



TC00360

Appeal number: LON/2007/0902

VAT – MTIC fraud – whether trader entitled to recover input tax – whether assessed transaction formed part of transaction chain which was connected with VAT fraud – yes – whether trader knew or should have known assessed transaction was connected with VAT fraud – trader knew of connection – appeal dismissed

FIRST-TIER TRIBUNAL

TAX

QUALITY IMPORT EXPORT LIMITED

Appellant

- and -

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

Respondents

**TRIBUNAL: JUDGE EDWARD SADLER
JOHN ROBINSON**

Sitting in public in London on 5 – 9 October 2009

Ferhad Hamid, a director of the Appellant, representing the Appellant

Miranda Bevan, counsel, instructed by Howes Percival LLP, for the Respondents

© CROWN COPYRIGHT 2010

DECISION

Introduction

5 1. This is an appeal by the company Quality Import Export Limited (“the
Appellant”) against a decision of The Commissioners of Her Majesty’s Revenue and
Customs (“the Commissioners”) to disallow a claim made by the Appellant for the
repayment of input value added tax in the sum of £89,250. The Commissioners
10 notified the Appellant of their decision by their letter to the Appellant dated 19 April
2007.

2. The claim made by the Appellant relates to its entitlement to deduct input tax for
its quarterly VAT accounting period 06/06. The Appellant carried on at that time the
business of trading in mobile telephones. On 30 June 2006 the Appellant purchased
1,250 units of mobile telephone handsets for £510,000 from another UK trader and
15 paid input tax on that purchase of £89,250. Later the same day the Appellant traded
on those handsets units, selling them to an overseas trader for £540,625. That was a
zero-rated transaction for VAT purposes and so, in brief, the Appellant claimed the
repayment of the input tax paid on its purchase of the handsets.

3. The Commissioners contend that the Appellant’s purchase and sale of the
20 handsets entered into by the Appellant on 30 June 2006 were part of a transaction
chain where there are two or more missing or defaulting traders who have evaded
VAT, and that accordingly the Appellant’s transactions on that day were connected
with the fraudulent evasion of VAT. They claim that the fraud is of the type now
widely known as MTIC (“Missing Trader Intra-Community”) fraud. They claim that
25 the Appellant knew that the transactions which it entered into on 30 June 2006 were
connected with the fraud, or alternatively, that the Appellant should have known
(because it had the means of so knowing) that those transactions were connected with
the fraud. They claim, on the authority of European and domestic case law, that this
entitles the Commissioners to refuse to repay the input tax claimed by the Appellant
30 in relation to those transactions.

4. The Appellant does not challenge the Commissioners’ contention that there was
VAT fraud on the part of missing or defaulting traders, or that the VAT fraud
occurred in the course of a chain of transactions which included the Appellant’s
purchase and sale on 30 June 2006. The Appellant does, however, challenge their
35 contention that the Appellant either knew that the transactions it entered into were
connected with the fraud or should have known that to be the case. The Appellant
argues that it took all the necessary precautions which the Commissioners
recommended to check that it was not involved in a chain of transactions which
involved missing or defaulting traders. In its Notice of Appeal to the tribunal the
40 Appellant expressed its grounds of appeal against the decision of the Commissioners
to refuse to repay the relevant input tax in these terms: “[The Appellant] believes it
took steps and followed guidance for this transaction hence it is unreasonable for
HMRC to believe that [the Appellant] knew or suspected that features of this
transaction were a scheme to defraud the revenue.”

5. At the hearing before us the Appellant was represented by Mr Ferhad Hamid, who is the sole director of the Appellant, and its controlling shareholder. Mr Hamid presented the Appellant's case in detail and cogently. It was clear that he had prepared his case very thoroughly and with the benefit of studying decisions in previous MTIC fraud cases. He made detailed written submissions in advance of the hearing, and prepared written closing submissions. He conducted the cross-examination of the Commissioners' witnesses in a careful and thorough manner. All in all Mr Hamid's presentation of the Appellant's case was very commendable and helpful to the tribunal. Miss Miranda Bevan of counsel appeared for the Commissioners. We are grateful to her, too, not just for her lucid and comprehensive presentation of the Commissioners' case, but also for her fair dealings with the Appellant – effectively a litigant in person – so as to ensure that all matters were properly put before the tribunal in the course of the hearing.

