TC04239

Appeal number: LON/2008/00429

VALUE ADDED TAX – Denial of input tax recovery as said to be connected with fraud – Whether properly denied - On facts neither, actual knowledge of fraud or only reasonable explanation of taxpayer's transactions shown by HMRC who had onus – Appeal allowed

FIRST-TIER TRIBUNAL
TAX CHAMBER

PACIFIC COMPUTERS LTD **Appellant**

- and -

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

TRIBUNAL: **JUDGE ADRIAN SHIPWRIGHT**

MRS SUSAN LOUSADA

Sitting in public at The Mayor and City of London Court, Basinghall Street, EC1V 5AR on 20-24, 27 - 31 January and 3 - 4 February 2014

Alistair Webster QC for the Appellant instructed by Litigaid Law

Christopher Foulkes, Counsel and Howard Watkinson, Counsel, instructed by the General Counsel and Solicitor to HM Revenue and Customs, for the Respondents

DECISION

Introduction

1. This decision concerns an appeal by Pacific Computers Limited ("the Taxpayer") against the denial of VAT input tax recovery to the Taxpayer by the Respondents ("HMRC") for the period 09/06.

2. This decision was notified by letter dated 13 February 2008 ("the Decision Letter"). The denial of input tax deduction, according to the Decision Letter, was because HMRC were "… satisfied that the transactions … formed part of an overall scheme to defraud the Revenue" and the Taxpayer knew or should have known of this.

3. The amount of input tax denied deduction was £428,525.74. It related to the input VAT for the Period 09/06. It is the denial of input tax recovery for this period alone that is the issue before us. We are not concerned with the position of input tax recovery in other periods as that is not the subject of the appeal before us.

Procedural Matters

4. The Parties wished to make their closing submissions in writing. We agreed to this.

5. HMRC asked for a period of six weeks to do this. This was, in part, we were told because of Court commitments. The Taxpayer did not object in the circumstances and we set out a timetable with which the Parties agreed.

6. This provided that HMRC's written closing submissions were to be provided by March 11 2014. The Taxpayer's closing submissions were to be provided by 19 March 2014. The Taxpayer's submissions were received on time.

7. The underlying rationale to this was that as it was the Taxpayer's appeal the Taxpayer should also have the last word[1].

8. The Respondents produced a closing submission of about 116 pages. It was wide ranging and much of it did not go to the essential issue in this case namely whether the test in *Mobilix* that the only reasonable explanation for the transaction in which the taxpayer was involved was connected to fraud bearing in mind the taxpayer's knowledge at the relevant time was satisfied. Much of it related to matters which were outside HMRC's knowledge let alone the Taxpayer's knowledge at the time in question. Much of it was not of assistance to the Tribunal. The Tribunal reread the document carefully a number of times before reaching this conclusion.

9. The Taxpayer submitted its helpful closing submissions which were to the point, of a sensible length within time.

10. HMRC then took it upon itself to submit a further set of submissions allegedly in reply to the Taxpayer's closing submissions which had been produced and filed in accordance with what the Tribunal had directed. These further HMRC submissions were of some considerable length. HMRC did this without informing the Tribunal or seeking leave to do so notwithstanding what had been said on the last day of the hearing and the usual way of proceeding. It being the Taxpayer's appeal the Taxpayer should have the last word.

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[1] See Transcript Tuesday, 4 February 2014 JUDGE SHIPWRIGHT page 32
[4.] I think that is something where normally the
[5] appellant would have the last word, and that is why one
[6] would start off here by saying that you make your
[7] closing submissions and the appellant replies to them.
[8] If you want to make further submissions then I think
[9] that needs to be a matter for leave….
[18] JUDGE SHIPWRIGHT: No, I think we will leave it as there is
[19] leave to ask to add further submissions but you have had
[20] your chance to make submissions and the written
[21] submissions will be there.

11. The Taxpayer, unsurprisingly, objected to this course of action taken by HMRC and filed a Notice of Objection dated 16 April 2014. However, the parties later agreed the original HMRC further submissions could be admitted provided the Taxpayer could have the last word if it wished and make the final submissions. The Tribunal in order to deal with this directed that:

"[1] The Respondents further submissions be admitted in the form that they were first sent to the Tribunal but with no amendments, additions or other variations.

[2} The Appellant has leave to submit such further representations, if any, in response to Respondents' submissions within 28 days of the issue of this direction.

[3] That no further submissions or applications of whatsoever nature whether relating to closing submissions or otherwise shall be made in this matter unless the prior written permission of the Tribunal (preferably as presently constituted) has been obtained.

[4] The Tribunal reserves to itself the issue of the costs occasioned by these further submissions and may if it considers it appropriate ask for further submissions as it sees fit but for the avoidance of doubt Direction 3 applies to this Direction 4".

12. This direction was issued in May 2014.

13. The Taxpayer submitted a document in response to the second set of closing submissions from HMRC. As Mr. Webster QC said "… The necessity for [his further closing submissions] and the consequential costs entailed is regretted". At eight pages these were considerably more focussed and of greater utility than the somewhat unfocused HMRC document.

14. The Taxpayer's document was dated 10 June 2014 and was short, to the point and helpful. It is not necessary to draw any contrast with the long unfocussed documents from HMRC which even after a number of readings we found not to be of any great utility.

15. These procedural matters have not led to the expedition of the disposal of this appeal. This is to be regretted It would have helped if HMRC had complied with the agreed normal procedure rather than trying seemingly to seek to obtain an advantage by not complying with it. The Tribunal has a duty to provide a fair trial and it is for this reason that certain norms are required to be observed. It is a pity HMRC did not assist with this.

16. We record these matters as we feel we have to do so, so that the appeal can be seen in its proper context and full information is available to any higher tribunal or court.

17. We have carefully considered our decision both on this point and generally to make sure that we have been fair to all the parties notwithstanding any procedural wrangles etc. We consider that we have achieved this. In all of this we have particularly borne in mind Article 6 of the Human Rights Convention concerning the right to a fair trial. We have sought to achieve this in all the circumstances bearing in mind that the trial should be fair to all the parties.

Common Ground

18. It was common ground between the parties that:
    - 18.1. The chains in the deals in question had been established;
    - 18.2. There was tax loss in the chains; and
    - 18.3. The tax loss was caused by fraud.

19. It was not disputed that, in broad terms, the Taxpayer's officers were aware of the existence of MTIC and carousel frauds and their relevance to the VAT system. It was disputed that they knew or ought to have known of the connection to fraud in the particular circumstances under consideration here.

20. It was not disputed that the deals were "back to back" in the sense that they were arranged to take place (in the sense of close or complete) essentially on the same day. The significance of this was a matter of dispute.

21. It was accepted that on some occasions payment lagged release of the goods in question. Again the significance of this was a matter of dispute.

The Issue

22. In essence, the issue in this case is whether or not the input deduction was correctly denied.

23. This requires a number of questions to be considered including the following.

23.1. Did the Taxpayer know that the Taxpayer's transactions had been or would be connected to fraud? Was there actual knowledge of fraud on the Taxpayer's part?

23.2. Should the Taxpayer have known that the only reasonable explanation for the transaction in which the Taxpayer was involved was that the transaction was connected to fraud? (See *Mobilix* [59] and *Else* UTT [20]). Was there imputed knowledge on the basis of *Mobilix*?

24. In both questions the onus of proof is on HMRC (cf. *Mobilix* at [81]). This onus is on the civil standard of proof i.e. the balance of probabilities.

25. HMRC considered that the transactions in the period 06/06 "… were connected with fraudulent evasion of VAT and took place as part of an orchestrated scheme to defraud the Revenue". However, HMRC did not deny input tax recovery on those deals and that period is not in issue before us. There was no evidence before us to stand up HMRC's assertion. Accordingly, we did not consider it further.

26. This decision is solely concerned with the denial of input tax recovery to the Taxpayer for the period 09/06. This was the subject matter of the appeal before us.

Abbreviations and Dramatis Personae

27. The following abbreviations and references to persons are used in this decision but as ever are subject to the requirements of the context.

27.1. "Allblast"	Allblast ApS, a Danish incorporated Company involved in the chains
27.2. "Andrew Miles"	Andrew Miles who was a director of the Taxpayer and is still a 30% shareholder of the Taxpayer and was and is a director of Taran – sometimes referred to as Mr Miles
27.3. "Astontek"	Astontek Ltd, a company incorporated in the UK involved in the chains
27.4. "CPU"	Computer Processing Units
27.5. "the Decision Letter"	the decision letter referred to in paragraph 2
27.6. "Doktor Ring"	Doktor-Ring Telecom Gmbh, a German incorporated company involved in the chains
27.7. "Forward Logistics"	Forward Logistics Limited , a company incorporated in the UK which acted as a freight forwarder
27.8. "Mr Donaldson"	Richard Donaldson a director of the Taxpayer company who was also the company secretary
27.9. "Mr Hall"	Andrew Hall, known as the Finance Director of the Taxpayer and at the relevant times not a shareholder in the Taxpayer
27.10. "HMRC"	the Respondent
27.11. "Jet Set Go"	Jet Set Go Limited, a company incorporated in UK involved in the chains
27.12. "JM Technology Systems"	JM Technology Systems Limited a Maltese incorporated company operating out of Rotterdam involved in the chains

27.13. "Masterpiece Technology"	Masterpiece Technology Limited, a company incorporated in UK involved in the chains
27.14. "Simon Miles"	Simon Miles, the brother of Andrew Miles who was a 10% shareholder in the Taxpayer
27.15. "MITT"	MITT (Rotterdam) BV, a Dutch freight forwarder
27.16. "MTIC"	Missing Trader Intra Community Fraud
27.17. "Mr. Mushtaq"	Imitiaz Mushtaq, the principal of Plazadome
27.18. "Plazadome"	Plazadome Limited, a company incorporated in the UK involved in the chains as the supplier on most occasions to PCL
27.19. "Mr Roach"	Marc [Marcus] Roach, the Managing Director of the Taxpayer and a 30% Shareholder in the Taxpayer
27.20. "Simpletech"	Simpletech Limited, a company incorporated in the UK involved in the chains
27.21. "Taran"	Taran Microsystems Limited, a company incorporated in England of which Andrew Miles was director and shareholder which had assisted PCL when it started up
27.22. "the Taxpayer"	Pacific Computers Limited, a company incorporated in England and sometimes referred to as "PCL"
27.23. "Tech Comp"	Tech Comp Limited a company incorporated in the UK involved in the chains
27.24. "Theresa Ching"	a person whom Mr. Donaldson had known for a number of years who was connected to Zaanstrait. She was also known to Mr. Roach
27.25. "UMBS"	United Mercantile Building Society, a Swedish "Building Society" which provided banking services to some of those involved here. PCL sought to open an account there to speed payment but the opening of the account was not completed and PCL did not have an account there
27.26. "Zaanstrait"	Zaanstrait BV, a company incorporated in The Netherlands with which Theresa Ching was connected

The Law

Statute etc.

