This is the successful MTIC appeal of Ulster Metal Refiners Limited where CTM instructed David Bedenham, tax counsel, to appeal to the Court of Appeal after 2 unsuccessful appeals in the Tax Tribunal and Upper Tribunal. CTM offered a contingency fee arrangement where 50% was paid upfront and the remainder only if successful.

The Court of Appeal found that both the Tax Tribunal and High Court Judges had made errors in law and overturned both Judgements. It highlights the importance of a) not always accepting a loss in the Tribunal, and b) instructing the right (and cost effective) barrister to fight what were extremely complex legal arguments.

IN HER MAJESTY'S COURT OF APPEAL IN NORTHERN IRELAND

ON APPEAL FROM THE TAX AND CHANCERY CHAMBER

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BETWEEN:

ULSTER METAL REFINERS LIMITED

Appellant

and

THE COMMISSIONERS FOR HER MAJESTY'S REVENUE AND CUSTOMS

Respondent

_____

Before: Gillen LJ, Weir LJ and McBride J

_____

McBRIDE J (giving the judgment of the Court)

Application

[1] The appellant, Ulster Metal Refiners Limited ("UMR") seeks permission to appeal against the decision of the Upper Tribunal (Tax and Chancery) ("UT"), dated 20 July 2016 whereby it dismissed the appellant's appeal from the First Tier Tribunal ("FTT").

[2] Mr Bedenham appeared on behalf of UMR and Mr Taylor appeared on behalf of the Commissioners for Her Majesty's Revenue and Customs ("HMRC"). We are grateful to both counsel for their well-researched and ably presented submissions.

Background

[3] UMR was incorporated in 1972. It is a company based in Northern Ireland and from 2016 it was engaged inter alia in soft drinks transactions.

Chronology of Proceedings

[4] On 1 October 2012 HMRC denied UMR the right to deduct input tax in the total sum of £462,854.00 in respect of 115 purchases of soft drinks in the periods 03/11 and 06/11.

[5] This decision was made by HMRC on the basis that the input tax arose from transactions connected with the fraudulent evasion of VAT and UMR knew or should have known of that fact.

[6] UMR appealed HMRC's decision to the FTT.

Proceedings before FTT

[7] A five day hearing took place before the FTT panel, Judge Jonathan Cannan and Mr John Adrain FCA, on 3, 4, 5, 6 and 11 November 2014. Thereafter, the parties made further written submissions on 18 and 25 November.

[8] As required by Rule 25 of the Tribunal Procedure (First Tier Tribunal) (Tax Chamber) Rules 2009, HMRC filed a Statement of Case alleging that the relevant transactions were connected with Missing Trader Intra-Community Fraud. HMRC compiled a spreadsheet setting out the transaction chains and specifically alleged that the supply chain had been traced to "hi-jacked" traders and therefore to fraudulent tax losses. UMR, as appears from its witness statements filed at the outset, denied fraud and specifically indicated that HMRC had incorrectly traced the supply chains.

[9] The FTT, after hearing evidence, did not find fraud on the factual basis put forward by HMRC but found fraud on a different factual basis. At paragraphs 146-147, the FFT stated as follows:

> "146. … However, the fraud we have found was not precisely the fraud Mr Taylor invited us to find. HMRC's case was that the tax loss arose with the hi-jacked traders. We have found that the tax loss was Irwin's failure to account for VAT on its supplies to the appellant. … It is not the detail of the fraud which is relevant. It is the existence of fraud, in this case the VAT fraud of Irwin itself.
>
> 147. We are satisfied therefore that on the facts as found there is a sufficient connection between the relevant transactions and the fraud of Irwin."

Permission to appeal to UT

[10] The appellant's application for permission to appeal to the Upper Tribunal was refused by Judge Cannan on 25 August 2015. The appellant then applied to the UT for permission to appeal and on 11 November 2015 Judge Roger Berner granted permission, on the basis the appeal grounds gave rise to arguable questions of law.

Proceedings before UT

[11] UMR's appeal to the UT was on the basis the proceedings before the FTT were procedurally unfair as the FTT made a finding on a factual basis HMRC had not led in evidence, had not advanced in argument and had not pleaded. As a result of this and because UMR was not afforded sufficient opportunity to respond to the new case, UMR was denied a fair hearing.

