TC01946

Appeal number LON 2007/1077

VAT – INPUT TAX – ***HMRC denied input tax claims totalling £8,327,278.00 in respect of 49 transactions of mobile phones and CPUs – Was there a VAT Loss? – Yes – Was the loss fraudulent? – Yes – Were the Appellant's transactions connected with the fraud? – Yes - Did the Appellant know or should have known that its transactions were connected to fraudulent evasion of VAT? – Yes the Appellant knew – Appeal dismissed – Reference to the CJEU – refused – Application to stay publication of the decision – Refused.***

FIRST-TIER TRIBUNAL
TAX

MAVISAT LTD **Appellant**

- and -

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

TRIBUNAL: Michael Tildesley OBE (Tribunal Judge)
Gill Hunter

Sitting in public at the Royal Courts of Justice, The Strand. London WC1 on 17 – 20; 24 - 28 October; 31 October & 3 November 2011 (17 & 24 were reading days).

Andrew Young counsel instructed by Dass Solicitors for the Appellant

Karen Robinson and Roshani Pulle counsel instructed by the General Counsel and Solicitor to HM Revenue and Customs, for the Respondents

DECISION

The Appeal

1. This appeal involved the disputed decisions of HMRC which were notified to the Appellant in letters dated 6 June 2007, 25 July 2007 and 2 January 2008. The decisions determined that the Appellant was not entitled to claim input tax repayment in the total sum of £8,327,278.00. The details of the specific claims were as follows:

(1) £1,929,578.22 claimed in respect of 14 transactions in the VAT period 04/06.

(2) £3,068,030 claimed in respect of 22 transactions in the VAT period 05/06.

(3) £2,312,012.50 claimed in respect of 7 transactions in the VAT period 06/06.

(4) £1,017,657.38 claimed in respect of 6 transactions in the VAT period 07/06.

2. HMRC submitted that the disputed transactions were an archetypal case of Missing Trader (Intra-Community) Fraud (MTIC). Moses LJ in *Mobilx Limited & Others v The Commissioners for Her Majesty's Revenue & Customs* [2010] EWCA Civ 517 at para.1 provided a succinct overview of the scale of MTIC fraud:

> "For many years, Her Majesty's Revenue and Customs (HMRC) have attempted to combat "missing trader intra-Community" VAT fraud. It is notorious that the trades in bulk mobile phones and computer chips are especially susceptible to that type of fraud. Latest published estimates (*Measuring Tax Gaps*, December 2009) disclose potential losses in 2005-2006 of up to £5.5 billion and in 2008-2009 of up to £2.5 billion. Lord Hope described the fraud as a "sophisticated attack on the VAT system", a "pernicious stratagem" and was of the view that Member States were justified in making use of "every means at their disposal within the scope of the Sixth Directive to eradicate it" (*Total Network SL v HMRC* [2008] UKHL 19 [2008] STC 644 § 6)."

3. HMRC contended that the transactions to which the Appellant's repayment claims related were connected with the fraudulent evasion of VAT and that the Appellant knew or should have known that its transactions were so connected. The Appellant disagreed with HMRC's contentions arguing that HMRC had failed properly to apply and state the law when examining the transactions giving rise to the claimed input VAT credits, and that HMRC's decision breached the Appellant's rights under the VAT Act 1994 and the VAT Directive.

4. Appellant's counsel in his closing submission argued that the Appeal involved grave and serious allegations against the Appellant and its director. In those circumstances the Tribunal must be clear as to the correct legal tests to apply. Counsel contended that in the light of recent developments Community law relating to repayment claims connected with the fraudulent evasion of VAT was no longer certain, in which case the Tribunal was obliged to refer a question to the Court of Justice for the European Union before making its determination on the Appeal.

HMRC disagreed with the Appellant's submission, arguing that the law was clear, and that the Tribunal should proceed with its determination.

The Evidence

5. The Tribunal heard evidence from the following persons for HMRC:

(1) Jayne Holden, the Officer with overall investigation of the Appellant's disputed repayment claims.

(2) Barry Patterson, the Officer on defaulting trader Zenith Sports.

(3) Malcolm Bycroft, the Officer on defaulting trader Midwest.

(4) Martin Evans, the Officer on defaulting trader 3D Animations.

(5) Dean Walton, the Officer on defaulting trader Vision Soft

(6) Moira Bamford, an Officer who visited the Appellant.

(7) David Ellis, an Officer who analysed the FCIB data on the Appellant's deals.

6. The witness statements of Timothy Reardon (Computec), Karen Davidson (Tradestar), Roderick Stone (Policy), Richard Meynell (FCIB evidence), Gordon Fyffe (Bullfinch) and Graham Taylor (C&B Trading) were unchallenged.

7. The witness statements of Jonathan Laing, Peter Goulding and Janice L'Argent were removed from the Tribunal bundles. The Officers had retired or left the service and their evidence was provided by other Officers.

8. Shamoon Alibhai, director, gave evidence for the Appellant.

9. Agreed bundles of documents were received in evidence. A transcript was kept of the evidence, and submissions.

Overview of the Law

10. Articles 167 and 168 of Council Directive 2006/112/EC provide:

> "167 A right of deduction shall arise at the time the deductible tax becomes charged.
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> 168. Insofar 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: 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".

11. Sections 24 to 26 of the VAT Act 1994 enact the right to deduct tax paid on goods and services used for the purposes of business into UK legislation. Thus a trader is entitled to the payment of input tax it claims.

12. The Court of Justice in the joint cases of *Axel Kittel v Belgium & Belgium v Recolta Recycling SPRL* (C-439/04 and C-440/04) established an exception to the right to deduct when the trader knew its transactions were connected to fraud. The Court stated:

> "51. In the light of the foregoing, it is apparent that traders who take every precaution which could reasonably be required of them to ensure that their transactions are not connected with fraud, be it the fraudulent evasion of VAT or other fraud, must be able to rely on the legality of those transactions without the risk of losing their right to deduct the input VAT (see, to that effect, Case C-384/04 *Federation of Technological Industries and Others* [2006] ECR I-0000, paragraph 33).
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> 52.It follows 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.
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> 53. By contrast, 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' are not met where tax is evaded by the taxable person himself (see Case C-255/02 *Halifax and Others* [2006] ECR I-0000, paragraph 59).
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> 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).
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> 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).
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> 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".

13. The Court of Appeal in *Mobilx Limited & Others v The Commissioners for Her Majesty's Revenue & Customs* [2010] EWCA Civ 517 clarified the test in *Kittel*

"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."

14. The Tribunal is obliged to consider four questions in determining this Appeal, and answer them all in the affirmative if the Appellant is to be denied its right to repayment. The questions were approved in the High Court decision of *Blue Sphere Global Limited v HMRC* [2009] EWHC 1150. The four questions are:

(1) Was there a VAT loss?

(2) If so was it occasioned by fraud?

(3) If so were the Appellant's transactions connected with such a fraudulent VAT loss?

(4) If so did the Appellant know or should it have known of such a connection?

15. HMRC has the burden of proving on the balance of probabilities its assertion that the disputed transactions were connected with the fraudulent evasion of VAT and the Appellant knew or should have known of their connection. In this Appeal the Appellant has put HMRC on proof to establish each element in the four questions posed in paragraph 14 above. The Appellant accepted that for the purposes of determining its state of knowledge at the relevant time, the Tribunal must examine that of its director, Shamoon Alibhai, the controlling mind for the company.

The Application for Referral to the Court of Justice

16. The substance of the Appellant's grounds for referring a question to Court of Justice was that

(1) The Court of Appeal decision in *Mobilx* can no longer be relied on as determinative of Community law and must not prevent the Tribunal from considering Community arguments which if correct must be applied.

(2) Upon a proper construction of *Kittel* the Appellant's supplies are not connected to fraudulent transactions. The Appellant contended that the *Kittel* analysis did not apply to chains of transactions, and that the knowledge test of *Kittel* is limited to knowledge of the activities of the immediate counter party (the Appellant's suppliers in the disputed transactions). The Appellant's contention is referred to as the *Privity of Contract* argument.

(3) Upon a proper construction of *Bulves AD v Bulgaria* [2009] ECHR 143 it cannot be correct for HMRC to accept output tax from suppliers and then deny the very same as input tax credit to the Appellant.

17. HMRC accepted that the Tribunal had power to refer a question in respect of Community law to the Court of Justice despite its view that the Court of Appeal decision in *Mobilx* had settled the outstanding issues in relation to the application of the legal test enunciated in *Kittel*. HMRC, however, strongly contested the substance of the Appellant's reasons for a referral.

18. The Tribunal considers it necessary to determine a procedural matter before examining the merits of the Appellant's application. This matter concerned the Appellant's view that the Tribunal should decide the application without making a determination on the factual matters in dispute. The Appellant argued that it would be inequitable to make findings of fact which may impugn the integrity and honesty of its director and controlling mind, Mr Alibhai, when the legal test was not clear.

19. Appellant's counsel at paragraph 25 of his closing submissions, however, acknowledged that there were a range of authorities which indicated that it was not usually necessary to seek a reference until the facts have been determined. Both the Court of Justice and national courts advise that reference should be made after the facts have been found, or identified by the National court or agreed by the parties (see for example *HP Bulmer Ltd v J Bollinger* [1974] Ch 401 & Joined cases 36/80 & 71/80 *Irish Creamery Milk Suppliers Association v Ireland* [1981] ECR 735).

20. Counsel did not consider the weight of authorities prevented referral of a question without determination of all the disputed factual issues. Counsel argued that there was sufficient consensus between the parties in respect of the key facts to frame an appropriate question for consideration by the Court of Justice. HMRC's counsel disagreed, stating that it was news to HMRC that any of the facts on this particular appeal were agreed.

21. The Tribunal notes that the Appellant made its Application for referral after the evidence had been heard. Given the weight of authorities and that the Tribunal is in a position to determine the facts which may result in the Appeal being allowed, the Tribunal decides to reserve consideration of the Appellant's application on its merits after its findings on the facts.

Background

22. The Appellant was a limited company which was incorporated on 11 June 2001 under the name *Speed 8825 Limited*. Between 11 June 2001 and 26 March 2002, the director and company secretary were Waterlow Nominees Ltd and Waterlow Secretaries Ltd respectively. On 4 February 2003, the company name was changed to Mavisat Limited by special resolution.

23. The Appellant was registered for VAT from 1 May 2003. In its application for VAT registration Mr Alibhai stated that its business was *mobile satellite services*. Within the same application, Mr Alibhai declared the estimated value of taxable supplies to be made in the next 12 months was £500,000, and confirmed that the Appellant did not expect to receive regular VAT repayments.

24. The principal place of business for the Appellant was declared to be 2 Wokingham Road, Reading, RG6 1JG. During the relevant periods, the Appellant rented premises at that address.

25. According to the Appellant's monthly VAT returns, the turnover of the business grew very slowly between 1 May 2003 and 30 June 2005 but increased substantially

from July 2005 onwards. The Appellant's turnover for the period 06/03 until 06/05 was £49,179 whilst its turnover for the period 07/05 until and including 07/06 was £76,677,058.

26. When he left University in 1995 Mr Alibhai joined a firm called RCX Computers as a sales person selling computers, laptops and hardware. Mr Alibhai's brother was a partner in RCX which operated a retail computer outlet on Kings Road in Reading. In 1998 Mr Alibhai took over the business from his brother and partner and formed a limited company under the name of Reading Computers Limited. On 1 April 1998 Mr Alibhai applied for the VAT registration of Reading Computers Limited which described its main business activity as a computer retailer. Mr Alibhai stated that Reading Computers sold computers direct to the public from its shop and through mail order. Mr Alibhai also asserted that Reading Computers carried out wholesale trades but acknowledged that he did not inform HMRC of this fact. Mr Alibhai sold Reading Computers Limited in 2002 to a Mr Durgesh Mehta because the reputation of the company had been damaged by a criminal trial involving the supply of alleged counterfeit Microsoft software. Mr Alibhai was one of ten defendants in the trial. He was acquitted of all criminal charges.

27. In 2000 Mr Alibhai set up another limited company under the name of Mobile Computer World which did not start trading until 2002 when it effectively resumed the retail business previously transacted by Reading Computers Limited. Mr Alibhai was appointed a director of Mobile Computer World on 3 January 2002.

28. On 26 March 2002, Mr Alibhai became one of the Appellant's directors. A Mr Azhar Hussain was appointed as the other director and company secretary for the Appellant. Messrs Alibhai and Hussain have remained in those posts to date.

29. Mr Alibhai stated that the Appellant was set up to sell satellite mobile phones which were directed at the armed forces in the UK and USA. Mr Alibhai accepted that this was a niche business, which did not produce the turnover as anticipated in the business plan. The Appellant's turnover in the first 26 months of its VAT registration was just under £50,000. The Appellant began trading in standard mobile phones from June 2005 which produced a turnover of £76 million in the space of 13 months.

Outline of the Disputed Transactions

30. The disputed April transactions involved the wholesale supply of both mobile telephones and computer processing units (CPUs). In ten of the deals the Appellant purchased mobile phones from a UK VAT registered company, Kingswood Trading Services Limited (Kingswood), and sold them to two customers in France, France Affaires and La Parisienne Du Commerce. In the other four deals involving CPUs the Appellant's supplier was UK VAT registered company, Tradestar International Limited (Tradestar), with the CPUs being sold onto Mikromkt, a Maltese registered company. The 14 deals were transacted over two days at the end of April 2006 (27 & 28 April 2006).

31. The disputed May transactions consisted of 22 wholesale supplies of mobile telephones to a company outside the UK. The Appellant's supplier and customer in each deal were the same: Tradestar (the supplier) and Mikromkt (the customer). The deals were conducted over period of five days at the end of May (26 May to 31 May 2006).

32. The disputed June transactions concerned seven wholesale supplies by the Appellant of mobile telephones to a company outside the UK. The Appellant's supplier and customer in each deal were the same: Tradestar (the supplier) and Mikromkt (the customer). Six of the deals were conducted on the last two days of June 2006, whilst the other one was transacted on 22 June 2006.

33. The disputed July transactions concerned six wholesale supplies by the Appellant of mobile telephones to a company outside the UK. The Appellant's supplier and customer in each deal were the same: Tradestar (the supplier) and Mikromkt (the customer). Three of the deals were conducted on the last day of July 2006, two deals on the 28 July 2006, and one on the 17 July 2006.

Defaulting Traders

34. Officer Holden conducted an extended verification of the 49 disputed deals which identified a defaulting trader responsible for the fraudulent tax loss in each of the deals. The evidence showed that the supply from the defaulting trader was linked to the Appellant's disputed supplies through a series of invoices, release notes and other documentation from the defaulter to the intervening traders and the Appellant.

35. The one exception to this was the supply on the 17 July 2006 (deal 44) where there was no invoice from the purported defaulter, Vision Soft, to the first line buffer, Globaltech. Limited. There were, however, a number of allocation and release notes provided by Global International Freight, the freight forwarder, to Officer Holden which enabled her to identify Vision Soft as the defaulting trader for the 17 July 2006 transaction. Officer Holden's analysis was corroborated by the evidence of the payments made by the various parties in this deal chain, which showed payments from Vision Soft to Proxi Partners for the goods transacted on 17 July 2006. The Tribunal is satisfied on the evidence which was set out more fully in paragraphs 7.3 to 7.11 of HMRC's Closing Submissions dated 3 November 2011 and adopted by the Tribunal that Vision Soft has been correctly identified as the defaulting trading for the 17 July 2006 deal.

36. The Tribunal makes the following findings of fact in respect of each alleged defaulting trader.

Computec Solutions Limited (Computec)

37. Officer Reardon's witness statement was admitted in evidence. HMRC alleged that Computec was the defaulting trader in four of the Appellant's April (Deals 1, 4 6 and 7) which involved supplies of CPUs.

38. Computec was registered for VAT on 1 November 2004 with an intended business activity of *software development and consultancy and computer components.* Various people appeared to have been director and secretary of the company prior to 3 April 2006 and 25 April 2006 when Fawad Qazi and Aboobacker Ummermoideen respectively became the director and secretary of the company. Computec submitted nil returns for the six VAT periods until 28 February 2006.

39. HMRC obtained allocation notes and release notes from a freight forwarder which suggested that Computec had acquired substantial quantities of mobile telephones from Estonia and Spain and subsequently released the items to UK purchasers. On 5 May 2006 HMRC issued a Regulation 25 Notice on Computec requiring it to submit a VAT return for the period ending 5 May 2006.

40. In the period July 2006 to April 2008 HMRC issued 17 VAT assessments to the total value of some £105 million which related to invoices to the value of £600 million issued between 3 April 2006 and 9 May 2006.

41. The assessment in the sum of £24,706,503 dated 27 July 2006 related to tax losses accruing from sales to Zenith Sports. Included within that assessment were tax losses accruing from sales of CPUs to Zenith Sports which were subsequently traced to the Appellant's April deals 1, 4, 6 and 7. Computec has not appealed or paid the assessments.

42. HMRC has received no communication from the company since 5 May 2006 other than from an insolvency practitioner in connection with the company's liquidation. Computec was made the subject of a winding up order on 24 January 2007.

43. The Tribunal finds that Computec incurred VAT losses in the sum of £752,119.99 in connection with its transactions in CPUs with Tradestar which were traced to the Appellant's four deals conducted in April 2006 (deals 1, 4, 6 and 7). The Tribunal is satisfied that the losses were fraudulent because:

(1) Computec was dormant for almost two years and then made some £600 million of sales within a month or so.

(2) Computec issued VAT invoices in respect of those sales yet failed to declare the resultant tax liability to HMRC.

(3) Computec (through its officials) failed to make contact with HMRC following its deregistration and effectively went missing.

Midwest Communications Limited (Midwest)

44. Officer Bycroft gave oral evidence on his statement HMRC contended that Midwest was the defaulting trader in five of the Appellant's April deals (deals 2, 5, 10, 11 and 14) which involved supplies of mobile phones.