28. The law in this area derives from the VAT Directive. It is currently set out in Title X of the 2006 Directive (28 November 2006). At the time of the transactions in question by PCL it was found in Title XI of the Sixth Directive (77/338EEC).

29. Title X of the 2006 Directive is not supposed to have changed the position and so far as is relevant reads:

"Article 167

A right of deduction shall arise at the time the deductible tax becomes chargeable.
Article 168
In so far as the goods and services are used for the purposes of the taxed transactions of a taxable person, the taxable person shall be entitled, in the Member State in which he carries out these transactions, to deduct the following from the VAT which he is liable to pay:
(a) the VAT due or paid in that Member State in respect of supplies to him of goods or services, carried out or to be carried out by another taxable person;
(b) the VAT due in respect of transactions treated as supplies of goods or services pursuant to Article 18(a) and Article 27;
(c) the VAT due in respect of intra-Community acquisitions of goods pursuant to Article 2(1) (b) (i);
(d) the VAT due on transactions treated as intra-Community acquisitions in accordance with Articles 21 and 22;
(e) the VAT due or paid in respect of the importation of goods into that Member State".

30. The UK statutory provisions are found mainly in sections 24 to 26 VATA and Regulation 29 of the VAT Regulations 1995.

31. Section 24 VATA provides:

"24. (1) Subject to the following provisions of this section, "input tax", in relation to a taxable person, means the following tax, that is to say—
(a) VAT on the supply to him of any goods or services;
(b) VAT on the acquisition by him from another member State of any goods; and
(c) VAT paid or payable by him on the importation of any goods from a place outside the member States, being (in each case) goods or services used or to be used for the purpose of any business carried on or to be carried on by him…
(6) Regulations may provide—
(a) for VAT on the supply of goods or services to a taxable person, VAT on the acquisition of goods by a taxable person from other member States and VAT paid or payable by a taxable person on the importation of goods from places outside the member States to be treated as his input tax only if and to the extent that the charge to VAT is evidenced and quantified by reference to such documents as may be specified in the regulations or the Commissioners may direct either generally or in particular cases or classes of cases;..."

32. Section 25 VATA provides:

"25. (1) A taxable person shall—
(a) in respect of supplies made by him, and
(b) in respect of the acquisition by him from other member States of any goods, account for and pay VAT by reference to such periods (in this Act referred to as "prescribed accounting periods") at such time and in such manner as may be determined by or under regulations and regulations may make different provision for different circumstances.
(2) Subject to the provisions of this section, he is entitled at the end of each prescribed accounting period to credit for so much of his input tax as is allowable under section 26, and then to deduct that amount from any output tax that is due from him.

33. Section 26 VATA provides:

"26. (1) The amount of input tax for which a taxable person is entitled to credit at the end of any period shall be so much of the input tax for the period (that is input tax on supplies, acquisitions and importations in the period) as is allowable by or under regulations as being attributable to supplies within subsection (2) below".

34. Regulation 29 of the VAT Regulations 1995 provides:

"29. (1) Subject to paragraph (2) below, and save as the Commissioners may otherwise allow or direct either generally or specially, a person claiming deduction of input tax under section

25(2) of the Act shall do so on a return made by him for the prescribed accounting period in which the VAT became chargeable.

(2) At the time of claiming deduction of input tax in accordance with paragraph (1) above, a person shall, if the claim is in respect of—

(a) a supply from another taxable person, hold the document which is required to be provided under regulation 13;…

provided that where the Commissioners so direct, either generally or in relation to particular cases or classes of cases, a claimant shall hold, instead of the document or invoice (as the case may require) specified in sub-paragraph 30 (a)… above, such other documentary evidence of the charge to VAT as the Commissioners may direct".

Case Law

35. We were provided with copies of the decisions in a number of cases all of which we have read and carefully considered. These included the following.

(a) Kittel v Belgium (Case C-439/04) Belgium v Recolta Recycling SPRL (Case C-440/04) [2006] All ER (D) 69 (Jul)

(b) HMRC v Moblix Ltd & Others [2010] EWCA Civ 517

(c)Maghageben kft and Peter David v Nemzett Ado-es Vamhivatal Deldudantuli Regonalis Ado Foigazatosaga (C-80/11 & C-141/11)

(d) Order of the Court (Tenth Chamber) of 16 May 2013 Hardimpex kft v Nemzeti AdoC-444/12

(e)Busseni Spa (C-221/88)

(f) Bruno & others (C-396/08)

(g) Gabor Toth v Nemzeti Ado (C-324/11)

(h) LVK-56 EOOD v Direktor (C643/11)

(i) Order of the Court (Fifth Chamber) of 28 February 2013 Forvards V SLA v Valsts ienemumme Case C-563/11

(j) Else Refining and Recycling Ltd v Revenue & Customs [2012] UKFTT 470

(k) JDI Trading Ltd v Revenue & Customs [2012] UK FTT 642

The Evidence

36. We were provided with 32 volumes of documents etc. These were agreed bundles. No objection was taken to any of the documents in the bundle and they were all admitted in evidence.

37. We heard oral evidence from the following witnesses:

37.1. Officer Victor Cumberbatch;
37.2. Officer Deborah Janet Toynbee;
37.3. Richard Donaldson;
37.4. Marc Roach;
37.5. Andrew Hall;
37.6. Leighton Birtchnell;
37.7. Dr Kevin Findlay;
37.8. Roderick Stone;
37.9. Vivien Barbara Parsons.

38. Witness statements were provided for these witnesses who were cross examined.

39. The Bundle included a number of other witness statements. In particular, these were from:

39.1. Officer Michael Clarke;
39.2. Officer Peter Dean;
39.3. Officer Downer.

40. Only the persons listed at 37 above gave oral evidence. The other persons providing witness statements did not nor were they cross examined. It is hard to decide what weight to

give to evidence that has not been tested by cross examination. Unless corroborated in some way or accepted by the parties we have not generally given such evidence great weight.

The Witnesses and their evidence

41. As this case is very much a fact dependent one we consider it would be useful to set out what we made of the witnesses we heard and their evidence. This is not intended to be critical but to assist in setting out in general terms what we made of the witnesses, how they gave evidence and what we made of what they said and asserted.

42. Much (indeed most) of the hearing was taken up with witness evidence[2]. The witnesses were cross examined. In the case of the Appellant's witnesses this was for a considerable time and on some topics whose relevance was not always pellucid. At times in the case of HMRC this bordered on the limits of what some might consider acceptable. We have concluded that those limits though were not actually crossed. However, it is important to record this to put matters in context.

43. This meant we were able to observe the witnesses closely when they were under challenge. The effect of that was that we were in a very good position carefully to consider their evidence and how it was given and what weight to give to it. We have carefully considered these aspects amongst others in reaching our conclusions. The Appellant's witnesses came through this very well which served to enhance their credibility and give greater credence to what they said. The way HMRC dealt with them enhanced this which was possibly not HMRC's intention.

44. We find, having seen them giving evidence, the Taxpayer's witnesses to be credible and reliable and honest in the evidence they gave. We accept their evidence and in the case of any conflict with other evidence we prefer it. It was not discredited in the course of cross examination. Such inconsistencies as emerged only went to reinforce our view on credibility and reliability. This is hard to put into clear words but essentially comes from having the benefit of both of us having seen and heard them particularly when being cross examined. We consider that they were not delivering a story made up after the event to account for what went on but trying to help the Tribunal by telling the truth. In any case of a conflict of evidence, as noted above, we prefer the evidence of the Appellant's witnesses.

45. We have carefully considered this position and what to put in this decision before doing so in order to be clear as to what we made of the witnesses. It is done on the basis of careful and sober reflection and consideration to assist the parties and any higher Court or Tribunal should this go any further. Any such body should be only too aware of the impression we formed of the Appellant's witnesses and why we believed their evidence. They came across, albeit with different personalities, as people who were trying to run their business sensibly and commercially and during this hearing trying to assist the Tribunal to the best of their ability. They did so in a calm, reflective and polite way whilst displaying realism, honesty and acceptance of the need to assist the Tribunal even when pushed extremely hard in cross examination. As noted above we found the Taxpayer's witnesses credible and reliable and honest in the evidence they gave.