Decision of UT

[12] The UT recognised that the complaint of procedural unfairness required it to reconstruct the procedural context. When carrying out this exercise, as appears from paragraph 30, the UT made the following findings:

(a) UMR did not dispute that the purchases were connected with fraud until approximately 8 weeks before the hearing and therefore the case proceeded to hearing on a basis not strictly in accordance with the parties' initial statements; and

(b) it was only during the course of hearing that UMR informed HMRC of another deal chain even though UMR knew from the outset that such a chain existed.

[13] Based on its understanding of the procedural context, the UT then proceeded to consider the question of procedural unfairness.

[14] The UT found at paragraphs 33 and 34 that, although the FTT found a case on a factual basis which HMRC had not pleaded, led evidence to support, or advanced in argument, it was a case which flowed logically from UMR's own case. The UT further held that UMR's counsel was on notice that

the FTT was considering finding fraud on a different factual basis, as evidenced by exchanges between counsel for UMR and Judge Cannan. During the course of these exchanges UMR was given the opportunity to make submissions on the new case. UMR's counsel however made no complaint he was taken by surprise or that UMR was disadvantaged because it had not come prepared to meet such a case. Since these complaints were not made to the FTT, it was too late for UMR to raise them for the first time on appeal. The UT determined that the conclusion the FTT reached was one which was properly open to it on the evidence before it.

Application for leave to appeal to Court of Appeal

[15] The applicant then applied to the UT for leave to appeal to the Court of Appeal. The UT was not persuaded that either of UMR's two grounds of appeal raised an important point of principle or practice or there was some other compelling reason why permission to appeal should be given. Accordingly, permission to appeal was refused on 13/9/16. The appellant thereupon applied to this court for leave to appeal pursuant to the Appeals from the Upper Tribunal to the Court of Appeal Order 2008, SI 2008 No 2834.

The grounds of Appeal

[16] The appellant submits the case merits further consideration by the Court of Appeal on the basis the UT erred in the following respects:

> "(i) In reconstructing the procedural context in which the FTT made its findings, the UT took into account various facts and matters that were simply incorrect or irrelevant and accordingly, the procedural context was not accurately reconstructed.
>
> (ii) In concluding that the FTT's approach and conclusions was one that did not give rise to procedural unfairness and was properly open to it the Upper Tribunal reached a decision that was perverse."

Submissions by the appellant's counsel

[17] The appellant's counsel submitted the UT erred in reconstructing the procedural context. In particular it erred in finding that UMR did not dispute the purchases were connected with fraud until 8 weeks prior to the hearing when in fact UMR challenged HMRC's case at the outset, as appears from the witness statements filed in 2003. In addition the FTT erred in finding that UMR in some way kept HMRC "in the dark" about the actual deal chain until the trial of the action. In fact HMRC was in possession of the same invoices as UMR and therefore HMRC was or should have been alert to the issue at the outset.

[18] Counsel further submitted that as the UT had completely misconstrued the procedural context any decision it made thereafter about procedural fairness was of necessity perverse.

[19] He contended the case involved important points of principle and practice. The UT itself had described this as an unusual case because it raised novel questions about the extent to which HMRC ought to be held to its pleaded case and the ability of the FTT to make a finding of fraud on a factual basis not advanced by HMRC.

[20] Mr Bedenham submitted that the FTT erred in finding fraud on a factual basis not pleaded by HMRC. He submitted HMRC was confined to its pleaded case and as HMRC had not amended its pleading it was not open to the FTT to come up with an alternative factual basis for a finding of fraud - the so called "third man theory".

[21] If, contrary to this submission, the FTT was entitled to come up with a "third man theory", he submitted the Tribunal must notify the parties of such an intention and afford them the opportunity to respond. He submitted the FTT failed to allow UMR to do. UMR was therefore taken by surprise and was not given an opportunity to meet the new case. As a result UMR were not given a fair trial.

Submissions by the respondent's counsel

[22] Mr Taylor submitted that the appellant had not set out any grounds to show why there was an important point of principle or practice or other compelling reason why permission to appeal should be granted. He further submitted that the core point in the appeal related to the question of procedural fairness. This point had been argued before the UT and rejected. In those circumstances this court ought to give particular deference to the fact two specialist tribunals had rejected UMR's case.

