appropriate to draw an adverse inference;

(3) HMRC could have sought production of the missing documents;

(4) the criminal investigation had caused the loss of some documents;

(5) the F-tT's finding that there had not been a deliberate attempt to conceal documents was open to it on the evidence and the F-tT did not direct itself that it was a legal test but rather its finding on the facts;

5 (6) in so far as the F-tT had a discretion in this respect, there were no grounds for an appellate tribunal to interfere with its exercise of its discretion.

65. We do not need to discuss in any detail the legal principles which apply when it is suggested that an adverse inference should be drawn where a party fails to call a relevant witness. However, since the parties and the F-tT referred to the leading case in this area, *Wisniewski v Central Manchester Health Authority* [1998] PIQR 324, we will set out the well known summary of principle by Brooke LJ in that case at page 340 where he said:

15 "From this line of authority I derive the following principles in the context of the present case:

(1) In certain circumstances a court may be entitled to draw adverse inferences from the absence or silence of a witness who might be expected to have material evidence to give on an issue in an action.

20 (2) If a court is willing to draw such inferences, they may go to strengthen the evidence adduced on that issue by the other party or to weaken the evidence, if any, adduced by the party who might reasonably have been expected to call the witness.

(3) There must, however, have been some evidence, however weak, adduced by the former on the matter in question before the court is entitled to draw the desired inference: in other words, there must be a case to answer on that issue.

25 (4) If the reason for the witness's absence or silence satisfies the court, then no such adverse inference may be drawn. If, on the other hand, there is some credible explanation given, even if it is not wholly satisfactory, the potentially detrimental effect of his/her absence or silence may be reduced or nullified."

30 66. This summary does identify some essential requirements before a court or tribunal may draw an adverse inference. Thus: (1) the party seeking the benefit of the inference must have adduced some evidence which shows there is a case for the other party to answer; (2) there must be a reason to expect that material evidence exists; (3) it is open to the party who resists the adverse inference to give a credible explanation, even a not wholly satisfactory explanation, as to why the evidence was not given. Apart from these basic requirements, there is much in the above summary of principle which is left open ended. We refer to the references to the court (or tribunal) being entitled to draw inferences "in some circumstances" and the court's power to be influenced by an explanation which is not wholly satisfactory. These indicate that 35 there is much about this approach which is not rigid and prescriptive. This reflects the circumstance that it is ultimately for the fact finding tribunal to make what it regards as appropriate findings of fact having regard to all the circumstances of the case including the fact, if this is established, that a party has not called an available witness and has not given a satisfactory explanation for not calling the witness.

67. We also agree with the general comment of Proudman J in *Commissioners for Her Majesty's Revenue and Customs v Sunico A/S* [2013] EWHC 941 (Ch) at [98] that where a court or tribunal is asked to draw an adverse inference, the suggested inference ought to relate to a specific matter.

5 68. Applying these principles to the present case, we would distinguish between witnesses who were not called and documents which were not produced. As to the absent witnesses, Mrs Ryan and Mr Gordon might have had material evidence to give. CCA, through Mr Trees' evidence and submissions of counsel did put forward reasons why Mrs Ryan and Mr Gordon were not called. The F-tT did not find these
10 explanations wholly satisfactory but it did make the finding that CCA had not deliberately held back material which would harm its case. That meant that the F-tT regarded this case as within the last principle stated in *Wisniewski* where it was for the F-tT to decide on the extent to which the potentially detrimental effect of not calling Mrs Ryan and Mr Gordon was reduced or nullified.

15 69. As to the missing documents, we doubt if an analysis based on the *Wisniewski* principles is particularly helpful. CCA, through Mr Trees, was contending that there were documents which had not been disclosed by it which would help its case. It was for the F-tT to decide whether to accept that evidence or whether to hold that because CCA had not produced the documents, it could not advance its case by asserting that
20 the unproduced documents were helpful to it. As we read the Decision, the F-tT was not prepared to find that the absent documents, which CCA could have produced, contained material which was helpful to CCA. Conversely, the F-tT seems to have been ready to hold in CCA's favour that there were other documents which did exist at one time but which no longer existed which would have revealed more due
25 diligence. We consider that those findings were open to it.

70. Turning to the specific points made by the F-tT which are criticised by HMRC on this appeal:

30 (1) the finding that there had not been a deliberate ploy to conceal matters was a finding which was open to the F-tT; the F-tT was not thereby stating a pre-condition to this effect had to be satisfied before it was open to it to draw an adverse inference;

(2) the F-tT did not depart from the principles in the cases which were cited to it;

35 (3) the reference to the burden of proof being on HMRC did not mean that the F-tT held that it was not possible to draw an inference adverse to CCA and favourable to HMRC; the F-tT did not make such an elementary error; the reference to the burden of proof appears to have been in the context of pointing out that HMRC had powers to obtain the missing documents;

40 (4) it was relevant to point out that HMRC had the power to obtain the missing documents, so far as they still existed, if it had wished to pursue the matter;

(5) the F-tT was right to find that some documents had gone missing as a result of the criminal investigation.

71. We also comment more generally that HMRC's submissions to the F-tT did not ask it to draw a specific adverse inference. This case was not like *Wisniewski* and the cases considered in that authority where there was a specific matter in dispute, where the first party had adduced some weak evidence in relation to that specific matter, and where the second party had a case to answer and the right inference for a fact finding tribunal to draw was that the second party was not calling an obviously relevant witness because of the fear that the witness would be unhelpful to the second party on the disputed matter. What HMRC submitted to the F-tT was that it should not believe Mr Trees' evidence that there were more documents which had not been disclosed and which helped CCA's case. We consider that the reference to the principles in *Wisniewski* only served to complicate the matter. The F-tT should have been left to decide what to make of Mr Trees' evidence. In the end that is what the F-tT did. Any lack of clarity in their reasoning, caused by reference to unnecessarily complicated reasoning, does not in the end detract from that.

72. We consider that the F-tT did not commit any error of law in these respects and we do not uphold any of the ways in which HMRC advanced Ground 2.