46. HMRC's witnesses did not assist us much. Officer Cumberbatch had the difficulty that his decision letter did not really survive scrutiny and that he had failed to notice the terms on the back of standard forms. His explanation for this was not convincing and is not accepted. If (which was not shown to be the case as we specifically find) someone higher up in HMRC was tempted to utter an oath in this respect on hearing the explanation we could fully understand and empathise. The rest of his evidence was aimed more at tax loss in the chain caused by fraud. This was not a matter of dispute but common ground between the parties. He showed little commercial awareness and knowledge which meant his comments on such matters whilst

[2] Hence the need for written submissions.

interesting could not carry the weight of an acknowledged and informed expert. It was thus hard to give his evidence any considerable weight. It was not put forward as expert evidence.

47. The other HMRC witnesses were of a different calibre. However, they were concerned with matters at a much higher level and in Dr Findlay's case with information not available at the time of the transactions and which, as he said, surprised him when it came to light.

48. The existence of the Grey Market was not a matter of dispute between the parties. Its extent and how far this was known at the relevant time was a matter of dispute. However, later work done on information not generally available at the relevant time and not available to the Taxpayer or its witnesses was not particularly illuminating in considering whether at the relevant time the only reasonable explanation for the Taxpayer's transactions was fraud.

49. Hindsight is often valuable but not as here in deciding whether at the time of the transactions the only reasonable explanation for the Taxpayer's transactions was fraud whether on an objective or subjective basis. We reach our conclusion accepting that Notice 726 on the technically different issue of joint and several liability had been issued and seen by the Taxpayer and that the Taxpayer accepted that there was fraud in the market place. We accept that the Taxpayer was trying to protect itself from fraud and used what means it could to do so including the limited matters provided by HMRC. Again we found the Appellant's witnesses' evidence of considerable assistance and to be credible and reliable and to the extent we can we do so as a matter of fact. If necessary this should be treated as repeated in findings of fact.

Findings of Fact

50. From the evidence we make the following findings of fact.

Pacific Computers Limited – The Taxpayer

51. The Taxpayer company was incorporated on 16 October, 1996.

52. Its objects included:

(a) "To carry on the business of selling computer hardware, software and service; to carry on as stockists, agents, wholesalers, retailers, hirers, leasers, importers and exporters of computers, computer software, computer peripherals and ancillary equipment, computer components, media and ancillary and allied equipment; …

(b) To act as manufacturers, dealers, stockists, agents, wholesalers, retailers, hirers, leasers, importers and exporters and consultants for all manner of electronic products …"

No point was taken on this by the parties.

53. The shareholdings in the company were as follows

Name	**Percentage**	**Comment**
Andrew Miles	30	was a director from 1997 but ceased to be in 2000 but retained shareholding
Marc Roach	30	director from 16 June 1997 to date
Simon Miles	30/10	later reduced to 10 per cent was a director from 1997 but ceased to be in 2001

Richard Donaldson	30	shareholder from 2000 director from 16 June 1997

54. Mr Hall was called a director but was not a shareholder at the relevant times He was responsible for the management of financial accounts and related matters.

55. The company had the ability to purchase in its own shares (see Article 7).

Taran

56. Taran was incorporated under the name Pointdown Limited on 30 September 1992.

57. Andrew Miles was a director of Taran and a shareholder.

58. He had allowed PCL to share his premises in the past through Taran but did not do so at time of transactions in question.

59. Taran had also allowed PCL to undertake "profit invoicing" using Taran's facilities etc. Taran allowed PCL to use its facilities, premises, database etc. in return for some of PCL's profit rather than fixed charges when PCL was starting up. This was not the arrangement at the time of the relevant transactions. It had been discontinued some time before.

60. On 14 November 2003 HMRC Officers executed a search warrant at Taran. This related to MTIC. Others, not including Taran, were convicted of conspiracy to cheat the Revenue as a result of raids carried out at the same time. Taran and its officers were not involved in the conspiracy charges.

61. The Taxpayer's witnesses said they knew nothing of the search warrant and associated matters. We accept their evidence and find as a fact that the Taxpayer's witnesses knew nothing of the search warrant and associated matters. We reject HMRC's assertion that they must have known about it. We find it unsurprising that PCL knew nothing of it. We do so having considered carefully HMRC's arguments that this could not be the case. Even if PCL had known of the raid we do not see that anything else, without more, would follow.

62. Taran traded with PCL but as Mr Roach said this "… was nothing more than two companies in the IT sector engaged in legitimate trading that represented 1.6% of our turnover" in 2002-03.

63. We accept Mr Roach's evidence that "… in relation to Taran's alleged connection to MTIC fraud [this] was … not information that was known to [PCL] at the material time".

PCL's Business

64. The general business of the taxpayer started off assembling and selling bespoke computer systems and selling hard drives , CPU's, memory and motherboards. It was a well-established business.

65. PCL had undertaken some brokering in the past.

Turnover and the effect of Marc Roach's absence

66. The turnover of the company in the quarter 12/04 was £2.02m but fell to £1.4m for the quarter ending 09/05.

67. The directors' report for the year ended 31 December 2011 included the following: "The Directors have indicated the reason for the decline in turnover and profits for 2005 were principally due to the absence of Marc Roach (Managing Director) from the business between May and September 2005 to oversee the rebuild of his house. – due to the problems experienced with the building firm. However, since he returned, towards the end of 2005 and through 2006 to date, Pacific has experienced an upturn in both turnover and profits".

68. We do not accept that PCL was "a business in decline" as HMRC sought to suggest. There was a reduction in turnover during Mr Roach's absence. This was to be expected as was a lull

before recovery after his return. Either way it was a business with a turnover in excess of £1m per quarter, hardly a business in decline.

Mr Miles

69. Mr. Miles was involved at the start of the PCL business. He was and remains a 30% shareholder.

70. The PCL business used the premises of Taran (Mr. Miles' company) and its databases etc. when it started trading. PCL was given "a leg up" by Mr. Miles through Taran but was charged for the privilege. This was the profit invoicing noted above.

71. As PCL grew it moved to its own premises which are not far away from Taran. There were still contacts though between the two businesses. In 2000 PCL moved to Unit 62, a separate office from Taran and in early November 2006 PCL moved into a new office complex at its current location (Units 63-64).

72. Mr. Donaldson had been contacted by Theresa Ching about supplying Zaanstrait with computer related and electronic goods wholesale. However, he was unable to source these goods at a suitable price. Accordingly, he contacted Taran to see if they could help. At this stage to Taran was unable to sell the goods sought to PCL at a price which made it economic for PCL to deal.

73. Mr. Donaldson kept telephoning his contact at Taran seeking to progress matters. Mr. Miles considered that this was disruptive to Taran's business. Accordingly, he confronted Mr. Roach about it (seemingly whilst Mr Donaldson was on leave). In the course of this confrontation Mr. Miles gave the name of Plazadome to Mr. Roach. This was apparently to stop the alleged disruption to Taran's business. Mr Miles also gave the name of Tech Comp as a potential supplier.

74. This was the evidence before us. HMRC challenged this very strongly but were unable to shake the witnesses on any point on this matter. We accept the Taxpayer's evidence on this matter concerning the introduction to Plazadome and find this as a matter of fact and to the extent we can we find this as a primary fact. HMRC did not call Mr. Miles which they could have done but chose not to do so. We do not draw any inference from this as HMRC sought to do the other way round. We note this fact for the sake of completeness.

75. We accept the Taxpayer's version of how the introduction to Plazadome came about and reject HMRC's speculation about this and also reject HMRC's challenge to this evidence which HMRC failed to stand up.

76. As we have said before we found the taxpayers' witnesses honest and truthful and accept their evidence having had the benefit of seeing and hearing them particularly when under cross examination. We accept the taxpayers' evidence on this aspect.

77. Since Mr. Miles was a 30 per cent shareholder in PCL he could still have made money out of the transactions and through PCL whether or not there was an option to sell the shares at a fixed price (e.g. dividend, purchase of own shares , payments to pass a special resolution etc.) We reject HMRC's challenge to this.

78. We accept the Taxpayer's evidence as to its introduction to Plazadome. We find this as a fact and to the extent possible we find this as a primary fact.

79. In doing so we have carefully considered all the objections to this HMRC sought to raise. However, HMRC have not succeeded in their objections and we make these findings on the basis of the evidence before us. These findings also have the advantage of fitting into the rest of the surrounding factual matrix. We do not consider that this makes them a convenient after thought dreamt up by the Taxpayer and its witnesses. We find that this was not the case. Anyone who heard the evidence objectively would have reached the same conclusion.

PCL's business and further expansion

80. As noted above PCL's was a well-established business selling computer related goods and services.

81. PCL was approached by Zaanstrait about supplying goods.

82. In February 2006 Mr Donaldson received a number of inquiries for the supply of CPU from a long standing contact, Theresa Ching. She was then at Zaanstrait.

83. Mr Donaldson told Theresa Ching in response to her request that he would need to investigate her inquiry since much would depend on the type and quantity of CPU's required.

84. It was agreed that the individuals should meet up. Hence Mr Donaldson and Mr Roach's trip to the Netherlands.

85. The original contact was by phone and subsequent negotiations took place by phone.

86. Mr Donaldson had not been involved in the wholesale of CPUs before. Hence the approach to an account manager at Taran.

Funding the new business etc.

87. Mr. Roach was clear in his evidence that he did not want the funding of the new business to interfere with existing business. This is not to suggest these were separate trades. We accept this evidence and so find as a matter of fact.

88. Accordingly, PCL approached its bank, HSBC, for funding to undertake this new business. This was one of the big four UK High Street banks. It was not a bank in Curacao or anywhere else abroad. It is still in existence and operating as a bank.