45. Midwest was incorporated on 15 June 2004. On that date, Brent Gardiner was appointed company secretary and director and Marian Rose Beckett was appointed

director. On 10 April 2006, Simon Powell-Smith was appointed company secretary. Midwest was registered for VAT with effect from 6 June 2005 and expected to trade in mobile phone contracts and handsets, a specific market which was considered unlikely to be used in MTIC fraud. Midwest's VAT1 indicated that it did not expect to receive regular repayments of VAT and that the estimated value of taxable supplies in the next 12 months was £100,000.

46. In March 2006, HMRC received information in the form of allocation and release notes from freight forwarders which suggested that Midwest might be involved in MTIC fraud. On 16 March 2006, HMRC officers visited the Peterborough address and spoke with Mr Powell-Smith who said that Midwest had not traded for 6 months. He also denied that Midwest had dealt with Global Access International and Hawk Logistics. Mr Powell-Smith, however, later that day sent a fax to HMRC indicating that he had misled HMRC. He accepted that he had been in touch with Hawk Logistics with regard to goods for supply to Global Access but that the deal had not gone through.

47. On 20 April 2006, Mr Powell-Smith informed HMRC that Midwest had commenced trading in the last 24 hours. He confirmed that Midwest was making efforts to contact EU traders to source its supplies. On 25 April 2006, Mr Powell-Smith informed HMRC that Midwest had purchased goods from Megatek in France and Hardware Traders in Germany, with all goods then sold on to UK traders. Mr Powell-Smith promised to forward HMRC details of all deals completed by Midwest.

48. A VAT return rendered by the company (without remittance) on 4 May 2006 showed net sales of over £664 million and net purchases within the UK of approximately £664 million. The return suggested that Midwest's output tax exceeded the input tax reclaimed by only £8,109.

49. Midwest's purchases in the UK involved supplies of £50 phone cards from a company known as Bestleg Limited. HMRC discovered that the principal place of business for Bestleg Limited was a residential address used as a mail drop. HMRC was unable to contact any official of Bestleg. The issuer of the purported phone cards only supplied cards in the denomination of US dollars. Mr Powell-Smith acknowledged that he had not checked whether the phone cards existed and not carried out due diligence on Bestleg. Midwest held no documentation evidencing the export of the phone cards. The company (Umbria Equitazione) to whom Midwest purportedly sold the phone cards was a wholesaler in saddles which did not deal in international pre-paid phone cards.

50. HMRC disallowed Midwest's claim for input tax credit in respect of the supplies from Bestleg in its 4 May 2006 return on the basis that the goods supplied were not as described on the invoices. On 10 August 2006 HMRC assessed Midwest for over £57 million in respect of the input tax wrongly claimed on the phone card transactions. The issue of the assessment pre-empted the creditor's meeting called by insolvency practitioners on behalf of Midwest. Midwest has not appealed against the assessment and made no payments against it.

51. Officer Bycroft advised that a letter dated 28 September 2010 was received from Grant Thornton, the liquidators appointed for Midwest which stated that they were expecting to recover £22,519 from Midwest's FCIB account and had secured default judgments against two of Midwest's customers. Officer Bycroft, however, confirmed at the hearing that the electronic folder as at 24 October 2011 showed that the liquidators for Midwest had submitted no payments in respect of the assessment.

52. HMRC also discovered that Midwest routinely overpaid its EU suppliers for the mobile phone deals, and in many cases made payments to third parties. In respect of the five deals involving the Appellant, Midwest acquired the goods from Hardware Traders Ltd Deutschland. Midwest paid a third party, Maks Information Technology based in Pakistan, for these goods at a value of approximately 117 per cent of the invoiced amount. Effectively Midwest operated as a conduit for a money transfer between its customer and the third party, for which it charged a small commission.

53. The Tribunal is satisfied that there was a tax loss occasioned by Midwest in respect of the five disputed deals. The tax loss arose from Midwest' s failed attempt to offset the output tax liability on its UK mobile phone supplies against the disallowed input tax claim on the fictitious supplies of phone cards from Bestleg.

54. The Tribunal finds that the tax loss occasioned by Midwest was fraudulent because of :

(1) The massive increase in turnover for the business over a short period of time.

(2) Mr Powell-Smith, the company secretary, provided false information to HMRC when asked about the nature and circumstances of the company's trade, in particular omitting to tell HMRC of its purported sales of phone cards to a company in Italy.

(3) The use of third party payments.

(4) The habitual overpayment of its suppliers (or third parties) for mobile phones which had the effect of depriving Midwest of the necessary resources to meet its VAT liabilities.

(5) The failed attempt by Midwest to offset its output tax liability on its mobile phone supplies against the input tax purportedly incurred on phone card transactions which were not genuine.

(6) The director of Midwest, Mr Gardiner, was made the subject of a disqualification order under the Company Directors Disqualification Act 1986 for a period of 13 years (with effect from 7 January 2009). The reason for the order was that he knowingly caused Midwest to undertake a method of trade which involved it in and put HMRC at risk of being subjected to MTIC fraud.

C&B Trading (UK) Limited (C&B)

55. Officer Taylor's witness statement was admitted in evidence. HMRC alleged that C&B was the defaulter in two of the Appellant's April deals chains (Deals 3 and 8).

56. C&B was incorporated on 30 January 2001 under the name *C and B Car Care Limited* which was registered for VAT with effect from 1 May 2003 and subject to quarterly returns. In its VAT 1 C&B described its business activity amongst others as *car valeting* with an estimated taxable turnover in the next 12 months of £80,000. C&B indicated that it did not expect to receive regular repayments of VAT and to conduct trade with the EU.

57. On 22 February 2006, C&B wrote to HMRC advising that it was to commence trading in chemicals and alloy wheels and that it had a new trading address. On or around 16 March 2006, HMRC received a further letter from C&B requesting that its trade classification be amended to *general trading*.

58. In April 2006, HMRC received information from Paul's Freight which suggested that C&B was trading in mobile telephones. As a result on 26 April 2006 HMRC officers made an unannounced visit to C&B's trading address. The officers were unable to gain access to the premises on that occasion. Officer Taylor made a call to the trader on 26 April 2006 and spoke with the company secretary, Mr Mooney, who confirmed that C&B had purchased mobile phones from a Czechoslovakian company and sold them onto UK companies. It was explained to Mr Mooney that C&B would have a large VAT liability in those circumstances.

59. In light of the discovery that C&B was acquiring large quantities of mobile telephones from the EU, a Regulation 25 letter was issued which brought forward the due date of the 04/06 return to 2 May 2006. A letter was also sent to C&B from HMRC advising it that its VAT registration had been cancelled with effect from 1 May 2006. No VAT return for the 04/06 period was ever rendered.

60. Officer Taylor made a further attempt to visit C&B on 2 May 2006 but was unable to gain access to its premises and obtained no response to telephone calls. C&B went into compulsory liquidation on 10 January 2007.

61. Assessments in excess of £82 million have been made against C&B. A number of those assessments, together with other mail, have been returned to HMRC marked *no longer here*. Included within the assessment made on 7 July 2006 were tax losses sustained in respect of two transactions which can be traced to the Appellant's April deals 3 and 8. C&B has not appealed or paid the assessments.

62. The Tribunal finds that C&B incurred VAT losses in the sum of £215,525.63 in connection with its transactions in mobile phones with VT (UK) Ltd which were traced to the Appellant's April deals 3 and 8.

63. The Tribunal is satisfied that the losses were fraudulent because of:

(1) The use of an existing company with a VAT registration number by new directors to trade in mobile phones. This ruse enabled the directors to circumvent VAT checks applied to new companies set up with the declared intention to trade in MTIC goods.

(2) The trade classification *other wholesale* and its failure to notify HMRC of its change of address allowed C&B to enter MTIC deals without coming to the attention of HMRC.

(3) C&B turned over more than £500 million within a month or so with no obvious infrastructure.

(4) C&B failed to account for VAT on the onward supplies of mobile phones to UK companies.

(5) C&B and its officers have had no contact with HMRC since the issue of the assessments, and the officers have effectively disappeared.

Bullfinch Systems Limited (Bullfinch)

64. Officer Fyffe's statement was admitted into evidence. HMRC alleged that Bullfinch was the defaulting trader in three of the Appellant's April deals (Deals 9, 12 and 13).

65. Bullfinch was incorporated on 28 May 2004 and registered for VAT with effect from 1 August 2005. The company director was named as Sanjay Pandya, appointed on 28 May 2004. Bullfinch's VAT1 declared that its business activities involved *software and security implementation, no hardware.* The VAT1 also stated that Bullfinch did not expect to receive regular repayments of VAT and that the estimated value of its taxable supplies in the next 12 months was £1million.

66. Bullfinch submitted two VAT returns in 2005. The first showed a turnover of over £7 million and a VAT liability of approximately £19,000 and the second showed a turnover of £1.5 million. Bullfinch agreed to provide a security deposit on 12 October 2005.

67. HMRC visits to freight forwarders revealed the existence of release notes and allocation notes which showed that mobile phones and CPUs were released to Bullfinch between 6 April 2006 and 9 May 2006 from the Czech Republic and Romania. On 11 May 2006 HMRC issued Bullfinch with a Regulation 25 letter requesting immediate submission of its VAT return for the period 04/06. The returns were never submitted and Bullfinch was deregistered from VAT on 13 May 2006.

68. HMRC raised assessments on Bullfinch totalling some £56 million in respect of its transactions conducted in April and May 2006. The assessment issued on 28 June 2006 included that VAT on the supply of 2,900 x Nokia N90 mobile telephones to IH Technologies Limited which was related to the Appellant's deal 12 (April). The assessment issued on 3 July 2006 incorporated the VAT on the supplies of1,650 x Nokia 8801 mobile telephones and 3,100 x Nokia N90 mobile telephones to The Wireless Warehouse which were related to the Appellant's April deals 9 and 13 respectively). Bullfinch has not appealed the assessments or made payments towards them.

69. There has been no contact with Mr Pandya, Bullfinch's director, since May 2006 with post sent to business and personal addresses being returned undelivered. It is believed that Mr Pandya has left the UK and is living overseas.

70. The Tribunal finds that Bullfinch incurred VAT losses in the sum of £347,165.75 in connection with its transactions in mobile phones with IH Technologies Limited and The Wireless Warehouse which were traced to the Appellant's April deals 9, 12 and 13.

71. The Tribunal is satisfied that the losses were fraudulent because:

(1) Bullfinch entered into transactions worth hundreds of millions of pounds between 6 April 2006 and 9 May 2006 with no real base for business operations.

(2) Bullfinch issued invoices charging VAT on its supplies during April and May 2006 but failed to declare its VAT liability on these supplies in a VAT return.

(3) Bullfinch and its director have had no contact with HMRC since May 2006. The director has left the jurisdiction and fled overseas.

3D Animations Limited (3D)

72. Officer Evans assumed responsibility for 3D in July 2008 following the resignation of Officer Lane. He gave oral evidence in support of his statement which was based on information from HMRC's electronic folder and his conversations with Officer Lane.

73. HMRC contended that 3D was the defaulting trader in the Appellant's May deals, which comprised 22 transactions involving supplies of mobile phones.

74. 3D Animations Limited ("3D") was incorporated on 5 April 2006 and registered for VAT with effect from 3 May 2006. The company officials in place at the date of incorporation resigned soon after incorporation. On 10 April 2006, Kalidas Gopal was appointed company secretary and on 15 April 2006, Gengatharan Sritharan was appointed director of the company. 3D declared in its VAT1 that its current and/or business activities were *design, multimedia and animation graphics.* The estimated taxable turnover for the next 12 months was said to be £89,000. 3D indicated that it did not intend to sell to or buy from other EU members states in the next 12 months. 3D was required to render monthly returns. No returns were submitted by the company, which was deregistered by HMRC before completing its first quarter as a VAT registered entity.

75. Stock release notes provided to HMRC by freight forwarders suggested that 3D had been allocated substantial quantities of stock from EC based companies. On 1 June 2006 Officer Lane visited 3D at its principal place of business. The property was a residential address which appeared to have been converted into offices. *3D Animations* had been written on a piece of paper which was taped to the front door. No-one was present during the visit and a Registration 25 letter (bringing forward the VAT return due date) and a 7 day de-registration letter were posted through the

letterbox. 3D failed to respond to any of the notices issued at the principal place of business. As a result it was deregistered for VAT with effect from 7 June 2006.

76. HMRC raised assessments against 3D totalling in the region of £128 million. The assessment dated 16 January 2007 to the value of £44,858,014 included transactions from 3D to Globaltech Services with a net value of £17,464,730 and VAT due of £3,056, 327.75 which were traced to the Appellant's 22 disputed May deals. 3D has not appealed the assessment and made no payments towards it. On 20 September 2006 3D was compulsorily wound up. The liquidator has been unable to recover the sums owed by 3D.

77. The records extracted from FCIB showed that 3D issued third party instructions with payments made to an account in the name of Kalidas Gopal.

78. The Tribunal finds that 3D incurred VAT losses in the sum of £3,056,327.75 in connection with its transactions with Globaltech Services which were traced to the Appellant's 22 deals conducted in May 2006.

79. The Tribunal is satisfied that these losses were fraudulent because:

(1) Almost immediately after 3D was incorporated and given a VAT Registration Number it acquired substantial quantities of mobile phones from the EU for onward sale in the UK, despite its assertions a month earlier that its business activities involved *design and animation*.

(2) The gross value of sales conducted by 3D Animations in the single month it held a VAT Registration Number was approximately £866 million.

(3) The sheer volume of transactions against a background of a new company which had no history in the trade sector and an insufficient infrastructure to support such a volume of trade.

(4) 3D continued to trade after the deregistration notices had been posted without making contact with HMRC.

(5) 3D issued VAT invoices but failed to declare the resultant liability to HMRC.

(6) The use of third party instructions which had the effect of depriving 3D of the wherewithal to meet its VAT liabilities.

Vision Soft UK Limited (VSUK)

80. Officer Walton gave oral evidence in support of his statement on the activities of VSUK drawn from the various databases held by HMRC. Officer Walton took over responsibility for VSUK from Officer L'Argent.

81. VSUK was the purported defaulting trader in respect of the Appellant's seven deals in June 2006 (deals 37 - 43) and one deal in July 2006 (deal 44). The deals involved supplies of mobile phones.

82. VSUK was incorporated on 8 October 2004 and registered for VAT with effect from 15 March 2005 (quarterly VAT returns). VSUK's VAT1 declared that its intended business activities were *software development, consultants and supply*. Further the VAT1 indicated that no purchases or sales were anticipated to or from other EU member states, and that it did not expect to receive regular repayments of VAT. The estimated value of VSUK's taxable supplies in the next 12 months was £80,000.

83. VSUK rendered five 'nil' returns for the periods 05/05 to 05/06 inclusive. In early July 2006, documents scanned and saved on HMRC's electronic folder suggested that VSUK had acquired goods from the EU. On 6 July 2006, an HMRC Officer visited VSUK's principal place of business which was found to be an address for a residential block of flats. In those circumstances HMRC cancelled the VAT registration of VSUK with effect from 6 July 2006 which was later amended to 13 July 2006.

84. HMRC issued assessments against VSUK to the total value of £12,122,801.37 in respect of unpaid VAT arising from its dealings in mobile phones and other goods. Some of those assessments related to the output tax outstanding on the eight transactions between VSUK and Global Tech Services Ltd which were linked to the Appellant's deals in June 2006 and its first deal in July 2006. VSUK has not appealed the assessments and made no payments on them.

85. The assessment against VSUK which related to the Appellant's disputed July deal 1 was made in respect of supplies completed after the date of the Appellant's deregistration. HMRC argued that the assessment remained valid because the value of the supplies (£1.4million) was well in excess of the VAT registration limit which meant that VSUK would have had to account for VAT on the supplies. The Appellant did not challenge HMRC's interpretation of VSUK's liability in respect of the July supplies of mobile phones. The Tribunal is satisfied that a tax loss has been occasioned by the actions of VSUK in connection with its supplies of mobile phones on 14 and 17 July 2006.

86. HMRC sent a number of assessments to the York Street address, together with the personal addresses of the company secretary and director as disclosed in Companies House records. The assessments have all been returned with the addressee said to be unknown. The Officers of VSUK have not contacted HMRC, and no VAT returns have been submitted since 05/06. VSUK was compulsorily wound up on 16 January 2008.

87. The Tribunal finds that VSUK incurred VAT losses in the sum of £2,528, 653.07 in connection with its transactions with Globaltech Services which were traced to the Appellant's seven deals conducted in June 2006, and its first deal in July 2006.

88. The Tribunal is satisfied that these losses were fraudulent because:

(1) The address of VSUK's principal place of business was changed without the required notification to HMRC. The officers of the company did not reside at the address declared on Companies House records.

(2) Following the appointment of Mohammad Shafiq as company director (June 2006), VSUK generated a turnover in excess of £60 million in just two months.

(3) VSUK did not render a VAT account in respect of its trading in June 2006. HMRC uncovered the trading from its analysis of records held by other traders and freight forwarders.

(4) VSUK has filed no accounts with Companies' House.

(5) No contact has been made by the company or its officers with HMRC regarding the assessments. VSUK effectively went missing after its trading in June and July 2006.

Zenith Sports (UK) Limited (Zenith)

89. Officer Patterson gave oral evidence in support of his witness statement on the activities of Zenith. He has been involved with the VAT affairs of Zenith since 2006. HMRC alleged that Zenith was the defaulting trader in respect of five of the Appellant's July deals (Deals 45 – 49).

90. Zenith was incorporated on 14 December 2004 and registered for VAT from 1 August 2005 to 13 December 2006 trading as i-Connect Technologies. Zenith's VAT1 declared its business activities as a *wholesaler of sports accessories, mobile phone accessories, memory and more.* Zenith stated that its expected taxable turnover in the next 12 months would be £100,000 and that it was unlikely to buy from or sell to other EU states during that period.

