TC03659

Appeal number: MAN/20O8/01363

TYPE OF TAX –VAT - section 61 penalty – no dishonesty – appeal allowed.

FIRST-TIER TRIBUNAL
TAX CHAMBER

JOHN WOOD **Appellant**

- and -

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

TRIBUNAL: JUDGE RICHARD BARLOW
MR PETER WHITEHEAD

Sitting in public at North Shields on 8, 10, 11, 12, 15, 16, 17, 18, 22, 23, 24 and 25 October 2012, and 15, 16, 17 and 18 July 2013.

The Appellant in person.

Mr James Puzey of counsel, instructed by the General Counsel and Solicitor to HM Revenue and Customs, for the Respondents

DECISION

1. Mr Wood appeals against a decision that he is liable to penalties totalling £1,137,603 under section 61 of the VAT Act 1994, (the Act), issued on the grounds that a company called Asgard UK Limited (Asgard) had evaded VAT (or in respect of one period sought to evade it) and that the company was liable to a penalty under section 60 of the Act. Mr Wood was a director of the company at the material times and it is alleged that the conduct of the company giving rise to the penalty involved dishonesty making it liable to a penalty. It is alleged that the conduct of the company giving rise to the penalty under section 60 of the Act was "in whole or in part attributable to the dishonesty of Mr Wood"; making him liable to the penalty under section 61.

2. The nature of the evasion of VAT alleged by the company is the claiming of a VAT credit to which it is alleged it was not entitled.

3. Sections 60 and 61 of the Act were repealed in 2007 but were subject to transitional and saving measures which mean that the penalties in this case, which relate to activities in periods before the repeal, are not invalidated by the repeal of those sections.

4. Section 61(5) and section 83(1)(o) of the Act appear to be intended to restrict the right of appeal under section 61 in a way that might be said to be contrary to the principles of fairness and the human rights of a person penalised under section 61. That is because there is a restriction on the appellant's ability to challenge the underlying liability to a penalty of the company. However, as our finding is that the Commissioners have failed to prove that Mr Wood acted dishonestly, our decision is based on that finding of fact and that makes it unnecessary for us to consider how far Mr Wood could in fact have disputed the liability of the company to a penalty under section 60 of the Act on which the penalty assessed on him depended.

5. It is not a defence to the section 61 penalty that no penalty had in fact been imposed on the relevant company under section 60. It would be enough that the relevant company was liable to a penalty. Again, as this decision is based on the finding of fact that the appellant was not dishonest the penalty is not payable whatever might have been our decision about whether the company would have been liable to a penalty.

6. This case was heard together with that of Mr David Langhorne and some of the evidence was common to both cases. The cases were not consolidated, nor could they have been, so a separate decision is required in both appeals.

7. The penalty alleged was notified to Mr Wood by a letter dated 21 March 2005 although another version dated March 2005 (no day specified) had also been issued in error alleging that the relevant section 60 penalty related to a different company.

8. There were separate penalties for each of the one month tax periods 01/02 to 01/03 inclusive and the penalties all relate to sums of input tax claimed by the company which HMRC say were evaded within the meaning of section 60 of the Act because the company had claimed a VAT credit to which it was "not entitled" except for the last period in which the repayment claimed was not paid by the Commissioners and so the allegation for that period is the that the company sought to evade the tax by claiming the tax credit to which it was "not entitled". In each period the penalty has been assessed as 90% of the tax allegedly evaded or sought to be evaded.

9. The VAT credits must be ones to which the company was "not entitled" because that is the wording used in section 60(2). It follows that it could be open to argument whether the facts of this case fall within that provision at all. The basic facts are that the input tax claims were in respect of transactions in which goods were bought by the company and were exported giving rise, in principle, to a claim for input tax without any corresponding output tax liability because the onward sale, being an export, was zero rated. The goods did exist, they were purchased from another UK supplier which was registered for VAT and they were exported so this was not a case where the whole transaction was what might be called a 100% sham, which might have been the case if, for example, the goods never existed or were not in fact exported.

