



TC00358

Appeal number: LON/07/0104

INPUT TAX – MTIC fraud – further decision after the appeal was remitted back by the High Court – whether the Appellant ought to have known of the fraud – yes in some of the transactions but not others

FIRST-TIER TRIBUNAL

TAX

OLYMPIA TECHNOLOGY LIMITED (No 2)

Appellant

- and -

**THE COMMISSIONERS FOR HER MAJESTY'S
REVENUE AND CUSTOMS (VAT)**

Respondents

**TRIBUNAL: TRIBUNAL JUDGE JOHN F AVERY JONES CBE
SANDI O'NEILL**

DRAFT DECISION

Sitting in public in London on 8 and 9 December 2009

Kieron Beal, counsel, instructed by Vantis Group Limited, for the Appellant

Philip Moser, counsel, instructed by Howes Percival, for the Respondents

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DRAFT DECISION

1. This is a further decision in the appeal of Olympia Technology Limited which was remitted back to us by Order of Lewison J see [2009] STC 643. Definitions in our earlier decision [2008] SWTI 1259 (“first Decision”) apply to this decision. As before, the Appellant was represented by Mr Kieron Beal, and the Respondent (“HMRC,” which should be taken to include HM Customs and Excise) by Mr Philip Moser.

2. The issue that was remitted to us was that we should have applied the test of whether an ordinarily competent director (also taking into account the knowledge of the senior employee Mr Jivraj) ought to have known about the connection with the fraud in the “straight chains.” It is accepted by the parties that if the Appellant had higher knowledge than the ordinarily competent director (whether through Mr Jivraj or otherwise) that should be taken into account.

3. So far as the law is concerned in [19] of our first Decision we said it was not necessary to decide who had the burden of proof on whether the Appellant ought to have known about the connection with the fraud. It is now clear that this is on HMRC. In this respect we follow the decisions of the Chancellor in *Blue Sphere Global Limited v HMRC* [2009] STC 2239 at [52]:

“The relevant knowledge that that BSG ought to have known that by its purchases it was participating in transactions that were connected with the fraudulent evasion of VAT; that such transactions might be so connected is not enough”

and of Christopher Clarke J in *Red 12 Trading Limited v HMRC* [2009] EWHC 2563 (Ch) at [90]:

“It is important to remember that the right to deduct input tax cannot be denied unless HMRC establishes the requisite knowledge (actual or constructive) on the part of the taxpayer”

and of Floyd J in *Calltel Telecom Limited v HMRC* [2009] STC 2164 at [7]:

“To justify such a refusal [to repay input tax] the tax authorities must prove that the taxpayer was himself being fraudulent, or knew or had the means of knowledge of fraud by others.”

We do not follow the observations on Lewison J in *HMRC v Brayfal Limited* CH/2008/APP 0082 (4 March 2008), which Mr Moser contended was HMRC’s preferred formulation, that the taxpayer must show that it could not have known of a connection with fraud, which are obiter and were made in the course of explaining the background to an issue of whether evidence should be admitted.

4. The law on the standard of proof has moved on since our first Decision. It used to be said that the more serious the allegation the less likely it is that the event occurred and the stronger (or more cogent) should be the evidence before a court concludes that the allegation is established on the balance of probability. The House of Lords in *In re B* [2009] AC 11 has clarified this. As Lord Hoffmann (with whom, Lord Rodger and Lord Walker agreed) said:

5 “There is only one rule of law, namely that the occurrence of the fact in
issue must be proved to have been more probable than not. Common
sense, not law, requires that in deciding this question, regard should be
had, to whatever extent appropriate, to inherent probabilities. If a child
alleges sexual abuse by a parent, it is common sense to start with the
assumption that most parents do not abuse their children. But this
assumption may be swiftly dispelled by other compelling evidence of
the relationship between parent and child or parent and other children.
10 It would be absurd to suggest that the tribunal must in all cases assume
that serious conduct is unlikely to have occurred. In many cases, the
other evidence will show that it was all too likely. If, for example, it is
clear that a child was assaulted by one or other of two people, it would
make no sense to start one’s reasoning by saying that assaulting
children is a serious matter and therefore neither of them is likely to
15 have done so. The fact is that one of them did and the question for the
tribunal is simply whether it is more probable that one rather than the
other was the perpetrator.”