91. On 27 March 2006 HMRC officers visited Zenith and formed the impression at that time that it was trading in sports goods. However, on 12 June 2006, the officers received a request from HMRC's MTIC team for an urgent visit to be made to Zenith. The visit did not take place not until 29 June 2006 owing to the non-availability of the trader. At the visit, Ms Basharat put herself forward as a director of the company, although Companies House records revealed that she resigned from that post on 1 June 2006. Ms Basharat confirmed that Zenith's main business activity was the wholesale supply of mobile telephones and CPUs. The daybook available suggested substantial sales had been conducted by Zenith.

92. By letter dated 21 July 2006, HMRC informed the company that its VAT liability to HMRC for the period 05/06 was £1,717, 527.75 and an assessment was raised in that sum. In February 2007 Zenith paid approximately £32,000 towards its VAT liability under the July 2006 assessment. Further assessments were issued against Zenith on 1 June 2007 and 18 December 2007 which incorporated the unpaid VAT on the supplies traced back to the Appellant's July deals. Zenith has made no payments in respect of the last two assessments. Zenith has not appealed against the assessments.

93. After February 2007 HMRC was unable to contact Zenith either by mail or by visits to the places of business. Zenith was compulsorily wound up on 16 January 2008, and dissolved on 22 September 2008.

94. The total amount outstanding by way of assessments, penalties and interest in respect of Zenith was £17,647,566.69 which included the sum of £1,434,721 raised by way of assessment issued on 1 June 2007. This assessment incorporated the VAT incurred on the sales made by Zenith traced directly to the Appellant's transactions in deals 45 – 49.

95. The Tribunal finds that Zenith incurred VAT losses in the sum of £1,434,721 in connection with its mobile phone transactions with Neon (Leicester) Limited which were traced to the Appellant's five deals conducted in July 2006 (deals 45-49).

96. The Tribunal is satisfied that these losses were fraudulent because:

(1) The principal business activity of Zenith changed from sports goods to mobile phones soon after registration for VAT.

(2) Zenith submitted no VAT returns for periods 05/06, 08/06 or 09/06 despite having issued VAT invoices during those periods;

(3) The net turnover for Zenith increased from £13,726 to £116,129,386 in the space of six months with there being no corresponding increase in staff, accommodation or capital;

(4) Zenith has repeatedly failed to respond to contacts made by HMRC and has failed to produce records as requested. Zenith effectively became a missing trader.

(5) Ms Basharat has been disqualified from acting as a company director for a period of 11 years (having given an undertaking) with effect from 26 February 2010. The schedule of unfit conduct cited that Zenith traded in such a manner that put HMRC at risk of MTIC fraud.

Was there a VAT loss occasioned by fraud in respect of the 49 disputed transactions?

97. The Appellant did not object to the admission of the witness statements of Officers Reardon, Taylor and Fyffe in respect of their evidence on the activities of the defaulting traders, Computec, C&B Trading Limited and Bullfinch. The Appellant made no substantial challenge to the evidence of Officers Evans, Walton and Patterson in respect of the defaulting traders, 3D Animations Limited, Vision Soft UK and Zenith Sports. The Appellant questioned Officers Evans and Patterson on the payments made by the traders to discharge their VAT liability. Officer Patterson accepted that Zenith Sports had made one payment of approximately £32,000 which the Tribunal was satisfied related to an earlier assessment than the ones which were connected to the Appellant's disputed deals.

98. The Appellant described Midwest as a failed contra-trader but did not develop its argument how that affected the issue of a VAT loss occasioned by fraud. The

Tribunal was satisfied on the evidence that Midwest did not discharge its VAT liability on the acquisition of the mobile phones which constituted the goods supplied in the Appellant's April deals 2, 5, 10, 11 and 14. This tax loss was occasioned by the fraudulent actions of Midwest with its attempt to offset its VAT liability by a repayment claim derived from fictitious supplies of phone cards.

99. Appellant's counsel stated that it had put HMRC to proof on the fraud in the supply chains. The Appellant had listened to the evidence and in some cases did not consider that the evidence was as cogent as it could have been. On the other hand the Appellant felt in some cases, on the balance of probabilities, that there have been tax losses and the likelihood that those losses were occasioned by fraud. Counsel pointed out that he was prohibited by the Bar Code to allege fraud against any person save in two circumstances which were that he had clear instructions from his instructing solicitor and that the information was sufficient to justify such allegations. Counsel did not have the necessary instructions, and was not in a position to accept on behalf of the Appellant that HMRC had met the necessary standard to prove the tax losses and that they were occasioned by fraud.

100.Counsel at paragraph 15(2) of closing arguments contended that any judicial determination as to allegations made against non-parties which have not been afforded the opportunity to attend the appeal or even an interview may compromise the rights of non-parties to a fair trial. HMRC counsel had no truck with this argument pointing out that it was perfectly proper for the Tribunal to determine allegations against persons who were not before the Tribunal. HMRC counsel cited the example of a criminal conspiracy trial where for one reason or another not all parties to conspiracy were before the court but that did not prevent the jury from making findings of fact adverse to the non-attending party.

101.The Tribunal observes that Appellant's counsel has made a sweeping generalisation about the cogency of the evidence adduced by HMRC in support of its allegations of fraudulent tax losses without specifying the purported flaws with it. The Tribunal considers that counsel has not presented a persuasive argument regarding the relevance of the alleged breach of the non-parties' right to a fair trial in respect of the Tribunal's findings on fraudulent tax losses. Equally the Tribunal is not convinced by HMRC's counsel's example of a conspiracy criminal trial. In the Tribunal's view there has been no breach of the non-parties' rights. The evidence showed that HMRC issued assessments against each of the defaulting traders for the unpaid VAT against which they were given a right to appeal to an independent Tribunal. The defaulting traders did not exercise their right of appeal.

102.The Tribunal has in paragraphs 34 to 96 evaluated the evidence presented by HMRC against each defaulting trader and made findings thereon. The Tribunal is satisfied on the evidence that there was a VAT loss in each of the 49 transactions entered into by the Appellant which can be attributed to the fraudulent actions of a defaulting trader, Computec (April deals 1,4,6,7) Midwest (April deals 2,5,10,11,14), C&B Trading (April deals 3, 8), Bullfinch (April deals 9,12,13), 3D Animations (May deals 15 -36), Vision Soft (June deals 37-43), and Zenith Sports (July deals 44-49). The Tribunal found that assessments had been raised against each of the

defaulting traders which had not been paid or challenged on Appeal by the said traders. The assessments included the VAT loss incurred on the deal chains which incorporated the Appellant's 49 transactions.

103. The Tribunal found features in the activities of each defaulting trader which demonstrated that the losses were occasioned by fraud. The features included, amongst others, significant differences in the actual trades conducted from the information supplied in the VAT 1 registration, excessively high turnovers achieved in short periods of time, incidence of third party payments, non payment of assessments, disqualification of company directors, and disappearing without trace. The Tribunal is satisfied on its findings that the tax losses occasioned by Computec, Midwest, C&B Trading, Bullfinch, 3D Animations, Vision Soft and Zenith Sports in relation to the Appellant's 49 deals in April to July 2006 were fraudulent.

Was each of the Appellant's transactions connected with a fraudulent VAT loss?

104. This question crystallised the crucial disagreement on law between the parties, and formed the basis of the Appellant's application for a referral to the Court of Justice. HMRC contended a correct interpretation of Community law supported a broad construction of the concept of connection. HMRC in its view considered that the connection had been established if it demonstrated that the Appellant's transaction was linked with the fraudulent loss through a series of intermediary transactions. In contrast the Appellant submitted that the connection was limited to the transaction between the Appellant and its supplier. The Tribunal will express its view on the law, if need be, at the conclusion of its fact finding.

105. The Tribunal considers that the disagreement on the correct legal test should not prevent it from making findings on the evidence relied on by HMRC to prove the connection between the Appellant's disputed transactions and the fraudulent tax loss. Officer Holden at paragraphs 76, 77, 102, 139, & 155-159 of her first witness statement traced each of the Appellant's 49 transactions to a fraudulent tax loss. The tracing exercise was based on documentation obtained from the Appellant, its supplier, its supplier's supplier and so on, the relevant freight forwarder and in some cases evidence from the FCIB databases. The Appellant made no significant challenge to the tracing exercise except the July 17 2006 deal[1] upon which the Tribunal has already adjudicated at paragraph 35. Appellant's counsel conceded that the supply chains were those as set out in the deal sheets compiled by Officer Holden except for the July 17 2006 deal.

106. The Appellant considered the evidence of Officer Ellis suspect regarding his analysis of the FCIB databases in relation to its transactions. The questions for the Tribunal are whether Officer Ellis' evidence was undermined by the Appellant's cross examination, and if it was the effect if any on the reliability of Officer Holden's tracing exercise.

[1] See paragraph 9, page 146 26.10.11 Transcript.

107.Appellant's counsel pointed out that Officer Ellis made in the region of 30 amendments to his witness statement, and that he admitted at the end of the cross examination that he was not completely sure about his evidence. The Tribunal considers that the strength of Officer Ellis' evidence must be assessed as a whole and not simply on a response to a specific question.

108.Officer Ellis in re-examination indicated that approximately 20 of the 30 amendments to his witness statement were either adding exhibit references or correcting typographical mistakes. Officer Ellis observed that many of the deals transacted by the Appellant consisted of the same parties. In those circumstances he decided to take a selection of eight deals which in his view covered all permutations of supplier and customer in the Appellant's transactions with at least one deal taken from each VAT period. The Tribunal considers Mr Ellis' choice of criteria for determining the sample was rational and capable of producing a representative set of transactions from which conclusions could be drawn.

109. Officer Ellis stated that his analysis of the FCIB material involved the exercise of judgment by matching payments to and from a particular account to invoice totals where available, and otherwise matching debits and credits using the quantum of payment, timing of payment (in relation to a corresponding received payment) and the Paris Server narratives as a guide. Officer Ellis accepted that payments were not always matched in amount which was because traders did not necessarily pay for each deal individually, but made bulk payments for multiple deals where they were transacted with the same supplier.

110.The Tribunal finds that the Appellant's concerns about the reliability of Officer Ellis' analysis exaggerated, and that his evidence corroborated the details of the tracing exercise conducted by Officer Holden.

111.The Tribunal is satisfied that Officer Holden's extended verification demonstrated that each of the Appellant's 49 deals was traced back and thereby connected to a fraudulent tax loss. The Tribunal accepted Officer Holden's evidence that the Appellant's suppliers as well as other parties in the deal chains had accounted for output tax on its transactions, and that the Appellant's immediate suppliers did not incur a tax loss in respect of their transactions with the Appellant.

Did the Appellant know or should have known?

Introduction

112.The burden was upon HMRC to prove on the balance of probabilities that the Appellant knew or should have known at the time of entering the disputed transactions that they were connected with the fraudulent evasion of VAT. In this Appeal it was Mr Alibhai's state of knowledge at the relevant time which was the question in issue. Appellant's counsel complained that listening to his learned friend for HMRC and her comments on Mr Alibhai's evidence that he could form the view that the burden was upon Mr Alibhai particularly having regard to HMRC's assertions of Mr Alibhai's failure to answer questions or produce relevant documents.

113.In the Tribunal's view a distinction should be drawn between the burden of proof and the evidential burden. HMRC shoulders exclusively the burden of proving that the Appellant had the requisite state of knowledge but in discharging its responsibility to prove what it asserts, the evidential burden is likely to be a shifting one with HMRC providing a set of facts demonstrating the requisite state of knowledge which demands an explanation from the Appellant. If the explanation given is plausible the evidential burden shifts back to HMRC.

114. HMRC invited the Tribunal to consider all the available and relevant evidence when determining the Appellant's state of knowledge. HMRC counsel considered the Appellant's submission that the Tribunal must look at each transaction in isolation was misguided. In HMRC's view the references in the ECJ decision in *Optigen v Customs and Excise Commissioners* [2006] STC 419 J/[47] to the treatment of each transaction individually and per se related to the requirement to consider whether, in respect of each impugned transaction, the relevant test was satisfied on the evidence. According to HMRC, this was a different principle to that of the identification of all evidence that was relevant to the application of the test to that given transaction. In short HMRC contended that the Appellant had confused and conflated the principle of consideration of each individual transaction with the question of the evidence to which the Tribunal should have regard when so doing. Support for HMRC's view on the evidence can be found in the decision of Christopher Clarke J in Red12 v HMRC [2009] EWHC 2563:

> "109 Examining individual transactions on their merits do not, however, require them to be regarded in isolation without regard to their attendant circumstances and context. Nor does it require the tribunal to ignore compelling similarities between one transaction and another or preclude the drawing of inferences, where appropriate, from a pattern of transactions of which the individual transaction in question forms part, as to its true nature e.g. that it is part of a fraudulent scheme. The character of an individual transaction may be discerned from material other than the bare facts of the transaction itself, including circumstantial and "similar fact" evidence. That is not to alter its character by reference to earlier or later transactions but to discern it.
>
> 110 To look only at the purchase in respect of which input tax was sought to be deducted would be wholly artificial. A sale of 1,000 mobile telephones may be entirely regular, or entirely regular so far as the taxpayer is (or ought to be) aware. If so, the fact that there is fraud somewhere else in the chain cannot disentitle the taxpayer to a return of input tax. The same transaction may be viewed differently if it is the fourth in line of a chain of transactions all of which have identical percentage mark ups, made by a trader who has practically no capital as part of a huge and unexplained turnover with no left over stock, and mirrored by over 40 other similar chains in all of which the taxpayer has participated and in each of which there has been a defaulting trader. A tribunal could legitimately think it unlikely that the fact that all 46 of the transactions in issue can be traced to tax losses to HMRC is a result of innocent coincidence. Similarly, three suspicious

> involvements may pale into insignificance if the trader has been obviously honest in thousands.
>
> 111 Further in determining what it was that the taxpayer knew or ought to have known the tribunal is entitled to look at the totality of the deals effected by the taxpayer (and their characteristics), and at what the taxpayer did or omitted to do, and what it could have done, together with the surrounding circumstances in respect of all of them."

115. HMRC concluded that when considering the application of the *Kittel* test to a given transaction, the Tribunal was not only entitled to, but must, look at all the available and relevant evidence. The Tribunal should look at the given transaction and the circumstances in which the transaction took place. Effectively the Tribunal should build a picture from the accumulation of detail and form a view on whether the detail proves that the Appellant had the requisite state of knowledge at the time of entering into each transaction.

116. The Tribunal agrees with HMRC on the scope of the evidence to be considered when determining the Appellant's state of knowledge. The Tribunal, however, has to be satisfied that the evidence demonstrates on the balance of probabilities that each of the Appellant's transactions was vitiated by knowledge of fraud. In that respect the Tribunal should not leap to the conclusion that the Appellant had the requisite knowledge merely because its transactions were linked to a fraudulent tax loss.

117. HMRC's primary position was that the Appellant had actual knowledge of the fraud. The Tribunal's intends to examine the facts relied upon by HMRC to prove its assertion of actual knowledge. The Tribunal's examination will follow the headings of the HMRC's final submission except that it will adopt an inside out approach by considering first those matters which the Appellant accepted were within its knowledge followed by consideration of the wider circumstances. By adopting this approach the Tribunal will avoid the trap of the wider circumstances exercising an undue influence on the Tribunal's assessment of the facts. The Tribunal starts with the Appellant's awareness of the prevalence of fraud in the mobile phone and CPUs trade sector.

Appellant's awareness of MTIC fraud

118.On 12 July 2005, HMRC's Redhill office sent a letter together with VAT Notice 726 (joint and several liability) to the Appellant. The letter advised the Appellant of the problems with businesses in its trade sector offering commodities involved in MTIC fraud, the scale of such fraud, and the procedure for clearing VAT numbers of prospective suppliers and customers with Redhill. On 4 October 2005, Mr Alibhai verified the VAT registration number of Tradestar with the Redhill Office (albeit that the verification request and reply had been made in the name of Mr Alibhai's associated company, Mobile Computer World Limited).

119.On 22 September 2005, HMRC Officers Bamford and Mackie visited the Appellant's premises and spoke with Mr Alibhai. The purpose of the visit was to begin the verification work for the 08/05 return submitted by the Appellant. At that

meeting, Mr Alibhai confirmed that he verified the EU VAT numbers for his EU customers with Redhill. He also confirmed that his only supplier in that period was Kingswood.

120. On 17 October 2005, HMRC wrote to the Appellant explaining that it was in the process of verifying the supply chain for three deals in the 08/05 period. The Appellant was advised in that letter that HMRC had good reason to believe that at least one business in each of the three chains could be considered a missing or defaulting or hijacked business.

121. The position was updated by HMRC by letter dated 21 October 2005. In that letter, HMRC advised the Appellant that *preliminary enquiries indicate a significant tax loss at the beginning of the deal chains* and that HMRC continued to consider whether the Appellant's actions amounted to an abuse of the right to claim input tax deduction.

122. On 9 November 2005, the Appellant was visited once again by Officers Wingrove and Bamford. The purpose of this visit was to commence verification of the return for period 09/05. Mr Alibhai enquired as to the whereabouts of the payment for the repayment claim for period 08/05 and was informed that HMRC's enquiries continued. According to the notes of the meeting kept by Officer Wingrove Mr Alibhai told the officers that he was aware that some other brokers dealing with phones from the *Doncaster flight* had been paid.

123. On 30 November 2005, a letter sent to the Appellant's representatives by HMRC advised that checks on the IMEI numbers provided in respect of the goods transacted in period 08/05 tended to suggest that the goods had been transacted in the UK before. This information was repeated in a letter dated 6 December 2005. The supplier to the Appellant in those deals was Kingswood, a company with which the Appellant continued to trade until and including period 04/06.