10. The exact parameters of how far a transaction, which is alleged to be a sham, must be shown, as a matter of law, to be such before no entitlement to input tax arises may be open to argument. But we need not consider that point as the ratio of this decision is that we have found, as a fact, that the appellant was not dishonest. Arguments about how far, in law, the transactions might have been held to be shams or otherwise not subject to a credit for input tax would therefore be irrelevant. Obviously some of the evidence that HMRC contends shows that the transactions were shams or otherwise not subject to a credit for input tax is relevant to be considered when deciding whether dishonesty has been proved.

The Commissioners' case concerning dishonesty.

11. The allegations against Mr Wood do not provide any direct evidence that he had acted dishonestly and the Commissioners' case is circumstantial though there is no doubt that circumstantial evidence can, in principle, prove dishonesty.

12. Mr Wood was a director and shareholder of Asgard which was registered for VAT from 1 December 2001. Asgard bought a large quantity of irrigation hose from a company called VPS Ltd (VPS) which was registered for VAT. VPS had manufactured the hose. That transaction was a taxable supply on which the standard rate of tax was payable. The Commissioners alleged in their statement of case that VPS sold most of the hose it manufactured to either Asgard or a company called Formel E Ltd (Formel) which was owned and managed by Mr Langhorne whose appeal was heard at the same time as this appeal.

13. VPS was alleged to be a company owned and operated by a Mr Thompson who had been a friend of Mr Wood from their schooldays and with whom Mr Wood had

been in business together on a previous occasion. VPS was set up by Thompson and, according to Thompson, a man named Volker Kappler (the V in the company name stands for Volker according to Thompson). There is no evidence that Mr Wood knew that Kappler was involved until after the transactions in this appeal had occurred and indeed HMRC agree that there is no evidence, other than Thompson's word, that Kappler was involved in VPS.

14. The Commissioners alleged that Asgard's main business was the purchase and export of the hose and that it bought all its hose from VPS and sold it all to a business called Tazar Industries (Tazar) in the UAE.

15. The evidence does not provide full details of Tazar. There is some doubt whether Tazar was a UAE company or a Free Zone Enterprise in Dubai, or both. But the Commissioners alleged that whatever was the precise legal entity to which the hose was exported it was operating under the name of Tazar and was in fact owned by Mr Thompson. Therefore Mr Thompson was selling the hose to his own company and the Commissioners allege that the interposition of a third party (Asgard) made no sense in ordinary commercial terms.

16. In addition, the Commissioners alleged that the hose was being sold to Asgard at £1.39 per metre but its true value was alleged to be between 10p and 20p. Asgard sold the hose on at £1.49 per metre.

17. Asgard's terms of business with VPS and Tazar were that it was not required to pay VPS until seven days after it had been paid by Tazar and that Tazar was not required to pay Asgard until 60 days after the hose had been installed in the ground.

18. Under the normal rules for crediting input tax, as was later accepted in principle by HMRC, Asgard would therefore be able to claim a repayment from HMRC well before it was required to pay a tax inclusive price to VPS. Indeed under the rules Asgard were obliged to claim the input tax in the period in which the supplies took place.

19. Whether the normal rules for input tax recovery were applicable or whether the special rules for terms similar to those applying in cases of goods sent on approval provided for by section 6(2)(c) of the Act were applicable was not an issue either party raised. It has become irrelevant to consider that in light of our decision that HMRC's case fails because of their failure to prove dishonesty.

20. It is not in doubt that a legitimate claim for input tax can be made whether or not the supplier has accounted for or intends to account for its output tax.

21. It was later alleged by the Commissioners that the input tax claim was itself artificially high because of the over valuation of the hose.

22. On 22 January 2003 officers of HMRC interviewed Mr Wood about the claims for input tax by Asgard and at that stage HMRC had formed the view that Thompson had acted fraudulently but that the claims by Asgard were repayable.

23. In fact at first HMRC proposed to Asgard that it should accept part only payment of the input tax which they were agreeing was payable in principle and to allow them to credit the unpaid part as part payment of VPS's unpaid output tax. Asgard took advice from a VAT consultant and rejected that suggestion. There is no legal basis for such a proposal and Mr Wood was so advised by his advisor. HMRC paid Asgard £1,231,275.37 in total.

The kidnapping of Mr Wood.