73. Quite apart from all of the above, we draw attention to the last sentence of [369] in the Decision. The whole debate for the purposes of Ground 2 was as to the way the F-tT went about its fact finding in relation to due diligence. In the last sentence of [369], the F-tT states that the precise extent of due diligence was not determinative. Thus, even if it had at some earlier point misdirected itself in relation to due diligence, it would not have affected the result and it would not be appropriate to remit the matter on the basis of such a misdirection.

Ground 3

74. We have earlier summarised Ground 3 as follows:

“The F-tT erred in law in taking into account an irrelevant consideration relating to connected criminal proceedings against one of CCA's suppliers, Future Communications.”

75. This ground of appeal refers to a statement made by the Judge in [392] of the Decision, which we will set out below. Before setting out the full statement of which criticism is made, we will refer to some earlier findings of the F-tT on which the statement was based.

76. At [65] - [68] the F-tT referred to a raid which HMRC carried out at CCA's premises on 1 June 2006. The F-tT described what happened and then at [69] stated:

“69 For CCA, there was no outcome to this event, carried out by what was referred to by the Crown witnesses as ‘law enforcement’ — which we understand to be the division of HMRC responsible for criminal investigations and prosecutions. Mr Trees was not asked to give any statement, he was not interviewed under caution or otherwise, he was not prosecuted or called as a witness in any prosecution, and there

was no subsequent communication with the officers responsible for CCA's VAT compliance; his documentation was simply removed for up to four years without explanation, and it seems likely that some of it has been lost. We now know that the raid was contemporaneous with one on Future Communications, three of whose officers were subsequently prosecuted, and we refer elsewhere to the outcome of those prosecutions, but Mr Trees was not at the time told that this was the context.”

77. Later at [197] the F-tT referred again to Future Communications and said:

“It is also noteworthy that, as we have seen, Future Communications was raided in a criminal investigation as long ago as June 2006, its main personnel subsequently prosecuted and convictions secured, yet no evidence from that source incriminating Mr Trees or CCA was presented.”

78. The passage in the Decision which is now criticised is the first sentence in [392] which is a paragraph in a section of the Decision, comprising [388] – [395], under the heading: “*Mr Trees’s knowledge*”. In that section of the Decision, the Judge discussed a number of matters which he considered were relevant to the question whether Mr Trees knew at the relevant time that the transactions which CCA were carrying out were connected with fraud. In that context, the Judge said:

“392 **Nor can it be irrelevant that the criminal investigation begun on 1 June 2006, leading as it did to trials and convictions of one of CCA's main trading partners, paid no attention to Mr Trees, to the point of not even taking a formal witness statement from him.** The conspiracy encircling CCA's trading was, as Mr Birchfield put it, a very large scheme in which it was possible for an innocent party to be caught up. It is quite credible that traders who had built up the trust of CCA over several years by offering them advantageous trading terms, should have seen the company as a useful cog in their machinery – and one which, if things went wrong, would be exposed to risk on its own account alone while leaving the conspirators holding the profits of the fraud.”

79. We were also referred, without objection from CCA, to a statement made by the Judge when, on 15 July 2013, he gave HMRC permission to appeal on this ground. He then said:

“The relevance of the criminal investigation and subsequent proceedings is seen by the tribunal as being that if, as was the commissioners’ primary submission, Mr Trees had actual knowledge that he was collaborating in a fraud on the Revenue it would be probable that in the investigation he would at least be examined as a possible co-conspirator with those with whom he traded and who were themselves later charged and convicted. Nonetheless, it is of general importance to establish whether the tribunal erred in law at paragraph 392 of its decision and took into account an irrelevant consideration, or whether it was entitled to have regard to related criminal investigations and proceedings in the context of the case.”

80. It is clear that when the Judge came to his overall conclusion in relation to the question whether Mr Trees knew that the CCA transactions were connected with fraud, he took into account the matters referred to in the first sentence of [392] as a relevant consideration. The contrary was not argued before us. HMRC submits that

those matters were irrelevant to the question of Mr Trees' knowledge. CCA submits that these matters were relevant and the Judge was entitled to take them into account and give them the weight which he thought fit.

5 81. We agree with HMRC on this point. The matters referred to in the first sentence of [392] were irrelevant to the question whether Mr Trees knew that the CCA transactions were connected with fraud. What the Judge seemed to be saying was: (1) the persons responsible for the criminal investigation must have thought that CCA was not involved in the fraud which they were investigating; and (2) that indicated that Mr Trees did not know that the CCA transactions were connected with fraud. We
10 consider that it is not possible to draw any inference as to what those persons actually thought about the involvement of Mr Trees and CCA from the fact that they did not contact Mr Trees in connection with the criminal investigations. There are many possible reasons why they did not contact Mr Trees, apart from the suggested reason. But even if it were appropriate to infer that those persons actually thought that Mr
15 Trees did not know of the relevant fraud, the belief of those persons has no probative value as to what Mr Trees did know. The Judge was required to determine on the evidence before the F-tT whether it had been demonstrated on the balance of probabilities that Mr Trees knew that the CCA transactions were connected with fraud. What other people thought at an earlier time, probably by reference to material
20 which was different from the evidence before the F-tT, was irrelevant.

25 82. We therefore conclude that HMRC has established that the Judge took into account an irrelevant consideration. The question as to Mr Trees' knowledge was one of the central questions to be determined by the Judge. At [387], the F-tT stated that the case was a borderline case. In determining a central question in a borderline case, the Judge took into account, in favour of Mr Trees and CCA, an irrelevant matter.

30 83. HMRC submitted that this irrelevant matter was considered by the Judge to be highly material. While CCA accepted that the Judge regarded this matter as relevant, it submitted that it had not been demonstrated that the Judge regarded it as highly material. We have no way of knowing what precise weight the Judge gave to this matter. He plainly gave it some weight. In a borderline case, a matter which has some weight is capable of affecting the outcome.

84. We consider that, on this ground alone, the Decision as to Mr Trees' knowledge cannot stand. We will consider at the end of our decision, when we have assessed the other grounds of appeal, what should now be done.