124. On 22 December 2005, HMRC wrote to the Appellant, advising it that the repayments for periods 09/05 had been released without prejudice to any action HMRC may take in future regarding the claims, and reminded the Appellant of its responsibility to carry out due diligence checks. The letter concluded that the supply chains for the periods in question included businesses which did not account for VAT charged.

125. On 20 February 2006, Officers Wingrove and Westgate visited the Appellant's premises in order to commence verification of the return for period 01/06. Mr Alibhai told officers that Kingswood Trading had carried out in-depth checks on the Appellant. Officer Wingrove told the Appellant that it was the suppliers to Kingswood which should be the subject of stringent checks.

126. On 14 June 2006 (and having been informed by letter that its return for the period 04/06 was to be the subject of extended verification), the Appellant was visited by Officers Devine and Sibbering. Mr Alibhai was asked whether he knew how MTIC

fraud operated. Mr Alibhai agreed he did and asked why HMRC did not *go after* the defaulters.

127.On 22 June 2006, HMRC wrote to the Appellant and informed it that enquiries so far as its 03/06 claim was concerned revealed that of the eight transactions selected for verification, all eight commenced with defaulting traders with a resultant tax loss in excess of £1.79 million. Two suppliers were used by the Appellant during period 03/06: Tradestar; and Kingswood. The Appellant, however, continued to trade with Tradestar until and including period 07/06.

128. HMRC also warned Mr Alibhai in his capacity as director of Mobile Computer World Limited which traded from the same premises as the Appellant about the problems of fraud in the computer trade sector. In this respect HMRC made contact on 3 February 2003, 8 December 2005 and the 1 February 2006. The last two visits dealt with HMRC's concerns with the authenticity of software supplied to the Appellant by Tradestar.

129. Mr Alibhai accepted that there was fraud within the wholesale CPU and mobile phone trade sectors[2] and that he had read Notice 726[3]. Mr Alibhai acknowledged that he understood the purposes of Notice 726 which set out the checks a trader might consider to minimise the risk of being involved in fraudulent trades including checks to establish the integrity of the supply chain.

130.Mr Alibhai disagreed that he ignored the warnings of HMRC about the existence of tax losses in the supply chains for the Appellant's deals. Mr Alibhai acknowledged that he continued to trade with Kingswood despite being informed by Officer Wingrove of tax losses in the deal chains for August and September 2005, when Kingswood was the Appellant's supplier. Mr Alibhai was of the view that Officer Wingrove had not pursued his concerns about the tax losses. According to Mr Alibhai Officer Wingrove failed to follow up his indication in the correspondence that he would notify the Appellant of the results of his enquiries. In the meantime HMRC had agreed to make the repayment claims for those periods, albeit without prejudice. Given those circumstances Mr Alibhai believed that it was reasonable to continue trading with Kingswood.

131.Mr Alibhai accepted that HMRC had raised concerns in December 2005 and February 2006 with him in his capacity as director of Mobile Computer World about the authenticity of software supplies from Tradestar. Further he acknowledged that in June 2006 the Appellant was told that there were tax losses in the supply chains for the Appellant's March 2006 transactions when Kingswood and Tradestar were its suppliers. Mr Alibhai asserted that he advised both Kingswood and Tradestar of the problems with the supply chains. Tradestar responded by advising the Appellant that it was using different suppliers from those in March 2006. In those circumstances Mr Alibhai decided to carry on trading with Tradestar but not with Kingswood because it was not prepared to give the same assurances as Tradestar.

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[2] See Mr Alibhai's second witness statement (C1-255)

[3] 23:24 46 27.10.11 & 23 -25 & 1-8 48 & 49 27.10.11

132. Finally Mr Alibhai denied that he mentioned the *Doncaster flight* to Officer Wingrove at their meeting on 9 November 2005. Mr Alibhai, however, in cross examination accepted that he had enquired of the freight forwarder who told him that the flight carrying the consignment of mobile phones had been held up in Holland but the problem had now been resolved with some of the traders receiving their input tax credits.

133.The Tribunal is satisfied that in the period prior to April 2006, Mr Alibhai was fully aware of the prevalence of fraud in the CPU and mobile phone wholesale trade sectors, and the risks that it carried for the Appellant's business. The Tribunal also finds that he was aware of the contents of Notice 726 and of the steps that he should take to avoid wherever possible the Appellant's deals being caught up with fraudulent transactions.

134.Mr Alibhai knew that the risks of fraud were real in view of the various warnings he received from Officer Wingrove about the existence of fraudulent tax losses in the supply chains for the Appellant's deals in August and September 2005 when Kingswood Trading was the Appellant's sole supplier. The Tribunal disagrees with Mr Alibhai's suggestion that he was given a clean bill of health by Officer Wingrove's failure to follow up with further information on the tax losses, and the fact that HMRC repaid the disputed VAT. The repayment claim was made without prejudice to further action by HMRC. Officer Wingrove had clearly drawn to Mr Alibhai's attention his concerns about the Appellant's due diligence. In the Tribunal's view Mr Alibhai knew from the contents of Notice 726 that the obligation was upon the Appellant to satisfy itself of the integrity of the supply chain, which would not have been difficult since Kingswood was the Appellant's sole supplier during August and September 2005. Following the information provided by Officer Wingrove the Appellant took no steps to address with Kingswood HMRC's concerns save obtaining copies of the last three VAT returns of Kingswood. The Appellant's decision to cease trading with Kingswood in June 2006 because it had not given the same assurances as Tradestar was, in the Tribunal's view, an empty gesture. From April 2006 the Appellant had effectively replaced Kingswood with Tradestar as its sole supplier[4], a decision which appeared to have no connection with HMRC's concerns about the tax losses in the supply chains involving Kingswood.

135. HMRC's concerns in December 2005 and February 2006 with Tradestar's supplies of software to Mobile Computer World of which Mr Alibhai was a director, appeared to have no influence on the Appellant's decision to conduct deals with Tradestar in March through to July 2006. The Tribunal considers Mr Alibhai's response to HMRC's notification of tax losses in all the Appellant's March 2006 deals inadequate. His letter to Tradestar did not mention that the Appellant's deals with it had been traced back to tax losses. Mr Alibhai accepted at face value without further enquiry Tradestar's response that it had changed its supplier and carried out the appropriate due diligence checks. The Tribunal holds that a responsible trader in the Appellant's position as at June 2006 with a history of tax losses in its supply chains

[4] In April 2006 there were just 4 deals with Kingswood, 10 with Tradestar, thereafter all the Appellant's deals involved Tradestar.

would have been slow without making other enquiries to enter into further trades with Tradestar. The Appellant nevertheless conducted further trades with Tradestar in June and July 2006.

136. The question mark raised by Mr Alibhai about the accuracy of Officer Wingrove's record of *Doncaster flight* at the November 2005 meeting had no evidential weight in respect of the Tribunal's findings. Mr Alibhai's dispute was solely concerned with the existence of an airport at Doncaster not with the substantive part of the Mr Wingrove's written record.

The Appellant's Commencement and Trade in the Mobile Phone Market

137. Mr Alibhai had previous experience of wholesaling trading in CPUs with Reading Computers and Mobile Computer World, apparently doing deals to the value of £10 million. Mr Alibhai, however, had no substantial experience of wholesaling in the mobile phone market before the Appellant entered into its first deals with Kingswood in June 2005. Mr Alibhai's explanation for trading in mobile phones was that he was a businessman and would buy and sell goods if there was a profit in it. His research and understanding of the mobile phone market was, however, limited to surfing the various websites (International Phone Traders, International General Brokers, and Ali Baba[5]). Mr Alibhai had not developed a business plan for the Appellant's trades in the mobile phone market.

138. According to Mr Alibhai, the Appellant sourced its customers and suppliers from the website platforms which he accepted were open to all traders participating in the market subject to the payment of a subscription. Mr Alibhai could not recall exactly how he first met representatives from Kingswood. He thought it might have been at a tradeshow but he knew that Kingswood was advertising on IPT (International Phone Traders website). Mr Alibhai had a previous trading relationship with Tradestar in his capacity as director of Mobile Computer World. Mr Alibhai was introduced to Mr Burgess, the director of Tradestar, by Mr Pandya, the director of Bullfinch, a defaulting trader in the disputed April 2006 deals. Mr Alibhai secured Micromkt as a customer from the Ali Baba website, whilst the Appellant's two French customers, La Parisienne du Commerce and France Affaires, were sourced from the IPT website.

139. The Appellant only purchased mobile phones from two suppliers during its time in the mobile phone business with effectively Kingswood and Tradestar operating as sole suppliers in specific periods of the Appellant's operations. Micromkt was the Appellant's customer in 39 of the disputed 49 deals. Mr Alibhai suggested that the Appellant had a larger database of potential customers and suppliers and in this respect he referred to the number of Appellant's requests for validation of VAT numbers with Redhill. During the disputed periods the Appellant requested validations on only eight companies, one of which was Micromkt, and no requests were made in May 2006.

[5] IGB and Ali Baba sell a wide range of products not just mobile phones).

140. The Appellant experienced a massive increase in turnover from £49,179 for a period of two years ending May 2005 to almost £76 million in a one year period from 1 June 2005 to 1 June 2006. The gross profit excluding VAT achieved by the Appellant on its mobile trade deals during the disputed period of four months was in the region of £1.8 million. Mr Alibhai acknowledged that he did not put *two and two together* in respect of the significant increase in turnover of the Appellant's trades with Tradestar during the period, and the effect of the Appellant's business on Tradestar's turnover. In Mr Alibhai's view, he had a market for selling the goods supplied by Tradestar.

141. The Appellant's approach and experience in the wholesaling of mobile phones and CPUs were in marked contrast with that for its original venture in mobile satellite services. In respect of the latter the Appellant prepared a detailed business plan setting out the potential market for its product, its competitive advantage, and a marketing plan working with established retailers (Car Phone Warehouse and Virgin), and network operators. The Appellant was unsuccessful with its product, a turnover of around £50,000 in two years, which illustrated the difficulties for new firms entering the competitive mobile technology market.

142. The Tribunal finds there was no rational commercial explanation for the Appellant's instant success in the wholesaling of mobile phones as measured by the rapid increase in turnover and the sizeable gross profits. The Appellant's research of the market was minimal which was restricted to investigating three websites, only one was a dedicated site to the wholesaling of mobile phones. The Appellant compiled no business plan unlike its venture with mobile satellite technology. The Appellant encountered no difficulties in securing supplies and orders despite the facts that they were gained from internet platforms open to the business community as a whole, and the Appellant's lack of history in the wholesaling of mobile phones. The Appellant did not have an extensive database of potential customers and suppliers. The reality was that the overwhelming majority of the Appellant's deals involved two suppliers (Kingswood and Tradestar) and one customer (Micromkt), which ran contrary to the depiction of the mobile phone wholesale market as highly competitive.

Funding and Banking

143.On 14 June 2006 Mr Alibhai informed HMRC that the Appellant's trading activities were funded from a UK bank account, transfer profits and intra-company loans from associated companies. HMRC's subsequent enquiries revealed the incompleteness of Mr Alibhai's response, and challenged the propriety of the Appellant's funding arrangements.

144.The pattern of the Appellant's wholesale trading in CPUs and mobile phones demonstrated that the Appellant's trades were dependent upon receipt of the repayment claims from HMRC. The Appellant completed no deals in periods 10/05, 11/05 and 12/05. The Appellant's inactivity during this period was connected to HMRC's investigation into the Appellant's repayment claims for periods 08/05 and 09/05, which were not authorised for payment until 22 December 2005. On release of

the repayment claims the Appellant entered into deals to the value of £5 million in January 2006.

145. Virtually all of the Appellant's disputed deals were transacted in the last days of each month, and not spread out during the trading period. In April to July 2006 the Appellant conducted no intra UK trades which would not have involved large repayment claims.

146. Mr Alibhai accepted that as the Appellant was an exporter there would inevitably be an initial shortfall between the sale monies received and the purchase monies paid for the goods because of the different VAT treatment of the supplies (zero-rated against standard-rated).

147. The Appellant's funding model for its business was illustrated by its arrangements for its April deals. The 14 transactions were completed on 27 and 28 April 2006 which enabled the repayment claim associated with these deals to be included in the April VAT return. On the 8 May 2006 the Appellant received its repayment claim for March 2006 which was used to fund its April transactions. Mr Alibhai confirmed that the Appellant had no contingency plan to meet its financial commitments arising from its trades if it did not receive a VAT repayment within the requisite time period. Mr Alibhai considered there was no need to plan for such an eventuality because the Appellant's claims had been verified before and had been paid.

148. The Tribunal considers Mr Alibhai's response complacent in view of the delayed repayments in respect of the periods 08/05 and 09/05, which had only been met on a without prejudice basis in view of the presence of carouselled goods in the Appellant's deal chains. In the Tribunal's view, Mr Alibhai was fully aware at the time of entering the disputed transactions of the possibilities that its repayment claims would be subject to extended verification and eventual refusal because of the high risk of fraud that existed in the Appellant's trade sector.

149. The weakness in the Appellant's financial planning was exposed in respect of its funding arrangements for the May, June and July 2006 disputed deals. From April 2006 the Appellant's repayment claims were delayed and eventually refused, which formed the basis of this Appeal. The consequence of HMRC's actions meant that the Appellant had a £5 million shortfall in respect of its trades during these months.

150. In cross examination Mr Alibhai was unable to give a satisfactory explanation of how the Appellant funded the £5 million shortfall in order to carry out its trading during the period of May to July 2006. It appeared that the shortfall was met by a loan of £1.15 million from the Appellant's associated company, Mobile Computer World, and a £3.8 million advance payment from its customer, Micromkt for potential supplies of goods.

151. The circumstances of the £3.8 million advance from Micromkt raised questions about the nature of the Appellant's relationship with its customer and sole supplier,

Tradestar, during this period and did not provide an answer to how the Appellant funded the transactions in May, June and July 2006.

152. The £3.8 million advance from Micromkt happened because the Appellant cancelled four deals in the 07/06 period (deals 45, 46, 48 and 49) after it had received payment from Micromkt, its customer in each deal, in the total sum of £3,871,950. Prior to the cancellation, the Appellant had made a part payment in the sum of £609,000 to its supplier, Tradestar, in respect of deal 45. Mr Alibhai stated that the Appellant cancelled these deals because it had received a letter from HMRC advising of tax losses in its supply chains and as a result of the information contained in that letter, made a commercial decision that it could not safely trade further with Tradestar.

153. Micromkt sent several letters to the Appellant requesting repayment of the £3.8 million but did not follow up the letters with legal action to recover the monies which were still outstanding at the time of the hearing.

154. Micromkt made the payment of £3.8 million on 7 August 2006 for the four deals in July 2006. The Appellant's decision to cancel the deals was not apparently made until late September 2006. The effect of the cancellation was that it enabled the Appellant to plug the funding gap between purchases and sales for transactions concluded in May and June 2006 which arose from HMRC's unwillingness to meet the Appellant's repayment claims. Mr Alibhai stated in cross-examination that Micromkt was paying for stock it was ordering for future orders and that he was using it to settle the Appellant's debt with its supplier for previous deals. Mr Alibhai's statement depicted Micromkt as the banker for its deals in the absence of repayments from HMRC rather than as its customer. His suggestion that Micromkt was paying for future stock contradicted the Appellant's deal documentation which showed that the payment of £3.8 million was for the transactions in mobile phones in July 2006.

155. At that time the deals were cancelled, the Appellant was owed £609,000 from Tradestar in respect of the part payment already made for one of the cancelled deals. On 22 September 2006, the Appellant's account was credited with £1.5 million from Tradestar in respect of an entirely separate transaction which did not happen. On 4 and 11 October 2006 the Appellant returned the £1.5 million to Tradestar in two separate payments despite that fact that it was still owed the £609,000 from Tradestar. Mr Alibhai's explanation for returning the money without recovering the debt was that Mr Burgess of Tradestar needed the money back so he gave it to him because it was a for a specific deal which did not go ahead. Mr Alibhai in cross examination confirmed that about £200,000 was still outstanding from Tradestar.

156. The Appellant's willingness to trade with Tradestar in October 2006 cast doubt on Mr Alibhai's principal reason for cancelling the four transactions in July which was that the Appellant could not safely trade with Tradestar.

157. The Appellant secured two loans from third parties at the end of March 2006 to assist with the funding of its deals. Mr Alibhai could not remember whether the Officers asked him about the loans at their meeting on 14 June 2006. Mr Alibhai did

not consider that he withheld details of the loans because there were entries of the monies loaned in the Appellant's bank statements which had been given to HMRC.

158. HMRC in a letter dated 19 July 2006 requested the Appellant to explain the entries in its bank account relating to Global Crown Technologies Ltd and CT Gardner. Mr Alibhai responded on 4 August 2006 indicating that they were loans. HMRC wrote to the Appellant requesting evidence of loan agreements or explanations as to why there were no such agreements in place in letters dated 5 September 2006, 17 October 2006 and 30 November 2006. On 15 December 2006, HMRC received a copy of a loan agreement between the Appellant and Global Crown Technologies that was dated 18 August 2006. No other loan agreements were provided.

159.Under cross-examination, Mr Alibhai accepted that the loan agreement between the Appellant and Global Crown Technologies post-dated the loan by several months and that the loans of £150,000 and then £50,000 had originally been obtained without any written agreement. Mr Alibhai was unable to recall, at the time the loans were made, what the timescale for repayment was, what the interest rate was, or whether provision was made for penalties in the event of late payment. It also appeared that the Appellant still owed Global Crown Technologies the £200,000. Mr Alibhai explained that the Appellant had initially repaid the £200,000 but that had been returned by Global Crown Technologies because it had been paid into the wrong bank account. Global Crown Technologies had taken no action to recover the outstanding sum.

160. Mr Alibhai stated that Mr Gardner was an employee of the Appellant who had been prepared to lend the company £50,000 from the proceeds of a house sale. The terms of the loan had not been reduced to writing. Mr Alibhai indicated that Mr Gardner had been repaid the loan.