24. On 14 March 2003 Mr Wood and Mr Langhorne were kidnapped in County Durham by men dressed as uniformed customs officers. They were beaten, threatened with guns and taken across the country to what Mr Wood believes to be premises owned by Kappler or one of his companies. There they were threatened again and demands for money were made. One of Kappler's companies, Superflexibles Ltd, alleged it was owed money by VPS or one of Thompson's companies. Indeed the money owed to Kappler's company was understood to relate to raw materials used to manufacture the hose that features in this case.

25. Approximately 20 minutes after Mr Wood and Mr Langhorne were released from their kidnap ordeal Kappler rang a customs officer, Karen McNeill, and gave her information.

26. Her notes of the conversation were heavily redacted because they included notes about information relating to serious crime given to Ms McNeill by Kappler. However the un-redacted parts of the notes include allegations by Kappler that he knew how "the hose scam" worked and that Thompson was "the personnel involved". He alleged that the hose was worth approximately 10p per metre and was being retailed (sic) by Thompson at £1.39 per metre. He also alleged that Tazar was owned by Thompson. In other words his allegations mirror those later made by HMRC.

27. In fact HMRC officers agree that they changed their minds about the correctness of the refunds of input tax to Asgard as a result of this information from Kappler and they then instituted further inquiries.

28. Kappler also asked Ms McNeill to confirm the amounts of input tax repaid to Mr Wood and Mr Langhorne's companies but according to her notes she declined to do so saying she was unable to discuss another company's affairs with him and he then told her that he knew the amounts anyway. Mr Wood believes that Ms McNeill acted improperly in her dealings with Kappler and suspects that she did tell him what he wanted to know but we do not find that to be the case. It seems someone told Kappler about the repayments but we see no reason to suspect Ms McNeill, rather it seems likely that Thompson may have told him. We consider that the fact that Kappler knew VPS were charging £1.39 per metre for the hose strongly supports the conclusion that it was Thompson who gave him the information.

29. Kappler said in the call immediately after the kidnap had ended that "a meeting had taken place" and that he "was confident that the monies would be repaid" which we take to be a reference to the money he said he was owed by Thompson. He added

"when people get money in the bank it goes to their head, but they get left a bit dented and smelly". Naturally that last statement was relied on later when Kappler was prosecuted and convicted of kidnapping. He was sentenced to 10 years imprisonment but he obtained a re-trial on an appeal to the Court of Appeal and was acquitted at the retrial.

30. The prejudicial statements made by Kappler in the calls to Ms McNeill and in an interview conducted by Mr Terrell, a customs officer, a few days before the kidnap were introduced into evidence in the appeal before us including a statement that Mr Wood was the brains behind the scam. When challenged as to why these statements were being introduced despite the fact that Kappler was not being called as a witness HMRC gave the excuse they so often give when introducing purely prejudicial evidence namely that it was "part of the background".

31. They also emphasised that Kappler had in fact been acquitted and clearly hoped that we would give weight to his allegations. They failed to draw to our attention that he remained a convicted criminal despite the acquittal for the kidnapping in that he had previously received a suspended prison sentence for an unrelated offence of false accounting.

32. We should make it clear that, although the prosecution formally agreed certain things about Mr Wood and Mr Langhorne for the purposes of the trial of Kappler, we note that Mr Wood and Mr Langhorne themselves did not agree with those allegations as they made clear in their evidence both at the trial and before the Tribunal. We do not regard the prosecution admissions as binding upon us. The same applies to remarks made by the Court of Appeal in the Kappler case. Those remarks were no doubt based on the prosecution admissions and in any case do not bind us as the fact finding tribunal in this appeal.

Evidence about the value of the hose.

33. Mr Wood believes that a witness who was due to give evidence that the hose was valued at 10 to 20 pence a metre was in fact connected to Kappler. That is not a fact we are able to decide.

34. On the day that witness, Mr Walton, was due to give evidence after the lunch adjournment Mr Puzey announced at 2pm that he had decided to withdraw the witness statement of Mr Walton and that the Commissioners would not seek to rely on Mr Walton's evidence and indeed that Mr Walton had left the building in which the hearing was taking place.