Lady Hale (with whom Lord Scott, Lord Rodger and Lord Walker agreed) said:

20 “70...Neither the seriousness of the allegation nor the seriousness of
the consequences should make any difference to the standard of proof
to be applied in determining the facts. The inherent probabilities are
simply something to be taken into account, where relevant, in deciding
where the truth lies.

25 72. As to the seriousness of the allegation, there is no logical or
necessary connection between seriousness and probability. Some
seriously harmful behaviour, such as murder, is sufficiently rare to be
inherently improbable in most circumstances. Even then there are
circumstances, such as a body with its throat cut and no weapon to
hand, where it is not at all improbable. Other seriously harmful
behaviour, such as alcohol or drug abuse, is regrettably all too common
and not at all improbable. Nor are serious allegations made in a
vacuum. Consider the famous example of the animal seen in Regent’s
Park. If it is seen outside the zoo on a stretch of greensward regularly
used for walking dogs, then of course it is more likely to be a dog than
30 a lion. If it is seen in the zoo next to the lions’ enclosure when the door
is open, then it may well be more likely to be a lion than a dog.”

5. Our understanding is that the dangers of the old formulation were first, that it
could be misunderstood to be increasing the civil standard of proof to something
above the balance of probability; and secondly, that it was illogical to start with
40 considering the seriousness of the allegation in a vacuum and assume that all serious
allegations were unlikely and therefore needed cogent proof. Now one starts with
determining the likelihood of the allegation having regard to the surrounding
circumstances and not in a vacuum. Having done so the only question is whether the
allegation is proved to the balance of probabilities. In other words, the inherent
45 probability itself includes the particular circumstances.

6. In [18] of our first Decision we said: “There is no disagreement that the standard
of proof is to the normal civil standard but one which takes into account the

improbability of fraud.” If this meant the improbability of fraud in a vacuum it was wrong. We therefore need to evaluate the evidence again in the light of this decision.

7. Generally on the law relating to MTIC fraud, we have a number of decisions of the High Court, three of which (*Mobilx Limited v HMRC* [2009] STC 1107, *Blue Sphere* and *Calltel*) are due to be heard by the Court of Appeal in February 2010. Of these *Mobilx* is the only one concerning straight chains where “ought to have known” was the issue. We have considered whether to wait for the Court of Appeal decision. Since our decision is in part in favour of each party and we would expect both parties to preserve their position by applying for permission to appeal we are issuing this decision in draft at this stage so that we can take into account any further guidance from the Court of Appeal. In doing this we appreciate that the Appellant has been waiting for repayment of input tax since April and May 2006 but we assume that they will not receive it until appeals have been exhausted.

8. We find the following further facts:

15 (1) Mr Jivraj did not give evidence at the original hearing but we find that he was a senior employee of the Appellant whose knowledge can be attributed to the Appellant. We said in our first Decision at [27(1)]: “Mr Murtaza (“Monty”) Jivraj was the son of a friend of Mr Habib’s father who was brought in as having some experience of mobile phones, having worked for Synectiv inspecting phones.” (We leave out of account the fact that Synectiv was the subject of an attempted criminal prosecution by HMRC.) Mr Habib’s witness statement described Mr Jivraj as having significant and expert knowledge of the industry within the UK.

25 (2) HMRC had warned Mr Jivraj in a letter of 26 January 2004 that of 25 transactions being verified, 6 traced back to missing traders, not being any of the traders involved in the transactions which are the subject of this appeal; and 13 to suspected missing traders which were being investigated further, and that in 8 cases there were third party payments in the chain. After telephone discussions and meetings Mr Jivraj wrote to HMRC on 16 February 2004 saying: “We have presented yourself and HMCE of the facts that we have always been committed to protect ourselves from the immoral surroundings. I am sure that our information has satisfied HMCE and you in this decision-making.” The input tax on all these transactions was repaid with repayment supplement and costs. At the time HMRC were looking at non-economic activity but they did not review this in the light of later ECJ decisions. No other warnings about the existence of fraud in their chains were ever given to the Appellant before the disallowance of the input tax in issue in this appeal.

40 (3) Mr Jivraj wrote a 9 page letter on 13 December 2006 in relation to the input tax in issue in this appeal. We infer that this was written with the aid of professional advice (for example, it quotes Lord Hoffmann’s test of standard of proof in *Rahman* that we quoted in our first Decision at [18], which we consider would not have been known to Mr Jivraj) and cannot be directly taken to be evidence of Mr Jivraj’s expert knowledge of fraud.