[23] In respect of the merits of appeal, he submitted the FTT was entitled to make the findings of fact it did as there was evidence before it to support such a finding and this evidence had been led by UMR. In these circumstances and in circumstances where HMRC was unaware of the exact details of the purchase chains UMR were referring to until shortly before the hearing, the Tribunal was entitled to make a finding on this alternative basis.

[24] UMR, he submitted, was not taken by surprise, as UMR had led the evidence and during an exchange between Judge Cannan and UMR's counsel, Judge Cannan made it clear that he was considering making a finding on this alternative basis. At no stage did UMR's counsel indicate his client required an adjournment to consider what further steps it needed to take to meet the case now being made against it. He further submitted that, there were no further steps UMR could take to resist the new claim made against it and in particular there were no other witnesses it could call.

Consideration

Leave to Appeal - Legal Test

[25] Article 2 of the Appeals in the Upper Tribunal to the Court of Appeal Order 2008 SI 2008 No 2834 provides:

> "Permission … for leave to appeal to the Court of Appeal in Northern Ireland shall not be granted unless the Upper Tribunal, or where the Upper Tribunal refuses permission, the appellate court, considers that-

> (a) the proposed appeal would raise some important point of principle or practice; or
>
> (b) there is some other compelling reason for the relevant appellate court to hear the appeal."

[26] This test has recently been considered by the Northern Ireland Court of Appeal in Martin v HMRC [2006] NICA 56 when Weir LJ endorsed the approach of Girvan LJ in McMahon t/a Irish Cottage Trading v Commissioners for Her Majesty's Revenue and Customs GIR8657 when he said:

> "On an application for permission to appeal from the rejection by the Upper Tribunal … of an appeal the question is … whether there is a compelling reason why the issue in which the claimant has failed twice at the two tiers of the tribunal system, which are competent to determine matters of that kind, should be subjected to a third judicial process."

[27] Similarly, in Tanfern v Cameron-MacDonald and Anor [2000] 1 WLR 1311 the English Court of Appeal considered the identical provisions of section 55(1) of the Access to Justice Act 1991 when Brooke LJ said at paragraph 42:

> "… It will no longer be possible to pursue a second appeal to the Court of Appeal merely because the appeal is `properly arguable' or because it has a `real prospect of success' … the decision of the first appeal court is now to be given primacy unless the Court of Appeal itself considers that the appeal would raise an important point of principle or practice, or that there is some other compelling reason for it to hear this second appeal."

[28] Further, in MA (Somalia) v Secretary of State for the Home Department [2011] 2 All ER 65 at paragraph 43 Sir John Dyson said:

> "Courts should approach appeals from (expert tribunals) with an appropriate degree of caution … they and they alone are the judges of the facts … Their decision should be respected unless it is quite clear that they have misdirected themselves in law. Appellate courts should not rush to find such misdirection simply because they might have reached a different conclusion on the facts or expressed themselves differently".

[29] This application raises the question whether a tribunal can make a finding on the basis of a "third man theory" that is, one which the judge suggests to the parties, but which has not been pleaded by the claimant. Secondly it raises the question whether, in the event that a tribunal is entitled to raise "a third man theory", what procedure it ought to follow in those circumstances. The UT itself acknowledged this was an "unusual case" because the FTT found fraud on a factual basis not pleaded or advanced by HMRC. We are satisfied this case raises important points of principle and practice which have not previously been adjudicated upon by the UT. For this reason we are persuaded that the appeal raises important points of principle and practice.

[30] We are further satisfied that the UT erred in its reconstruction of the procedural context. In particular it erred in finding that UMR did not dispute the case made by HMRC until 8 weeks before trial and erred in finding that UMR in some way had kept HMRC 'in the dark' about the correct supply chain. The UT therefore viewed the complaints of procedural unfairness through a prism which was fundamentally flawed. As a result, as appears from the judgment, it completely failed to address the question whether it was open to the FTT to raise a 'third man theory'. Further its analysis of the exchanges between Judge Cannan and UMR's counsel, to ascertain whether UMR were put on notice of the 'third man theory' and given a sufficient opportunity to meet it, was flawed as these exchanges were viewed through a prism of a procedural context which was fundamentally flawed.