35. Mr McWhannell expressed his dissatisfaction about this having occurred without his being given an opportunity to cross examine had he wished to do so or the courtesy of prior warning but, as the statement was withdrawn, he did not press the point. Mr Wood, as a litigant in person, was clearly significantly confused. We assured both parties that although we had read the statement of Mr Walton we would now ignore it and we have done so.

36. We should add that there was an issue about whether the hose examined by Mr Walton was in fact relevant to this appeal at all as there were alleged discrepancies between the sample taken by the police and the description of the hose examined by Mr Walton. Police Sergeant Halliday gave evidence and although we do not need to make a finding about this issue as it has become irrelevant in the absence of any credible evidence about the value of the hose, whether the sample was a sample of the correct hose or not, we record that we accepted his evidence. The provenance of the hose sample is at least doubtful.

37. The Commissioners then relied on evidence from a Mr Hartley, a self-employed business consultant with a degree in marketing, who had worked for a manufacturer of porous pipes between 1997 and 2008.

38. He made no mention of his instructions nor did he state himself to be aware of any responsibilities he might have as an expert witness. We find that he was not qualified to give evidence as an expert.

39. He referred to prices charged for hose in 2002 by his former employers, for whom he now acted as a consultant. We are not satisfied that he was able to confirm that the type of hose his former employers were selling was equivalent to that which was being sold by Asgard. None of the sales he was referring to were to the UAE.

40. Before it could be said that evidence had proved that the hose in this case was overvalued by comparison with other hose sold by other suppliers it would be necessary to establish that the hoses were sufficiently similar and that the market in which they were being sold was also sufficiently analogous to make a comparison worthwhile.

41. Mr Hartley's evidence failed to achieve either of those conditions and whilst other forms of evidence might have established an over-valuation none was presented.

42. Evidence from the Government Chemist about the apparent make-up of the hose added nothing so far as the value of the hose was concerned.

43. We have already indicated why we are not prepared to act on Kappler's assertions and that includes the statement that he alleged the hose was worth 10p a metre.

44. We therefore have to proceed on the basis that the over-valuation has not been proved.

45. We would add that even if the over-valuation had been proved that in itself would not necessarily have proved that Mr Wood knew it was over-valued.

The evidence about Mr Wood and Mr Thompson's dealings prior to those relevant to the appeal.

46. Mr Wood does not deny that he had been friendly with Thompson since their secondary schooldays. They had been involved in a business venture together through a company called Nutretech which went wrong when the BSE outbreak made

the product they were dealing with unsaleable. That venture had involved the processing of human food waste into animal feed but new regulations introduced to combat the spread of BSE had made the business non-viable.

47. Mr Wood had lost money as a result of that venture and when Thompson approached him about the transactions concerned in this appeal he said he felt that was offered the business opportunity, in part at least, as some sort of recompense for the loss he had suffered. We find that convincing and given that Thompson had not acted dishonestly in respect of the failed venture we do not agree with HMRC that the prior relationship is in any way an indication that Mr Wood knew the hose venture was dishonest.

The evidence about Thompson's involvement with Tazar.

48. We are satisfied that Thompson did have some sort of proprietorial interest in Tazar. The evidence was not complete or fully clear but documents from the Dubai Chamber of Commerce do show that Thompson was at least a part owner of Tazar and/or that a company of which he was a director (Parlex Ltd) was the parent company of Tazar and that Thompson was the manager in charge of Tazar. On the other hand there was also some evidence that suggested that Thompson only owned 50% of Tazar. He himself said he owned 40% when he gave evidence at the kidnapping trial. In addition there was at least a possibility that Tazar consisted of both a UAE company and Dubai Free Zone Enterprise in which case it would not be exactly clear which of those entities the Chamber of Commerce was referring to.

49. We find that whatever the true legal form and facts about the ownership of Tazar, at the very least, Thompson had a significant interest in it.

The evidence about how Mr Wood became involved.

50. It was part of HMRC's case that the deals between VPS and Asgard were both unnecessary (in that Thompson's company could have sold direct to Tazar which was at least partly his company) and that the terms of business were suspiciously favourable to Asgard (in that Asgard did not have to pay VPS until it had been paid by Tazar) and that Asgard was adding no value to the hose but would receive a profit for very little effort.