89. PCL produced a business plan to support its application for the funding. The application was successful and the funding was provided by the bank. As noted above the bank was one of the big four banks with whom PCL already banked.

90. HMRC sought to make much of differences in what the business plan set out and what actually happened. Whilst these matters were interesting they do not show at this was part of a contrived fraud of which PCL knew or ought to have known.

91. Our understanding is that it is not unusual in business for matters in practical operation to differ from the prior theoretical planning stage.

92. Mr. Roach told us in his evidence, which we accept, he did not want the new business to exceed its funding. Accordingly, when the funding was used up in the preceding quarter and the relative input tax had not been repaid PCL stopped the new business until repayment of the input tax put it back in a position to trade in this area within its funding.

93. This does not show anything other than commerciality in what was done. In our view it shows a degree of commercial and financial prudence.

Mechanics of the new business

94. The new business needed to be run in an orderly way and a methodology developed to this. Mr Hall was charged with doing this.

95. This was an ongoing process. Mr Hall used checklists. He said this was a new business arrangement to him as he had not been involved in it in this way before.

"Checklists"

96. Mr. Hall produced an indicative "checklist" of what he thought would be needed to be done in the new business. He told us in his evidence, which we accept, that it was primarily for him and his use that the checklists were produced. They were intended to help him get all of the paperwork for a deal right. He told us and we accept this that he modified this as he went along to fit in with the practicalities of what PCL had to do in its new business. He also told us that he was responsible for the paperwork and that his colleagues were much more concerned with doing the deal than the niceties of some fine points of paperwork. We also accept this. Mr Roach agreed. He said he was not keen on doing paperwork by which we understood him to mean he preferred doing the deals etc. rather filling out forms. We believe him.

97. HMRC sought to make much of the "checklists" and how they had or had not been completed or dealt with. They were clearly not a complete or perfect record of what was

done. They were not intended to be. There were omissions and errors in them. We do not consider this unusual in a business context. They were working documents primarily for Mr. Hall's use. We do not consider that they were bits of paper designed for this case and to divert attention and we so find. To do that a more perfect set of documentation would surely have been produced. They were working documents. They were not complete records of everything done and that was never their intended function.

98. We reject HMRC's suggestions that these were a diversion or that they had not been dealt with properly. We find as a fact that the checklists were used for the purpose they were designed, which was to assist Mr Hall. We reject any suggestion to the contrary.

Bank accounts

99. PCL generally banked with a UK High Street bank (HSBC) from whom it obtained the finance to carry out the new business as we have found above.

100. PCL found that payments from some of its customers who used another financial institution took time to receive value in PCL's account.

101. This was in respect of payments from UMBS.

102. Accordingly PCL looked into having an account with this institution in the hope that it would speed up the receipt of payments. In the end it did not open an account.

HMRC visit to PCL 9 November 2006

103. Officers Cumberbatch and Toynbee visited PCL on 9 November 2006. They spoke to Mr Roach and Mr Hall.

104. Although much was made of this visit it did add clarity to the question for decision. The visit report is in the Bundle.

Plazadome

105. Plazadome was an English incorporated Company ostensibly carrying on business as a shop and as a wholesaler of electronics and computer related items.

106. It did so from premises which were understood to be essentially a shop with a large storage area behind.

107. Plazadome was introduced to PCL by Mr. Miles as we have already found.

108. The principal of Plazadome was Mr. Mushtaq.

109. Mr. Roach went to visit Mr. Mushtaq at Plazadome. Mr. Roach told us he considers himself to be a good judge of character and competence. He discussed relevant matters with Mr. Mushtaq and Mr Roach told us he found him very well informed and knowledgeable.

110. Having visited Mr. Mushtaq, Mr. Roach decided that PCL would buy from Plazadome. We have no reason to consider that this was not a genuine commercial decision. We find as a fact that it was a genuine commercial decision and to the extent possible we find this as a primary fact.

111. All the purchases relating to this side of the business in the period in question by PCL were from Plazadome.

112. PCL accepted that Plazadome was not an authorised Apple dealer. This is to be expected of someone dealing in the grey market. We did not find this remarkable as HMRC sought to suggest.

113. HMRC told us of the denial of input tax recovery to Plazadome and similar matters. There was no evidence before us to show that the denial of input tax recovery etc. to Plazadome was known to PCL at the relevant time(s). We find that this was not known to PCL at the relevant time and we do so as a matter of fact.

Zaanstrait

114. Zaanstrait was a Dutch company

115. Most of the sales by PCL in the period in question were to Zaanstrait.

116. Theresa Ching was at Zaanstrait at the time. We accept that it was inquiries from her that started this wholesaling element of the business.

Documentation etc.

117. PCL would receive enquiries about the supply of goods and then see whether it could match them.

118. If PCL could find goods which matched the buyer's requirements it would send a purchase order to the supplier. This was essentially Plazadome in the period in question as it could supply the goods at a price which made it economic for PCL to deal. This does not make what was done by PCL uncommercial or fraudulent.

119. PCL would then send sale documents to the buyer.

120. Terms and conditions were included in documentation. There could well have been a "Battle of Forms" but this is not unusual in business. Title to goods was to pass on payment. This did not mean that goods could not be shipped on hold i.e. before title had passed on full payment or released. This was a decision for the business which might well be an entrepreneurial one.

121. Whilst there may be some technical legal theoretical issues on the documents business is essentially a practical matter. "Ship on hold" essentially recognises this and we accept that this is a normal business risk. The risk of ship on hold was essentially the cost of returning the goods to the UK if a buyer in the country in question could not be found. This was not shown to be a disproportionate cost in a business context and we so find.

122. The various forms used by the various parties in the chain would doubtless say that title only passed on full payment and may or may not have had retention of title clauses in them. It is not uncommercial to "take a view" on a transaction nor does it make it associated with fraud.

Insurance

123.PCL had insurance which was not shown not actually to be in force nor that the goods in question were not covered and we so find.

The Goods and Inspection

124.The goods involved in the deals in question were CPUs and iPods ("the Goods").

125.Mr Birtchnell told us that during 2006 he and other members of the warehouse team carried out the visual inspection, counting and testing a number of consignments of CPU that had been delivered to PCL. This was under the direction of Mr Roach and Mr Hall.

126.On 10 May 2006 Mr Birtchnell drove to Feltham to carry out a visual inspection of a consignment of CPUs at Forward Logistics, the freight forwarder.

127.Mr Birtchnell found this a large and busy operation.

128. The checks were thorough during period 06/06 and carried out by PCL. They were not always carried out by PCL in the same way in the quarter in question PCL having got used to the way the business operated and what others could do.

129. We draw no adverse inferences from the way PCL dealt with inspections in period 09/06 and reject HMRC's suggestions to the contrary.

The Deals

130.The deals in question here are 13 of the 14 deals in the period 09/06.

131. Deal 27 is not a deal where input tax recovery was denied and explains why the appeal is actually only concerned with 13 deals. The following list is taken from HMRC's opening. It was not disputed.

Deal Number	Purchase Date	Supplier Name	Supplier Invoice Number	Product Name	Units	I/T Claim
15	04-Aug-06	Plazadome Ltd	8374	AMD 3800+ 64 Bit Dual Core	1440	£ 15, 876
16	08 August 2006	Plazadome Ltd	8378	Apple iPod White/Black	1195	£23, 840.
17	10 August 2006	Plazadome Ltd	8382	iPod Nano	1261	£34, 057.
18	15 August 2006	Plazadome Ltd	8388	iPods	1413	£28, 505.
			8389	iPods	993	£26, 815.
19	18 August 2006	Plazadome Ltd	8391	iPods	1957	£36, 045.
20	25 August 2006	Plazadome Ltd	8403	iPods	2155	£40, 918.
21	31 August 2006	Plazadome Ltd	8405	Intel P4 3.0GHz - SL7Z9	2205	£30, 870.
			8406	Intel P4 3.0GHz - SL7Z9	1260	£17, 640.
22	07 September 2006	Plazadome Ltd	8416	iPods	620	£11, 284.
23	08 September 2006	Plazadome Ltd	8418	iPods	1890	£27, 783.
			8420	iPods	945	£13, 891.
24	11 September 2006	Plazadome Ltd	8425	AMD 3500 CPU	4320	£29, 597.
			8426	AMD 3500 CPU	2400	£16, 443.
25	18 September 2006	Plazadome Ltd	8435	P4 3.0GHz - SL7Z9	1575	£23, 703.
26	20 September 2006	Plazadome Ltd	8441	P4 3.0GHz - SL7Z9	1575	£23, 428.
27	22 September 2006	Plazadome Ltd	8445	Intel P4 (RET)D945	505	£7, 158.3
28	25 September 2006	Plazadome Ltd	8447	Intel P4 D945	1000	£14, 350.
			8448	Intel P4 D930	1000	£13, 475.

Note: Deal 27 UK deal where input tax recovery is not in dispute

132. The 13 deals in question involved the same traders occupying the same "buffer" positions relative to the Taxpayer's "broker" position. In 12 of the deals JM Technical was the defaulter. The expressions "buffer" and "broker" are used here for convenience and do not signify that the person in that position was necessary involved in the MTIC fraud.

133. In chain 16 the defaulter was Jet Set Go.

134. We find that the deals were "back to back" deals in the sense that they were arranged essentially to take place on the same day but this does not of itself showed fraud or the means of knowledge of fraud. Many sales of residential property involve chains and all complete on

the same day. It certainly does not show that the only reasonable explanation for PCL's transactions was fraud.