6. Despite the advocacy skills of Mr Hamid, it is our decision to dismiss the Appellant's appeal. The weight of the evidence is unquestionably against the Appellant, and it is our finding that the relevant transactions entered into by the Appellant on 30 June 2006 were connected with the fraudulent evasion of VAT; that the Appellant knew this to be the case; and that accordingly, having regard to the relevant case law, the Commissioners are entitled to refuse the Appellant's claim for repayment of input tax in relation to the relevant transactions.

An outline of MTIC fraud

7. MTIC fraud transactions have now been described and examined in a number of tribunal and (on appeal) High Court cases, and it is not required here to describe such transactions in their varying forms. As is now well known, and as we heard in evidence, such fraud has been responsible for enormous losses to the UK Treasury – estimated for the fiscal year 2005-06 to be as much as £4.5 billion. It is helpful, to set the context for this appeal, to describe in outline how such fraud is perpetrated and how traders such as the Appellant can find themselves connected with such fraud. It is also helpful in explaining the terminology which is now applied to such cases and the parties involved.

8. The fraud and transaction chain in the present case is known as a “simple” fraud chain (in contrast to the more complex “contra” fraud chain, with which we are not concerned). The goods traded are of high value and small bulk, typically hi-tech goods, and frequently mobile telephones, as in the present case. They can be traded easily and in large quantities at very high values, and physical delivery (as opposed to the goods being held by an intermediary to the order of a trader) is not necessarily taken by each of the traders in the chain.

9. Trader A (who will perpetrate the fraud) is a UK trader who purchases the goods from a trader located in another EU Member State. Trader A is registered (or appears to be registered) for UK VAT purposes. Trader A is importing the goods into the UK, and pays no VAT at that point. Trader A sells on the goods to Trader B, and charges VAT on that supply of the goods. Trader B is also registered for UK VAT purposes, and is known as a “buffer” trader. Trader A fails to pay to the Commissioners the

VAT it has charged to Trader B and the Commissioners are unable to recover that amount from Trader A, who is now the “defaulting trader” or a “missing trader”. The Commissioners cannot recover because Trader A simply goes missing, or because Trader A has used another trader’s VAT registration number – what one might call
5 VAT identity fraud.

10. Trader B might or might not know of Trader A’s fraud, but in any event sells at a small profit to Trader C, another “buffer” trader, charging VAT on the supply, and, in the normal way, accounting to the Commissioners for the difference between the input tax it paid to Trader A and the output tax charged to Trader C. Trader C then
10 trades on the goods, and there may be a chain of “buffer” traders, each UK VAT registered, and each making a small profit and accounting for VAT in the normal way. In due course the goods are purchased by Trader X (again, UK registered for VAT purposes), who sells them by way of export to an overseas purchaser. Trader X may or may not know of Trader A’s fraud. In MTIC fraud terminology Trader X is known
15 as the “broker” or the “exporter”. As he is exporting the goods, Trader X is not required to charge VAT to his overseas customer, and so in his VAT return claims, by way of repayment, the full amount of his input tax paid, that is to say, the VAT which the “buffer” trader charged to Trader X on that trader’s supply of the goods to Trader X.

20 11. Thus the loss to the Commissioners is the VAT which Trader A, the “defaulting trader”, fails to pay to them, although the loss is manifested when the Commissioners repay to Trader X, the “broker”, the input tax which he is claiming. If the Commissioners can legitimately deny Trader X the right to claim repayment of his input tax, they have repaired the loss from Trader A’s fraudulent default, so that, in
25 the result, Trader X bears that loss. As is described below, the courts have held that the Commissioners cannot shift their loss in this way onto Trader X unless the circumstances are such that Trader X is connected in some way with the fraudulent default and, additionally, either knew of that fraud or should have known of it.