51. On the face of it those allegations are true and carry a good deal of weight. Mr Wood's explanation is that, although he was aware that Tazar was connected with Thompson in some way, he was unaware of the full details of that. He said that Thompson had described himself as a minority shareholder in Tazar.

52. More to the point, Mr Wood claimed that Thompson had explained why he wanted an intermediary between VPS and Tazar. He had said that he had previously dealt with third parties in the UAE in deals involving a proposal for a fish drying plant which had ended unsatisfactorily and that he now had a bad reputation in the UAE and that the potential customers would not deal with him. Mr Wood said that he found that plausible because when he had been involved with Nutretech he had seen

faxes and emails from the UAE addressed to Thompson raising complaints about the fish drying plant.

53. Mr Langhorne's evidence was that Thompson had claimed that his relationships with the UAE had been damaged by the failure of an enterprise called Nutretech and that he was therefore not able to deal with Tazar directly. As his appeal was heard at the same time as the appeal of Mr Wood the evidence about that having been said by Thompson is consistent with Mr Wood's evidence and both appellants' evidence is therefore corroborative of the other's.

54. Mr Wood also said that Thompson had claimed that the end purchaser of the hose was the UAE government. In February 2002 Mr Wood said he had met Mr Omer, a manager of Tazar and possibly a co-owner with Thompson, and he had also claimed the UAE government was the customer for the hose.

55. The story about previous problems for Thompson in the UAE may well have been entirely untrue but the relevant issue for the purposes of this appeal is whether or not Mr Wood believed it to be the true explanation for Asgard's involvement on favourable terms. If he believed it to be true it would be, from his point of view, an innocent explanation about why the transactions were taking the form they were.

56. HMRC both contend and agree that Thompson was acting dishonestly and described how he had falsified VPS records, wrongly claimed input tax and deliberately failed to declare output tax. Those facts make it at least plausible that he might have duped Mr Wood and told him lies as Mr Wood claims was the case.

57. Although Mr Wood had had some previous business experience he is in effect a technical expert in the polymers field and not a seasoned businessman and he certainly had not had experience of any export trade or dealing with the UAE or any other Far East country as a businessman as opposed to advising as a polymers expert.

58. He also pointed out that when he had worked for ICI that company had often sold goods to distributors and traders who sold the product on unchanged.

59. We do not find it inherently unlikely that he would have found Thompson's explanation plausible. We observed him giving evidence and observed the genuine sense of grievance he now feels against Thompson whom he now believes to have been fraudulent as HMRC claims. We find his explanation convincing and we find that he did believe there was a genuine reason for Asgard being involved in the transactions.

60. Mr Wood produced evidence of expenditure he had incurred on premises for Asgard and it is clear that these were entirely inconsistent with Asgard being simply a shell to be used as part of a sham. It is true that the premises might have been used for other purposes even if the transactions involved in this appeal were shams but the expenditure goes some way to indicating an intention on the part of Mr Wood to trade legitimately. The goods in question were also moved to Asgard's premises. That too is consistent with genuine trading as otherwise it would appear it would have been

easier for all concerned if the hose had simply gone straight from VPS's premises to the UAE with Asgard simply acting as a paperwork processor.

61. Mr Wood admits that he knew from the outset that another company was also supplying hose to the UAE sourced from VPS. It later became apparent that was Formel E. HMRC appear to think this suspicious though we do not see why it should be thought to be so. Mr Wood produced a letter from an area sales manager of Univar which describes that company as Europe's largest chemical distributor which and in which the manager states that it is common practice for customers to want more than one source of supply in order to minimise the risks of price fixing and to avoid a situation where a sole supplier can dictate more onerous terms that would be the case where more than one supplier is involved.

The questions about the quality of the hose.

62. Soon after the hose was delivered to Asgard and exported to the UAE it became apparent that there were serious issues about its quality. At first it seemed only that the boxes in which it was delivered were defective but it then became clear that Tazar was contending that the hose was not fit for its purpose and was defective. These issues also affected the supplies to Formel E and the issues arose before the kidnapping of Mr Wood and Mr Langhorne.