(4) Mr Jivraj wrote the Appellant’s paper of 28 July 2004 “Good Practice in Tackling Fraud.”

(5) The Appellant had a document “guidelines for verifying a potential customer/supplier.”

5 (6) Mr Jivraj wrote the Appellant’s evidence to the House of Lords Committee dated 23 January 2007 quoted at [39] of our first Decision.

(7) Accordingly, the Appellant, through Mr Habib its director and Mr Jivraj its senior employee, were fully alive to the dangers of fraud in the mobile phone market, though they were in no better position than anyone else in the industry to know the inherent probability of fraud.

10 (8) We referred at [38] of our first Decision to the Memorandum of Understanding between HMRC and members of the industry. We should add that this became unworkable in about 2000.

15 (9) We have made some further findings of fact in paragraphs 18 and 20 relating to the Appellant’s customers which it is more convenient to include there.

9. Mr Kieron Beal contends in outline:

(1) It is important to identify the fraud, as Lewison J said in this appeal at [91]. The fraud in issue is that the importer in each of the 15 straight chains viewed separately always intended to default. As the ECJ said in *Kittel*, Case C-439/04:

20 “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’.”

25 (2) As Lewison J said in this appeal at [99]:

30 “In the case of a ‘straight’ MTIC fraud it seems to me that a taxable person who is not himself a dishonest co-conspirator will not be deprived of his right to reclaim payment of input tax unless he knew or should have known of a connection between his own transaction and the fraud of the missing trader.”

35 HMRC have not identified what facts the Appellant should have known about or what enquiries it should have made and what the outcome of those enquiries would have been.

40 (3) The facts of this case are quite different from those in *Mobilx* in which Floyd J said at [87] (and repeated it in *Calltel* at [8]):

“I agree entirely with the Tribunal when it said that ‘there must come a time when a trader, told that every one of his purchases followed a tainted chain, is compelled to recognise that without a significant

change in his trading methods every one of his future purchases is more likely than not also to follow a tainted chain’.”

Here there had been no warnings by HMRC of missing traders in the Appellant’s chains, apart from one in 2004 following which HMRC paid the input tax.

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(4) A trader who takes all reasonable precautions to ensure that the transactions are not connected with fraud does not lose the right to deduct input tax: *Kittel* at [51]. As we said in [14] of the first Decision and by Lewison J on the appeal at [88], this does not impose any positive duty on the trader to take such precautions. Mr Hellier said the same in *Honeyfone v HMRC* (2008) VAT Decision 20667:

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“41. It seems to us that paragraph 51 of *Kittel* provides a safe harbour for a trader outside the walls of which he *may* be sunk, but it does not go so far as to say he *will* be sunk or to impose a positive duty. Outside the harbour he will be sunk only if he sails into a storm of which he knew or should have known.”

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(5) The European Court of Human Rights in *Bulves v Bulgaria* [2009] ECHR 143 has found that in the absence of any indication of direct involvement in fraudulent abuse of a VAT chain of supply, or knowledge thereof, penalising a fully compliant recipient of a supply for the actions of a supplier over which it has not control and no means of monitoring or securing compliance, goes beyond what is reasonable and upsets the fair balance between the general interest of the community and the protection of the right of property.

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(6) Since the connection between the Appellant’s transactions in the straight chains and the fraud of the missing trader has been found, the sole issue is whether on the balance of probabilities the Appellant should have known of that connection.

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10. Mr Philip Moser contends in outline:

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(1) The test is that set out by Lewison J said in the appeal in this case at [99] quoted above. Or as Floyd J said in *Mobilx*, the only other straight chain case:

“The essential question is a simple one: was it, or should it have been apparent to *Mobilx*, by the beginning of April 2006 that if it continued to deal in CPUs as it had been doing for the last two years, its transactions were more likely than not to be connected with fraud?”

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(2) Lewison J also said at [91]:

“I accept that the honest trader need not know the identity of the missing trader but unless he knows or should have known that that there was (or was likely to be) a missing trader somewhere in the dirty chain, I do not see how it can be said that he knew or should have known that his transaction was connected with fraud. In fact, in the case of a ‘straight’ MTIC fraud the missing trader will always be the

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importer of the goods, so his position in the chain (if not his identity) will be a fact which can be known.”