35 **Ground 5**

85. We have earlier summarised Ground 5 as follows:

“The Ft-T misapplied the test in *Kittel* in that:

- (1) It considered a more onerous test than that prescribed by law;
- (2) It applied the burden and standard of proof to individual pieces of evidence as
40 opposed to considering the totality of the evidence;

- (3) It adopted an overly sceptical approach to circumstantial evidence;
- (4) It paid insufficient regard to the “should have known” limb of the test;
- (5) It misinterpreted the case advanced by HMRC as being a case of dishonesty and, in particular, it was wrongly influenced by the opinion of the officers of HMRC as to the nature of the fraud; and
- (6) It considered it relevant that the criminal investigation had paid no attention to Mr Trees.”

86. We note that the point made in (6) above was also the subject of Ground 3, with which we have already dealt. However, HMRC further deployed the point made in (6), in conjunction with the points made in (1) and (5), as its first substantive argument to the effect that the Judge misapplied the test in *Kittel* by holding that CCA could not be held to “know” that its transactions were connected with fraud unless it was also held to be dishonest and/or a knowing party to a conspiracy to defraud.

87. It was common ground before the F-tT that the test in *Kittel*, as expounded in *Mobilx* required it to ask whether CCA knew or should have known that the CCA transactions were connected with fraud.

88. In relation to the first part of the test, i.e. whether CCA knew that its transactions were connected with fraud, the F-tT had to address the case which was presented by HMRC on the facts. HMRC advanced the case that CCA and Mr Trees were dishonest and were in effect a party to the conspiracy to defraud. It was HMRC’s choice to put its case on the facts in that way and the F-tT had to deal with that case. Thus, when the Judge discussed HMRC’s case, he was not refining the *Kittel* test and holding that over and above knowledge that the transactions were connected with fraud, there had to be a finding that CCA was dishonest and/or that CCA was a party to a conspiracy. In any event, when the Judge came to make his essential findings on the first part of the test in *Kittel*, he correctly directed himself as to the relevant test and made his findings. He held, on those findings of fact, that HMRC had not established that CCA knew that its transactions were connected with fraud. We therefore reject the first argument put forward by HMRC under this ground of appeal.

89. The second argument put forward by HMRC under this ground of appeal relates to the way in which the Judge handled the circumstantial evidence. This submission only relates to the decision of the Judge. The Member’s reasons combined a number of circumstances in support of his overall conclusion that Mr Trees actually knew that CCA’s transactions were connected with fraud. However, HMRC submitted that the Judge looked at the circumstances individually and made individual assessments in relation to each so that he never stood back and formed an assessment of the combined weight of all the relevant circumstances.

90. It is open to HMRC to rely on circumstantial evidence to prove that a trader knew that his transactions were connected with fraud. So much is clear from *Mobilx*, in particular, at [83] approving the earlier comments of Christopher Clarke J in *Red 12 Trading Ltd v Revenue and Customs Commissioners* [2010] STC 589 at [109] – [111]. In addition, HMRC cited to us the observations of Hewart LCJ in *R v Weaver* (1930) 21 Cr App Rep 20 at 21 where he said:

5 “It has been said that the evidence against the applicants is circumstantial; so it is, but circumstantial evidence is often the best. It is evidence of surrounding circumstances which, by undesigned coincidence, is capable of proving a proposition with the accuracy of mathematics. It is no derogation of evidence to say that it is circumstantial.”

91. It is also clear that when one considers the impact of circumstantial evidence, it is important to consider the evidence as a whole and not to restrict oneself to considering the impact of each circumstance taken alone and in isolation from the others. The matter was well put in the old criminal case of *R v Exall* (1866) 4 F & F 10 922 by Pollock C.B., summing up to the jury, as follows:

“As it is, it is not much. By itself it would be insufficient, but there are other circumstances in the case, and especially the fact that the watch was found upon him before midday, on the morning after the burglary. Thus it is that all the circumstances must be considered together.

15 It has been said that circumstantial evidence is to be considered as a chain, and each piece of evidence as a link in the chain, but that is not so, for then, if any one link broke, the chain would fall. It is more like the case of a rope composed of several cords. One strand of the cord might be insufficient to sustain the weight, but three stranded together may be quite of sufficient strength.

20 Thus it may be in circumstantial evidence—there may be a combination of circumstances, no one of which would raise a reasonable conviction, or more than a mere suspicion; but the whole, taken together, may create a strong conclusion of guilt, that is, with as much certainty as human affairs can require or admit of.”

25 92. We also draw attention to the following comments of Rix LJ in *JSC BTA Bank v Ablyazov (No. 8)* [2013] 1 WLR 1331 at [52]:

“It is, however, the essence of a successful case of circumstantial evidence that the whole is stronger than individual parts. It becomes a net from which there is no escape.”

30 This comment was not cited to us but it is entirely in line with the submissions made to us by HMRC.

93. When dealing with a case based on circumstantial evidence, a fact finding tribunal has to do two things. First, it must make its findings as to what the circumstances actually were. Secondly, having determined what the circumstances were, it has to 35 determine what inference to draw from all such circumstances taken together. In the first part of this exercise, the tribunal necessarily will look at the alleged circumstances individually; for the second part of this exercise, the tribunal must look at the circumstances in combination. In this case, the Judge carried out the first part of the exercise by making his findings of fact as to the alleged circumstances. The 40 question for us is whether, having made his findings on the individual circumstances, the Judge failed to stand back and consider the combined effect of the circumstances in the round. In order to assess that matter we need to consider all of the material in the “Conclusions” section of the Decision to see how the Judge came to, and expressed, his conclusion.

94. The Conclusions section of the Decision has the following sub-headings (we have added the numbers for ease of later reference):

- (1) Admissibility of Mr Stone's evidence;
- (2) Missing evidence;
- 5 (3) Evidence from previous cases;
- (4) Mr Fletcher's credibility;
- (5) The grey market;
- (6) The underlying frauds – the law
- (7) A split decision;
- 10 (8) Mr Trees's knowledge;
- (9) Banking evidence;
- (10) Due diligence;
- (11) Insurance;
- (12) Reliance on HMRC
- 15 (13) Samsung Serenes
- (14) The tribunal's decision.