161.The Appellant's payments and receipts for its wholesale trades in CPUs and mobile phones were made through its FCIB account which was opened sometime in 2005. Almost all the traders which featured in the Appellant's deal chains held an account with FCIB.

162.Officer Stone in his witness statement which was not challenged by the Appellant stated that between 2005 and 2006 many EU suppliers, UK defaulting traders, buffers, brokers, contra brokers and overseas customers in the computer and mobile phone sector whose transactions were connected to MTIC fraud opened bank accounts off shore. According to Officer Stone, the most popular off-shore bank was the First Curaco International Bank (FCIB) in the Netherlands Antilles. Officer Stone pointed out that off-shore financial transactions lacked transparency and were beyond the reach of the UK's anti-money laundering laws.

163.Mr Alibhai said that the Appellant chose FCIB because it was the bank that most people in the industry used and that its then current bank, Barclays, closed the Appellant's account because it did not like trading in mobile phones. Mr Alibhai, however, produced no correspondence from Barclays in which the decision to close

the account was discussed. Further, the Barclays account remained open from June 2005 (when the decision to close the account was apparently notified to Mr Alibhai) to January or February 2006.

164.The Tribunal finds that the Appellant's financial arrangements made no commercial sense for handling a business with a multi-million turnover. The Appellant did not have a sound capital footing for its business activities. Mr Alibhai did not see the point of cash flow forecasts or having plans in place to deal with cash flow difficulties. Mr Alibhai assumed that the Appellant would receive the VAT repayment which would fund the short fall between the purchase and sales monies caused by the differential VAT treatment of the respective supplies. The Appellant knew that his assumption of automatic repayment was problematical because of the Appellant's experiences with the repayment claims for the 08/05 and 09/05 periods. The pattern of the Appellant's dealings was rigid and determined by the date of the VAT return and did not reflect the highly competitive market in mobile phones as asserted by Mr Alibhai.

165. The actual arrangements employed by the Appellant to meet the cash flow difficulties during the disputed periods were far removed from normal commerce operating at arms length. The details of the cancelled July deals revealed a degree of interdependence and co-operation which would not be expected from traders purportedly operating independently and seeking the best deal. The Appellant's customer, Micromkt, was content for the Appellant to use a considerable sum of its money to discharge past debts of the Appellant and relaxed about repayment of those monies. Equally the Appellant appeared unconcerned about recovering the money owed to it by its supplier, Tradestar. The Appellant's loans with Global Crown Technologies and its employee were also bereft of commercial features, and a further indication of the unconventional manner in which the Appellant ran its wholesale business in CPUs and mobile phones.

166. The Tribunal was unconvinced about the Appellant's reasons for choosing FCIB as the bank through which it conducted its financial transactions for the wholesaling of mobile phones and CPUs. The Tribunal finds that the lack of transparency associated with off-shore accounts provided the Appellant with the means to avoid scrutiny of its deals by the UK authorities. The Tribunal agrees with HMRC's observation that the use of FCIB accounts by the Appellant and its trading partners was not coincidental. The Tribunal also considers that HMRC has made a valid observation that if Mr Alibhai was aware of Barclays Bank's concerns, it was yet another factor which ought to have alerted him to the existence of fraud within the mobile phone trade sector.

Business Model / Payment Terms

167. HMRC adduced evidence which showed that in 13 of the disputed deals the Appellant shipped goods out of the UK to its EU customers before the Appellant had received payment from its customer and before the Appellant paid its supplier. Mr Alibhai gave different accounts when asked to explain how the Appellant was able to ship out goods for which no payment had been made to the Appellant's supplier.

168. Initially, Mr Alibhai indicated that he did not pay for goods until the Appellant had received payment. He indicated that on occasion, the Appellant was permitted to send goods to its customer *ship on hold* which enabled the goods to be shipped abroad and allocated to the Appellant's customer, but not released until payment was made. When asked whether he sought permission from the Appellant's suppliers to remove goods from the country prior to payment, Mr Alibhai indicated he could not remember. Mr Alibhai was asked whether he believed the Appellant's supplier had title to the goods at that time. His response was that this was not a matter of concern to him. When asked similar questions by the Tribunal at the conclusion of his evidence, Mr Alibhai indicated that the Appellant's supplier would have been aware that the goods had been removed from the country and that it would have been the shipper who would have informed the supplier of that. Mr Alibhai suggested that in those circumstances, the Appellant's supplier would have had title to the goods in question.

169. The Tribunal formed the view that Mr Alibhai was not concerned about how the Appellant was permitted to ship out goods for which it had not paid. Mr Alibhai did not know the terms of trading of one of the Appellant's suppliers, Kingswood. He assumed that Kingswood retained title to the goods until payment was made but was unable to point to a declaration to that effect on any of the invoices issued by Kingswood. His disinterest about whether his supplier had title to the goods was incomprehensible, if Mr Alibhai was serious about the bona fides of the Appellant's transactions.

170. The Tribunal agrees with HMRC's submissions that it defied logic and commercial reality that an Appellant was able to relinquish possession of goods of substantial worth without payment having been made for them, or any security for payment being given. Further it was equally illogical that, notwithstanding that a supplier retained (or purported to retain) title to goods pending payment, a trader allocated stock was given permission to export it.

171. The Tribunal concludes that Mr Alibhai's disinterest and limited recall of the arrangements were intended to deflect attention from the significance of the evidence. The Tribunal is satisfied that the arrangements whereby the Appellant was permitted to ship out goods to its customer before payment demonstrated a high degree of co-operation and trust between the Appellant and his trading partners which would not normally be a feature of arms-length commercial deals with values in excess of £100,000. In short the Tribunal does not understand why the Appellant's supplier would take the risk unless it knew that the arrangements were pre-ordained.

Contracts and Specifications

172. The Appellant had no formal written contracts with its suppliers and customers with the result that there was in place no formal return/exchange policy should the CPUs or mobile phones be shown to be faulty. A further consequence of the absence of written contracts was the fact that matters such as transfer of title, payment and delivery terms were not the subject of any formal agreement.

173.The Appellant did not set out the specifications of the mobile phones ordered in its commercial documentation (purchase orders or invoices). Mr Alibhai asserted that it was unnecessary to write down the specifications because he would have told the Appellant's trading partners the specifications which were UK, European specification.

174.The inspection reports for some of the disputed deals showed that the mobile telephones traded included two pin chargers which could only be used in mainland Europe. Mr Alibhai believed that a three pin plug or adaptor would also be included with the mobile phones. Mr Alibhai's belief was, however, derived from his experience of buying an Orange phone not from his own investigation of the goods traded by the Appellant. Mr Alibhai's belief was questionable particularly as he acknowledged that the inspection reports commissioned by the Appellant described the entire contents of each box. Those inspection reports did not mention a second charger or adaptor. Further Mr Alibhai accepted that if the boxes contained only two pin chargers, each of the individual boxes of mobile telephones would need to be opened and modified in order to be made suitable for use by a UK consumer.

175.In cross-examination, Mr Alibhai was asked what provisions were in place to ensure that the Appellant could prove the precise specification of stock ordered if a dispute arose. Mr Alibhai explained that there were no such provisions because such a thing never arose. When asked why such a dispute was unlikely to arise, Mr Alibhai answered: "*Because why would we have US phones or a phone with a different language number and they're being sold in the UK?* According to HMRC the clear import of his answer when read in context was that the Appellant did not trade in US phones and would not have traded in US specification phones.

176. HMRC drew Mr Alibhai's attention to inspection reports which showed that the Appellant supplied Nokia 8801 telephones which were specifically designed for the American market. Mr Alibhai's explanation for the discrepancy was that *American stock* referred to tri-band mobile phones which were sold in the UK and could be used by UK citizens travelling to the USA.

177.Mr Alibhai explained that CPUs were sold in sealed boxes and if the seal was broken the CPUs would be devalued. Tradestar in its invoices to the Appellant stated that any damages or discrepancies of any kind must be notified in writing within 24 hours of the receipt of the goods. The inspection report for deal 7 identified under the heading of *discrepancies* that the CPU boxes had been resealed. Mr Alibhai accepted that he had not reported the discrepancy to Tradestar stating that the price agreed with the Appellant would have been lower to reflect the fact that the boxes had been resealed.

178. The Tribunal agrees with HMRC's contention that it would be a reasonable expectation for the Appellant to have in place formal written contracts and specifications with its trading partners, particularly in light of the high value nature of the items traded. The Tribunal was not impressed with Mr Alibhai's explanation that the Appellant did not need the protection of written specifications because of the

unlikelihood of a dispute with its trading partners. The absence of such formalities was contrary to arms length trading between independent traders.

179. The Tribunal considers that Mr Alibhai should have been put on notice that the Appellant was trading in goods not destined for the UK market. Mr Alibhai did not question why mobile phones with two pin chargers or described as American stock had somehow ended up in the UK. Mr Alibhai's assertion that there was a market for Nokia 8801s in the UK was in the Tribunal's opinion an afterthought when he realised the implications of the questions put to him in cross-examination. Mr Alibhai adduced no evidence that at the time of entering into the disputed deals he raised questions about the specifications of the mobile phones described in the inspection reports.

180. Equally the Tribunal is satisfied that Mr Alibhai did not notice that the inspection of the CPU boxes for deal 7 reported that the boxes had been resealed. The Tribunal does not accept his explanation that the deficiency was reflected in the price. The Tribunal considers that *resealing* was such a fundamental deficiency that no prudent trader would have proceeded with the purchase.

181. In the Tribunal's view, Mr Alibhai's complacent approach towards the specifications of the mobile phones and CPUs did not fit with his assertion that he took all reasonable precautions to avoid complicity in deal chains connected with fraud.

Movement of Goods

182. HMRC identified discrepancies in the documentation for the transportation of goods in relation to some of the disputed supplies, which were:

(1) A refrigerated vehicle (registration PO24 34A) was used to transport five consignments of mobile telephone handsets on 28 April 2006 (deals 9,10,12,13, and 14).

(2) There was insufficient time to deliver the goods supplied in deals 3 and 5 to an address in Paris when the transportation documents revealed that the vehicle carrying those items travelled from Dover to Calais on 29 April 2006 on the 1215 hours crossing (90 minutes' duration) and returned (apparently having delivered the goods) on a crossing which arrived in the UK at 1740, the journey between Calais and Paris on a conservative estimate taking 2 hours 47 minutes.

(3) There was insufficient time to deliver the goods supplied in deals 15 – 17 to an address in Madrid when the transportation documents revealed that the vehicle carrying those items left the UK using the Channel Tunnel on 8 June 2006 at 0055 hours, returning on the ferry from Calais to Dover at 2155 hours on 8 June 2006. The journey between Coquelles, France, to Madrid, Spain and back to Calais is estimated to take some 32 hours.

(4) There was insufficient time to deliver the goods supplied in deals 33 – 35 to an address in Madrid when the transportation documents revealed that the vehicle carrying those items left the UK using the Channel Tunnel on 18 June 2006 at

1430 hours, returning on the ferry from Calais to Dover at 1945 hours on the same day.

183. The Appellant did not respond to HMRC's request in its letter dated 19 January 2007 for an explanation for these discrepancies. The Appellant did not challenge Officer Holden's evidence on the transportation documentation. Mr Alibhai's approach to the discrepancies was summed up in his second witness statement where he stated that the Appellant relied on CMRs and ferry tickets to evidence dispatch. Mr Alibhai gave the impression that the only function of the transportation documentation was to establish compliance with HMRC's formalities. Mr Alibhai as a prudent trader well aware of the risks of fraud in the Appellant's trade sector should have been using the information from the documentation to assess whether the deals were legitimate. In the Tribunal's view the discrepancies were yet another example of the Appellant ignoring signs that its transactions may not be bona fide.

Insurance

184. Mr Alibhai stated that the Appellant held a marine insurance policy which had been taken out in April 2006 and that the annual premium for that policy was £60,000. Mr Alibhai produced in evidence two pages of a marine cargo insurance policy to support his assertion.

185. The Tribunal, however, is satisfied that the Appellant did not have insurance for the disputed transactions because:

(1) Mr Alibhai repeatedly ignored HMRC's requests to provide information on insurance. Mr Alibhai only supplied information in 2008, and a copy of the two page documentation in 2009. Mr Alibhai has supplied only two pages of a 21 page document, with no explanation whatsoever as to why the remaining pages have not been produced.

(2) Mr Alibhai confirmed in evidence that he could not recall obtaining a copy of the marine insurance policy at the time the disputed deals were conducted.

(3) The information in the two pages was inadequate. The document gave no indication of the start date of the policy save that the document was dated 26 June 2006. On the information provided it would appear that the policy did not cover shipments to Spain which was critical for the Appellant's supplies to Micromkt.

(4) Mr Alibhai supplied no evidence of payment for the policy.

186.Mr Alibhai indicated that prior to taking out the marine insurance policy the Appellant's goods were insured via the freight forwarder's policy. In one respect this evidence was irrelevant because it was Mr Alibhai's case that the disputed deals were covered by the terms of the marine cargo policy. In any event there was no evidence that the Appellant's goods were insured via a policy held by the freight forwarder. The invoices from the freight forwarders included no charge to the Appellant for insurance.

187.Appellant's counsel argued that even if the goods were not insured at the time of the transactions, it was not a matter which went to knowledge because the decision

whether to insure the goods was a commercial one for the trader. This, however, was not the case advanced by Mr Alibhai who asserted that the Appellant's goods were insured. The finding that the Tribunal did not believe Mr Alibhai on the question of insurance goes to his credibility, and raises questions about his motive for misleading HMRC on the insurance position.

Due Diligence

Commercial Checks on Trading Partners

188.The Appellant's commercial checks on Tradestar included a certificate of incorporation; a certificate of VAT registration; a blank trading account form and questionnaire; a Redhill verification of Tradestar's VAT registration number requested by Mobile Computer World on 28 September 2005; annual accounts for year end 31 August 2005; director's passport copy; two invoices addressed to Tradestar and dated March 2006; and a completed trading account application form dated March 2006.

189.The Appellant's checks on Kingswood included: a letter of introduction from the company; details of company personnel; certificate of incorporation; certificate of registration for VAT; and director's passport copy.

190.The Appellant's checks of its French customers were restricted in the case of La Parisienne du Commerce to a trading account application form dated 30 September 2005 and utility bills which post-dated the deals with the company. In respect of France Affaires, the checks consisted of trade reference details, letter of introduction; bank details; a completed trade account application form; director's passport copy and VAT documentation.

191. Finally the Appellant's checks on Mikromkt comprised a letter of introduction; bank details; certificate of incorporation; a completed trade account application form; and the results of a Redhill check dated 17 March 2006.

192.The Appellant did not perform third party independent checks on its trading partners, such as credit checks, trade and bank references. Mr Alibhai in cross-examination appeared at first not to understand the significance of independent checks. He then considered that the Appellant could do nothing more than what it did. Mr Alibhai took the view that his visits to the premises of the Appellant's suppliers and his meetings with their directors satisfied the requirement of independent checks. He also pointed out that Micromkt's director had visited the Appellant's premises on a number of occasions. Mr Alibhai believed that credit checks and trade and bank references served no useful purpose. The Appellant was not giving credit to its suppliers and customers. The referees were either unlikely to give a bad reference or in the case of the banks would not supply one. Mr Alibhai asserted that the Appellant was a member of *CreditSafe* but he was unable to provide documentation corroborating payment of the *CreditSafe* subscription. In any event Mr Alibhai accepted that he did not use the service of *CreditSafe* for credit checks.

193.The Tribunal considers that the Appellant operating under a business model of allowing goods to be dispatched overseas without payment would have been interested in the creditworthiness of its customers. In the Tribunal's view it was noteworthy that the Appellant held no financial information whatsoever on its French customers and on Micromkt.

194.The Tribunal disagrees with Mr Alibhai's assertion that credit checks on its suppliers were pointless. The Tribunal endorses HMRC's observation that had the Appellant conducted a credit check in respect of Tradestar, it would have established that Tradestar had a credit rating of £15,000 (June 2007 check) and a financial stability rating of *above average risk*. Despite this, the Appellant purchased goods worth in excess of £4.2 million in April 2006 alone without even an enquiry as to whether Tradestar was a company which could itself afford goods at that value or whether it was itself able to obtain credit at that level.

195. The Appellant continued to trade with Kingswood until April 2006 despite being informed by HMRC in October and December 2005 that the supplies secured from Kingswood had been traced back to a tax loss. In those circumstances a prudent trader would have stepped up its due diligence on Kingswood before continuing to trade with it. The Appellant did not do so, save obtaining copies of the last three VAT returns from Kingswood. Similarly the Appellant after being informed on 22 June 2006 that its eight deals in period 03/06 with Tradestar had been traced back to a tax loss took minimal steps to assess Tradestar's bona fides before deciding to do further deals with it in July 2006.

196. The Appellant's approach to due diligence of its trading partners was contrary to its express intentions in its trade application form which stated that it would be validating the information in the forms against those held on databases from the electoral register and fraud prevention agencies. The Appellant advised that the information gained from this validation exercise may be used for *debt tracing, the prevention of money laundering and the management of your account*. The Appellant warned its prospective trading partners that *it may pass information to organisations involved in fraud prevention to protect its customers and itself from theft and fraud.* The Appellant has not replied to written HMRC's requests for evidence of such searches and checks[6].

Freight Forwarders

197. The Appellant made no enquiries of its freight forwarders about the origin of the goods traded, and the length of time for which they have been in the UK. Mr Alibhai's assertion that the freight forwarder would not have provided such information was not supported by evidence that he had ever asked such questions and been refused the information. Mr Alibhai accepted that information about the country of origin and length of time in the UK did not betray any commercial confidentiality whatsoever. The Tribunal notes that the Appellant was prepared to ask the freight forwarder about the delays regarding the *Doncaster* flight. Also the freight forwarder

[6] See paragraph 323 of Officer Holden's first witness statement dated 5 May 2009.

was prepared to tell the Appellant about the other traders receiving their input tax claims[7].The Appellant adduced no evidence of due diligence checks on the freight forwarders themselves.