The test to be applied is whether the Appellant should have known that there was (or was likely to be) a missing trader in the chain.

5 (3) Taking reasonable precautions was not of itself determinative of knowledge. However, on the basis of what the Appellant had already discovered, it was more likely than not that the deals were connected with MTIC fraud. Alternatively it should have made further enquiries.

(4) *Bulves* was not a case on MTIC fraud.

10 11. We start by applying the new formulation of the law on the standard of proof. The problem we now face is that at the time of the deals in question our understanding is that nobody in the industry knew of the inherent degree of probability of fraud in mobile phone deals. Suppose that it had been generally known that on average one in every thousand transactions in mobile phones was connected to fraud. This was not
15 something that could be completely ignored but equally it was not something that put a trader on notice that any odd feature of the transaction was likely to indicate fraud; the inherent probability was essentially de minimis. But suppose the probability had been generally known to be that on average one or two in ten such transactions was connected to fraud, then fraud is something that the trader should be actively looking
20 out for and any odd feature would almost certainly put him on notice that fraud might be indicated. Our figure of one or two in ten is not an attempt to put an accurate figure on a particular percentage but to indicate that given that there are 15 straight chain transactions in issue in this appeal, at least one on average would be fraudulent. Naturally the nature of the odd feature is also relevant, it being more likely to be fraud
25 if the business of another party to the transaction had just changed to dealing in mobile phones having previously been involved in a wholly different business or having been dormant. An odd feature that was more consistent with fraud than not could indicate that fraud of the importer in a particular chain was more likely than not. What makes it even more difficult is that (with hindsight, and therefore something that cannot be taken into account in determining the inherent probability) we now
30 know that the inherent probability was rapidly changing. Mr Stone’s evidence as summarised in [21] of our previous decision was that

35 “There was a sharp increase in exports [of mobile phones] after the Advocate General’s Opinion in *Bond House* (16 February 2005), with the largest volume following the ECJ decision (12 January 2006). EU exports of mobile phones reached maximum monthly peaks of around £500m in 2002 but then fell sharply in 2003 and 2004. From early 2005 they built up steeply from a low figure to a maximum monthly peak of £4bn in the quarter March to June 2006 and a similar but
40 smaller pattern emerged for non-EU exports. Figures given in the House of Lords European Union Committee Report on Stopping the Carousel: Missing Trader Fraud in the EU, 25 May 2007, HL Paper 101 (“House of Lords Committee”) at evidence p 62, show that the value of MTIC-related trade rose from £4.4bn in the quarter to
45 December 2005, to £11.6bn in the quarter to March 2006, and to £14.3bn in the quarter to June 2006, reducing to £2.2bn in the quarter

to September 2006 and further reducing to £0.6bn in the quarter to December 2006. ”

5 What his evidence did not do was to give any measure of the inherent probability that was generally known at the time of the deals in question in this appeal in April and May 2006. Indeed this evidence points to the fact that circumstances were changing so rapidly that nobody was likely to have an up-to-date view on the inherent probability of fraud.

10 12. We have to judge this inherent probability ourselves on the basis of what was generally known at the time of the deals. The best we can say is that the inherent probability of fraud was something that existed and could not be ignored. We consider that it was certainly greater than our example of one in a thousand transactions and was not therefore de minimis, and that it was closer to our example of one or two in ten transactions but we cannot put a figure on how close because there is no material on which to base that judgment that did not use hindsight. The uncertainty also goes to the reasonableness of taking precautions because what precautions are reasonable must depend on the probability of fraud. This uncertainty makes it extremely difficult to judge whether in this case the Appellant should have known that there was likely to be a defaulting trader who imported the goods at the start of the chain.

15 20 13. On the meaning of “ought to have known” in English law we were taken to *White v White* [2001] 1 WLR 481 in which the House of Lords were interpreting an English law test of “knew or ought to have known” in the light of a Directive in which the test was “knew.” In spite of the different circumstances there is support for the English law test of ought to have known connoting negligence. Mr Beal pointed out that HMRC had conducted the case on the basis of recklessness rather than negligence, and that *Kittel* was in terms of becoming an accomplice to fraud, for which more than negligence was required. We prefer not to apply different legal tests by analogy but to concentrate on the test applicable to MTIC fraud cases, particularly that in the decision of Lewison J in this appeal.