135.HMRC say "the fact that… requirements could be instantly match suggests that the deals were artificially contrived". We note the use of the word "suggests". We do not consider HMRC have shown that "requirements could be instantly matched…" and we so find. Even if it had been shown we do not consider it would necessarily mean that the deals were artificially contrived on the Taxpayer's part or that the Taxpayer should have known of this. We reject HMRC's suggestion to the contrary.

The Decision Letter

136.The notification of the decision to deny input tax recovery was made by letter dated 13 February, 2008. This is the Decision Letter. The Decision Letter included the following matters:

137."… the Commissioners are satisfied that the transaction set out in the attached appendix form part of an overall scheme to defraud the revenue. The Commissioners are also satisfied that there are features of those transactions, and conduct on the part of Pacific Computers Limited, which demonstrate that you knew or should have known that this was the case. Accordingly all right to deduct the input tax claimed in respect of these transactions is denied.…

In the making of this decision the Commissioners have taken into account the following information features of trade evident from reviewing the activities of Pacific Computers Limited over a period of time:

- The transactions in period 09/06 have been traced to tax losses and defaulting traders. All these transactions have been notified to you in a joint and several liability letter. The schedule is attached here.
- Pacific did not consistently keep a record of all serial numbers for the transactions under consideration. It would be expected that the business would record serial numbers to insure the goods were not stolen and as a check against the possibility of dealing in the same goods more than once, which would be a clear indicator of connection with carousel fraud. It would also be expected that such records would be necessary for commercial purposes, to enable the company to validate any return goods claims (i.e. that the goods returned were actually goods that the company had supplied). The fact that Pacific did not keep, request to be kept or check serial numbers suggest that it knew it would not receive any returned goods etc. because the transactions have all been prearranged and were part of a scheme to defraud the revenue
- The deals were back to back, being made on the same day or within two or three days, the same amount of goods and the same product. Pacific was never left with stocks that it hadn't sold. It would be expected that a conscientious business carrying on a commercial venture would, if it was buying goods to then sell on, hold unsold stock, or, if it was contacted first by a customer and then went out to source the goods, that there would be a delay between obtaining the order and finding someone able to supply the precise quantities and specifications of goods required by the customer. The fact that these requirements could be instantly match suggests that the deals were artificially contrived.
- Despite the high value of the goods being purchased and sold Pacific did not enter into any formal written contracts with its suppliers, customers or freight forwarders during the period under review. This means that there was no formal returns/exchange policy for any party should the goods be found to be faulty, the matters such as transfer of title, payment and delivery terms were also not subject to any formal agreement. It would be expected of a business carrying on a normal commercial trade

would ensure that the dressing such cases would be set out in a formal written agreement. This suggests that Pacific knew it would not need for more contracts because the transactions had all been prearranged and were part of a scheme to defraud the revenue.

- A trader in a legitimate market trading in goods worth of millions [*sic*] of pounds would not deal with the others without first satisfying himself that his suppliers could supply what they contracted to supply, and that his purchasers could pay for what they had agreed to purchase. It is not enough to contend the goods would not be paid for until they have been expected, nor handed over until paid for. In a genuine market, traders dependent, as Pacific was, on payment by the purchasers in order that it could itself pay its suppliers would not commit to a purchase without near certainty that the purchaser will pay, and would not commit itself to a sale without near certainty that its own suppler was in a position to deliver. Here, neither its due diligence nor its contractual obligations provided Pacific with any true assurance that, assuming they were genuine, arm's length deals, they would be honoured by its counterparties. Instead, it exposed to the risk that it would be left with goods for which its purchasers could not pay, or that it would be unable to fulfil orders from its customers. The conclusion to be drawn from Pacific's approach is that, again, it knew perfectly well that its suppliers and customers would not let it down because the transactions have all been prearranged.
- Due diligence undertaken on the supplier and customers (but not, apparently, on the freight forwarders) prior to the trades taking place consisted of amongst other things:
    - Credit checks
    - Visits to places of business;
    - Copies of the VAT and incorporation certificates;
    - Bank details; and
    - Copies of passports.

  This could not have provided Pacific with adequate assurance that it was not involved in the MTIC fraud chain before entering into the transactions. It suggests that it went through the motions of due diligence with the objective and demonstrating compliance with HMRC examples because it knew that its customers and suppliers would not let it down and because the transactions had all been prearranged…"

Tax loss etc.

138.It is common ground that there was tax loss caused by fraud in the chains. There is nothing before us to show that the Taxpayer was aware of this when it entered into its transactions and we so find.

139.We find as a fact and to the extent possible as a primary fact that the Taxpayer had no actual knowledge of fraud in the chains.

140.We have carefully considered all the evidence before us in reaching this conclusion and do so both subjectively and objectively from the perspective of the Taxpayer and its officers and that of an officious bystander. We make this finding on the balance of probabilities and because there was no evidence before us to show otherwise and no evidence laying a foundation from which an inference could be drawn.

141.We reject HMRC's assertion that PCL had actual knowledge of the fraud at the relevant times as there was nothing before us to support HMRC's assertion.

142. This leaves open at this stage "the ought to/should have known" question which we consider elsewhere in this decision. More accurately this should be the *Mobilix* question whether fraud was the only reasonable explanation for PCL's transaction. It was not shown to be the case.

Record of all Serial Numbers

143.The Goods were not mobile phones and did not carry the equivalent of an IMEI (International Mobile Station Equipment Identity) number that could be easily scanned electronically. The goods here were iPods and CPUs.

144.We were told that IPods could not be scanned electronically in the way that mobile phones can be. We accept this.

145.CPUs, we were told, would need to be placed into a motherboard in order to be tested and for the serial number to be recorded. We also found the marking on the CPU we were shown too small to read with the naked eye.

146.Accordingly random tests of the goods were made rather than electronic scans. This makes commercial sense to us and was a reasonable approach in the circumstances and we so find.

147.The boxes were X rayed to see if the real goods such as CPUs have been replaced, for example, by pieces of glass in the case is CPUs. Again this made commercial sense to us and was a reasonable precaution.

The deals were back to back

148. It was common ground that the deals were "back to back" in the sense that they were arranged to take place essentially on the same day. It is not uncommon for this to be the case. One only has to think of chains in the residential property markets or "shorting" of securities. There was no evidence before us to show that this was not the case here. We find that the transactions were commercial and to the extent we can we find this as a primary fact.

149.This structure made commercial sense to us and was a reasonable approach in the circumstances.

150.There was no evidence before us that there was anything improper on the part of the Taxpayer in participating in back to back deals here. Rather the contrary was the case as it made financial and commercial sense as in the case of a chain of residential property transactions completing on the same day.

151.On the evidence before us there was nothing untoward on the part of the Taxpayer in participating in back to back transactions. We find this is a matter of fact having had the benefit of seeing and hearing the witnesses and reject HMRC's suggestions to the contrary.

Pacific did not enter into any formal written contracts or have terms and conditions

152.This seems to have arisen because HMRC had not looked at the back of the taxpayers order forms. The back of these forms set out the Taxpayer's standard terms and conditions. We are surprised that this was not picked up before the hearing.

153. Further the assertions seem to ignore the existence of the Sale of Goods legislation which deals with matters such as title, fit for purpose etc. The purchase was by one UK Company from another UK Company. It also ignores the Contracts (Applicable Law) Act 1990 which would deal with the position on a sale to an EU member state company.

"Satisfied suppliers could supply, and purchasers could pay"

154.PCL undertook at least the due diligence recorded in the Decision Letter on suppliers and purchasers.

155.This "consisted of amongst other things:

- Credit checks
- Visits to places of business;
- Copies of the VAT and incorporation certificates;
- Bank details; and
- Copies of passports".

156.We find that this has been proved to be the case and do so as a matter of fact.

157.The position with freight forwarders appeared to be different although visits had taken place. We did not consider this to be uncommercial.

Due Diligence with the objective of demonstrating compliance with HMRC examples

158. The Taxpayer (as was said in the decision letter and noted above) carried out the following due diligence "… which consisted of amongst other things of:

- Credit checks
- Visits to places of business;
- Copies of the VAT and incorporation certificates;
- Bank details; and
- Copies of passports".

159. We find this as a matter of fact.

160. We do not find that the due diligence was done with the objective of demonstrating compliance with HMRC examples as HMRC suggested. No evidence was before us which led to the conclusion that due diligence was done for that purpose or which led to reasonable grounds for making such an inference.

161. We find that the transactions concerning PCL were commercial transactions on PCL's part whatever others may have intended and to the extent we can we find this as a primary fact. We decline to draw any inferences to the contrary as there was nothing before us on which to found such inferences.

162. We consider that PCL's due diligence was not perfect but was commercial and sensible and we so find. We also remind ourselves in so doing that the Court of Appeal has told us to concentrate on the explanation for the taxpayer's transactions rather than focussing on due diligence (see Moses LJ at [75] and [82] in *Mobilix* set out below).

Clarke Schedule

163. The evidential value of the chain tracing based upon the Clarke Schedule is uncertain. The state of the evidence is unsatisfactory.

164. As Mr Webster submitted "Whilst the strict rules of evidence do not apply, there must be some critical evaluation of the evidence presented by the Respondents. They seek to persuade the Tribunal to rely upon this evidence upon the bases that:

164.1. It had been served, but the Appellant had not sought the underlying material; and

164.2. The Appellant had not sought to cross-examine Clarke upon it".

165. He continued "What it [HMRC] cannot do is to produce a schedule without any underlying material and then ask the parties and the Tribunal simply to accept it".

166. We agree with Mr Webster and do not accept the Clarke Schedule. We do not consider at any rate that it would have added much to what was before the Tribunal.