[31] As a consequence we are satisfied the appellant has suffered "a wholly exceptional collapse of fair procedure" as referred to by Lord Dyson in R (Cart) v UT [2012] 1 AC 613. In addition this is a case where it is strongly arguable that there has been an error of law which has had truly drastic consequences. In particular UMR has sustained a loss of almost £500,000. For these reasons we consider there are also compelling reasons why permission

to appeal ought to be granted. Accordingly we find that the high hurdle has been met and we grant permission to appeal.

Consideration of substantive appeal

[32] In order to determine whether the statutory test for leave to appeal was met, it was necessary for this court to consider the merits of the case and for this reason the case was dealt with by way of a "rolled up" hearing. At the end of the hearing counsel for each party was given leave to file further submissions in respect of the substantive issues. Both the respondent and appellant filed written submissions. The appellant's submissions focussed on what remedy the court should grant in the event the appeal was allowed and made no further submissions on the substantive appeal. The respondent's submissions repeated many of the points made at the oral hearing in respect of the substantive appeal and then dealt with what order the Court should make in the event the appeal was allowed.

[33] Rule 25 of the Tribunal Procedure (First Tier Tribunal) (Tax Chamber) Rules 2009 requires HMRC to deliver a statement of case. The statement of case must, in accordance with Rule 25(2)(b) "set out the respondent's position in relation to the case". HMRC set out its case on the basis that there was a missing trader because the supply chain had been traced to "hi-jacked traders and to fraudulent tax losses". In contrast UMR in its witness statements made it clear that it did not accept any part of HMRC's case and specifically indicated that HMRC had incorrectly traced the supply chains.

[34] As noted by Lewison LJ in The Prudential Assurance Co Ltd v Commissioners for Her Majesty's Revenue and Customs [2016] EWCA Civ 376 at paragraph 20, pleadings play an important role in our adversarial system:

> "It is for the parties (subject to the control of the court) to define the issues on which the court is invited to adjudicate. This function is the purpose of statements of case. The setting out of a party's case in a statement of case enables the other party to know what points are in issue, what documents to disclose, what evidence to call and how to prepare for trial. It is inimical to a fair hearing that a party should be exposed to issues and arguments of which he has had no fair warning. If a party

> wishes to raise a new point, he should do so by amending a statement of case."

And further at paragraph 24 he stated:

> "Parties to litigation are entitled to know where they stand and to tailor their expenditure and efforts in dealing with (and only with) what is known to be in dispute".

[35] Thus pleadings, by enabling a party to know the case he has to meet play a central role in ensuring a fair trial.

[36] It is well established that in ordinary civil litigation involving allegations of fraud, the obligations in respect of pleadings are heightened. The fraud must be "distinctly alleged" and it must be sufficiently particularised. As Lord Millet said in Three Rivers District Council v Governor & Co of the Bank of England (No 3) [2003] 2 AC 1 at paragraph 186:

> "This is only partly a matter of pleading. It is also a matter of substance. As I have said, the defendant is entitled to know the case he has to meet. But since dishonesty is usually a matter of inference from primary facts, this involves knowing not only that he is alleged to have acted dishonestly, but also the primary facts which will be relied upon at trial to justify the inference. At trial the court will not normally allow proof of primary facts which have not been pleaded, and will not do so on a case of fraud. It is not open to the court to infer dishonesty from facts which have not been pleaded, or from facts which have been pleaded but are consistent with honesty. There must be some fact which tilts the balance and justifies an inference of dishonesty, and this fact must be both pleaded and proved".

[37] As noted in Blue Seer Global Ltd v HMRC [2008] UKVAT 20694 at paragraph 30 these principles apply just as much in tax appeals heard in the FTT as they do in other litigation.

[38] The nature of a case can change prior to or during the course of a hearing. In such circumstances it has long been established that a party can apply to amend its pleadings to raise any new points.

