[2011] UKFTT 649 (TC)

TC01491

Appeal number: TC/2009/10020 and TC/2009/10294

VAT – MTIC – preliminary hearing – application to admit late evidence – allowed in part subject to undertaking – application for disclosure – allowed in part – costs - dismissed

FIRST-TIER TRIBUNAL

TAX

MASSTECH CORPORATION LIMITED (IN ADMINISTRATION) **Appellant**

- and -

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

TRIBUNAL: Mrs B Mosedale (Tribunal Judge)

Sitting in public at 45 Bedford Square, London WC1 on 3 August 2011

Mr Goodwin, Counsel, instructed by the Khan Partnership, for the Appellant

Mr P O'Doherty, Counsel, instructed by the General Counsel and Solicitor to HM Revenue and Customs, for the Respondents

DECISION

1. The appeal is against HMRC's decisions given in March 2009 to refuse the Appellant input tax recovery claim made in respect of four periods in 2006 totalling some £12million. HMRC refused the claims on the basis that the Appellant's purchases were connected to fraudulent evasion of VAT and the Appellant knew or should have known this.

Late admission of evidence

2. HMRC applied on 4 July 2011 to rely on the expert witness statement of a Mr A Prescott dated 28 June 2011.

3. They also apply to rely on three statements from an HMRC officer Mr Mendes. The statements are dated 20 June 2011, 21 July 2011 and 29 July 2011. The first of these three statements gives evidence about matters relating to the alleged deal chains to which HMRC allege the Appellant's purchases are connected, discovered by Officer Mendes on the Dutch server of the First Curacao International Bank ("FCIB"). The second and third witness statement gives evidence about matters relating to the alleged deal chains which the Officer discovered on the Paris server of the FCIB.

4. HMRC also apply to rely on a statement by another HMRC officer, Mr D Young served at the same time in respect of the Paris server of the FCIB.

5. Lastly they apply to rely on further statements by two witnesses who have already given evidence, Mr G Smith and Mr N Humphries.

The law

6. I was refered to the decision of the House of Lords in *O'Brien v Chief Constable of South Wales Police* [2005] 2 WLR 1038. The case was very different to the one before me concerning as it did the admission of similar fact evidence. Nevertheless, in considering the admission of similar fact evidence Lord Bingham gave guidance applicable to all cases where the admission of evidence is opposed:

> "The second stage of the inquiry requires the case management judge or the trial judge to make what will often be a very difficult and sometimes a finely balanced judgment: whether evidence or some of it…which is ex hypothesi legally admissible, should be admitted. For the party seeking admission, the argument will always be that justice requires the evidence to be admitted; if it is excluded a wrong result may be reached…..the importance of doing justice in the particular case is a factor the judge will always respect. The strength of the argument for admitting the evidence will always depend primarily on the judge's assessment of the potential significance of the evidence, assuming it to be true, in the context of the case as a whole.

> While the argument against admitting evidence found to be legally admissible will necessarily depend on the particular case, some objections are likely to recur. First, it is likely to be said that admission of the evidence will distort the trial and distract the attention of the decision-maker by focusing attention on issues collateral to the issue to be decided….Secondly, and again particularly when the trial is by jury, it will be necessary to weigh the potential probative value of the evidence against its potential for causing unfair prejudice: unless the former is judged to outweigh the latter by a considerable margin, the evidence is likely to be excluded. Thirdly, stress will be laid on the burden which admission would lay on the resisting party: the burden in time, cost and personnel resources, very considerable in a case such as this, of giving dislcoure; the lengthening of the trial, with the increased costs and stress inevitably involved; the potential prejudice to witnesses called upon to recall matters long closed, or thought to be closed;…..In deciding whether evidence in a given case should be admitted the judge's overriding purpose will be to promote the ends of justice. But the judge must always bear in mind that justice requires not only that the right answer be given but also that it be achieved by a trial process which is fair to all parties."

7. My attention was also drawn to the case of Mr Justice Lightman's decision in *Mobile Export 365 Limited* [2007] EWHC 1737 (Ch) where he said "The presumption must be that all relevant evidence should be admitted unless there is a compelling reason to the contrary" (paragraph 20).

8. The conclusions I draw from these cases and from general considerations of fair hearings are as follows:

- Only relevant evidence should be admitted;
- Such evidence should nevertheless be excluded where there is a compelling reason to do so;
- Whether there is a compelling reason to do so will be a balancing exercise the object of which is to achieve a trial that reaches the correct decision by a process fair to all parties;
- To conduct that balancing exercise the Tribunal must consider the likely probative value of the evidence, any unfair prejudice caused to either party, good case management and any other relevant factor.
- Unfair prejudice includes the factors listed by Lord Bingham which were particularly relevant in that case but in this case, not being a trial by jury, perhaps of less relevance. Unfair prejudice would include a party being ambushed so that it is strategically disadvantaged or put in a position that it has no time to bring evidence in rebuttal.