95. We consider that it was necessary for the Judge to consider the circumstances in (5), (8), (9), (10), (11) and (13) in combination, rather than separately. However, the Judge came to his finding, in section (8) of the above summary at [393] to [395], that
20 Mr Trees was not “a knowing participant in a fraud on the Revenue” and that he was not satisfied that a *bona fide* trader should have realised that his transactions *were* connected with fraud before he had considered the effect of the matters in sections (9) to (11) and (13). It seems to us that he decided the case in favour of CCA without regard to the matters in sections (9) – (11) and (13) and when he later dealt with the
25 matters in (9) to (11) and (13), he effectively said: “because I have decided that Mr Trees neither knew nor should have known that the transactions were connected with fraud, these later matters are not inconsistent with that finding”.

96. It is true that in [411] of the Decision the Judge expressed his overall conclusion in these terms:

30 “411 Having regard to all these considerations, neither of the two circumstances required by the authorities to be present has been established on the balance of probabilities in relation to the transactions under appeal and the appeal must therefore succeed.”

35 Thus, [411] comes after the Judge has referred to all the relevant matters and does refer to “all these considerations”. We do not however think that [411] can be fairly read as a finding that having regard to the combined weight of the circumstances in (5), (8) (9), (10), (11) and (13), HMRC has not proved the relevant allegations against CCA. We think that the way in which the Judge expressed his findings in favour of

CCA in section (8) of the Conclusions and the way in which he later dealt with sections (9) to (11) and (13) clearly reveals that he did not approach the circumstantial evidence in the correct way.

5 97. We have hesitated before reaching the above conclusions as to the Judge’s
treatment of the circumstantial evidence. We should not be over ready to subject the
Decision to a detailed syntactical analysis. Nonetheless, having attempted to read the
Decision in a fair and realistic way, we do reach the conclusion that the Judge erred in
10 law in his handling of the circumstantial evidence in this case. Given that the Judge
regarded the case as a borderline one, it was very important for him to approach the
circumstantial evidence in the correct way and we find that he failed to do so.

98. We will next consider the third submission by HMRC under Ground 5 to the
effect that the Judge paid insufficient regard to the second limb of the *Kittel* test as to
whether CCA should have known that its transactions were connected with fraud.
15 This submission had two limbs. The first limb was that the Judge applied the wrong
test as to “should have known” and the second limb was that, in substance, the Judge
did not deal with HMRC’s case that CCA should have known that its transactions
were connected with fraud.

99. The legal test laid down in *Kittel* for denying a trader the right to claim input tax is
20 that it must be proved that the trader knew or should have known that its transactions
were connected with fraud. There is no limitation in *Kittel* itself as to how HMRC can
go about proving that the trader should have known of the connection with fraud. One
way of proving it is to show that there was no reasonable explanation for the
transactions other than fraud. That possible way of proving that the trader should have
25 known is expressly referred to by Moses LJ in *Mobilx*, see, in particular, at [59], [74],
[75] and [84]. However, it was pointed out by Proudman J in *GSM Export (UK) Ltd v
Commissioners for Her Majesty’s Revenue and Customs* [2014] UKUT 0529 (TCC)
at [19], that proof that there was no reasonable explanation for the transactions other
30 than fraud is only one way in which it could be proved that the trader should have
known but it was not the only way. It was not suggested before us that this was
incorrect. Building on that foundation, HMRC submitted that the F-tT had gone
wrong in the present case because in [2] and [26] of its Decision, it identified the issue
as being whether CCA knew, or whether for CCA the only reasonable explanation
35 was, that its transactions were connected with fraud. It was suggested that it had
thereby wrongly excluded any other method by which it might be shown that CCA
should have known that its transactions were connected with fraud. We do not accept
this submission. The F-tT’s formulation of the issues in this case was very similar to
how the matter was described in *Mobilx* and reflected the way in which the case was
argued before it.

40 100. We turn then to the second limb of the argument on “should have known”.
HMRC submitted that the Judge paid “insufficient regard” to its alternative case that
CCA should have known that its transactions were connected to fraud. It was also
submitted that the Judge “did not specifically address the second limb in his
conclusions at all”. There was no criticism of the Member in this respect; it will be
45 remembered that he held that CCA actually knew that its transactions were connected

with fraud so that there was no need for him to address HMRC’s alternative case. As will be seen, we need to consider this limb of the argument in some detail.

101. We have already summarised the content of the Decision. At [241] – [306], the F-tT summarised the submissions for CCA. Those submissions included the
5 contention that in a contra trading case like the present, there was no real room for the “should have known” limb of the test. Conversely, the submissions for HMRC addressed the first limb of the test which requires actual knowledge but then put forward the alternative submission, correctly summarised at [354] – [355] of the
10 Decision that CCA should have known that its transactions were connected with fraud. HMRC’s submission on this point was a very detailed one and we have set out at paragraph 28 above the twenty specific points which HMRC relied upon and which were repeated at [354] of the Decision.

102. As explained earlier, the Judge set out at [388] – [393] the reasons for his conclusion that CCA did not know that its transactions were connected with fraud.
15 Then at [394] – [395], the Judge said this:

“394 HMRC’s officers all agreed that CCA could not have verified the transactions upstream and downstream of its own. Mr Kerr has nonetheless put forward a list (at paragraph 354 above) of some 20 grounds on which Mr Trees should have known that there was no reasonable explanation for his transactions other than a connection to
20 fraud. These concerns relate essentially to the pattern and manner of CCA’s trading in regard to which it has been indicated that the expert evidence about the market is conflicting; features which appear to the outside observer as unusual — the types of trade, the peaks in volumes, the apparently incestuous character of dealings, and so on — may on Mr Attenborough’s evidence be consistent with the peculiarities of a
25 specialised wholesale market, especially during the boom years of the economy.

395 I do not see therefore an adequate basis on which to support the conclusion that a *bona fide* trader, taking reasonable precautions and being of normal prudence, should have realised that his transactions *were* connected to fraud. That the transactions might
30 have been so connected, or even that it was ‘more likely than not’ that they were so connected, could well be argued and on that basis I might be persuaded; but that is in itself insufficient to lose the appellant its right to deduct input tax.”