25 30 14. We have reviewed the evidence in the light of Lewison J’s judgment in this appeal and the new understanding of the standard of proof, both as a whole and in relation to individual transactions. It is important not to lose sight of the good features of this case, such as that the Appellant had been trading in mobile phones since 2000, the written terms and conditions which required that the suppliers carried out due diligence checks on their suppliers and did not make third party payments, obtaining declarations by suppliers and customers that they had carried out reasonable commercial checks and applied the terms of Notice 726, the existence of the trade protocol questionnaire, insurance cover, including obtaining confirmation from freight forwarders of their liability insurance as required by the Appellant’s insurance, independent inspections of all goods, 100% IMEI recording and checking that the same phones had not been dealt in before by the Appellant (21,000 IMEI numbers were passed on to HMRC in the two months in question), including checking that a 20% sample were genuine stock, giving HMRC’s Redhill office full particulars of each transaction, and the lack of any warnings by HMRC, except in 2004 following

which it repaid the input tax. We would not alter our first decision except in the following respects.

15. So far as the suppliers are concerned we said at [46] of our first Decision that there was little unusual about them. We went on to review the circumstances of London Mobile Communications Limited about which we had found at [40(2)(c)]:

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Graydon report dated 17 January 2006. Sole trader, above normal credit risk; non-trading at 30 September 2004; amended VAT registration 18 January 2006 showing trade classification retail of mobile telephones. Letter from the accountants of 17 January 2006 informed the Appellant that the company was trading but gave no further information. The Appellant has known the director for “some years” (witness statement), changed to “maybe six or seven months” (cross-examination), then changed to “maybe a year then, or two” when the discrepancy was pointed out, before the deals in question.

15 The company was incorporated on 19 September 2003 and Mr Darren Lietch, the only shareholder, was appointed director on 19 September 2003. Its introductory letter said that it had been trading since November 1994 but Mr Lietch may have been trading as a sole trader under the name London Mobile Communications before incorporating the company (our reference above to “sole trader” is an error; the Graydon Report says “private limited”). The original VAT registration was on 1 October 2004. The company signed the supplier declaration form on 17 January 2006 confirming that it had carried out due diligence checks, completed a trade protocol questionnaire on 2 February 2006, and signed the purchase business terms and conditions on 2 February 2006. We concluded about this at [46] as follows:

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“Although London Mobile Communications Limited had an amended VAT certificate on 18 January 2006 we do not think that Mr Moser is correct in saying that it had changed hands then as the director who signed the contractual conditions had been appointed on 19 September 2003 and was listed in the Graydon report as the holder of all the shares. The amendment to the VAT certificate could have been a change in the bank details. We do not regard the fact that it was dormant over 18 months before the deal as particularly relevant. The fact that its trade classification is that of retail of mobile phones is not so far removed to be indicative of fraud.”

35 We have reviewed this conclusion particularly in the light of the revised understanding of the standard of proof. We now consider that the fact that the company had been dormant in September 2004 and had (or might have) recently changed the type of business as more suspicious. On the other hand, the director was known to the Appellant for a period, the length of which is uncertain, and it had made enquiries of the company’s accountants to obtain verification that the company was trading, who told them that the accounts for the year ended 30 September 2005 had been prepared but were not yet final. This suggests that the change from being a dormant company must have occurred before 30 September 2005. We consider that on balance these factors were insufficient to indicate that the Appellant ought to have known that there was fraud in the chain.

16. Mr Beal contended that the circumstances of the customer was irrelevant to whether the Appellant ought to have known of the fraud of the importer at the beginning of the chain, although he accepted that the relationship with the customer could indicate that the entire deal was uncommercial. He went as far as to say in his
5 submissions “in principle we could have sold to a nunnery these mobile phones and provided that they accounted for the acquisition of VAT and the import VAT and provided that it was not established that selling to a nunnery was part of an orchestrated fraud, it is nothing to the point that it was a nunnery.” In other words, he contends that the customer, against whom no fraud is alleged, can never tell one
10 anything about the fraud by the missing trader who is the importer at the start of the chain. Mr Moser put the opposite view equally strongly, that looking at the customer would put one on notice that the transaction was likely to be connected with fraud without the need for making further enquiries. He relied on the statement of Floyd J in *Calltel* at [81]:

15 “For my part I have no difficulty in seeing how the purchaser who is not in privity of contract with the importer aids the perpetrators of the fraud. He supplies liquidity into the supply chain, both rewarding the perpetrator of the fraud for the specific chain in question, and ensuring that the supply chains remain in place for future transactions. By being
20 ready, despite knowledge of the evasion of VAT, to make purchases, the purchaser makes himself an accomplice in that evasion.”