Inspections

198.The Appellant engaged A1 and Global International Freight, amongst others, to carry out 100 per cent inspections of the goods and provide the Appellant with the IMEI numbers for the mobile phones. Mr Alibhai accepted that a company which obtained and retained IMEI numbers might be afforded some protection against fraud.

199.The Appellant provided HMRC with the IMEI numbers for the April deals in an electronic format and in a timely manner. The Appellant, however, did not supply HMRC with the IMEI numbers for the mobile phones traded in May, June and July 2006 until December 2006, and only after eight separate requests from HMRC for this information. Further the Appellant provided them in paper form only which made it virtually impossible for HMRC to check the numbers against the NEMESIS database.

200.The Tribunal is not convinced that the Appellant obtained IMEI numbers for the mobile phones at the time that they were traded. Mr Alibhai offered no rational explanation for the delay in providing HMRC with the numbers for the May, June and July deals. The Appellant was not billed for inspection costs by Global International Freight in respect of some of the deals. Also the inspection reports produced by Global International Freight did not mention an IMEI inspection. Finally although Mr Alibhai maintained that the Appellant had the IMEI numbers, he could not recollect when the Appellant received them.

201.The inspection reports provided by the Appellant in respect of its CPU deals in period 04/06 revealed the following:

(1) Box number BH096W92 appeared on both the inspection report for April deal 4 and the inspection report for April deal 7.

(2) Box number BH09F919 appeared on both the inspection report for April deal 1 and April deal 4.

(3) Box number BH08YX14 appeared on both the inspection report for April deal 7 and that for a deal completed in period 03/06.

202.Mr Alibhai indicated that he was unaware of the duplications at the time the deals were conducted. Mr Alibhai did not keep an electronic database of the box numbers traded in order to check whether the Appellant had traded the same box twice. Mr Alibhai suggested that the duplications in 1) and 2) above were due to the goods being shipped on the same day.

[7] Mr Alibhai denied knowledge of Doncaster airport but accepted that he had made enquiries of freight forwarders and that the freight forwarders told him about receipt of input tax credits (see 28 October 2011 15-25 (18); 1-9 (19).

Tribunal's Conclusions on Due Diligence

203. Mr Alibhai had received Notice 726 on various occasions prior to entering the disputed transactions. He knew of the recommendation in the Notice that traders should make sufficient checks on the integrity of the supply chains to ensure that their trades were not caught in fraudulent supply chains. Mr Alibhai was fully aware of the risks of fraud affecting the Appellant's trades after being informed by HMRC that the Appellant's deals in October and November had been traced to tax losses.

204.Given the above context the Appellant's checks on the integrity of its trading partners and of the goods were plainly inadequate. The Appellant took the information given to it by its trading partners at face value, and did not independently verify the accuracy of the information. The Tribunal finds Mr Alibhai's reasons for not performing checks on the creditworthiness of the Appellant's suppliers and customers unconvincing. The Appellant did not step up its due diligence on its suppliers after being informed that their supplies had been traced back to tax losses.

205. Equally the Appellant had no effective systems in place to ensure that the goods traded were not caught up in fraud. The Tribunal was satisfied that the Appellant did not examine the information on box numbers and IMEIs in the inspection reports provided by A1, Global International Freight and others. The evidence demonstrated that Mr Alibhai did not have the reports on the IMEI numbers of the mobile phones at the time the Appellant entered the disputed deals. The fact that the Appellant did not use the information in the inspection reports suggested that the Appellant was simply going through the motions.

206. The Appellant argued that the purpose of due diligence was to protect itself. The Appellant did not consider the collection of IMEI numbers particularly good protection. The Appellant collected the numbers because they were required for the purpose of securing a repayment claim. The fact that the goods may have been traded before was not indicative of fraud. The Appellant considered incredible HMRC's suggestion that the freight forwarder would give information about the number of traders involved with the goods and the length of time that the goods had been in UK. According to Mr Alibhai this did not happen in the real world. The Tribunal does not accept the validity of the Appellant's submissions. In one respect the submissions did not reflect Mr Alibhai's evidence in which he accepted that he would take all reasonable steps to avoid the participation of the Appellant in fraud. In the Tribunal's view the submissions were directed at downplaying the inadequacies in the Appellant's checks on the integrity of its trading partners and that of the traded goods. The plain fact was that the Appellant conducted no effective due diligence.

The Wider Circumstances

207. Mr Alibhai asserted that he knew nothing of the transactions outside the Appellant's transactions with its customers and suppliers. The Appellant's purported lack of knowledge had no bearing upon the relevance of the evidence adduced by HMRC of the wider circumstances appertaining to the Appellant's disputed deals. The High Court in *Red 12* and the Court of Appeal in *Mobilx* confirmed the importance of

looking at all the circumstances in deciding the issue of knowledge. The Tribunal's findings on the big picture are set out below under various headings.

Structure and length of the deal chains

208. Officer Holden's tracing exercise showed that the structure of each chain headed by five of the seven defaulting traders (Computec, C&B, 3D Animations, Vision Soft and Zenith Sports) followed the same pattern in respect of the identity of the traders and their position in the chain.

209. Although the structure of the chains was not identical in respect of those chains commencing with the remaining two defaulting traders, Midwest or Bullfinch, they nonetheless shared similarities. In the deals commencing with Midwest (deals 2, 5, 10, 11 and 14 of the 04/06 period) and Bullfinch (deals 9, 12 and 13 of the 04/06 period), the Appellant purchased the goods from Kingswood, which in turn had purchased the goods from Mitek Computer Components. IH Technologies appeared as the first line buffer to the defaulting trader in four of the deals involving Midwest and one of the deals with Bullfinch. The Wireless Warehouse was the first line buffer in the remaining two deals involving Bullfinch. Dualite made an appearance as a buffer in three of the Midwest Deals.

210. The chains for each of the disputed 49 deals had between five and seven UK registered traders as participants. The goods for each deal were held at a freight forwarder, which indicated that the participants were not adding value to the goods sold in the respective chains.

211. All the participants in the Appellant's 49 deal chains were exclusively wholesalers. There were no manufacturers, authorised distributors, retailers or end users in the chains. Also none of the telephones or CPUs purchased in the course of the 49 deals was sold through the Appellant's retail business.

Mark ups

212. The Tribunal finds the following in respect of the mark ups for the April 2006 deal chains:

(1) In the ten deals that Kingswood acted as supplier to the Appellant its mark up per unit was £3 in respect of six deals and £2 per unit in respect of the remaining four.

(2) In each of those ten deals Mitek achieved 50 pence per unit regardless of the type and quantity of product purchased.

(3) Dualite secured a mark up of 25 pence per unit in each deal in which it acted as a buffer trader.

(4) SWEG achieved a mark up of 50 pence per unit in each deal in which it acted as a buffer trader;

(5) IH Technologies' mark up was 15 pence per unit in each deal in which it acted as a buffer trader.

(6) The gross profit made by some of the buffer traders in the April deals was less than £1,000 (for example, IH Technologies, Dualite, and Deepend Trading).

(7) Each party to the four deals involving supplies from Tradestar achieved a mark up of no more than 20 pence (Zenith Sports 20p; Capital 10p, Universal 10p, and Tradestar 15p) compared with the £3.25 by the Appellant.

213.The Tribunal finds that the mark ups achieved by each trader in the May 2006 chains excluding the Appellant remained the same regardless of make, model, quantity sold, namely:

- Globaltech Services 20 pence per unit
- Linbar 10 pence per unit
- Capital Distribution 20 pence per unit
- Universal Traders 25 pence per unit
- Tradestar 15 pence per unit

214.The Tribunal finds the mark ups achieved by each trader in the June 2006 chains excluding the Appellant remained the same regardless of make, model, quantity sold, namely:

- Globaltech Services 20 pence per unit
- Linbar 10 pence per unit
- Capital Distribution 10 pence per unit
- Universal Traders 10 pence per unit
- Tradestar 15 pence per unit

215.The Tribunal finds the mark ups achieved by each trader in five of the six July 2006 chains excluding the Appellant remained the same regardless of make, model, quantity sold, namely:

- Neon Leicester 10 pence per unit
- Linbar 12 pence per unit
- Tradestar 15 pence per unit

216. The evidence showed that the Appellant's mark ups for the disputed deals did not follow a particular pattern. The Appellant's mark up for each of the deals, however, was significantly more than the other traders in the respective supply chains. The mark ups achieved by all the companies in the 49 disputed deals except Kingswood and the Appellant never exceeded 50 pence per unit. The Appellant, on the other hand, secured mark ups of many multiples of that made by the other traders in the respective chains. The Appellant's evidence on the level of overheads incurred in the export of the goods was found in the invoices from Global International Freight. For example in deals 42 and 43 the inspection, administration and freight overheads amounted to £0.71 and £0.62 per unit respectively. The mark ups achieved by the Appellant in those deals was £15 and £10 per unit respectively. The Tribunal is satisfied that the additional overheads incurred in exporting the goods constituted a

small proportion of the margin achieved by the Appellant and did not explain the wide disparity in the level of mark ups achieved by the Appellant as compared with the other traders in the deal chains.

Connections between the Parties in the Deal Chains

217.La Parisienne du Commerce was the Appellant's customer in five of the disputed April deals. In the second quarter of 2006 La Parisienne du Commerce purchased goods from UK based traders valued at £90 million. The details of those transactions revealed that other UK companies (AMR GB Limited, AR Communications and Electronics Limited, and Blue Wire Communications Limited) involved in the April 2006 deal chains as buffer traders had also supplied goods directly to La Parisienne du Commerce during that same quarter. The profits available to those buffer traders would have been far greater had they sold directly to La Parisienne du Commerce instead of to another buffer trader in the Appellant's deal chains.

218. France Affaires was the Appellant's customer in five of the disputed April 2006 deals where Kingswood was the Appellant's supplier. France Affaires had an established trading relationship with Kingswood prior to April 2006. In periods 07/03 and 08/03 Kingswood supplied goods direct to France Affaires. Likewise France Affaires gave Inter Communications Limited as a trade reference to the Appellant in September 2005. Inter Communications Limited was a buffer trader in the Appellant's disputed deal 2. The Tribunal observes that the profits available to Inter Communications Limited and to Kingswood in the disputed deals with the Appellant would have been considerably more had they sold direct to France Affaires.

219. Tradestar acted as the UK distributor of an accounting package developed and owned by Bullfinch, one of the defaulting traders in the disputed April 2006 deals. Further Mr Alibhai acknowledged that he knew Sanjay Pandya, the director of Bullfinch from around 2003/04. According to Mr Alibhai, Mr Pandya offered him stock of IT equipment from one of his other businesses and not from Bullfinch. Mr Alibhai stated that he tried to deal direct with Bullfinch over the accounting software but Mr Pandya refused, saying that Mr Burgess of Tradestar had the sole distribution rights. Mr Alibhai pointed out that this was how he first made contact with Mr Burgess.

The Appellant's Customers

220.La Parisienne du Commerce and France Affaires shared the same Chief Executive, a man named *Zheng Wang*. Also it would appear that the respective managers of the two French companies were related as father and son. Both French companies had customers in common: Spanish companies 300 Infortec SL and CDM Comercio Y Distribution; and Austrian companies TMEA Trading and KBS Handels. The Spanish and the Austrian companies were the purported recipients of the goods traded by the Appellant with La Parisienne du Commerce and France Affaires in March and April 2006.

221. Officer Holden adduced evidence which demonstrated that 300 Infortec SL was deregistered for VAT on the grounds that it was a missing trader on 11 July 2006. CDM Comercio Y Distribution was deregistered for VAT on the grounds that it was a missing trader with effect from 20 September 2006. The Austrian authorities considered the activities of TMEA Trading suspect. The company had only a virtual office in Austria; all payments for goods were made via the FCIB; and no official of the company could by contacted by the authorities. KBS Handels likewise had no storage facilities in Austria and that the goods traded in at no stage crossed Austrian borders.

222. Officer Holden stated that the French VAT authorities had been unable to locate the settlement documents of both La Parisienne du Commerce and France Affaires in respect of their purchases in April 2006 from the Appellant. Officer Holden was unable to assist the Tribunal about the meaning of settlement documents.

223. According to Officer Holden, Mikromkt was a Maltese-based company. Its director, however, was a British national living in Spain named Ben Faizal Junglee. Mr Junglee was also the director of Fullravens SL which was the subject of a civil investigation by HMRC over an unlawful means conspiracy. In November 2004 the High Court granted a worldwide freezing injunction against Fullravens SL. HMRC's case against Fullravens SL was currently dormant as there was no information on the company's whereabouts or the existence of significant assets.

224. The Maltese Authorities advised Officer Holden that Mikromkt made substantial acquisitions during the first quarter of 2006 but had failed to submit a VAT return. Following investigations, the Maltese authorities concluded that the Mikromkt was a conduit trader which purchased goods from and sold them onto companies outside Malta, the goods at no stage having entered Malta.

225.Mikromkt sold the goods which had been supplied by the Appellant in April and May 2006 to a Polish based company, PPUH Kamar which was deregistered with effect from 22 June 2006. PPUH Kamar described its economic activity as *gastronomic services* and did not declare intra-community acquisitions in the first and second quarters of 2006.

226. According to Officer Holden, Mikromkt traded with the Appellant until and including 07/06. The total value of Mikromkt's purchases from the Appellant in the first three quarters of 2006 was in excess of £46 million. In the VAT quarter until 31 October 2006, Mikromkt purchased goods valued at £14 million from a new supplier, MM Leicester Limited. The 11 deal chains in respect of which MM Leicester acted as supplier to Mikromkt traced back to a tax loss and defaulting trader. Input tax repayments claimed by MM Leicester for those eleven supplies were denied by HMRC. MM Leicester appealed against the decision of HMRC but its appeal was struck out by the Tribunal. Thus every deal conducted by Mikromkt in 2006 was traced back to a tax loss, regardless whether the supplier was the Appellant or MM Leicester.

Money Flows

227. The Tribunal decides that the analysis of the various FCIB accounts for eight transactions given by Officer Ellis was sound and substantiated by the documentary evidence. The Tribunal is satisfied that the analysis demonstrated circularity of payments in each of the eight deals scrutinised. The Tribunal did not consider that the Appellant's cross-examination undermined Officer Ellis' conclusion on circularity. Essentially the Appellant picked out isolated examples of where the Electronic Banking Reference number (EB)[8] suggested that a trader may have made a payment out before a payment in. Officer Ellis gave a rational explanation for his choice of payments which were based upon the narrative in the print-outs and that the said party had the funds already in its account with which to make the payment. The Tribunal also placed weight on the fact that all the payments analysed by Mr Ellis were made in Sterling regardless of the domicile of the paying and recipient companies.

228. The evidence showed that in each of the eight deals analysed by Officer Ellis the payment of the individual traders in their respective chains was made on the same day[9] which was always in the subsequent month to when the deals were purportedly transacted. The evidence suggested a high degree of co-operation between so called independent traders, a link with the timing of VAT repayments to the Appellant, and that the payment by the Appellant's customer triggered payments by the traders in the Appellant's deal chains.

229. The corollary of the facts found in paragraph 228 was that each trader continued to trade in goods in which it had no title until the Appellant's EU customer behaved atypically, and paid the Appellant. The Tribunal considers there was no logical reason for a trader to provide thousands of pounds worth of stock to another trader without payment and await a significant period of time before the Appellant's customer made payment. The position of the Appellant's EU customer was equally irrational. For no disclosed reason, the customer decided to pay the Appellant even though the Appellant did not hold title at the moment of payment.

230. Officer Meynell analysed the order times and order dates available for the eleven traders in the money chains for deals 10 and 39. HMRC accepted that the de facto timings of the payments may not be correct. The Tribunal, however, was persuaded by HMRC's argument that the timing differentials between payments made in the respective deals were reliable and relevant. The timing differentials showed that the three rounds of payments were completed in three hours or less.

231.Officer Meynell produced an additional chart in deal 39 which showed that four IP addresses were shared by the eleven participants in that money flow chain. In respect of the first round of payments, the same IP address was used by the Appellant, its supplier and customer (together with the defaulting trader in that chain). In respect

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[8] The print-outs analysed by Officer Ellis did not give the timings of the payments simply the date. Officer Ellis also agreed that the EB numbers may not necessarily reflect the correct timing sequence for payments see T 26.10.11 para 25 126 to para 10 127.

[9] Deal 10 May 2006 was the one exception where the Appellant's customer (Micromkt) paid on 5 June compared with the 14 June for the remaining traders in the deal chain.

of the second round of payments, the same IP address was used by the Appellant and its customer. The Appellant argued that the Tribunal should disregard the evidence of the shared IP addresses because it was not put to Mr Alibhai by HMRC. Equally HMRC pointed out that the Appellant did not challenge the evidence adduced by Officer Meynell. In the Tribunal's view, the evidence speaks for itself, and agrees with HMRC that there was no legitimate reason why two parties in a single transaction chain should share an IP, if those parties were trading legitimately and at arms length.

Carouselling of Goods

232. HMRC adduced evidence to demonstrate that a substantial quantity of the CPUs and the mobile phones traded by the Appellant in the disputed deals had been examined previously or subsequently by HMRC at a point of export which indicated that the goods were carouselled.

233.The evidence showed that at least 110 boxes of CPUs out of 322 boxes traded by the Appellant in March and April 2006 were wholesaled by other UK traders before and after the Appellant had supplied them in disputed deals.