103. If [394] and [395] were intended to deal with HMRC’s alternative case that Mr
35 Trees/CCA should have known of the connection with fraud, then it is distinctly odd that those two paragraphs appear under the heading “*Mr Trees’s knowledge*”. We also note that [394] was expressed differently in the original Decision and was subsequently corrected. As originally expressed, [394] stated that the twenty points put forward by HMRC were to support HMRC’s case that Mr Trees “must have
40 known” that there was no reasonable explanation for his transactions other than a connection of fraud. An allegation that Mr Trees “must have known” is relevant to the allegation of actual knowledge rather than to HMRC’s alternative case. Further, given the detailed way in which HMRC had presented its alternative case, it is curious that the Judge did not have a distinct part of the Decision, with a separate heading, where
45 he addressed this alternative case.

104. In its skeleton argument, HMRC submitted that the Judge did not specifically address the alternative case as to “should have known” in his conclusions “at all”. However, it seemed to us that at the hearing of this appeal, HMRC accepted that the alternative case was dealt with in [394] to [395]. HMRC’s case was then re-focused as a submission that those paragraphs were the only paragraphs dealing with the alternative case and, as such, they were inadequately reasoned. HMRC referred us to the standard which must be achieved, by a decision maker when giving reasons for a judicial decision, as laid down in *Flannery v Halifax Estate Agencies Ltd* [2000] 1 WLR 377 and *English v Emery Reimbold & Strick Ltd* [2002] 1 WLR 2409.

105. There was no dispute as to the standard to be achieved as regards the adequacy of reasons for a judicial decision. We cite two passages from the authorities which offer the necessary guidance. The first is from *Flannery v Halifax Estate Agencies Ltd* [2000] 1 WLR 377 at 381-382:

“(1) The duty is a function of due process, and therefore of justice. Its rationale has two principal aspects. The first is that fairness surely requires that the parties especially the losing party should be left in no doubt why they have won or lost. This is especially so since without reasons the losing party will not know (as was said in *Ex p Dave*) whether the court has misdirected itself, and thus whether he may have an available appeal on the substance of the case. The second is that a requirement to give reasons concentrates the mind; if it is fulfilled, the resulting decision is much more likely to be soundly based on the evidence than if it is not.

(2) The first of these aspects implies that want of reasons may be a good self-standing ground of appeal. Where because no reasons are given it is impossible to tell whether the judge has gone wrong on the law or the facts, the losing party would be altogether deprived of his chance of an appeal unless the court entertains an appeal based on the lack of reasons itself.

(3) The extent of the duty, or rather the reach of what is required to fulfil it, depends on the subject matter. Where there is a straightforward factual dispute whose resolution depends simply on which witness is telling the truth about events which he claims to recall, it is likely to be enough for the judge (having, no doubt, summarised the evidence) to indicate simply that he believes X rather than Y; indeed there may be nothing else to say. But where the dispute involves something in the nature of an intellectual exchange, with reasons and analysis advanced on either side, the judge must enter into the issues canvassed before him and explain why he prefers one case over the other. This is likely to apply particularly in litigation where as here there is disputed expert evidence; but it is not necessarily limited to such cases.

(4) This is not to suggest that there is one rule for cases concerning the witnesses’ truthfulness or recall of events, and another for cases where the issue depends on reasoning or analysis (with experts or otherwise). The rule is the same: the judge must explain *why* he has reached his decision. The question is always, what is required of the judge to do so; and that will differ from case to case. Transparency should be the watchword.”

106. The second source of guidance is *English v Emery Reimbold & Strick Ltd* [2002] 1 WLR 2409 at [16] – [21]:

“16 We would put the matter at its simplest by saying that justice will not be done if it is not apparent to the parties why one has won and the other has lost.

5 17 As to the adequacy of reasons, as has been said many times, this depends on the nature of the case: see for example Flannery's case [2000] 1 WLR 377, 382. In *Eagil Trust Co Ltd v Piggot-Brown* [1985] 3 All ER 119, 122 Griffiths LJ stated that there was no duty on a judge, in giving his reasons, to deal with every argument presented by counsel in support of his case:

10 “When dealing with an application in chambers to strike out for want of prosecution, a judge should give his reasons in sufficient detail to show the Court of Appeal the principles on which he has acted and the reasons that have led him to his decision. They need not be elaborate. I cannot stress too strongly that there is no duty on a judge, in giving his reasons, to deal with every argument presented by counsel in support of his case. It is sufficient if what he says shows the parties and, if need be, the Court of
15 Appeal the basis on which he has acted... (see Sachs LJ in *Knight v Clifton* [1971] Ch 700, 721).

18 In our judgment, these observations of Griffiths LJ apply to judgments of all descriptions. But when considering the extent to which reasons should be given it is
20 necessary to have regard to the practical requirements of our appellate system. A judge cannot be said to have done his duty if it is only after permission to appeal has been given and the appeal has run its course that the court is able to conclude that the reasons for the decision are sufficiently apparent to enable the appeal court to uphold the judgment. An appeal is an expensive step in the judicial process and one that makes
25 an exacting claim on judicial resources. For these reasons permission to appeal is now a nearly universal prerequisite to bringing an appeal. Permission to appeal will not normally be given unless the applicant can make out an arguable case that the judge was wrong. If the judgment does not make it clear why the judge has reached his decision, it may well be impossible within the summary procedure of an application for
30 permission to appeal to form any view as to whether the judge was right or wrong. In that event permission to appeal may be given simply because justice requires that the decision be subjected to the full scrutiny of an appeal.

19 It follows that, if the appellate process is to work satisfactorily, the judgment must
35 enable the appellate court to understand why the judge reached his decision. This does not mean that every factor which weighed with the judge in his appraisal of the evidence has to be identified and explained. But the issues the resolution of which were vital to the judge's conclusion should be identified and the manner in which he resolved them explained. It is not possible to provide a template for this process. It need not
40 involve a lengthy judgment. It does require the judge to identify and record those matters which were critical to his decision. If the critical issue was one of fact, it may be enough to say that one witness was preferred to another because the one manifestly had a clearer recollection of the material facts or the other gave answers which demonstrated that his recollection could not be relied upon.