63. Mr Wood made efforts to resolve these issues including travelling to the UAE on 14 October 2002 and 2 November 2002. There is no doubt that he made these trips as he produced his passport which had been stamped by the UAE authorities. On those occasions he said that he negotiated with Mr Nazar Omer and Mr Sam George who were representing Tazar. Negotiations were about the quality issues concerning the hose.

64. Both Mr Wood and Mr Langhorne gave evidence that when Mr Wood made these trips to the UAE he was acting on behalf of both Asgard and Formel E. We find that Mr Wood's purpose in visiting the UAE was to try to resolve the quality issues relating to the hose.

65. Mr Terrell, in his fourth witness statement, referred to various documents produced by Mr Wood and Mr Langhorne which they contended proved that the quality issues were genuine disputes. Mr Terrell then contended that "if this entire scenario … was simply a means to commit fraud" then the documents were "exactly what [he] would expect to see because there was to be no payment for the goods and the manufactured dispute would excuse this whilst still allowing VAT repayment claims to be made". It may be true that Mr Terrell would expect that but the argument is circular.

66. In particular we hold that Mr Wood's trips to the UAE are consistent with the contention that Tazar was asserting that there were defects in the hose and that he was making genuine efforts to resolve the issues that had arisen. Of course we have no way of knowing whether there were actual defects in the hose but Mr Wood's trips to the UAE are consistent with his believing that there was a genuine issue. That is also

inconsistent with the case put forward by HMRC that these transactions were entirely sham transactions and that Mr Wood knew that to be the case. Had Mr Wood known that these transactions were shams it is inherently unlikely that he would have incurred the trouble and expense of travelling twice to the UAE.

67. In that context it is worth noting that the documents about the quality issue had been raised by Tazar on 1July 2002 (concerning the packing) and 30 September 2002 (so far as the performance of the hose itself was concerned). Those issues were therefore raised well before Mr Terrell began his investigation in January 2003 and before officer Adams uplifted Asgard's documents on 29 October 2002. In other words the documents raising the quality issue pre-date the earliest date on which Mr Wood could be said to be aware that HMRC were investigating.

68. Whether or not the uplifting of the documents could have alerted Mr Wood to the fact that an investigation was under way is a matter of conjecture but subsequent events point to his having had no inkling that was the case.

69. Mr Wood's first visit to the UAE predated the uplifting of the documents. That is significant evidence to suggest that the trips to the UAE were genuine attempts to resolve the quality issues.

70. Those facts are at least consistent with the appellant's case that there was a genuine dispute which supports his case that the transactions, at least looked at from his point of view, were apparently genuine.

71. Mr Wood produced evidence in the form of notes and in some cases faxes sent to HMRC which showed that up to 16 January 2003 he was dealing with various HMRC offices chasing the repayment of input tax which had been claimed and submitting a duplicate return for the November 2002 period. He said that he had not been invited to the interview which took place on 22 January until after the 16 January as he would not have been pursuing the claim in the way he was up to as late as 16 January had he by then known he would be attending the interview on 22 January.

72. Even after the interview it seems Mr Wood would not have thought that he was under investigation because, as HMRC admit, it was initially their view that the transactions were fraudulent so far as Thompson was concerned but not so far as Mr Wood was concerned. They took a different view only after Kappler had become involved and made the allegations he made in early March 2003.

73. The importance of the timings is that we find that the question of the quality of the hose arose before Mr Wood had any reason to think HMRC were investigating the transactions in any other than a routine way. He took significant steps to try to satisfy the purchaser and to resolve the issues about the quality; also before HMRC had indicated any intention to investigate. Those steps involved the expenditure of money and time. Those actions are, we find, entirely inconsistent with the allegation that Mr Wood was involved in transactions he knew to be fraudulent or a sham. Had the transactions been known by Mr Wood to be a sham then he would not have taken these steps at least not before he knew HMRC were investigating. Had he taken these

steps only after he knew HMRC were investigating, that might have been an indication that he knew the transactions were shams but that is not what happened. We have in mind that, if these steps had only been taken after HMRC made it known they were investigating, it might have been said that the steps were just being taken to convince them that there was an innocent explanation but that is not what happened.