(We read the reference to “knowledge of the evasion of VAT” as including means of knowledge.) We agree in principle with Mr Moser. While we agree with Mr Beal that the circumstances of the customer can not logically tell you anything directly
25 about the fraud of the importer at the start of the chain, we consider that the unusual circumstances of the customer are indicators that could, depending on the nature of the circumstances, indicate that on the balance of probabilities there is a fraud elsewhere in the chain when the inherent probability of fraud is a factor to be taken into account.

30 17. Our conclusion about the customers in our first Decision was:

35 “47. The customers are less straightforward. Although most of the trading activities could include wholesale trading in mobile phones, doubtful cases include (1) World Communications’ activity being electrical household goods, (2) URTB’s activity of *Autres commerces de gross de biens de consommation*, which may not have been understood by the Appellant, as Mr Habib does not speak French, but which we believe means wholesaler of consumer goods (in the French VAT registration), and “import export telecommunication” (in the Graydon report) and the reference to mobiles in the NACE code, in
40 spite of the other references to restaurants, and (3) Paris 2000 Sarl’s activity in the Graydon report of “wholesale of clothing and footwear” but the Belgian VAT Registration Certificate dated 17 March 2006 clearly shows import and export of mobile phones, implying a recent change of activity. It is noticeable that the Code of Conduct with the industry does not mention the classification of trading activities as
45 something to look out for, except possibly under the very general

heading “What knowledge do credit search companies used by you have of the supplier [customer]?”.

5 48. There are also some very out-of-date accounts for the customers: URTB 31 December 2002; Paris 2000 and World Communications both 31 December 2003, and no accounts at all in the case of Polska Telefontia, World Cellular, or Dantec but we put this information in a similar category as credit risk; the Appellant was not relying on their credit worthiness or their net worth.

10 49. One of the questions relating to the customer in the Code of Conduct is “How long have they been trading and do they have any history in the trade?” Polska Telefontia had been registered only in August 2005, and Dantec in January 2005. Paris 2000 was previously a clothing company, had changed hands in January 2006 and was VAT registered for mobile phone trading in March 2006. The Code of
15 Conduct lists items to be considered and this is something that the Appellant clearly did not take into account. However, this factor does not give any indication about possible fraud, as would have been the case, for example, if Paris 2000 had still been registered as a clothing company.

20 50. So far as we are aware all the goods were delivered to the same country as the customer’s establishment, except for the deals with Polska Telefontia which were shipped to Paris as the Appellant explained that the freight forwarder had no secure warehousing facilities in Poland. Mr Moser pointed to the delivery of Dantec’s
25 phones to Madrid, where the warehouse was, rather than Barcelona, where Dantec was, but we see nothing unusual in this, particularly as the Code of Conduct refers to the country (“Are the goods to be delivered to the country where the customer is resident or are they to be delivered to another country?”). We are also not aware of any other
30 factors relating to the customers in the Code of Conduct that were not satisfied.

35 51. A more prudent or cautious trader might have tried to obtain further references and/or information about the trading activities of especially those companies like URTB, Dantec, Paris 2000 and World Communications where the first contact appears to have been in 2006 and the Appellant had not met the customer. However, we are mindful of the fact that Mr Habib did not speak French, Spanish or Polish and consider that it would not have been easy for him to discover facts that might have made him more cautious. It is also the case that the
40 emphasis in Notice 726 is on the supplier and the supply chain, for example the reference to the purchase price in para 2.5, the supplier in para 4.5 (“We advise you to carry out checks to establish the legitimacy of your supplier to avoid being caught up in a supply chain where VAT would go unpaid”) and the questions relating to the
45 supplier in para 8.1; the customer is mentioned only at para 8.2.”