234. HMRC's analysis of the IMEI numbers provided by the Appellant in relation to the mobile phones traded in April 2006 showed that 310 pieces of consignment had been examined by HMRC at a point of export in the UK prior to the occasions of the Appellant's transactions and 253 pieces of consignment had been examined by HMRC at a point of export in the UK on occasions after the Appellant had exported the goods. HMRC was unable to conduct a detailed analysis of the IMEI numbers for the mobile phones traded in May to July 2006 because the Appellant only supplied them in paper form. HMRC took a small sample of these IMEI numbers which indicated that eight pieces of consignment had been examined by HMRC at a point of export in the UK prior to the Appellant's transactions (including one piece which had been recorded six times previously).

235. Mr Alibhai denied knowledge of the goods being carouselled stating that he was only aware of his purchase and sale. HMRC in letters dated 30 November 2005, December 2005 and July 2006 advised the Appellant that a significant number of its supplies in mobile phones had been traded before in the UK, some of them several times. Mr Alibhai disagreed that he was put on notice that the Appellant's deals were connected with fraud. According to Mr Albhai he was not surprised with the prior trading of mobile phones because they were commodities.

236.The Tribunal was satisfied that a significant number of the goods traded by the Appellant in the disputed deals had been carouselled which in the Tribunal's view demonstrated the fraudulent nature of the Appellant's deal chains.

Evaluation of the Evidence on Knowledge

237.HMRC's primary assertion was that the Appellant had actual knowledge that its transactions were connected with fraud. HMRC submitted that the evidence led firmly

and plainly to the conclusion that the disputed deals conducted by the Appellant were connected with a fraudulent scheme (or schemes) involving many parties playing a number of roles. The scheme involved planning the nature and direction of the transaction chains in respect of certain goods with the purpose of defrauding the Revenue. Further each party including the Appellant, therefore, knew with whom it should trade in respect of given goods. The Appellant, therefore, knew that its deals were being contrived and were connected with the fraudulent evasion of VAT.

238. Mr Alibhai asserted that he knew nothing about the wider circumstances beyond the Appellant's immediate deals with its suppliers and customers. The Tribunal adopted an inside/out approach to HMRC's evidence on the Appellant's knowledge by considering first those facts which Mr Alibhai accepted were within his knowledge. A summary of the Tribunal's findings on those matters is set out below:

(1) Mr Alibhai was fully aware of the prevalence of fraud in the CPU and mobile phone wholesale trade sectors, and the risks that it carried for the Appellant's business. Also he was aware of the contents of Notice 726 and of the steps that he should take to avoid wherever possible the Appellant's deals being caught up with fraudulent transactions. (see paragraph 133).

(2) Mr Alibhai knew that the risks of fraud were real in view of the various warnings he received from HMRC about the existence of fraudulent tax losses in the Appellant's supply chains. (see paragraphs 134 & 135).

(3) A responsible trader in the Appellant's position as at June 2006 with a history of tax losses in its supply chains would have been slow without making other enquiries to enter into further trades with Tradestar. The Appellant nevertheless conducted further trades with Tradestar in June and July 2006. (see paragraph 135)

(4) There was no rational commercial explanation for the Appellant's instant success in the wholesaling of mobile phones as measured by the rapid increase in turnover and the sizeable gross profits. The Appellant's research of the market was minimal. The Appellant compiled no business plan unlike its venture with mobile satellite technology. The Appellant encountered no difficulties in securing supplies and orders despite the facts that they were gained from internet platforms open to the business community as a whole, and the Appellant's lack of history in the wholesaling of mobile phones. The reality was that the overwhelming majority of the Appellant's deals involved two suppliers (Kingswood and Tradestar) and one customer (Micromkt), which ran contrary to the depiction of the mobile phone wholesale market as highly competitive (see paragraph 142).

(5) The Appellant's financial arrangements made no commercial sense for handling a business with a multi-million pounds turnover. The Appellant did not have a sound capital footing for its business activities. The pattern of the Appellant's dealings was rigid and determined by the date of the VAT return and did not reflect the highly competitive market in mobile phones as asserted by Mr Alibhai. (see paragraph 164).

(6) The actual arrangements employed by the Appellant to meet the cash flow difficulties during the disputed periods were far removed from normal commerce

operating at arms length. The details of the cancelled July deals revealed a degree of interdependence and co-operation which would not be expected from traders purportedly operating independently and seeking the best deal (see paragraph 165).

(7) The Appellant's reasons for choosing FCIB as the bank through which it conducted its financial transactions for the wholesaling of mobile phones and CPUs were unconvincing. The lack of transparency associated with off-shore accounts provided the Appellant with the means to avoid scrutiny of its deals by the UK authorities (see paragraph 166).

(8) It defied logic and commercial reality that the Appellant was able to relinquish possession of goods of substantial worth without payment having been made for them, or any security for payment being given. Further it was equally illogical that, notwithstanding that a supplier retained (or purported to retain) title to goods pending payment, a trader allocated stock was given permission to export it (see paragraph 170).

(9) The arrangements whereby the Appellant was permitted to ship out goods to its customer before payment demonstrated a high degree of co-operation and trust between the Appellant and his trading partners which would not normally be a feature of arms-length commercial deals with values in excess of £100,000 (see paragraph 171).

(10) Mr Alibhai's explanation that the Appellant did not need the protection of written specifications because of the unlikelihood of a dispute with its trading partners was unconvincing. The absence of such formalities was contrary to arms length trading between independent traders (see paragraph 178).

(11) Mr Alibhai should have been put on notice that the Appellant was trading in goods not destined for the UK market. Mr Alibhai did not question why mobile phones with two pin chargers or described as American stock had somehow ended up in the UK. Mr Alibhai adduced no evidence that at the time of entering into the disputed deals he raised questions about the specifications of the mobile phones described in the inspection reports (see paragraph 179).

(12) Mr Alibhai as a prudent trader well aware of the risks of fraud in the Appellant's trade sector should have been using the information from the documentation to assess whether the deals were legitimate. In the Tribunal's view the discrepancies were yet another example of the Appellant ignoring signs that its transactions may not be bona fide (see paragraph 183).

(13) The Appellant did not insure the goods despite Mr Alibhai's assertions to the contrary, which raised questions about his motive for misleading HMRC on the insurance position (see paragraphs 186 & 187).

(14) The Appellant's checks on the integrity of its trading partners and of the goods were plainly inadequate. The Appellant took the information given to it by its trading partners at face value, and did not independently verify the accuracy of the information. The Appellant did not step up its due diligence on its suppliers after being informed that their supplies had been traced back to tax losses (see paragraph 204).

(15) The Appellant had no effective systems in place to ensure that the goods traded were not caught up in fraud. The Appellant did not examine the information on box numbers and IMEIs in the inspection reports provided by A1, Global International Freight and others. The evidence demonstrated that Mr Alibhai did not have the reports on the IMEI numbers of the mobile phones at the time the Appellant entered the disputed deals. The fact that the Appellant did not use the information in the inspection reports suggested that the Appellant was simply going through the motions (see paragraph 206).

(16) The plain fact was that the Appellant conducted no effective due diligence (see paragraph 206).

239.The Tribunal's findings on those matters which Mr Alibhai accepted were within his knowledge fell within three overall themes.

240.The first theme highlighted the total absence of a commercial rationale for the Appellant's deals within a highly competitive market. The Appellant's instant and continuing success as a wholesaler in mobile phones and CPUs without substantive market research and adequate financial planning ran counter to the usual principles of commerce. The Appellant's deals were conducted with a small select group of suppliers and customers and characterised by a degree of interdependence and co-operation which was far removed from arms length commercial dealings. Finally the concept of commercial risk was alien to the disputed transactions. The Appellant entered into high value deals without any meaningful checks on its trading partners and goods. On a significant number of occasions the Appellant parted with goods without payment and adequate insurance cover for the goods transported. Every transaction of the Appellant in the disputed periods proceeded smoothly to a successful conclusion

241. The second theme concerned Mr Alibhai's total disregard of the presence of fraud in the Appellant's trade sector. Mr Alibhai was fully aware of the indicators and risks of fraud and the steps necessary to minimise those risks. Mr Alibhai, however, chose to ignore the indicators and the warnings given to him by HMRC, and failed to implement the necessary steps to protect the Appellant from fraud.

242. The final theme was Mr Alibhai's unwillingness to stand back and reflect on the manner of the Appellant's business in the wholesaling of mobile phones and CPUs. At no time did Mr Alibhai question the Appellant's instant success in its new venture and the bona fides of its transactions after being informed of their connection with fraudulent transactions. Mr Alibhai's stance in this respect was more surprising given the Appellant's experience of starting up its new venture with mobile satellite services and the difficulties of achieving a profitable business.

243.The Tribunal finds these three themes add up to a compelling case that the Appellant's transactions were contrived and pre-ordained for which there was no commercial rationale. Mr Alibhai's acquiescence with the arrangements coupled with his disregard of indicators and warnings of fraud strongly indicated that he knew that each of the Appellant's disputed transactions was not bona fide and connected with fraud.

244. When the Tribunal takes account of its findings on the wider circumstances the accumulation of detail presents an overwhelming case that Mr Alibhai's knew that each of the Appellant's transactions was connected with fraud.

245. A summary of the findings on the wider circumstances are as follows:

(1) The structure of each chain headed by five of the seven defaulting traders followed the same pattern in respect of the identity of the traders and their position in the chain (see paragraphs 208 & 209).

(2) The long length of the deal chains with five or seven UK registered traders which indicated that the participants were not adding value to the goods sold in the respective chains (see paragraph 210).

(3) All the participants in the Appellant's 49 deal chains were exclusively wholesalers. There were no manufacturers, authorised distributors, retailers or end users in the chains (see paragraph 211).

(4) The pre-determined nature of the mark ups achieved by the traders in the deal chains excluding the Appellant. The mark ups achieved by each trader in the May and June 2006 chains and five of the six July deals remained the same regardless of make, model and quantity sold (see paragraphs 212 to 215).

(5) Although the Appellant's mark ups for the disputed deals did not follow a particular pattern. The Appellant's mark up for each of the deals, however, was significantly more than the other traders in the respective supply chains. The additional overheads incurred by the Appellant in exporting the goods did not explain the wide disparity in the level of mark ups achieved by the Appellant as compared with the other traders in the deal chains (see paragraph 216).

(6) The presence of existing trading relationships between La Parisienne du Commerce and France Affaires with other traders in the deal chains including Kingswood, one of the Appellant's suppliers, questioned why those traders did not deal directly with the Appellant's customers in pursuit of greater profit (see paragraphs 217 & 218).

(7) The dubious nature of the trading conducted by the Appellant's customers and their links with other businesses connected with tax losses (see paragraphs 220 -226).

(8) The presence of circularity of payments in each of the eight deals analysed (see paragraph 227).

(9) All the payments were made in Sterling regardless of the domicile of the paying and recipient companies (see paragraph 227).

(10) Officer Ellis' evidence suggested a high degree of co-operation between so called independent traders, a link with the timing of VAT repayments to the Appellant, and that the payment by the Appellant's customer triggered payments by the traders in the Appellant's deal chains (see paragraph 228).

(11) No logical reason for a trader to provide thousands of pounds worth of stock to another trader without payment and await a significant period of time

before the Appellant's customer made payment. The position of the Appellant's EU customer was equally irrational. For no disclosed reason, the customer decided to pay the Appellant even though the Appellant did not hold title at the moment of payment (see paragraph 229).

(12) A significant number of the goods traded by the Appellant in the disputed deals had been carouselled (see paragraph 236).

246. The Tribunal's findings on the wider circumstances revealed striking similarities in the membership, the organisation and the length of the deal chains with each party other than the Appellant receiving a pre-determined mark-up. The arrangements whereby the parties were prepared to release high value goods without payment highlighted a high degree of co-operation between them. These features were not characteristic of arms length trading between independent traders but rather of an orchestrated body of persons brought together to achieve a common objective. The high incidence of circularity of funds and goods together with the fact that each deal was traced back to a fraudulent tax loss demonstrated that the common objective was to defraud revenue.

247. The Appellant held the position of broker in each of the deals chains. The Appellant's role was critical for the successful execution of the frauds which in itself was persuasive evidence that the Appellant knew that its transactions were connected with fraud. The large profits and the variable mark up achieved by the Appellant as compared with the other traders reflected the risks it took as the broker for the deals. Unlike the other traders, the Appellant as broker took the highest risk in that it would submit a substantial repayment claim to HMRC which may be refused. The high profit and mark up was a reward for taking that risk.

248. The Appellant argued that the conduct of the proceedings by HMRC gave the impression that it had the burden of proving that its transactions were not connected with fraud. In the Appellant's view, HMRC's case was based on Mr Alibhai's failure to answer questions and adduce sufficient evidence to back up his assertions. In this respect the Appellant maintained that HMRC had not carried out a proper investigation into grave and serious allegations. HMRC did not interview Mr Alibhai prior to the Appeal hearing and the first time that he had the opportunity to put the Appellant's case was in cross examination in the witness box. According to the Appellant, HMRC's conduct of the investigation compromised the fairness of the proceedings.

249. The Tribunal disagrees with the Appellant's depiction of the proceedings and investigation as unfair. These proceedings concerned HMRC's refusal of the Appellant's VAT repayment claims and did not involve contraventions of the criminal law. Officer Holden had given Mr Alibhai many opportunities to provide further information and clarification of her enquiries into the Appellant's trading activities which Mr Alibhai as a general rule did not take up or responded late[10]. Further HMRC

[10] Examples of Mr Alibhai's failure to respond or late responses are cited in paragraphs 158, 183&185(1). Officer Holden's witness statement provides other examples (see paragraphs

disclosed its case against the Appellant and of its contention that the Appellant knew or should have known of the connection of its transactions with fraud from 31 March 2008.The Tribunal is satisfied that Mr Alibhai was fully aware of HMRC's case against the Appellant for a significant period of time and that he was given many opportunities to provide explanations and supporting documentary evidence.

250.Equally the Tribunal rejects the Appellant's submission that HMRC did not discharge its burden of proving the case it asserted and that it relied on Mr Alibhai's responses. The Tribunal considers that the Appellant was confusing the burden of proof with the evidential burden. As explained earlier the nature of these proceedings was such that HMRC put its case to Mr Alibhai who was given the opportunity to bring evidence to counter and undermine HMRC's case. The Tribunal decided that Mr Alibhai was singularly unsuccessful in casting doubt on the evidence presented by HMRC.

251.The Tribunal considers that Mr Alibhai was not an impressive witness. He did not give plausible answers to why he did not carry out specific checks and heed the warnings of HMRC Officers. He did not provide a persuasive explanation for the success of the Appellant's business. At times he sought to deflect answers by referring to the passage of time or by the existence of documents which had not been produced for the hearing[11]. Mr Alibhai's response to the non-production of documents was that the Appellant's previous solicitor had a lien over these documents because of the Appellant's non payment of legal charges. The Tribunal notes that the Appellant did not supply documentary evidence of the lien and of the previous solicitor's refusal to co-operate with the Appellant's preparation for its Appeal. Whatever the truth of the lien, it did not explain why some of those documents were not available to the Tribunal because according to Mr Alibhai they were already in the Appellant's possession and could be retrieved by accessing its computer.

252.The Appellant asserted that it only knew of the circumstances of its immediate transactions and that the details of the deal chains were outside of its knowledge. The Appellant's case was that it was carrying out real transactions conducted on acceptable commercial principles for the wholesale trade. The Appellant's assertion of undertaking commercial business deals was dismissed by the Tribunal's finding of the total absence of a commercial rationale for the transactions. The Appellant's assertion, however, was undermined by its own final submissions which stated that the question of insurance was a commercial decision and that there was no legal requirement to carry out IMEI checks. In this respect the Appellant's submissions subverted Mr Alibhai's evidence that the Appellant had insured the goods, and performed the IMEI checks.

253.The Appellant relied on aspects of the evidence of Officers Holden and Ellis to cast doubt on HMRC's portrayal of the wider circumstances in relation to knowledge.

287,295,302,307,313,318,342,400,419,425,450,452,454,458,461,462,464,486,489,501 of 1st witness statement: & paragraph 22 of 2nd statement) (continuation of footnote 10).

[11] See 5-25 & 1-18 133 and 134 Transcript 3.11.2011 for examples of documents not provided as revealed in the transcripts.

Officer Holden stated that a legitimate trader would be unable to go beyond its immediate supplier, and there was no evidence that the Appellant was aware of the source of its goods other than its supplier. Officer Holden accepted that the Appellant's immediate suppliers did not cause tax losses and that the other parties had accounted for output tax as well as immediate suppliers. The Tribunal did not consider these aspects of Officer Holden's evidence significant in determining the Appellant's knowledge of the connection of its transactions with fraud. HMRC contended that the Appellant was not a legitimate trader, and that the Appellant's suppliers were not the defaulting traders responsible for the tax losses. The question of the Appellant's knowledge of the source of goods was not relevant to the disputed issue.

254. The Appellant's challenge in respect of Officer Ellis' evidence was potentially more damaging to HMRC's case, particularly the elicitation of Officer Ellis response that *he was not completely sure about his evidence.* The Tribunal formed the view, however, that his assertion of circularity of funds stood up on close examination of the evidence adduced. The Tribunal interpreted Officer Ellis' response as an honest assessment of the scope of his evidence not a denial of its validity. In any event the Tribunal's findings on circularity of funds formed a small part of the accumulation of detail which demonstrated the Appellant's knowledge of the connection of its transactions with fraud.

255.The Tribunal is satisfied that its findings on the question of knowledge substantiated HMRC's case that the Appellant's disputed transactions were part of contrived deal chains, and not the product of a negotiations involving independent traders selecting their trading partners by reference to normal market forces. The essential features of contrived deal chains were that the participants in the chains were told who to buy from and sell to and the success of the scheme depended upon each party performing its part. The findings demonstrated that Mr Alibhai was a willing participant in the contrived deal chains and not an innocent dupe. Mr Alibhai's acquiescence with the arrangements coupled with his disregard of indicators and warnings of fraud and the easy profits secured by the Appellant from the deals showed that he knew what was expected of the Appellant in the contrived chains and was told with whom the Appellant should trade. In short it was plain to Mr Alibhai that the disputed transactions undertaken by the Appellant were connected with fraud.