- Considerations of good case management will include the need for a sanction against a party which adduces late evidence particularly where the evidence could have been produced earlier; it will recognise the desirability of adhering to trial dates and avoiding unnecessary costs.

The application to admit the FCIB Evidence

9. I find that the Paris server evidence (Mr Mendes' second and third witness statement and Mr Young's witness statement) have to be considered together as sensibly one could not be admitted without the other. For instance, Mr Mendes' evidence is that the same IP address was used to the move the money for all participants in an alleged deal chain, including the money moved on behalf of the Appellant. Mr Young's evidence will include the integrity of the Paris Server data and the meaning of IP addresses.

10. The Appellant opposed the application. They conceded the evidence is relevant. But they said (rightly) it is highly complex evidence which would take time to understand in order to effectively challenge it. Apart from the statements, it comprised 8 lever arch files of exhibits. Mr Hussain, the Appellant's principal witness currently works abroad and is unable to give instructions immediately in any event. They might need to apply for further disclosure if the evidence were admitted perhaps to access the Paris server data themselves to test its integrity.

11. They point to the fact that HMRC agreed in February this year to the trial date being fixed for 12 September. HMRC had not previously indicated that they would be applying for the admission of this evidence. The Appellant urges me to stick to the trial date. There should come a time when no further evidence should be adduced and sensibly that should be after the hearing has been set down.

12. They cited cases where Judges had refused late admission of evidence as unfair: *Brayfal Limited CH/2008/APPELLANT 82*, *Xentric Ltd TC 544*, *Purple Telecom Ltd* and *Europeans Ltd VTD 20796.* They considered I should follow these cases.

My decision

13. FCIB evidence is likely to be of important probative value. It is alleged to show that the movement of money on a significant proportion of a sample of alleged deal chains in this case was circular. A judge is likely to draw the conclusion from this (if proved) that the deal chains (if proved) were orchestrated for the purposes of fraud.

14. This is of significance to the first limb of *Kittel:* whether the purchases of the Appellant were connected to fraudulent evasion of VAT. This is because if it is shown that the Appellant's purchase was one in a chain orchestrated for the purpose of fraud it is connected to that fraud (even if the defaulter and/or acquisition cannot be identified bearing in mind that the money chain may not be identical to the invoice chain).

15. It may be found to be relevant to the second limb of *Kittel:* whether the Appellant knew or ought to have known of the fraud. This is because a Tribunal may conclude that the Appellant's purchase and sale may not have been freely negotiated if it is proved that they were part of a preordained series of transactions.

16. Nevertheless, I find its probative value is not necessarily such that a fair trial could not be held without it. There is a great deal of other evidence on which HMRC rely to show that the *Kittel* test is satisfied: they do not rely solely on the FCIB evidence.

17. Of more significance is that Mr Mendes' evidence shows the log-on timings for the money movements in a sample of alleged deal chains. This is potentially evidence of actual knowledge of the appellant of the orchestrated nature of the deal chains.

18. Of even greater significance is that Mr Mendes' evidence shows that in respect of one set of money movements relating to an alleged chain all the instructions to make payment, including the appellant's, have come from the same IP address. If HMRC can prove that this is true, and if they can prove that, using the same IP address means it was the same person accessing all the various accounts, it seems to me that, unless the Appellant can offer a satisfactory explanation, a Tribunal is likely to find that the Appellant must have known its transactions were connected to fraud. This may be "smoking gun" evidence.

19. HMRC assert the integrity of the data and of the significance of an IP address: I consider that this evidence requires an answer from the Appellant and that it is potentially of such significance to the Tribunal in reaching a just verdict that excluding it risks an unfair result.

20. The evidence is of such potential probative value that admitting it might not lengthen but rather shorten the hearing.

21. Is there a compelling reason to exclude such potentially probative evidence? Although vitally important the Tribunal reaches the right answer, it is as important that the hearing is fair.

22. Six weeks is not enough for the Appellant to test the integrity of the data nor to obtain evidence in rebuttal (such as evidence which might show that there is no significance to the same IP address being used). Nor is it long enough for the Appellant to make applications for disclosure it might wish to make.

23. I cannot admit the evidence and adhere to the trial date. The question is therefore whether it is fair to adjourn the hearing to give the Appellant time to properly consider and test the evidence or fairer to refuse to admit it at all.

24. The adjournment of this hearing is of no administrative inconvenience to the Tribunal which by administrative oversight has failed to list the hearing in a room large enough to contain the 20+ attendees and 80+ bundles and is as of today's hearing actively (but so far unsuccessfully) seeking another more suitable hearing venue than Court 2 at Bedford Square.