30 12. In the present case, the Appellant is in the position of the “broker” (Trader X), who exported the goods in question and now claims repayment from the Commissioners of the input tax it paid on purchasing the goods from a “buffer” trader.

The legal issues

35 13. This case is principally concerned with matters of fact, and the legal issues – the domestic statutory and Directive rights of the Appellant to claim repayment of input tax and the domestic and European case law applying those rights – were not in dispute between the parties. It is, of course, necessary to set out those issues so that the facts can be related to them in order to reach a decision on the Appellant’s appeal.

40 14. At the European level the right to deduct input tax (and therefore to claim a repayment of input tax when, in a VAT accounting period, input tax exceeds output tax) is found in Articles 167 and 168 of the Council Directive of 28 November 2006

Article 167

5 A right of deduction shall arise at the time the deductible tax becomes chargeable.

Article 168

10 In so far as the goods and services are used for the purposes of the taxed transactions of a taxable person, the taxable person shall be entitled, in the Member State in which he carries out these transactions, to deduct the following from the VAT he is liable to pay:

(a) the VAT due or paid in that Member State in respect of supplies to him of goods or services, carried out or to be carried out by another taxable person....

15 15. These provisions are given effect within the UK by the Value Added Tax Act 1994 (“VATA 1994”) and regulations made under VATA 1994.

20 16. Section 24(1) VATA 1994 provides the definition of “input tax”, which, for the purposes of the present case means “...VAT on the supply to [a taxable person] of any goods or services...being...goods or services used or to be used for the purpose of any business carried on...by him.” Section 24(6) provides for regulations relating to input tax.

17. Section 25(1) VATA 1994 requires a taxable person to account for and pay VAT by reference to VAT accounting periods (quarterly periods in the case of the Appellant), and section 25(2) VATA 1994 then provides:

25 Subject to the provisions of this section, [the taxable person] is entitled at the end of each prescribed accounting period to credit for so much of his input tax as is allowable under section 26, and then to deduct that amount from any output tax that is due from him.

18. Section 26(1) VATA 1994 provides:

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

35 By virtue of section 26(2) VATA 1994, the input tax must, in order to be creditable, be attributable to taxable supplies made by the taxable person in the course or furtherance of his business.

19. The regulations referred to in sections 24 and 26 VATA 1994 are the Value Added Tax Regulations 1995. Regulation 29 specifies that a person claiming a

deduction for input tax shall make a claim for credit for input tax in his VAT return, on the basis of a VAT invoice in the required form provided to him by the supplier of the goods in question.

5 20. Turning back to the Appellant's appeal, there is no dispute between the parties as to the interpretation of these various provisions or, setting aside the fraud/knowledge of fraud issue central to this case, as to their application: the Commissioners accept (subject to that central issue) that the Appellant is a taxable person making taxable supplies in the course or furtherance of his business, that the input tax claimed is attributable to such taxable supplies, and that the input tax claim meets the requirements specified by the applicable regulations.
10

21. The Commissioners, on the authority of a line of cases before the European Court of Justice and the UK national courts, have challenged the right of a taxable person to claim credit for input tax, where that person otherwise satisfies the legislative requirements to claim such credit, but where there is fraud by another person in a related transaction.
15

22. As to the European cases, it is sufficient to refer only to the decision in the joined cases of *Kittel v Belgium* C-439/04 and *Belgian State v Recolta Recycling SPRL* C-440 [2006] ECR I-6161, which sets out the principles which are to be applied by a national court in deciding whether input tax can be claimed as a credit where there has been fraud related in some way to the transactions carried out by the claimant. The following are the key passages of that decision relevant to this appeal:
20

25 "51 ...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)...

30 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....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....

35 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 [VAT] Directive, be regarded as a participant in that fraud, irrespective of whether or not he profited by the resale of the goods.

40 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....

5 61 ...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.”