[39] The appellant, relying on the authority of Al-Medenni v Mars UK Ltd [2005] EWCA Civ 1041 submitted that the FTT could not find against UMR on a basis which HMRC had not made out in its original pleadings. Dyson LJ stated at paragraph 21:

> "In my view the judge was not entitled to find for the claimant on the basis of the third man theory. It is fundamental to our adversarial system of justice that the parties should clearly identify the issues that arise in litigation, so that each has the opportunity of responding to the points made by the other. The function of the judge is to adjudicate on those issues alone. The parties may have their own reasons for limiting the issues or presenting them in a certain way. The judge can invite, and even encourage, the parties to recast or modify the issues. But if they refuse to do so, the judge must respect that decision."

[40] As appears from the factual circumstances of Mars there was no hint of a "third man theory" in the witness statements or in the way in which the case was opened or in the evidence of the claimant's witnesses. In such circumstances we accept that it would not be open to a tribunal to pursue a "third man theory", as there would be no evidential basis for such a theory.

[41] We do not however, find that Mars lays down a general principle that a tribunal can never find for a claimant on the basis of a "third man theory". Rather we are satisfied that it is open to a tribunal or court to raise a "third man theory" when there is evidence or material before it to support such a theory.

[42] In this case we are satisfied there was evidence before the FTT which entitled it to raise a "third man theory". In particular there was evidence of fraudulent transactions on the basis of the supply chains as set out by UMR.

[43] As noted in Three Rivers a defendant is entitled to know the case he has to meet. In a fraud case this includes knowing the primary facts upon which fraud is alleged. When a tribunal wishes to find for a claimant on the basis of a "third man theory" there are a number of steps that it must take to ensure that the defendant is afforded a fair trial. In particular it must inform the parties clearly of the "third man theory" and then afford to the parties sufficient opportunity to respond to the new case and if necessary permit an adjournment to allow the parties time to make decisions about what further investigations they should carry out, what further evidence or disclosure they should seek, what further witnesses they should call and what further submissions they should make. These steps are essential and central to meeting the requirement of a fair hearing as they ensure the party has an opportunity to know exactly the case he has to meet and an opportunity to meet it.

[44] We have considered the exchanges between Judge Cannan and UMR's counsel as set out in the transcript. We are not satisfied that Judge Cannan clearly indicated to UMR's counsel that the tribunal was considering finding for the claimant on a different factual basis to that advanced by HMRC. This view is corroborated by the fact that HMRC never at any stage indicated it wished to rely on an alternative factual basis to find fraud and it never applied to amend its pleadings. Further, even though all the parties were given the opportunity to make further written submissions to the FTT after the hearing, no party made submissions in respect of the new alternative factual basis for a finding of fraud.

[45] As a result we are satisfied UMR was taken by surprise. It was not afforded an opportunity to meet the new case which was now being made against it. If it had been properly alerted to this by the tribunal, UMR would have had the opportunity to consider whether to apply for an adjournment and to consider whether it now wished to seek further disclosure, whether to call further witnesses (which it seems it could have done), or whether to make further submissions. The failure of the tribunal to permit this meant UMR was denied a fair hearing.

[46] We therefore find there was procedural unfairness and we allow the appeal.

Remedy

[47] The appellant contends that the court should in accordance with its powers under section 14 of the Tribunal Courts and Enforcement Act 2007, remake the decision and order that the appellant had a right to deduct input tax. The appellant further contends that the matter should not be remitted to the FTT as this would, inter alia, give HMRC a 'second bite of the cherry', that is, a chance to amend the case it previously made so it can now rely on the 'third man' theory; be anathema to speedy justice and finality of litigation and would cause real prejudice to UMR as delay hampers the ability of UMR to gather evidence and because UMR has "no more money to fight the case". The respondent contends that this court is not in a position to remake the decision as it has not been called upon to and has not considered the evidence in the case, nor has it arrived at any findings of fact. In these circumstances it is submitted that the matter should be remitted to the FTT. The respondent further submits that remittal to FTT is not giving HMRC a 'second bite of the cherry' as the 2007 Act provides for such a course of action.

[48] This court has not heard nor been asked to reconsider the evidence in this case and therefore we are satisfied we should not remake the decision. Taking account of all the circumstances, we are satisfied that it is in the interests of justice that the case should be remitted to a differently constituted FTT for a re hearing and we order accordingly.

[49] We will hear counsel in respect of costs.