45 20 The first two appeals with which we are concerned involved conflicts of expert evidence. In Flannery's case [2000] 1 WLR 377 Henry LJ quoted from the judgment of Bingham LJ in *Eckersely v Binnie* (1988) 18 Con LR 1, 77–78 in which he said that “a coherent reasoned opinion expressed by a suitably qualified expert should be the
50 subject of a coherent reasoned rebuttal”. This does not mean that the judgment should contain a passage which suggests that the judge has applied the same, or even a superior, degree of expertise to that displayed by the witness. He should simply provide

an explanation as to why he has accepted the evidence of one expert and rejected that of another. It may be that the evidence of one or the other accorded more satisfactorily with facts found by the judge. It may be that the explanation of one was more inherently credible than that of the other. It may simply be that one was better qualified, or manifestly more objective, than the other. Whatever the explanation may be, it should be apparent from the judgment.

21 When giving reasons a judge will often need to refer to a piece of evidence or to a submission which he has accepted or rejected. Provided that the reference is clear, it may be unnecessary to detail, or even summarise, the evidence or submission in question. The essential requirement is that the terms of the judgment should enable the parties and any appellate tribunal readily to analyse the reasoning that was essential to the judge's decision."

107. CCA submitted that we should not permit HMRC to advance the contention that the Decision was inadequately reasoned. CCA submitted that the grounds of appeal did not clearly bring home to CCA or to the F-tT that HMRC wished to contend that the reasons in the Decision were inadequate in this respect. CCA drew attention to the discussion in *English v Emery Reimbold & Strick Ltd* [2002] 1 WLR 2409 at [25] where the Court of Appeal considered the course to be adopted where an appellant sought permission to appeal a judgment on the ground that it was inadequately reasoned. In such a case, the judge should consider whether it was appropriate for him to provide further reasons. Although that discussion related to the position of a judge in court proceedings, the same recommendation should apply to a judge in the F-tT. Indeed, rules 40 and 41 of the 2009 Rules require a judge in the F-tT, when considering an application for permission to appeal, first to consider whether to review his decision. An application for permission to appeal on the ground of inadequate reasons should cause the F-tT to consider whether it would be appropriate to give further reasons, using the powers conferred by these rules. In the present case, at the stage at which HMRC sought permission to appeal in relation to Ground 5, there does not appear to have been any thought given to whether the Judge should give further reasons for his conclusions in [394] to [395].

108. There is some force in these objections by CCA. It would have been better if, from the outset, HMRC had made it more clear that it intended to challenge the adequacy of the Judge's reasons in this respect. If that had been done, then the Judge might have been prepared to give further reasons in relation to [394] to [395]. In view of the passage of time since the Decision was released and in view of the risk of ex post facto rationalisation by way of further reasons, we do not think that it would be fair to the Judge or to HMRC to ask the Judge to supply further reasons at this stage. Nonetheless, we take the view that this ground of challenge is open to HMRC pursuant to its ground of appeal that the Judge paid "insufficient regard" to its alternative case. We consider that on a fair reading, this formulation of the challenge allows HMRC to argue that the way in which the Judge dealt with its alternative case was "insufficient" in that the Judge gave inadequate reasons for his dismissal of that alternative case.

109. We will therefore examine [394] and [395] to see if they meet the requisite standard for reasons for a decision. CCA submitted that these two paragraphs gave adequate reasons for the Judge's conclusion on what was a matter of fact.

5 110. The first sentence of [394] states that HMRC agreed that CCA could not have verified the transactions upstream and downstream of its own. That does not by itself answer the submission made by HMRC that the combination of the twenty points summarised in [354] compelled the conclusion that CCA should have known that its transactions were connected with fraud because there was no other reasonable explanation for them.

10 111. The second sentence of [394] merely refers to the list of twenty points in [354]. The third sentence of [394] states that the expert evidence about the grey market was conflicting. In order to understand that statement, it is necessary to go to the parts of the Decision which dealt with the grey market. That topic was dealt with at [376] – [382] where the F-tT had said:

15 “376 Detailed evidence was given about the operation of what, it is common ground, was a legitimate market in mobile handsets in 2006. Both Mr Fletcher and Mr Attenborough made careful estimates of what they believed would have been the conditions of that market, basing themselves on the limited number of hard facts available and making informed estimates for the rest. And it will be seen that in the
20 evidence of these two witnesses the views of the one often contradict the views of the other, both in detail and in regard to the broad picture.

25 377 Thus, there was disagreement over the size of the legitimate grey market in 2006 and in regard to the extent to which the 2010 figures are likely to be falsified by MTIC fraud directed against other EU states, if there is any. There are also serious gaps in the information regarding the position outside a restricted area of mainly western Europe, when it is entirely possible that the situation is related to trading beyond.

30 378 Of particular concern to us, however, was the disagreement as to what types of trading can be regarded as authentic and which not, leaving the tribunal in doubt as to one of the crucial issues in the case — whether HMRC are right in asserting that CCA's trading was uncommercial and contrived in the way that Mr Kerr suggests. While these two witnesses were clearly competent persons in the context of their respective professions, it is no criticism of them to say that neither has had any firsthand
35 experience of the operation of this market, and that they were able draw on the experience of others only to a limited extent.

40 379 It is regrettable that there is therefore no impartial evidence before the tribunal about how the legitimate trade in the grey market in question actually functioned; there is no trader from that era to say from firsthand knowledge: ‘that is – or is not – how things were done’; ‘this is, or is not, typical of authentic trading’. We are concerned with what seems, in principle, to be a specialised trading market and it is common knowledge that specialised markets do not operate in the way that simple retail distribution chains do. While it may well be appropriate to take judicial notice of the
45 manner in which commerce at large is normally conducted, it can be unsafe to attempt the same exercise in regard to a specialised market.