256.The decision for the Tribunal is whether at the time the Appellant entered into each of the disputed transactions it knew that the particular transaction was connected with fraud. In order to arrive at that decision the Tribunal is required to have regard to all the available and relevant evidence and is not restricted to consideration of the evidence for each transaction in isolation (see paragraph 114). The Tribunal is satisfied from its findings that the Appellant was told who to trade with before taking part in the deals, otherwise they would not have gone ahead. The Tribunal holds that its findings demonstrate that the Appellant knew at the time that it entered each of the 49 disputed deals that that particular deal was connected with fraud.

Reference to the European Court of Justice

257.The Appellant contended that the Tribunal was not bound by the Court of Appeal decision in *Mobilx* in circumstances where the law is not *Acte Clair.* According to the Appellant, the Tribunal has a free standing obligation arising under section 2(1) of the European Communities Act 1972 to disapply any rule of national law or procedure which conflicts with Community law.

258. The Appellant contended that the scope of the Court of Justice in *Kittel/Recolta* was narrow, being confined to cases involving either the perpetrator of a fraud or a willing counterparty of such a perpetrator. In the Appellant's view, this narrow construction was consistent with the French text of the *Kittel* judgment, and with the way in which the French authorities have applied the *Kittel* test.

259.The Appellant pointed out that the Court of Appeal in *Mobilx* had decided that the material consideration was whether the trader knew or had the means of knowing that there was another transaction in the chain characterised by fraud irrespective of whether the fraudulent trader was one with which the trader dealt directly. In the Appellant's view, the Court of Appeal's interpretation of the scope of denial of the right to repayment as a result of fraudulent activity was not consistent with the narrow construction of the Court of Justice.

260.The Appellant contended that having regard to this uncertainty with the scope of the denial the Tribunal would commit an error of law if it found in favour of HMRC's position that the Appellant's transactions were connected with fraud as a result of the presence of a fraudulent defaulter located several steps removed in the chain from the Appellant's suppliers. In view of the Tribunal's findings on the Appellant's state of knowledge, the interpretation of *connected with fraud* is decisive in determining the outcome of the Appeal.

261.The Appellant argued that its submissions on the uncertainty of the law in relation to the extent of the *connection with fraud* were supported by the decision of the European Court in *Bulves AD v Bulgaria* [2009] ECHR 143 and the reference in *Bonik* (C-285/11).

262.HMRC submitted that the Appellant had not identified sufficiently, if at all, and certainly not with sufficient precision the question of interpretation which ought to be referred to the Court of Justice. In HMRC's view the question appeared to be about the connection with fraud, and the assertion that the scope of *Kittel* decision only applied to the Appellant's transactions with its immediate suppliers.

263.HMRC argued that the Appellant had misinterpreted the *Kittel* decision. HMRC acknowledged that the facts of *Kittel* concerned a specific contractual agreement between the applicant and its supplier and that the question answered by the Court of Justice related to those specific facts. The principles, however, established by *Kittel* were, in HMRC's view, not restricted to those facts. HMRC pointed out that the Court of Justice in paragraph 56 of *Kittel* which set out the test for denying the right to repayment did not use the word *seller.* Thus according to HMRC a proper reading of *Kittel* supported the proposition that a taxpayer's right to repayment can be refused

if he knew his transactions were connected with fraud, regardless of where that fraud was occasioned in the chain of transactions.

264. HMRC maintained that its interpretation of *Kittel* must be right as a matter of logic and common sense. According to HMRC, if the Appellant's argument was correct, a taxpayer with full knowledge of the fraud could defeat the *Kittel* objective of preventing the use of Community law for abusive or fraudulent ends by inserting a buffer trader into the chain and distancing himself from the fraudulent defaulter.

265.HMRC submitted that the Appellant's narrow construction of the *Kittel* decision was rejected by the Court of Appeal in *Mobilx*, which involved consideration of the application of the *Kittel* test to a chain in which the taxpayer did not transact directly with the fraudster.

266. HMRC considered that there was no substance to the Appellant's argument that the French language version of *Kittel* supported a narrow construction and be preferred over the English language version. HMRC stated that all the language versions of the judgment produced by the Court of Justice are equally authentic. If there are divergent language versions the approach adopted by the Court is to interpret the provisions by reference to the general purpose rather than grammatical nuances.

267.HMRC argued that the ruling in the *Bulves* case had no relevance because its facts were very different from those considered in this Appeal. This case involved no tax loss to the State and no allegation of fraud in the VAT system of which the applicant had knowledge or means of knowledge. Likewise HMRC submitted that the Tribunal could safely proceed to determine without reference to the matters to be litigated in the *Bonik* case. Essentially the ten questions referred to the European Court in the *Bonik* case make no allusion to existing case law and no allusion to the principles enunciated in *Kittel.*

268.The Upper Tribunal in *Powa (Jersey) Ltd v HMRC* [2012] UKUT considered effectively the same arguments advanced by the Appellant in this Appeal. The Upper Tribunal saw no merit in the French language argument and decided there were no grounds to make a reference to the Court of Justice on the narrow construction point and on the questions posed in the *Bonik* case. Mr Justice Roth said:

> **"**37**.** I have reached my conclusion on the basis of analysis of the ECJ jurisprudence that privity with a fraudulent trader is not a condition for refusal to credit input tax. But as a matter of English authority, the issue has been determined by the judgment of the Court of Appeal in *Mobilx Ltd v HMRC* [2010] EWCA Civ 517, [2010] STC 1436. In his judgment, with which Carnwath LJ and Sir John Chadwick agreed, Moses LJ conducted a thorough analysis of the European case law and explained that in *Optigen* the ECJ held that a fraudulent transaction does not meet the objective criteria which determine the right of the trader to deduct input tax. He observed that *Kittel* represented a development of the law by enlarging the category of those who fell outside the objective criteria "to those who themselves had no intention

of committing fraud but who, by virtue of the fact that they knew or should have known that the transaction was connected with fraud, were to be treated as participants": see at [41]

38. Further, explaining the test in *Kittel,* Moses LJ stated at [59]:

> "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 the *Kittel*."

Significantly, he continued at [62]:

> "The principal of legal certainty provides no warrant for restricting the connection, which must be established to a fraudulent evasion which immediately precedes a trader's purchase. If the circumstances of that purchase are such that a person knows or should know that his purchase is or will be connected with fraudulent evasion, it cannot matter a jot that evasion precedes or follows that purchase. The trader's knowledge brings him within the category of participant. He is a participant whatever the stage at which the evasion occurs."

39. Although Moses LJ's judgment does not expressly consider the argument about translation in Kittel that was addressed to me, he would clearly have been aware of the point since it is expressly mentioned in the judgment in Blue Sphere Global at [18], one of the three judgments which was under appeal before the Court of Appeal in Mobilx. I cannot see that it makes any difference to the analysis if the expression "involved in" were to be substituted for "connected with" in the quoted passage. Hence, the judgment of the Court of Appeal is clear authority, binding on the Upper Tribunal, that the fact that the trader claiming credit for input tax did not deal directly with a fraudulent trader but was more remote in the chain does not preclude his being denied repayment under the rationale of Kittel.

40. I was told that an application for permission to appeal against the judgment in *Mobilx* to the Supreme Court had been dismissed as inadmissible, and on that basis I was urged to make a reference to the ECJ of this question based on the translation point. But even if that course were open to me, given that, in my judgment, the alternative translation discussed above does not impinge in any way on the rationale and principle as explained in *Mobilx,* I would see no ground upon which a reference would be justified. I should add that the fact that there has been a subsequent reference to the ECJ made by the Bulgarian court in Case C-285/11 *Bonik,* EJ 2011 C238/08, which includes a question or questions related to this point and to which my attention was drawn subsequent to the hearing, does not alter my view".

269. The Tribunal has a broad discretion in deciding whether or not to refer a question to the Court of Justice. The Tribunal's exercise of its discretion depends upon whether an arguable point of Community law has been raised. The Appellant argued that the law relating to the scope of the *Kittel* decision was not clear in relation to the meaning of the *connection with fraud,* and determination of this issue was critical to the outcome of this Appeal. The Tribunal considers there is no substance to the

Appellant's submissions. The Tribunal adopts the analysis of HMRC and follows the detailed reasoning of Mr Justice Roth in *Powa (Jersey) Ltd.* The Tribunal notes that Mr Justice Roth considered the Appellant's argument on the different language versions of *Kittel* as misconceived (see paragraph 28 of the decision).

270.The Tribunal decides that the Appellant has raised no arguable point of Community law and there are no grounds to refer a question to the Court of Justice. The Tribunal is bound by the Court of Appeal decision in the *Mobilx.*

Application to Stay

271. On 8 December 2011 the Appellant's representative drew the Tribunal's attention to a decision of the Upper Tribunal in *Mynt Limited & others* dated 29 November 2011. This decision ordered the appeals or applications for permission to Appeal in four separate cases involving missing trader fraud to be stayed until 28 days after the promulgation of the judgments of the European Court of Justice in references C-80/11 (*Mahageben),* C-142/11(*David*), C-285/11(*Bonik*) and C-324/11 (*Toth*).

272.The Appellant's representative stated that

> "We feel it is important that the Tribunal is made aware of this decision before releasing its decision in our client's appeal and consider that the Tribunal may wish to direct the parties to lodge further written submissions on any points arising from the decision (*Upper Tribunal)".*

273.The Tribunal requested HMRC's views as to whether the suggestions of the Appellant's representative had merit. HMRC did not think so.

274.On 12 January 2012 the Appellant made a formal application for a direction that the Tribunal stand over this Appeal until the Court of Justice delivered its judgments on the references mentioned in the Upper Tribunal decision in *Mynt* together with the reference in the Latvian case of *SIA Forvards* (C-563/11).

275.The Appellant argued that it would be unjust for the Tribunal to refuse a stand-over and require the Appellant to argue its case upon the basis of what the Court of Appeal said in *Mobilx.* Further the reasoning in *Mynt* applied just as much, if not more so, to those cases which have been heard but where a decision is expected. It makes no sense whatsoever for significant time and money to be wasted on gathering evidence and preparing cases pursuant to a legal test which may be found by the Court of Justice to be incorrect. The Appellant suggested that the Tribunal might consider whether to make a reference to the Court of Justice. Finally the Appellant noted that HMRC had applied for permission to appeal the decision in *Mynt,* and at the very least the Tribunal should stand-over this appeal behind HMRC's application for permission to Appeal.

276.The Tribunal decided to deal with the formal application by means of written submissions to be lodged and exchanged by 23 February 2012. The parties did not

object to this course of action. The Appellant relied on its existing submissions, whilst HMRC made an additional one dated 22 February 2012.

277.HMRC objected to the stand-over arguing inter alia that the *Mobilx* decision was binding on the Tribunal, the nature of the pending references had no relevance to the outcome of the Appeal, a lengthy and open ended stay would be contrary to the overriding objective of dealing with cases fairly and justly, no assistance can be derived from the decision in *Mynt*, and that the Appellant would suffer no prejudice by the Tribunal proceeding to judgment.

278.HMRC advised the Tribunal that it had renewed its application for permission to Appeal to the Court of Appeal direct. The Upper Tribunal had refused an earlier application for permission in respect of *Mynt* on 4 January 2012.

279.The Tribunal considers the Appellant's grounds for its Application confused and did not directly address the circumstances of this Appeal in which evidence and argument including a request for a reference have already been heard. In this respect it is instructive to refer to the Upper Tribunal's reasoning refusing HMRC's application for permission to Appeal the *Mynt* decision. Judge Bishopp at paragraph 3 stated that

> "The first proposed ground is that I failed to recognise properly that the decision of the Court of Appeal in *Mobilx* is binding on this Tribunal. In my view that ground is unarguable. There is no possible doubt that the decision in *Mobilx* bound and binds me, and I see no basis on which it could properly be said that I failed to recognise and respect that fact. It is not a case in which I have, as the application claims, refused to apply the decision. I have done no more than to defer a decision until a court higher than the Court of Appeal has had the opportunity of reconsidering and expanding upon what it said in *Kittel*. Had the hearing before me been of the substantive appeals it would of course have been necessary to follow *Mobilx*, but the applications were for summary directions dismissing the appeals and the applications for appeal, where different considerations to apply".

280.The Tribunal takes from the above extract that in hearing the substantive Appeal the Tribunal is bound by *Mobilx*. Further the Upper Tribunal had limited its discretion to stand-over to summary matters which involve different considerations from those in substantive appeals.

281. At the beginning of this hearing the Appellant was aware of the pending application before the Upper Tribunal in the *Mynt* case but was content for the hearing to proceed. The Tribunal considers that it would be contrary to the overall objective of dealing with cases fairly and justly to delay publication of its decision. The considerations of standing-over an appeal where evidence has been heard and final submissions made are materially different from those with summary applications and applications for permission. In the Tribunal's view once a substantive appeal has been heard there is a legitimate expectation on the part of the parties that finality is brought to this stage of the Appeal process. Also the duration of stand-over on the terms proposed is likely to be significant which may raise the spectre of a re-hearing whatever the outcome of the references to the Court of Justice. The Tribunal refuses

the application for stand-over including the option of awaiting the outcome of HMRC's renewed application for permission to appeal the *Mynt* decision.

Decision on the Substantive Appeal

282. Articles 167 and 168 of Council Directive 2006/112/EC provide that a trader is entitled to the payment of input tax it claims.

283. The Court of Justice in the joint cases of *Axel Kittel v Belgium & Belgium v Recolta Recycling SPRL* (C-439/04 and C-440/04) established an exception to the right to deduct when the trader knew its transactions were connected to fraud.

284. In *Mobilx* the Court of Appeal dismissed a submission that the principles enunciated by the Court of Justice in *Kittel* cannot be applied as part of UK domestic law without specific legislation.

285. Lord Justice Moses decided at paragraph 59 of *Mobilx* that

> "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".

286. Lord Justice Moses on the question of *connection with fraud* said at paragraph 62:

> "The principle of legal certainty provides no warrant for restricting the connection, which must be established, to a fraudulent evasion which immediately precedes a trader's purchase. If the circumstances of that purchase are such that a person knows or should know that his purchase is or will be connected with fraudulent evasion, it cannot matter a jot that that evasion precedes or follows that purchase. That trader's knowledge brings him within the category of participant. He is a participant whatever the stage at which the evasion occurs."

287. In *Megtian Limited (in Administration) v The Commissioners for HMRC* [2010] EWHC 18 (Ch) Brigg J at paragraphs 37 and 38 provided helpful guidance on the question of knowledge:

> "In my judgment there are likely to be many cases in which a participant in a sophisticated fraud is shown to have actual or blind-eye knowledge that the transaction in which he is participating is connected with that fraud, without knowing, for example, whether his chain is a clean or dirty chain, whether contra-trading is necessarily involved at all, or whether the fraud has at its heart merely a dishonest intention to abscond without paying tax, or that intention plus one or more multifarious means of achieving a cover-up while the absconding took place.
>
> Similarly, I consider that there are likely to be many cases in which facts about the transaction known to the broker are sufficient to enable

> it to be said that the broker ought to have known that his transaction was connected with a tax fraud, without it having to be, or even being possible for it to be demonstrated precisely which aspects of a sophisticated multi-faceted fraud he would have discovered, had he made reasonable inquiries. In my judgment sophisticated frauds in the real world are not, invariably susceptible as a matter of law, to being carved up into self-contained boxes even though, on the facts of particular cases including *Livewire* that might be an appropriate basis for analysis".

288. Lord Justice Moses in *Mobilx* approved the dictum of Christopher Clarke J in *Red 12* in respect of the facts that the Tribunal should have regard to in determining the knowledge of the taxpayer. In effect the Tribunal should have regard to all the circumstances:

> "111. Further in determining what it was that the taxpayer knew or ought to have known the tribunal is entitled to look at the totality of the deals effected by the taxpayer (and their characteristics), and at what the taxpayer did or omitted to do, and what it could have done, together with the surrounding circumstances in respect of all of them."

289. In applying the above law to the facts of this Appeal the Tribunal is required to make findings on the following four questions (see *Blue Sphere Global Limited)*:

(1) Was there a tax loss?

(2) If so, did this loss result from a fraudulent evasion?

(3) If there was a fraudulent evasion, were the Appellant's transactions which are the subject of this appeal connected with that evasion?

(4) If such a connection was established, did the Appellant know or should it have known that its transactions were connected with a fraudulent evasion of VAT?

290. The Tribunal's findings in respect of each of the questions are as follows:

(1) There was a VAT loss in each of the 49 transactions entered into by the Appellant which were attributable to a fraudulent default by the following traders, Computec (April deals 1,4,6,7) Midwest (April deals 2,5,10,11,14), C&B Trading (April deals 3, 8), Bullfinch (April deals 9,12,13), 3D Animations (May deals 15 -36), Vision Soft (June deals 37-43), and Zenith Sports (July deals 44-49) (see paragraph 102).

(2) The tax losses occasioned by Computec, Midwest, C&B Trading, Bullfinch, 3D Animations, Vision Soft and Zenith Sports in relation to the Appellant's 49 deals in April to July 2006 were fraudulent (see paragraph 103).

(3) Each of the Appellant's 49 deals was traced back and thereby connected to a fraudulent tax loss (see paragraph 111).

(4) The Appellant knew at the time that it entered each of the 49 deals that that particular deal was connected with fraud (see paragraph 256).

291.The Tribunal, therefore, dismisses the Appeal and upholds HMRC's decisions refusing input tax in the total sum of £8,327,278.10.

292.The Tribunal orders the Appellant to pay HMRC its costs in relation to the Appeal and if not agreed to be taxed by the appropriate body.

293.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: 29 March 2012