25. It is of considerable inconvenience to the Appellant who has already started to prepare for what is listed as a 15 day case (but which on their timetable as given to me at the hearing will be at least a 16 day case). It is also the case that it is HMRC who has withheld the VAT and therefore, should the Appellant win its case, any delay keeps it out of its own money for longer.

26. Was this inconvenience necessarily inflicted on the Appellant? Is HMRC to be criticised for not producing this evidence earlier? I accept HMRC's evidence that Paris Server information only became available to them late last year and officers were only trained to use it from February this year. I take into account that there are a great deal of cases in which MTIC fraud allegations are made by HMRC and only limited resources to carry out time intensive investigations of money chains and conclude that it is unlikely the evidence could have been made available much earlier in this case and certainly not so much earlier that it would not have jeopardised the hearing date of 12 September. HMRC could not have known until they looked at the evidence that they would find potentially significant evidence on logon times and identity of IP address.

27. HMRC admit that the Dutch server evidence was served later than it should have been. It was available earlier but due to a misunderstanding the officer thought it should be held back until the Paris server evidence was ready.

28. Weighing up the potential probative value of the evidence against the inconvenience to the Appellant of a delay in the hearing, I concluded that the Paris Server evidence should be admitted subject to making up for at least some of the prejudice to the Appellant of losing its hearing date in costs (in particular costs already incurred in preparing for the hearing which have to be duplicated later). I conclude it should be admitted as a whole because the evidence of money movements is integral to the use of IP addresses and vice versa and it cannot sensibly be divided. I also admitted Mr Mendes' first witness statement concerning the Dutch server for the same reason: his subsequent statements refer back to this evidence. By itself, taking into account both its lateness and the lower potential probative value of the Dutch server evidence I would not consider its admission could justify the loss of the hearing date. But as I admitted the Paris server evidence, the Dutch server evidence was also admitted as they are linked.

29. I am aware that I have come to a different conclusion to the Judges in the cases cited to me by the Appellant but each case is decided on its own particular facts and in this case the crucial distinction is the potentially highly probative nature of the evidence sought to be admitted.

30. On the question of adjournment, it seems fairer to me to give a unilateral option to the Appellant to have the hearing adjourned rather than determining it *will* be adjourned and I directed accordingly. It may be that the Appellant has an answer to the identity of the IP address which does not require much time to prepare and they would prefer not to lose their hearing date.

31. Nevertheless, even if the Appellant opts not to adjourn the case, I accept that the late admission of the evidence would cause prejudice in that more preparation work has to be done.

32. I cannot order HMRC to make good the prejudice in costs: this is a complex case but one in respect of which the Appellant has opted out of the costs regime. Therefore, my order was that *only if* HMRC give an undertaking to make good the Appellant's costs as specified by me as arising out of the late admission of this evidence will the evidence be admitted.

Admission of Mr Prescott's witness statement

33. Mr Prescott is an expert on insurance matters and his statement is to the effect that the insurance taken out by the Appellant was very irregular and inappropriate to the needs of the Appellant. HMRC allege that it goes to the credibility of the Appellant and also tends to show that the Appellant knew of the (alleged) contrived nature of the trading.

34. The appellant opposes the admission of the evidence as too late in the day. It is expert evidence and they would need to adduce expert evidence in rebuttal. HMRC said it had taken them a long time to identify an expert in this field: it could be presumed it would similarly take the Appellant a long time to instruct an expert.

35. The witness statement was served on the Appellant six weeks ago. It is six weeks to the hearing. Nevertheless, HMRC have known of the nature of the Appellant's insurance policy for at least two years: it is mentioned in the Statement of Case and reference to it has been made in the witness statements of some of HMRC's officers.

36. I considered all the factors in relation to this witness statement as to the others. I concluded on balance by itself that it would be unfairly prejudicial to the Appellant to admit it now and not adjourn the hearing as it would deprive them of the chance to obtain expert evidence in rebuttal.

37. I also concluded, that if this hearing were not to be adjourned for other reasons, then it should not be admitted subject to an adjournment because HMRC were slow in producing this evidence and its potential probative value was not of such magnitude that it really must be in front of the Tribunal. In particular, other witnesses gave evidence in respect of the insurance policy (in particular it is alleged that other traders in the cell used the same policy) and the Tribunal would be able to draw any appropriate inferences they considered proper from this evidence if proved. Further, counsel would be able to make submissions about the appropriateness of the policy on which the Tribunal might feel able to draw conclusions even without the benefit of an expert.

38. Nevertheless, the witness statement was of probative value and the only bar to its admission was that the Appellant did not have time to deal with it properly. Therefore I directed that if the hearing was adjourned for another reason (such as the Appellant's exercise of its right to an adjournment under my direction in relation to the admission

of the Paris server witness statements) then this witness statement should be admitted. Otherwise it is not admitted.