380 Many of the practices and patterns of trade revealed by the evidence seem to require explanation: the buying and selling of large quantities of goods with little or no subsidiary detail in regard to them; the apparently formulaic nature of the trading in the UK to UK deals; the standard margins of profit in such deals; the substantial absence of written terms of business; the payment of monies decoupled from the passing of title; the use of the UK as a trading hub for intra-European continental trade; the use of sterling as the currency in the case of all the export trades; the course of trading between the same parties; the peak in trade volumes in 2006, and so on.

381 The fact that expert evidence was adduced by both parties as to the functioning of this market, however, underlines the point that the assessment of behaviour in the grey market as authentic trading or as contrived activity requires specialist knowledge. Messrs Fletcher and Attenborough have assisted the tribunal to the best of their abilities, but the evidence of each throws doubt on the adequacy of the reasoning adopted by the other in areas in which there can clearly be legitimate disagreement. And although Mr Attenborough has not addressed this case specifically, his evidence touching the types of behaviour to be expected is consistent with the view that CCA's trading was not necessarily untoward or suspicious.

382 We are left therefore to assess the facts, conscious of having inadequate information about this market, and to remember that the burden of proving contrivance lies on the Revenue. In the circumstances, we cannot regard any of the peculiar features just described as inevitably pointing to uncommercial trading or as clear indicators of bad faith. They may do so, but it has not been shown that the probability is that they do so point and the only firsthand evidence of the way this market works is that of the appellant himself.”

112. In [382], the F-tT held that the matters which required explanation might show bad faith but it had not been shown that the probability was that they did so. This point appears to be echoed in [394] where the Judge said that the features which appeared to be unusual might be consistent with the peculiarities of a specialised market and in [395] where the Judge said that the transactions might have been connected with fraud but that did not justify a finding that CCA should have realised that they were connected with fraud.

113. HMRC submitted that the F-tT when referring to Mr Attenborough in [381], and the Judge when referring to Mr Attenborough in [390], had appeared to hold that Mr Attenborough's evidence supported the conclusion that the trading patterns in this case were not necessarily consistent with fraud. As against that, the F-tT stated in [381] that Mr Attenborough had not addressed this case specifically. Further, HMRC submitted that Mr Attenborough's evidence did not deal with many of the points made in the list of twenty matters and in particular did not deal with the question of risk (referred to in (i), (iii), (iv) and (v)), due diligence (referred to in (xi)), no goods returned (referred to in (xiii)), consistent markups (referred to in (xiv)), same offshore bank (referred to in (xv)), links between suppliers (referred to in (xiv), (xv), (xvi), (xvii) and (xviii)), nor did he deal with other matters such as the insurance of the goods, the patterns in the supply chains and the non-existent goods.

114. We were not taken to the detail of the evidence which was given by Mr Attenborough but counsel for CCA did not appear to us to dispute the broad thrust of HMRC's submission as to the matters which had not been addressed by Mr Attenborough.

5 115. HMRC also cited to us the decision of the Upper Tribunal in *S&I Electrical plc v Commissioners for HM Revenue and Customs* [2015] UKUT 0162 (TCC) where the
10 Upper Tribunal upheld the decision of the F-tT to the effect that the trader in that case ("S&I") should have known that its transactions were connected with fraud. The decision of the Upper Tribunal contains a discussion as to the relevant test being an
15 objective one where the matter is judged through the eyes of the reasonable businessman involved in the trade in question. The trade in that case, as in the present case, involved the sale of mobile telephones in the grey market. On the question as to whether the tribunal needed evidence of the normal characteristics of legitimate trade in the grey market, the Upper Tribunal said:

15 "64. In our judgment (as we indicated in relation to Ground 1) [counsel for S&I] goes too far in his submission that the FTT could not determine whether S&I should have known of the connection with fraud of the 79 transactions without evidence of the normal characteristics of legitimate trade in the grey mobile phone market. In
20 accordance with the extract from Lord Reed's judgment in *Healthcare at Home Ltd v Common Services Agency*, the FTT's task was to apply the impersonal standard of the reasonable businessman to the facts which it found, on the basis of the evidence which it heard, as to the circumstances in which S&I carried out the transactions in issue. Would the reasonable businessman have concluded that S&I ought to have known that the only reasonable explanation for the transactions was that they were connected with
25 fraud?

65. It is true that the FTT was required to invest the reasonable man for these purposes with the characteristic of being a reasonable businessman with ordinary competence, but in our judgment a reasonable businessman with ordinary competence is not so
30 egregious or specialist a variant of the anthropomorphic conception of justice that the FTT needed evidence of the normal characteristics of legitimate trade in the grey mobile phone market, or any other expert evidence, in order fairly and justly to apply the required impersonal standard."

116. We also note the F-tT's comment in [382] that the only firsthand evidence of
35 the way the grey market worked was Mr Trees. We have therefore considered the reasons the Judge gave for holding that Mr Trees did not actually know that CCA's transactions were connected with fraud. In that respect, the Judge said at [389] that he was inclined to believe Mr Trees in certain respects and he added at [389] to [390]:

40 "388 The same was true when it came to the question of the rationality of trading patterns now apparent – for example, CCA's main suppliers also selling direct to CCA's EU customers (of which Mr Trees was unaware), or the customers not cutting CCA out as they could have done. The case was very properly put to Mr Trees that these and suchlike factors indicated a contrived pattern of trade designed to suit a non-commercial purpose. The responses Mr Trees made included the assertion that he did
45 not spend time speculating idly about possible other trade patterns that might be taking

place, but that he just got on with buying and selling when the opportunity was there. My impression was of a businessman who was essentially pragmatic in his approach to situations and not given to theorising about how the markets could most efficiently operate knowing that they frequently do not do so, and being unable to know of course what other factors – commercial or otherwise – might or might not be at work.

390 Thus, on the question of the apparent inefficiency of importing goods to the UK from the EU and then re-exporting them back to the EU, which could suggest an irrational market, Mr Trees's response was that he never thought of querying the situation because, whatever its explanation, it offered an opportunity for him; he evidently contended himself with the knowledge that there are all sorts of reasons why markets don't function as an uninitiated observer might expect them to. It is crucial to this issue that much of what is now clear about the trading patterns surrounding CCA's transactions has been discovered as a result of the commissioners' lengthy investigations; and it is relevant also that Mr Attenborough's evidence is consistent with imports to and exports from the UK being a feature of the legitimate market, with the UK functioning as a trading hub.”