23. In the domestic courts the application of the *Kittel* decision has been the subject of a number of cases. In the High Court cases of *The Commissioners for Her Majesty's Revenue and Customs v Livewire Telecom Limited*; *The Commissioners for Her Majesty's Revenue and Customs v Olympia Technology Limited* [2009] EWHC 15 (Ch) there is an extensive review of the European and domestic cases on MTIC fraud cases by Lewison J. His summary of the current state of the jurisprudence of the European Court of Justice (at paragraph [76]) includes the following principles:

- 15 (1) It is disproportionate and contrary to Community law to require a person who is a careful and honest trader to assume liability for the frauds of others;
- (2) It is also disproportionate to hold a taxable person liable for fraudulent acts of third parties over whom he has no influence;
- 20 (3) A trader who does take every precaution that could reasonably be required of him, and does not realise that he is participating in VAT fraud, must be entitled to rely on the legality of his own transaction;
- (4) A person who knew or should have known that by his purchase he was taking part in a transaction connected with the fraudulent evasion of VAT is to be treated in the same way as a person who fraudulently exercises the right to deduct;
- 25 (5) It is not contrary to Community law to require a supplier to take every step that could reasonably be required of him to satisfy himself that the transaction which he is effecting does not result in his participation in tax evasion;
- 30 (6) Likewise a taxable person can be expected to act with all due diligence and care; and
- (7) Whether a taxable person knew or should have known that he was participating in a transaction connected with the fraudulent evasion of VAT must be determined having regard to objective facts or factors.
- 35

24. If the input tax credit is to be refused to the trader there must be a fraudulent evasion of VAT and the trader's transaction must be connected with that fraud. It has been held that if the trader's purchase and sale of the goods in question form part of a chain of transactions in the course of which VAT was fraudulently evaded, then the trader's transaction is connected with the fraud, since the trader aids the perpetrators of the fraud by supplying liquidity into the supply chain. It is not necessary that there should be privity of contract between the perpetrator of the fraud and the trader:

40

Calltel Telecom Limited v The Commissioners for Her Majesty's Revenue and Customs [2009] EWHC 1081 (Ch). Thus, in MTIC terminology, if goods are traded by the defaulting or missing trader and thence by one or more buffer traders before reaching the broker trader, the broker trader's purchase of the goods will be connected with the fraud perpetrated by the defaulting or missing trader.

25. As to the question whether the trader should have known of the connection between his transactions and the fraud, it is clear from the *Livewire Telecom* decision that the test is an objective one (what it is reasonable to expect a competent trader taking part in those kinds of transactions to have known), not a subjective one (what it is reasonable to expect the actual trader himself to have known) (see paragraphs [120] to [125]). In that case the objective test as to constructive knowledge is viewed from the slightly different perspective of what precautions (in terms of enquiries and other due diligence) the trader should be expected to take in order to reach a conclusion as to whether or not his transactions are connected with the fraud, and it was decided that "the test does not require the taxable person to take every possible precaution: merely every precaution reasonably required" (at paragraph [123]) (applying the test in the *Kittel* case, at paragraph [51] of the decision in that case). Further, if the trader in fact fails to take every precaution reasonably required to ascertain whether his transactions are connected with the fraud, but, had he taken every such precaution, he would not have discovered the connection, he is not to be taken as having constructive knowledge of the fraud.

26. On the question of taking "every precaution reasonably required" to determine whether or not a trader should have known of the fraud in the chain, it has been held that a trader cannot simply rely on "unsuspicious" results from standard due diligence checks made on his supplier if there are indications apparent from the nature of the trading transactions he has entered into which should arouse his suspicions. In the case of *Mobilx Limited (In Administration) v The Commissioners for Her Majesty's Revenue and Customs* [2009] EWHC 133 Ch Floyd J accepted that a trader cannot be expected to make enquiries beyond his immediate supplier (who, as a matter of commercial confidentiality, is unlikely to reveal to the trader details of his (the supplier's) own supplier and supply contract terms). However, a due diligence enquiry of the immediate supplier may not be the extent of the precautions which a trader is reasonably required to take if he is to show that he should not have known of the fraud. He said this (at paragraph [7]):