Application for admission of Mr Smith's further statement

39. This further statement was Mr Smith's response to a witness statement of Mr Hussain the principal witness for the Appellant. It comprised comment and no new evidence.

40. For this reason I dismissed the application to admit it. Mr Smith's opinions can, if HMRC chose, be put in submissions to the Tribunal at the hearing.

Application for admission of Mr Humphries' further exhibits

41. Mr Humphries' "statement" similarly did not contain new evidence but one new overview schedule and updates of schedules already provided.

42. In the event the Appellant withdraw its objection to the admission of the new schedules on the condition that HMRC gave a full explanation of which documents in Mr Humphries' existing statement they replaced. I directed accordingly.

Appellant's application for disclosure

43. The Appellant made an application by letter dated 4 July 2011 for disclosure of some 13 items. HMRC had largely complied with this request by the time of the hearing of the application. The outstanding items were:

> 3. Visit report re visit on 15 February 2007;
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> 6. Aide Memoir
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> 8. Means of knowledge ("MOK") submission;
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> 9. HMRC policy team's response to the MOK submission;
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> 10. A copy of instructions to HMRC officers;
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> 13. whether HMRC suspected or knew, at any time before the material transactions the subject of this appeal were carried out, that any of the traders in any or all of the material transaction chains (including the contra-chains), were defaulters, contra-traders or were engaged in MTIC fraud. If so, further and better particulars are sought. If not, written confirmation of the same is sought.

44. HMRC agreed that it ought to disclose items 3, 6, and 10 but wanted another 14 days in which to do so. The Appellant was content to agree to the 14 days and I made an order to this effect.

45. The Appellant requested disclosure of item 13 because, it said, it would be relevant to their case to show what HMRC knew about defaulters and contra-traders in the chains because it was part of their case that the Appellant would not have traded if they had been provided with appropriate warnings.

46. HMRC opposed this application because the issue is what the Appellant knew at the time and not what HMRC suspected at the time. They saw it as a fishing expedition and disproportionate to its likely probative value in the appeal.

47. The Appellant requested disclosure of the MOK submission and policy unit's response to it because it was their experience that the material might show that the Appellant was not at the time suspected of involvement in MTIC. They wanted to know how HMRC viewed the Appellant at the time.

48. HMRC opposed this application on the grounds that the contents of the MOK submission were in effect subsumed within the witness statements of the relevant witnesses.

49. My decision was to order disclosure of items 8 and 9 but not item 13. Although I was not convinced that the MOK submission and its reply by themselves were relevant to the hearing being just the opinion of HMRC officers of the Appellant, nevertheless those witnesses do express their opinion of the Appellant in the decision letter and in their witness statements and therefore it is right that the Appellant be given a chance to cross examine them on whether that opinion has changed as the credibility of those witnesses *is* relevant.

50. I refused to order disclosure of item 13 as I was not persuaded of its relevance but I was persuaded the disclosure sought would be very onerous in the context of the very large numbers of traders allegedly involved in cells of contra-trading. I was not persuaded of its relevance because, as it was explained to me by the Appellant, they would put the case that the Appellant would have behaved differently if warned. It is their case that they were not warned: it cannot make any difference to that fact whether HMRC could or should have warned them.

51. The information might of course be relevant to a judicial review of HMRC's actions but the appeal is against input tax refusal and is not a review of HMRC's actions.

Costs

52. The Appellant applied for the costs of today's hearing on the basis that under Rule 10 they had incurred wasted costs or HMRC's behaviour was unreasonable. This appeal is, as stated above, categorised as a complex case but one in respect of which the Appellant has opted out of the costs regime.

53. Whereas if this Tribunal had an unfettered costs jurisdiction, it may well have been appropriate to award some costs at least to the Appellant on the basis that today's hearing largely centred on HMRC's application for late admission of evidence, the Appellant's opposition to which was to some extent successful and in any event a hearing might have been avoided if HMRC's application was not late.

54. Our jurisdiction is not unfettered. The Appellant has to show that that wasted costs were incurred or that HMRC acted unreasonably in making the application. We

do not find that they did or that the costs were wasted in the sense of s29 of the Tribunals Courts and Enforcement Act 2007. We have already found that the Paris server evidence was only recently available. The Dutch server evidence and Mr Prescott's could have been served earlier but due to inefficiencies (but not deliberate behaviour) on HMRC's side were not: we do not consider HMRC acted unreasonably in seeking to admit the relevant and probative evidence late. And in the event HMRC were largely successful.

55. 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.

TRIBUNAL JUDGE
RELEASE DATE: 17 August 2011