Microsoft

167. The Taxpayer accepted that it had bought counterfeit software. There was no evidence that this was done deliberately by the Taxpayer. It would seem that this was done unwittingly by PCL. We agree with Mr. Webster QC who said at paragraph 10 of his second closing submissions … "As stated in evidence, PCL was one of a number of companies and institutions, including state institutions, who were sold counterfeit software. To suggest that this would have, or should have, made PCL's officers especially suspicious of the transactions to which this appeal relates rather ignores the different natures of the transactions. There is no parallel. The evidence obscures, or of an earlier minutes, the issues and should be ignored by the Tribunal". We have recorded the position and our views in case they are of any use in any further proceedings in respect of this appeal.

Overview

168. In broad terms, we would summarise our findings as follows:

168.1. The Taxpayer's witnesses came across as honest and reliable and we accept their evidence having seen them pushed hard;

168.2. PCL and its officers whilst aware of MTIC in general terms had no actual knowledge of fraud in the chains at the relevant times;

168.3. The deals in question were carried out commercially and in an honest manner

as far as PCL was concerned;

168.4. The Decision Letter did not survive any sensible scrutiny;

168.5. HMRC failed to show anything or to show anything from which it could be inferred that PCL ought to have known or had the means of knowledge objectively or subjectively of fraud in the chains at the relevant time(s)[3];

168.6. HMRC failed (inter alia because they were unable to show the matters set out in the preceding subparagraph) to show that the only reasonable explanation for PCL's transactions was connection with fraud.

169. HMRC failed to discharge the onus of proof of showing either:

169.1. That PCL had actual knowledge of connection to fraud of PCL's transactions; or

169.2. That PCL ought to have known of the connection to fraud in its transactions or that fraud was the only explanation for PCL's transactions within the approach in *Mobilix*.

170. Insofar as we have not already found these matters as matters of fact we do and to the extent possible we find them as matters of primary fact.

Submissions of the Parties

The Taxpayer`s submissions in outline

171. In essence, the Taxpayer argued that:

171.1. It did not have actual knowledge of the fraud in the chains; and

171.2. There was nothing that showed it should or ought to have known that there was fraud in the chains. It was not the case that the only reasonable explanation for the Taxpayer's purchase was fraud.

172. The gist of the Taxpayer's argument as we understood it was that HMRC had failed to show that the only reasonable explanation for the Taxpayer's involvement in the transactions was fraud. The onus to do so was on HMRC and it had not discharged that burden.

173. HMRC had failed to show this for the simple reason that it was not true. More than mere assertion from HMRC was needed for HMRC to stand up its case.

174. The Taxpayer's appeal should therefore be allowed as HMRC had failed to make out its case.

175. It was not the case that the only reasonable explanation for PCL's involvement was fraud. The involvement of an innocent party was a reasonable explanation and had the merit of being true. It was the case here.

176. The Taxpayer also raised a number of specific points which we have dealt with in the Discussion below.

177. We hope it will not be thought discourteous not to detail all the points. They are available for any higher tribunal or court in the Taxpayer's helpful and succinct submissions in writing.

178. The Taxpayer argued that the Taxpayer's appeal should be allowed as HMRC had failed to make out HMRC's case either as to actual knowledge or imputed knowledge on the *Mobilix* basis.

179. The appeal should be allowed with costs.

HMRC`s submissions in outline

180. HMRC's Opening Submissions said (at paragraph 1.10):

"The Respondents' overarching submission is that all 14 [sic] of the Appellant's transactions in 09/06 VAT period were part of an overall MTIC fraud scheme involving a web of companies and chain of "transactions" the sole aim of which was to defraud the Revenue of VAT due to it. The transactions were orchestrated and contrived for such a purpose and had no ordinary commerciality to them".

[3] This is not to suggest that this was the test.

181. In essence, HMRC asserted that the 13 "broker"[4] transaction chains were contrived as part of an overall scheme to defraud the Revenue and the Taxpayer knew or should have known that the transactions in which the taxpayer was involved were connected with the fraudulent evasion of VAT.

182. The Taxpayer's transactions were connected with the VAT fraud and the Taxpayer must have known of that connection to have played such an integral role and taken such a significant share of the profits. In other words, HMRC alleged that PCL was thoroughly involved in the fraud.

183. In the absence of actual knowledge the Taxpayer should have known of the connection of its transactions with MTIC fraud by virtue of the cumulative circumstances presented to it, not least the fact that it was able to make large profits from doing little more than arranging for a consignment of goods across the English Channel. It was adding no value to the goods whatsoever.

184. The previous involvement of Doktor Ring, Masterpiece and Plazadome in MTIC fraud is a strong indicator of MTIC fraud here. The CD records recovered during a search of the home of an individual fraudster contained hundreds of files covering the period April 2005 to January 2006. These contained deal chains materially similar to those under consideration (though not involving Pacific). The discs contained the blueprints and documentation necessary for preordained transaction chains to facilitate MTIC fraud.

185. The same company appears at both ends of the PCL deal chain in deals 17-22, 25, 26 and they were thus carousels. As completion of the carousels required Pacific to sell to the right purchaser then over so many transaction chains a carousel pattern cannot be attributed to coincidence and Pacific must have been told from whom to purchase, to whom to sell, and of what prices and when. Doktor Ring 17 J&P Imports & Exports 18 Allblast 19, 20, 21, 22.

186. The geography of the transactions makes no commercial sense. The Goods left MITT and returned to MITT shortly thereafter sometimes on the same day.

187. Goods were essentially sold by one Dutch Company to another Dutch Company and bringing the goods into the UK was for the purpose of MTIC fraud. There was no commercial reason for doing so. In a normal market one Dutch Company would have bought direct from the other Dutch Company at a cheaper price than would be the case when the UK Company chain were added in.

188. The CPU transactions were part of a wider circularity of CPUs designed to facilitate a MTIC fraud. A small group of exporters paid an integral role in the MTIC fraud. The same entities crop up time and time again. The companies appear to be interchangeable.

189. The values and profit show the transactions were no part of any commercial market.

190. The CPU transactions were part of a wider circularity of CPUs designed to facilitate a MTIC fraud. A small group of exporters played an integral role in the MTIC fraud. The same entities crop up time and time again. The companies appear to be interchangeable.

191. The values and profit show the transactions were not part of any commercial market.

192. There were parties in the circularity who had previously been involved in MTIC fraud. There were also links between brokers in the circularity. It was inconceivable that this was not known.

193. The patterns of trade here do not exhibit characteristics of the grey market. The volume of trade exceeded the legitimate grey market and showed no characteristics of business trading.

194. The Clarke schedule supported all of this.

195. PCL received payment from its customer before it paid Plazadome. PCL was selling goods that did not belong to it and in breach of Plazadome's sales invoice terms.

[4] This was the word HMRC used and nothing is to be taken from its use in this decision.

196.It was thus clear that PCL knew or must be treated as knowing that the transaction chains were connected with fraud. Fraud was the only explanation for the transactions.
197.Accordingly, the appeal must be dismissed and dismissed with costs.

Discussion

Introduction

198. We set out at the start of this Decision our view of the issue and some questions relevant to deciding the case. We considered that, in essence, the issue in this case is whether or not the input deduction was correctly denied.

199.This requires a number of questions to be considered including the following.

199.1. Did the Taxpayer know that the Taxpayer's purchase had been or would be connected to fraud? Was there actual knowledge on the Taxpayer's part?

199.2. Should the Taxpayer have known that the only reasonable explanation for the transaction in which the Taxpayer was involved was that the transaction was connected to fraud? (See a *Mobilix* [59] and *Else* UTT [20]). Was there imputed knowledge on the basis of *Mobilix*?

200.As noted above in the light of the common ground between the parties the essential issue in this case is whether the only reasonable explanation for the Taxpayer participating in the transactions in which the Taxpayer was involved was fraud. In broad terms, this is the case for both actual knowledge and "ought to have known" cases on the *Mobilix* basis. We set out our understanding of the law next and it is that which we have applied rather than a shorthand summary as used here.

Our Understanding of the Law

201. Arnold J. helpfully set out his view of the law from the case law in *Else Refining And Recycling Limited v HMRC* FTC/86/2012. We respectfully and gratefully adopt this.

202. He said

"**The law**

[6.] In Joined Cases C439/04 and C440/04 *Kittel v Etat Belge* [2006] ECR I-616 the Court of Justice of the European Communities (Third Chamber) held as follows:

"[54.] As the Court has already observed, preventing tax evasion, avoidance and abuse is an objective recognised and encouraged by the Sixth Directive (see Joined Cases C-487/01 and C-7/02 *Gemeente Leusden and Holin Groep* [2004] ECR I-5337, paragraph 76). Community Law cannot be relied on for abusive or fraudulent ends (see, inter alia, Case C-367/96 *Kefalas and Others* [1998] ECR I-2843, paragraph 20; Case C- 373/97 *Diamantis* [2000] ECR I-1705, paragraph 33; and Case C-32/03 *Fini H* [2005] ECR I-1599, paragraph 32).

[55.] Where the tax authorities find that the right to deduct has been exercised fraudulently, they are permitted to claim repayment of the deducted sums retroactively (see, inter alia, Case 268/83 *Rompelman* [1985] ECR 655, paragraph 24; Case C-110/94*INZO* [1996] ECR I-857, paragraph 24; and *Gabalfrisa*, paragraph 46). It is a matter for the national court to refuse to allow the right to deduct where it is established, on the basis of objective evidence, that that right is being relied on for fraudulent ends (see *Fini H*, paragraph 34).

[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.

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

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

[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'.