117. Based on these findings, we do not think that it can be said that because Mr Trees did not think that CCA's transactions were connected with fraud, a reasonable trader would not, or should not, have known that. We say that because we consider that we cannot equate the reasonable trader's thinking on the subject with Mr Trees' failure to think about the subject, as described by the Judge.

118. We return to the question whether the Judge gave adequate reasons for rejecting HMRC's submission based in particular on the twenty points it put forward that CCA acting as a reasonable trader should have known that its transactions were connected with fraud. Notwithstanding the extremely brief treatment this subject received in [394] and [395] we have attempted to look elsewhere in the Decision to see if the matter is adequately explained. In this way, we have considered the findings about the grey market, about Mr Attenborough and about Mr Trees. Having done that exercise we reach the conclusion that the Judge has not given adequate reasons for rejecting HMRC's submissions on this point. In particular, we conclude that:

- (1) the Judge's treatment of HMRC's alternative case was too brief;
- (2) the twenty points required much more by way of an intellectual exchange from the Judge than they received;
- (3) the twenty points did not receive a coherent reasoned rebuttal from the judge;
- (4) Mr Attenborough's evidence, even as explained by the F-tT, did not amount to a rebuttal, much less a reasoned rebuttal, of those points;
- (5) the Judge ought to have formed his own assessment of the alternative case and was not able to decline to do so on the basis that he did not have expert evidence to help him.

119. We therefore conclude that the Judge's decision on this point discloses an error of law because it is inadequately reasoned.

Taking stock at this point

120. We have concluded that HMRC has established the following errors of law in the Decision:

- 5 (1) the Judge took into account an irrelevant consideration as to Mr Trees not being the subject of a criminal investigation;
- (2) the Judge did not assess the circumstantial evidence as a whole;
- (3) the Judge did not give adequate reasons for rejecting HMRC's alternative case.

10 121. Before considering Ground 8, we think it would be helpful to determine the appropriate course to take in the light of the above and whatever the position might be in relation to Ground 8.

15 122. It is not appropriate merely to remit the matter to the F-tT for further reasons as to HMRC's alternative case. The failure to give reasons is only one of the grounds on which the appeal has succeeded. The provision of further reasons will not remedy the other errors of law in the Decision. In any event, as stated earlier, in view of the passage of time since the Decision was released and in view of the risk of ex post facto rationalisation by way of further reasons, we do not think that it would be fair to the Judge or to HMRC to ask the Judge to supply further reasons at this stage.

20 123. We do not consider that we could or should ourselves decide the issues which were before the F-tT. It would plainly be inappropriate for us to reach a conclusion as to the extent of Mr Trees' actual knowledge when we have not had the benefit of hearing for ourselves the oral evidence which he gave and as to which the Judge and the Member formed conflicting views. It might be suggested that we could reach conclusions on HMRC's alternative case which involves an objective assessment of what a reasonable trader should have known. However, if we decided that point against HMRC, HMRC would still be entitled to ask for the matter to be remitted to the F-tT for a decision on Mr Trees' actual knowledge. It seems to us that it would be better for the F-tT to consider the alternative case at the same time. Thus, we conclude that the matter will have to be remitted to the F-tT. We do not consider that it would be appropriate to remit the matter to the same constitution of the F-tT. We consider that fairness and justice requires that the matter is decided by a tribunal which has not previously expressed its conclusions on the matters in dispute.

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Ground 8

35 124. We will now consider what if anything we should decide in relation to Ground 8. We have earlier summarised Ground 8 as follows:

“The Judge erred in law in his approach to the banking evidence in that:

- (1) His conclusions were inconsistent with the evidence to the extent that they were not conclusions which a reasonable tribunal could have reached;
- (2) He wrongly disregarded relevant evidence;

(3) He failed to take into account the detailed submissions made on behalf of HMRC;

(4) His conclusions were based on errors of fact;

(5) He took account of irrelevant matters; and

5 (6) He failed to give an adequate explanation or reasons for dismissing the banking evidence.”

125. The banking evidence before the F-tT was very extensive. HMRC’s and CCA’s submissions in relation to Ground 8 are very detailed. At the hearing of the appeal, we were invited to consider a great deal of the banking evidence which had been before
10 the F-tT for the purpose of determining whether the Judge had made errors of fact in his description of this evidence, whether he had reached a conclusion which a reasonable tribunal could not have reached and whether his reasons for his conclusions in this respect were adequate. As it happened, the time available for the hearing of the appeal did not permit the parties to develop orally all of their
15 submissions in relation to the banking evidence and we agreed that, if necessary, we would deal with the matter by ourselves reading the banking evidence and considering each side’s detailed written submissions. However, what did emerge from the oral submissions on the banking evidence was that the submissions gave rise to many points of detail where there was considerable argument as to what the basic facts
20 were.

126. Our view is that we should not further address Ground 8 in this decision. It is already clear that the matters in dispute will have to be remitted to a differently constituted F-tT. That tribunal will be expected to deal with the matters comprehensively. If HMRC continues to rely on the banking evidence, which we
25 assume it will wish to do, then that evidence will have to be tested and appraised by the F-tT. Its views of the banking evidence will be what will matter. It will be expected to give its reasons for the views it ultimately forms.

127. The arguments before us on this appeal did not raise any issue of legal principle on which our ruling would be helpful to the F-tT following the remission of this case.
30 If we were to address Ground 8 in further detail, there would be a danger that we would have to comment on what are essentially factual assessments which ought to be left to the ultimate fact finding tribunal. In these circumstances, the time needed on our part to reach a properly considered decision on Ground 8 and to express our reasons for that decision would be disproportionate to any possible benefit thereby
35 secured.

The result

128. In the result, we will set aside the decision of the F-tT and direct that the matters in dispute be remitted to be determined by a differently constituted tribunal.

MR JUSTICE MORGAN

JUDGE TIMOTHY HERRINGTON

**JUDGES OF THE UPPER TRIBUNAL
RELEASE DATE: 24 JUNE 2015**

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