18. We must re-visit these conclusions in the light of the new understanding of the law on the standard of proof. We consider that particularly suspicious factors would be that the business had recently changed to dealing in mobile phones after it had previously been dormant having previously carried on an unrelated business. The

Appellant accepted this by not trading with a company called Storme International which had changed its name from Storme Clothing Limited. While the reason could be innocent, it does suggest, when one is alerted to some probability of fraud, that someone might have been using the customer in connection with a fraud. While it would be wrong to assume that a customer without a long trading history will be party to a fraud, we think it incumbent on a trader in this industry to make further enquiries to try to ensure that there are no other factors which point to fraud. As we said in our first Decision we do not consider that credit rating as such is relevant in circumstances in which the Appellant was not giving the customer any credit, but equally it is not something which can be ignored in combination with other features. One of the Appellant's "Guidelines for Verifying a Potential Customer/Supplier" included passing details to HMRC including "check their credibility and financial history. On that basis we need to reconsider the following (where we have added items not included in our first Decision these are findings of fact):

(1) URTB Sarl, of which our first decision listed these facts:

"Graydon report dated 16 March 2006. Credit rating 2 (out of 5; 1 being highest risk), previously 9 (used for non-trading companies); latest accounts 31 December 2002 which showed negative shareholders funds; requirement to file annually; business *Autres commerces de gross de biens de consommation* (French VAT registration), "import export *telecommunication cosmetique et textile*, restaurants (traditional)" (Graydon report) "5530 licensed restaurants and cafes including fast food outlets, take aways and mobiles" (NACE code in Graydon report). The Appellant has had a business relationship with them since March 2006 but never met the director."

We consider that the combination of unusual factors is important. The type of business is odd, as is the out of date information (which on its own would not matter, see [48] of our first Decision quoted above) coupled with the short length of time the Appellant had known them.

(2) Paris 2000 Sarl, of which our first decision listed these facts:

"Graydon report dated 9 May 2006. Credit risk 1 (highest risk out of 5); latest accounts 31 December 2003; activities wholesale of clothing and footwear; sale of shares on 12 and 13 January 2006 to Manor Sheriff but Mr Habib was unaware of this; Belgian VAT Registration Certificate dated 13 March 2006 gives the activity as *importation et exportation de materiel telephonique mobile.*"

The significant factors were that its business had recently changed to dealing in mobile phones having been in the clothing business, and the Appellant did not know that the ownership had recently changed.

(3) Navigo.It Spa, of which our first decision listed these facts:

"Navigo.It Spa (Italy); Graydon report 22 May 2006 (deal 12 May 2006). Credit rating 5 (out of 5) low risk; sales Eur 113m, profit Eur 1.6m, shareholders funds Eur 2.9mn in 2004. Graydon activity: wholesale of various machines, tools and equipment for industry, trade, navigation, handcraft & agriculture, wholesale of radio-electric,

telephonic and television materials. March 2006 VAT certificate gives the activity as *ingrossi di elettrodomestici di apparecchi radiotelevisi.*”

Although we did not mention it, the owner had also given himself as a reference. The Graydon report was not seen before the transaction. All they knew was the recent VAT certificate showing what seems to be a business that includes dealing in mobile phones. The Appellant did not therefore know whether this was a recent change in type of business nor how long or successfully the company had been trading at the time of the deals.

(4) Dantec Enterprises SL and World Communications Imp-Exp SLU, which are mentioned in [51] of our first Decision quoted above, on the basis that the Appellant had not dealt with them for long and the latter did not return the trading conditions until after the deal.

(5) Polska Telefonía is mentioned in [48], [49] and [50] of our first decision, which listed the following facts:

Polska Telefonía (Poland). Graydon report dated 19 April 2006 (after the deal) (business name of sole trader Jan Strzelecki); credit rating 8 (risk unknown); no other financial information given; first registered 28 August 2005.

The information known by the Appellant about this customer is minimal.

19. Our conclusion is that in relation to URTB Sarl and Paris 2000 Sarl the Appellant was put on notice that there was something odd about the transaction which raised doubts about their credibility (one of the Appellant’s factors in their Guidelines). In relation to the sale to Paris 2000 the Appellant’s supplier was London Mobile Communications Limited, about which we concluded that the unusual features were not on their own sufficient, but in combination with the unusual features about Paris 2000, we conclude that together they are. We apply Lewison J’s conclusion in this appeal at [99]:

“In the case of a ‘straight’ MTIC fraud it seems to me that a taxable person who is not himself a dishonest co-conspirator will not be deprived of his right to reclaim payment of input tax unless he knew or should have known of a connection between his own transaction and the fraud of the missing trader.”