[60.] It follows from the foregoing that the answer to the questions must be that where a recipient of a supply of goods is a taxable person who did not and could not know that the transaction concerned was connected with a fraud committed by the seller, Article 17 of the Sixth Directive must be interpreted as meaning that it precludes a rule of national law under which the fact that the contract of sale is void – by reason of a civil law provision which renders that contract incurably void as contrary to public policy for unlawful basis of the contract attributable to the seller – causes that taxable person to lose the right to deduct the VAT he has paid. It is irrelevant in this respect whether the fact that the contract is void is due to fraudulent evasion of VAT or to other fraud.

[61.] By contrast, where it is ascertained, having regard to objective factors, that the supply is to a taxable person who knew or should have known that, by his purchase, he was participating in a transaction connected with fraudulent evasion of VAT, it is for the national court to refuse that taxable person entitlement to the right to deduct."

[7.] In *Mobilix Ltd v Commissioners for Her Majesty's Revenue and Customs* [2010] EWCA Civ 517, [2010] STC 1436 the Court of Appeal had to consider the proper interpretation and application of the ECJ's decision in *Kittel.* Moses LJ, with whom Carnwath LJ (as he then was) and Sir John Chadwick agreed, considered the meaning of the words "should have known" and held as follows:

"[51.] Once it is appreciated how closely *Kittel* follows the approach the court had taken six months before in *Optigen*, it is not difficult to understand what is meant when it is said that a taxable person 'knew or should have known' that by his purchase he was participating in a transaction connected with fraudulent evasion of VAT. In *Optigen* the Court ruled that despite the fact that another prior or subsequent transaction was vitiated by VAT fraud in the chain of supply, of which the impugned transaction formed part, the objective criteria, which determined the scope of VAT and of the right to deduct, were met. But they limited that principle to circumstances where the taxable person had 'no knowledge and no means of knowledge' (§ 55). The Court must have intended *Kittel* to be a development of the principle in *Optigen*. *Kittel* is the obverse of *Optigen*. The Court must have intended the phrase 'knew or should have known' which it employs in §§59 and 61 in *Kittel* to have the same meaning as the phrase 'knowing or having any means of knowing' which it used in *Optigen* (§55).

[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."

[8.] Moses LJ considered the extent of knowledge that was required at [53]-[60]. He held at [55] that it was not sufficient for HMRC to show that the trader should have known that he was running a risk that his purchase was connected with fraud. He concluded:

"[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.*

[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."

[9]. Moses LJ held at [61]-[62] that this approach did not infringe the principle of legal certainty. As he said in [61]:

"…It is difficult to see how an argument to the contrary can be mounted in the light of the decision of the court in *Kittel*. The route it adopted was designed to avoid any such infringement.

A trader who decides to participate in a transaction connected to fraudulent evasion, despite knowledge of that connection, is making an informed choice; he knows where he stands and knows before he enters into that transaction that if found out, he will not be entitled to deduct input tax. The extension of that principle to a taxable person who has the means of knowledge but chooses not to deploy it, similarly, does not infringe that principle. If he has the means of knowledge available and chooses not to deploy it he knows that, if found out, he will not be entitled to deduct. If he chooses to ignore obvious inferences from the facts and circumstances in which he has been trading,

he will not be entitled to deduct."

[10]. Moses LJ considered the facts of the appeals before the Court of Appeal at [67]-[80]. In relation to the appeal by Blue Sphere Global Ltd he held at [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."

[11.] Moses LJ considered questions of proof at [80]-[85]. He held at [81] that the burden lay upon HMRC to prove the trader's state of knowledge. He went on at [82]:

"But that is far from saying that the surrounding circumstances cannot establish sufficient knowledge to treat the trader as a participant. As I indicated in relation to the BSG appeal, Tribunals should not unduly focus on the question whether a trader has acted with due diligence. Even if a trader has asked appropriate questions, he is not entitled to ignore the circumstances in which his transactions take place if the only reasonable explanation for them is that his transactions have been or will be connected to fraud. The danger in focussing on the question of due diligence is that it may deflect a Tribunal from asking the essential question posed in *Kittel*, namely, whether a trader should have known that by his purchase he was taking part in a transaction connected with fraudulent evasion of VAT. The circumstances may well establish that he was."

[12.] At paragraph [84] he said:

"Such circumstantial evidence … will often indicate that a trader has chosen to ignore the obvious explanation as to why he was presented with the opportunity to reach a large and predictable reward over a short space of time."

203.We note in particular from this that "***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***." (emphasis supplied, see Moses LJ with whom Carnwath LJ as he then was and Sir John Chadwick agreed set out above as well)

204.We have used this as our starting point and guiding principle in deciding this case. However, in so doing we have not disregarded the other case law but have used it as a guide

star in seeking to ask the right questions. We also note that we are not to focus unduly on the question of due diligence. We have attempted not to be fixated by due diligence but have tried to bear in mind reality and commerciality in particular in reaching conclusions bearing carefully in mind the guidance from the Court of Appeal.

205.We take from this that on the basis of *Mobilix* in the light of the relevant factual circumstances, the Tribunal must be satisfied on the basis of cogent evidence, that at the time PCL entered its deal it either knew that there was a connection between those transactions and the fraud or that the only reasonable explanation for the transactions in question was that they were connected with fraud. The threshold is a high one and deliberately set by the Court of Appeal, if input tax recovery is to be denied. The onus is on HMRC on the balance of probabilities.

206.HMRC came nowhere near even satisfying a low threshold in this case.

Actual Knowledge of fraud – not shown

207.There was no evidence before us that showed actual knowledge of fraud on the part of the Taxpayer. There was no evidence before us that showed actual knowledge of fraud on the part of any of the Taxpayer's witnesses. This is not a case of actual knowledge and we so find and to the extent possible we so find as a fact and a primary fact

208.HMRC did not point to any evidence of actual knowledge or to matters which were sufficient to found the drawing of such an inference from all the circumstances. HMRC did not establish the basis from which such inferences could be drawn. The cross examination of the Taxpayer's witnesses and the way it was done with the consequent finding of their reliability and credibility made it even harder to conclude that there could be actual knowledge. We decline to make the inferences HMRC invited us to do and find that there was no evidence of actual knowledge on PCL's part in this case.

209. We have carefully considered whether or not the transactions were too good to be true and so the only reasonable explanation for them was fraud. We consider that would raise some questions as to commerciality on which we have already made our finding above namely we have found and find the transactions were commercial on PCL's part. However, we do not consider that HMRC has discharged the onus of showing that the only reasonable explanation for the taxpayer's transactions was fraud.

210.HMRC also submitted [paragraph 6.2 of their Opening] "… the fact [sic] that the transactions were orchestrated by fraudsters as part of the said overall scheme [to defraud the Revenue] , only allows two possibilities in relation to the Appellant's state of knowledge:

i. The Appellant was involved because it was a knowing party to the scheme; or
ii. The Appellant ignored the obvious and should have known that its transactions were connected with fraud".

211. We do not accept that those were the only two possibilities. There was also, for example, the possibility that PCL was an innocent party who knew nothing of the fraud. This in our view is the most likely explanation. It has not been shown to be an explanation for the transactions taking place which is unreasonable. More accurately it has not been shown that the only explanation for PCL's transactions was connection to fraud as *Mobilix* would require for HMRC to succeed.

212.The assertion also assumes that PCL knew at the relevant time(s) that the transactions were orchestrated by fraudsters as part of the an overall scheme to defraud the Revenue. The submission specifically goes "…to the Appellant's state of knowledge…". There was no evidence that PCL knew that the transactions were orchestrated by fraudsters as part of the an overall scheme to defraud the Revenue".

213. HMRC have failed to show actual knowledge nor to stand up the argument that the only reasonable explanation for PCL's transactions was fraud. There was no evidence before us on which to base such a finding or inference.

Doktor-Ring etc.

214. HMRC said in opening (para 6.5) "Doktor-Ring…, Masterpiece, … and Plazadome were companies engaged in the facilitation of MTIC fraud on a grand scale. In 2005, they undertook a series of transactions that were demonstrably contrived for the purposes of a sophisticated MTIC fraud".

215. There was no evidence before us that PCL knew of this at any relevant time and we so find as a matter of fact. Indeed there was no evidence before us that it was known to HMRC at the relevant times.

216. HMRC said compact discs were obtained by Officer Downer in February 2008 which contained much information and templates relating to MTIC. They had been obtained by the police in October 2006 (i.e. after the end of period 09/06). Whilst they may be of interest there is no connection shown to PCL or the transactions to which PCL's appeal relates.

217. The Respondents assert these were blueprints for a criminal enterprise. They went on to say "… numerous individuals have been convicted of conspiracy to defraud and money laundering offences in relation to the contents of the discs".

218. This may well be the case. However, PCL is a company not an individual and we were taken to no evidence that PCL information was on the discs or that it was in any way involved. Accordingly, we do not see what weight it has other than to show certain companies in the chain may have been involved in fraud. PCL had already agreed that this was the case. It does not go to PCL's actual knowledge or that the only reasonable explanation for PCL's transactions was fraud. It may explain fraud in the chain and related matters but of itself it does not go to PCL's transactions.

219. Whilst this may be interesting information we do not see that it helps us answer the question was the only reasonable explanation for the transactions PCL took part in fraud? It does not go to what PCL did or did not do or know.

220. We note HMRC's assertion but in the absence of evidence linking it to PCL we can do no more. It does not assist us in respect of PCL's position.