The investigation.

74. At the interview on 22 January it seems very clear that HMRC were viewing Mr Wood as an innocent party. Mr Terrell said "you have given me answers to all the questions I've given you. You have co-operated fully".

75. It is significant that after the interview HMRC had proposed the part payment we have already referred to at paragraph 23 above. That proposal was made on 4 February 2003. If it is supposed that Mr Wood was in fact aware that the transactions were fraudulent, as HMRC allege, and given that it was clear that Mr Thompson was under investigation, as we find was clear from the interview; then it might have been expected that Mr Wood would have been only too happy to have received part of the input tax rather than to risk the investigation continuing or being extended to include him. Indeed if the transactions had been wholly a sham as HMRC allege and that Mr Wood knew that and the goods were worth only a fraction of what they were purported to be worth, which HMRC also allege Mr Wood knew; then agreement to accept part payment of input tax, which would have ended the enquiries, would have been affordable as well as tempting from Mr Wood's point of view.

76. His taking advice from Mr Braim, the consultant, followed by a rejection of the offer of part payment is at least consistent with Mr Wood's innocence if not actually indicative of it.

Financial transactions between Asgard and other relevant parties.

77. Asgard bought a product called masterbatch from VPS and sold it to Tazar but after the quality issues arose about the hose, Tazar refused to pay for the masterbatch. Mr Terrell claims that was not credible because there was no issue about the quality of the masterbatch. We do not agree. Clearly a claim of defective supply over one product may result in a refusal to pay for another where the recipient of the defective goods feels it has a claim against the supplier and may assert it need not pay for the non-defective goods as some sort of set off, whether or not a set off was allowable in the strict letter of the law. The supplies of masterbatch are largely irrelevant to this case though their existence does potentially indicate some evidence that, contrary to what HMRC contend, Asgard was not set up solely for the purpose of a scam relating to the hose.

78. HMRC also contend that it was significant that Tazar paid Asgard £96,670 for some of the hose, contrary to the terms of the agreement which, as already mentioned, were that payment was only due after the hose had been installed. HMRC also allege that the payment Tazar made was in fact financed by VPS through a chain of third parties.

79. Mr Wood explained that, even if it was the case, he was unaware that VPS had indirectly funded Tazar's payment to Asgard. No evidence was called to suggest that he did know that. He also claimed that the Cleveland police had investigated the funding of VPS. He produced a letter from Cleveland police which said that no suspicious financial transactions were found to have been undertaken by Asgard.

80. After the trial of Kappler HMRC reported to the Criminal Injuries Compensation Authority the fraud the prosecution had admitted at the Kappler trial and said to have been committed by Mr Wood and Mr Langhorne. Mr Wood said this prompted the Cleveland police to investigate again but they told Mr Wood they would be taking no action.

81. We find that although the actual reason why Tazar paid Asgard £96,670 is unclear there is no reason to conclude that the payment or its acceptance by Mr Wood and Asgard was suspicious from their point of view and so it was not evidence that Mr Wood knew about any VAT fraud.

82. Other payments to VPS by Asgard were repayments of a loan from that company and we do not regard it as suspicious, at least looked at from Mr Wood's point of view, that VPS was willing to lend money to Asgard. We have already explained that Mr Wood was given what he believed to be a true account of why VPS and Thompson wanted him to go into business with VPS and that involved setting up Asgard. In addition, Mr Wood said he believed Thompson to be a very wealthy man. Whether Thomson was very wealthy of not we cannot say but we believed Mr Wood's evidence on that point and find it credible that he would not have been suspicious about Thompson's willingness to lend money through VPS to fund the setting up of Asgard.

83. Payments to VPS should be seen in that light and at least some of them were repayments relating to the loans. Some payments were also due for masterbatch supplies and they were apparently not subject to the term that they were only payable after Tazar had paid Asgard.

84. Payments to a factoring company acting on behalf of VPS were made by Asgard while other payments were made direct to VPS which probably should also have been made to the factoring company. We heard evidence about this from Gillian Ellis of Bibby Factors. Although a careful reading of the documents by someone more familiar with legal and accounting practices than Mr Wood might have alerted the reader to the fact that VPS were seeking payments that should have been made to the factoring company, we find that Mr Wood made the payments to the wrong entity innocently.