"Suspicious indications obtained by a trader from carrying out due diligence checks on its supplier are one, but not the only basis from which it may properly be inferred that a trader knew or should have known of its implication in VAT fraud. The test to be applied is that set out in paragraph 61 of the [*Kittel*] Judgment, and indeed in the Court's final determination at the end of the judgment. Paragraph 51 needs to be understood in the sense that "all reasonable precautions" may, in some cases, involve ceasing to trade in specified goods in a particular market, at least in the particular manner in which the trader undertakes that trade. Such a situation may conceivably arise where, from other indications available to the trader, the trader knew or should have known that it is more likely than not that, despite all due diligence

checking, any further goods traded in the same way will be implicated in VAT fraud.”

27. It is also the case, perhaps self-evidently, that the question as to the knowledge or constructive knowledge of the trader as to the connection to the fraud must be asked at the time he enters into the transactions giving rise to the input tax credit claim: at the time he entered into those transactions did he know of the connection to the fraud or should he have known of it.

28. In summary, therefore, if the trader is to be denied his right to claim input tax: there must be a fraud (such as the fraudulent evasion of VAT); there must be a connection between the trader’s own transactions and the fraud (as is the case if goods are traded in a chain of transactions incorporating the transaction giving rise to the fraud and the trader’s transactions); the trader, at the time he entered into the relevant transactions, either must have known of that connection or should have known of that connection; in determining whether the trader should have known of that connection, the test is objective – what the competent trader ought reasonably to have known; and in applying that test it is required that the trader takes every precaution reasonably required, which may extend beyond relying only on due diligence enquiries of his immediate supplier.

The burden of proof and standard of proof

29. It is clear, and was accepted by the Commissioners in this appeal, that it is for the Commissioners to prove that there has been a fraudulent evasion of VAT and that there is a connection between the Appellant’s transactions for which it is claiming the input tax credit and the fraud.

30. As to the question of where the burden lies in establishing whether the Appellant knew or should have known, of the fraud, the Commissioners referred to the tribunal’s decision on the point in the case of *Calltel Telecom Limited v The Commissioners for Her Majesty’s Revenue and Customs* [2007] UK VAT 20266, at paragraph [71]:

“...we think that it is incumbent on the Commissioners to raise a case, not necessarily amounting to proof but sufficient to demand an answer, that there were facts or circumstances which support, or at least are consistent with, the conclusion that the appellant knew, or should have known, of fraud in the chain....But if the Commissioners are able to mount a case which demands some explanation, the burden shifts to the appellant to show that he took the precautions which could reasonably have been required of him and that, despite his having done so, he did not know, and could not have known, of the fraudulent purpose of others.”

31. Subsequent tribunal cases have adopted this approach with regard to the burden of proof on the knowledge and constructive knowledge issues. It seems a fair approach in dealing with what otherwise is the difficulty for the appellant of proving a negative. Miss Bevan proposed this approach for the purposes of this appeal, although she drew

our attention to conflicting dicta on the point in recent High Court decisions. As will appear, in this case the nature and extent of the evidence presented by the Commissioners was such that we were able to conclude that the Appellant must have known that the transactions it entered into were connected with fraud, so that the question as to where exactly the burden of proof lies on this matter was not an issue.

32. The standard of proof, both with regard to the proof that fraud occurred and with regard to proof of the remaining issues we have to decide (the connection of the Appellant's transactions to the fraud; the knowledge or constructive knowledge which the Appellant has of the fraud) is the normal standard for civil cases, namely that the fact in contention more probably occurred than not.

The evidence before us

33. We had in evidence before us, on behalf of the Commissioners, witness statements from five officers of the Commissioners; and on behalf of the Appellant we had two witness statements from Mr Hamid. Each witness statement was supported by a substantial number of exhibits, and in total there were four trial bundles, each a lever arch file.