Carousels

221. HMRC submitted "… There is no commercial explanation for companies at both ends of the chains dealing in the same goods again in such a short period of time. Crucially, to ensure the completion of the carousels, PCL had to sell the goods to the right company. The Respondents submit that over so many transaction chains the carousel pattern cannot be attributed to coincidence, and that PCL must have been told from whom to purchase, to whom to sell, at what prices and when".

222. There was no evidence before us that showed PCL knew of the carousels or was in receipt of instructions as to what to do.

223. HMRC had not laid a sufficient evidentiary base from which we could make the inference they invited us to. We decline to make such an inference.

224. We are concerned with PCL's position here and not the chain of transactions and whether or not that was fraudulent and involved tax loss. In this case the onus of proof is on HMRC in respect of PCL not the other persons in the chain. HMRC seem at times to merge the chain and PCL. It is common ground that there is fraud in the chain. Our task is to consider whether or not the only reasonable explanation for PCL's transactions was fraud.

225. The carousel argument does not assist in that task particularly when PCL has accepted that there was fraud in the chain which caused a tax loss. HMRC were taking a holistic view of the chain rather than a more individualistic view of PCL and its transactions. This does not mean that all the circumstances do not need to be considered but rather they have to be considered in the context of the precise question the Tribunal has to answer in respect of the taxpayer who is making the appeal.

226. Merely because PCL appears in a chain of transactions which involved tax loss through fraud does not mean that PCL knew or ought to have known this was the case or in more correct language the only reasonable explanation for PCL's transactions was fraud. The onus of proof is on HMRC to show this was the case in respect of PCL.

227. We find HMRC have failed to discharge this burden of proof.

Anomalies in the documentation

228. HMRC sought to point to what they considered anomalies in the documentation.

229. PCL accepted that the documentation was not perfect. As we have recorded above Mr Roach was more concerned with doing the deal than with the niceties or finer points of the paperwork.

230. We consider this in the circumstances before us to be a neutral matter. It does not show actual fraud or that fraud was the only reasonable explanation for PCL's transactions.

Shipping and payment

231. HMRC drew attention to the number of days between shipping and final payment. This varied between one day and 18 days.

232. We note this but consider it not unusual in a commercial context and that it does not show actual fraud or that fraud was the only reasonable explanation for PCL's transactions.

"Collusive banking arrangements"

233. HMRC say all the parties to the transaction chains except Plazadome and PCL used accounts at UMBS. We note that even on HMRC's own submission PCL does not hold an account at UMBS.

234. They further submit that there can be no honest explanation for what were collusive banking arrangements. This may well be the case but PCL are not shown to be part of the collusion.

235. We reject the argument on collusive banking arrangements in so far as it relates to PCL. We do this as there is no evidence before us to support it as far as PCL is concerned and we so find.

Contrivance

236. The Respondents submitted that the correct inference to be drawn by the Tribunal from the "evidence of contrivance" is that those behind PCL knew of the connection between the Appellant's transactions and the fraudulent evasion of VAT (para 6.90 of Opening).

237. The alleged lack of commerciality reinforces this say HMRC.

238. The transactions were not part of an ordinary commercial market, but rather were part of highly orchestrated overall schemes to defraud the Revenue. This was because:

238.1. The majority of the deal chains were carousels;

238.2. The geography of the transactions makes no commercial sense;

238.3. The length of the deal chains shows they lack any commercial rationale;

238.4. The back to back nature of the trading and the time to complete the deal chains is suggestive of contrivance;

238.5. The lack of any manufacturer, retailer or end user within the deal chains shows an absence of commercial function;

238.6. The fixed mark up within the chains suggests contrivance;

238.7. The presence of Plazadome, Masterpiece and Doktor Ring in the chains who were involved previously in MTIC fraud suggests the chains were part of an orchestrated scheme to defraud the Revenue;

238.8. The pattern of trade shows orchestration is inexplicable by ordinary market forces;

238.9. There was no commercial sense in PCL's supplier not dealing directly with PCL's customers as they were already acquainted with them;

238.10. The CPU's were part of a wider circularity inexplicable by reference to ordinary commerce;

238.11. The absence of the characteristics of grey market traders in the Appellant's trading suggest part of a scheme to defraud the Revenue;

238.12. There were inconsistencies in the documentation;

238.13. Several of the other participants in the chains showed indicators of knowing participation in fraud;

238.14. The collusive banking arrangements would not be seen in ordinary commerce. However, HMRC accepted that PCL did not bank at the same bank(s) as the others in this chain.

239. Again this looks at the chain rather than the position of PCL. It is a "bootstrap" argument based on the assertion of contrivance.

240. HMRC have not established contrivance or knowledge of contrivance on PCL's part. To the extent that we have not already done so we find this as a fact.

241. Accordingly, we reject this argument.

Failure to look at PCL's transactions rather than the chain as a whole

242. HMRC approached this case by looking at the whole of a chain and asserting that because there was a tax loss caused by fraud in the chain it therefore followed that the Taxpayer's transactions could only be explained by fraud. Such an overall regulatory approach may be appropriate in some circumstances but does not address the issue of the Taxpayer's position which is what the Tribunal is concerned with.

243. This "regulatory" approach can be seen in many places, for example, the assertion that because of the Taxpayer's integral role and significant share of profits it followed the Taxpayer knew or ought to have known of the fraud. This is a pure non sequitur. Even if the premise had been proved, which it had not, the conclusion does not necessarily follow.

244. The assertion that the same company was at both ends of the chain and because many companies were in the same position in the chains PCL must have been told when and what to buy and sell again does not necessarily follow.

245. There was no evidence before us to support this assertion and it misses the point that it is the Taxpayer's transactions and knowledge and associated matters that the Tribunal is concerned with here. Who started off the chains and the position of brokers cannot be assumed to have been known to the taxpayer. There was no evidence before us to show that this was known to PCL and nothing on which to begin to find an inference.

246. We reject these arguments and the argument that the sales were known by the Taxpayer to be Dutch to Dutch sales.

247. We do so because there was no evidence before us to support these assertions and nothing on which to find any such inference. To the extent that we have not already done so we find such acts as a necessary to support the rejection of these assertions and the invitation to make such inferences. To the extent possible we find these matters as matters of primary fact.

248. The suggestion that making a profit out of buying and selling goods without doing any work on them is interesting but somewhat naïve. It is the way that many stock and commodity exchanges work. We reject this argument.

249. The argument that the values and profit show the transactions were not part of a commercial market was interesting but not stood up by any evidence that could have been available to PCL at the time of the relevant transactions. Dr. Finlay said he was surprised at his findings. This was work done some time after the relevant period and was not available to PCL at the time of the relevant transactions.

250. We did not find that the Clarke schedule added much to the position. If it were to be given significant weight it would have needed to have been proved by cogent evidence including working documents and a witness who could be cross examined as to how it was produced. This was not the case. Accordingly, it is hard to give it to any significant weight.

251. We did not understand the relevance to these circumstances of the Microsoft issue. PCL accepted that it had acquired counterfeit computer software some time before the period in question. We do not see how this shows that at the relevant time(s) fraud was the only explanation for PCL's deals transactions. We reject this argument.

Overview

252. We find that HMRC have not shown that PCL had actual knowledge of fraud.

253. We find that HMRC have not shown that the only reasonable explanation for PCL's involvement in its transaction(s) was fraud within the meaning set out by the Court of Appeal in *Mobilix*. The evidence did not show this to be the case and there was no foundation laid before us from which any such inference could be drawn. To the extent that we have not already done so we find such facts as are necessary to support the rejection of these assertions and the invitation to make such inferences.

254. Consequently we find that HMRC have failed to show either:

254.1. Actual knowledge of or involvement in fraud by PCL; or

254.2. That PCL had the means of knowledge or ought to have known that the only reasonable explanation of PCL's involvement in the transactions was fraud.

255. We again repeat that assertion is not evidence.

256. The way the case was presented by the starting point of looking at the chains as a whole rather that the taxpayer's position was unhelpful to HMRC's case. HMRC should consider how and by whom its cases are presented. This is not to suggest that on the evidence before us any different result would have been achieved but it does raise the question of the value for money of an almost three week trial when the evidence was not there to get the result HMRC wanted. It is to suggest that a more precise analysis of the evidence and the likely outcome is needed. We accept that we are making these comments after the benefit of a full hearing.

Costs

257. Both parties sought costs if they had won and both accepted, when the Tribunal asked, that this was a case where costs could be awarded. Essentially, this was because it was an old case started before cost position was changed.

258. As presently advised we see no reason here why costs should not follow the event as is usually the case. We can also see arguments that the cost should be awarded on an "indemnity" basis.

259. We invite the Taxpayer to tell the Tribunal within seven days of the release of this decision if it wishes to apply for costs and if so on what basis.

260. HMRC may then, within seven days of the Taxpayer informing the Tribunal of what it wishes to do concerning costs, notify the Tribunal of such objections to what the Taxpayer has said concerning costs (if any) as are relevant.

261. There shall be no further submissions in respect of costs unless invited by the Tribunal.

262. We remind HMRC the Tribunal directions are there to be obeyed or not there for HMRC to decide whether it wishes to comply. We would not wish a repeat of the position in April. For the sake of completeness we remind both parties the directions of the tribunal are there to be obeyed.

Outcome and Disposal

263. We have found: HMRC have failed to show either:

263.1. Actual knowledge of or involvement in fraud by PCL; or

263.2. That PCL had the means of knowledge or ought to have known that the only reasonable explanation of PCL's involvement in the transactions was fraud.

264. Accordingly, the appeal is allowed.

265. The position as to costs is dealt with above.

266.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.

ADRIAN SHIPWRIGHT
TRIBUNAL JUDGE

RELEASE DATE: 20 January 2015