SA Holdings.

85. Mr Wood and Mr Langhorne were involved in setting up a company called SA Holdings after the transactions with which this appeal is concerned had occurred. That company in fact failed because both of them were too traumatised by the

kidnapping to be able to attend to business activities. In fact they had to go into hiding with their families to safe houses for some time.

86. Steps had been taken to do market research at some cost to Mr Wood and Mr Langhorne in connection with the setting up of SA Holdings and we find that it was a genuine enterprise.

87. The relevance to this case is that it was alleged that they had used it as a means sending the money they had received from HMRC by way of input tax repayments to Dubai in circumstances where they would then not be in a position to pay VPS for the hose even if Tazar eventually did pay for it.

88. The issues about the quality of the hose had certainly put it in doubt whether Asgard would ever be paid and therefore whether it would ever be in a position to pay VPS and certainly one consequence of that would have been that VPS would not have been able to pay its output tax. In principle, unless the fraud had been proved that would not have been Mr Wood's responsibility. Eventually what should probably have happened would have been the issue of credit notes and a cancellation or fundamental re-assessment of the VAT position of both Asgard and VPS but that never happened because of the trauma associated with the kidnapping.

89. Mr Wood lost all the money he had put into SA Holdings and his evidence was that in effect he does not know exactly what happened to it but it seems probable from what he does know that Thompson and his associates in Dubai managed to take it. We find Mr Wood's evidence is truthful on these points – that is to say we find that he truly believes that is what happened to the money and certainly that he has not had the benefit of any of it.

90. We find that at the time Mr Wood was involved in setting up SA Holdings it simply did not occur to him that doing so would have any effect on the VAT position and that subsequently the failure to re-order the VAT position of Asgard became impossible as both Asgard and SA Holdings had collapsed as a result of the fraud of Thompson and the trauma post the kidnap.

Our conclusions.

91. We have found that the respondents' case fails so far as the allegation of under-valuation is concerned and we repeat that even if the valuation had been found to be exaggerated we also find that Mr Wood was not aware of that fact.

92. We have found that Mr Wood was given and genuinely believed the reason why his company was involved in the transactions even though he knew that Thompson had some sort of proprietorial interest in Tazar.

93. We have found that the Mr Wood took steps which were inconsistent with the allegation that the transactions were shams or similar or at least were inconsistent with his knowing they were shams or similar.

94. We have found that Mr Wood's actions after the transactions went wrong were consistent with his being honest and indeed were inconsistent with his being dishonest.

95. On those grounds we find that HMRC have not proved the necessary dishonesty. Considering all the evidence we have reached a positive conclusion that Mr Wood was not dishonest. Our decision is not based only on a failure by HMRC to prove dishonesty.

96. We acknowledge that it can be dangerous for a fact finding tribunal to base its decision only on an impression about a witness's truthfulness but we would add that having observed Mr Wood giving evidence and being cross examined rigorously and at times aggressively we have formed the following conclusions. Mr Wood has a genuinely held sense of grievance about how he has been treated by Thompson and his associates in Dubai. The manner in which he gave evidence over a number of days further convinced us that he had not acted dishonestly and the genuine sense of grievance forms part of what we found convincing about his evidence. He also feels a sense of grievance about how HMRC have treated him. Whilst we do not necessarily agree with all he complains about, the genuineness of that sense of grievance is also supportive of our conclusion that he had not acted dishonestly. If Mr Wood had been dishonest we would not have found it likely he could have kept up the pretence of genuine grievance through such a long cross examination.

97. This document contains full findings of fact and reasons for the decision. Any party dissatisfied with this decision has a right to apply for permission to appeal against it pursuant to Rule 39 of the Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules 2009. The application must be received by this Tribunal not later than 56 days after this decision is sent to that party. The parties are referred to "Guidance to accompany a Decision from the First-tier Tribunal (Tax Chamber)" which accompanies and forms part of this decision notice.

RICHARD BARLOW
TRIBUNAL JUDGE

RELEASE DATE: 27 May 2014