Here the connection is already found as a fact. That the Appellant should have known of the connection is something that can be inferred on the balance of probabilities from the existence of unusual features in the chain even though the features do not directly demonstrate any connection. While we regard the deals in which URTB and Paris 2000 were the customers (6 chains in all) as near the borderline, we consider that, even though the Appellant did not know the exact probability of fraud in the chain, they ought to have concluded that it was more likely than not that there was fraud by a potentially missing trader in those chains, and it would have been better not to have done the deals.

20. The deals with Polska Telefonía went through in a very short time on the day after the first contact. The first approach by Polska was by fax on 3 April 2006. The

customer form, selling terms and conditions and the two purchase orders (faxed at 1518 and 1519) are all dated 4 April 2006, which is the date of the deals. The inspection request form by the Appellant and the inspection report by Aberdale Logistics Limited are both dated 4 April 2006 although the report was faxed at 1020
5 on 5 April 2006. The shipment instructions to ship to hold (faxed at 1610) and the international consignment note are also dated 4 April 2006. The goods were received in France on 5 April 2006. Polska faxed to the Appellant at 1600 on 4 April 2006 a “goods/service received acceptance note.” The Appellant faxed the invoices to Polska at 1418 (4 pages sent), 1433 (6 pages) and 1612 (2 pages). HMRC confirmed the
10 validity of the VAT registration on 5 April 2006. The price was received on 10 April 2006 and the goods were released on the same day. A strange feature is that Polska faxed at 1517 and 1518 on 4 April 2006 two “Supplier Declarations” saying that they had not entered into a third party payment with their suppliers, and had carried out due diligence with their suppliers, when their supplier was the Appellant. We assume
15 that these should have been customer declarations and should have referred to their customer but the Appellant did not notice. In recording times above we assume that Polish time is one hour ahead of UK time. We consider that the Appellant should have made further enquiries about Polska Telefonica and not completed the deals before receiving the Graydon report. Since we do not know what the further enquiries
20 would have revealed we consider that they ought to have concluded that it was more likely than not that there was fraud by a potentially missing trader in those chains, and it would have been better not to have done the deals.

21. In relation to Navigo.It Spa we consider that the Appellant should have made further enquiries and not completed the deal without having received the Graydon
25 report. But since we know what that report revealed, even if they had received it we consider that they would have been justified in continuing with the deal on the basis that the additional information in the report would not lead to a conclusion that the Appellant ought to have known that the fraud of the importer in the chain was more likely than not, and so the lack of enquiries was not relevant. It is an example of
30 Lewison J’s point in the appeal in this case at [88]:

“In my judgment (as I think Mr Anderson in the end accepted) if a taxable person has not taken every precaution that could reasonably be expected of him, he will still not forfeit his right to deduct input tax in
35 a case where he would not have discovered the connection with fraud even if he had taken those precautions.”

22. We do not consider that the circumstances of Dantec or World Communications would lead to a conclusion that the Appellant ought to have known that the fraud of the importer in the chain was more likely than not.

23. Our revised decision on the straight chains is therefore that we allow the appeal in
40 respect of deals 1561, 1565, 1566, 1568, 1574, 1575 and 1576; and we dismiss it in respect of deals 1558, 1559, 1560, 1567, 1570, 1572, 1573 and 1580. Rather than setting out what we think is the amount of input tax we consider that it is safer to let the parties agree this and only return to us if there is any doubt.

24. In the light of our decision we invite the parties to make representations about costs in principle (without a schedule of costs) within 30 days of the date of release of this decision.

5 25. Both parties have a right to apply for permission to appeal against this decision pursuant to Rule 39 of the Rules. 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.

10 26. As we have indicated in paragraph 7 above this decision is issued in draft pending the Court of Appeal decisions in the three appeals named in that paragraph. Following that decision we direct the parties to indicate to the Tribunal within 30 days whether they wish this appeal to be restored for further hearing or whether they are content for us to finalise our decision.

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JOHN F AVERY JONES

TRIBUNAL JUDGE
RELEASE DATE: 19 January 2010

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