34. The principal witness for the Commissioners was Mr Lee David Nevin, an officer of the Commissioners in their team dedicated to MTIC fraud cases. He had taken control of the Appellant's case following the retirement of the officer whose decision is the subject of the Appellant's appeal. His evidence was principally based on his examination of the papers in the case and his verification of the investigations, actions and decisions of his retired predecessor. Mr Nevin had prepared four witness statements, and he gave extensive oral evidence at the hearing and was cross-examined by Mr Hamid. Mr Nevin's evidence related to the Appellant's business; the trading transactions entered into by the Appellant; the VAT fraud perpetrated by one or more parties in chains of transactions which included transactions entered into by the Appellant; the Appellant's awareness of MTIC fraud and the due diligence it carried out with regard to its suppliers and other matters relating to the Appellant's knowledge or constructive knowledge of fraud in the chains of transactions; and the Appellant's banking arrangements.

35. The Commissioners' second witness was Mr Terence Mendes, a Higher Officer of the Commissioners who gives technical advice to his colleagues involved with MTIC fraud cases with particular regard to data obtained from the First Curaçao International Bank ("FCIB"). Mr Mendes had prepared a witness statement and also gave oral evidence at the hearing, and was cross-examined by Mr Hamid. Mr Mendes's evidence related to the banking arrangements of the Appellant with FCIB; the bank accounts held with FCIB by other parties in the chain of transactions which included the transactions entered into by the Appellant; and the movement of funds between FCIB accounts held by those parties and the Appellant.

36. We had the benefit of two witness statements prepared by Mr Roderick Guy Stone, an officer of the Commissioners whose principal duties are to provide technical oversight and co-ordination in relation to MTIC compliance and enforcement

activities. Mr Stone's witness statement was not objected to, and he did not give oral evidence at the hearing. His evidence related to the nature and extent of MTIC fraud; the policies adopted by the Commissioners to combat such fraud (with particular reference to traders in mobile telephones and the "grey market" in such goods); the
5 offshore banking arrangements used by traders; and the internet websites used by traders to seek out or offer trading deals in mobile telephones. His evidence was about such matters in general, industry-wide, terms, and did not relate specifically to the Appellant or the chain of transactions with which it was related.

37. We also had witness statements from two further officers of the Commissioners,
10 Miss Sarah Jane Allen and Mr William James Baker, both of whom had been involved with the VAT affairs of the Appellant. The Appellant made no objection to their witness statements. Miss Allen's evidence related to compliance visits made by her to the Appellant prior to the June 2006 transactions with which this case is concerned, and her issue to the Appellant of various VAT Notices relating to MTIC
15 fraud and the precautions a trader should take to protect his right to recover input tax. Mr Baker's evidence related to his scrutiny of an input tax credit claim made by the Appellant in the period to 31 December 2005 in connection with a certain transaction by way of the zero-rated export of mobile telephones and the subsequent repayment of tax by way of acceptance of that claim for credit. Mr Baker's evidence also related
20 to a subsequent visit to the Appellant where he discussed with Mr Hamid the due diligence checks he should carry out on suppliers and the terms of the VAT Notices on MTIC fraud in this regard.

38. For the Appellant Mr Hamid served two witness statements. He also gave oral evidence at the hearing and was cross-examined by Miss Bevan. His evidence related
25 to the setting up and conduct of the business of the Appellant; the checks made by the Appellant on its suppliers; the purchase and sale transactions entered into by the Appellant on 30 June 2006 giving rise to the disputed input tax credit claim and the due diligence carried out with respect to the supplier of the mobile telephones in question; the enquiries made of the freight forwarders holding the goods; and the
30 specification of the goods.

The findings of fact

39. The Appellant was incorporated in June 2000. It was registered for VAT purposes with effect from 1 December 2002, but did not begin trading until its VAT quarterly
35 accounting period 09/04. Its principal place of business is at 48 The Broadway, Tolworth, Surrey. Since June 2005 the Appellant's trade category for VAT purposes has been "telecommunications". The Appellant makes quarterly VAT returns.

40. Mr Ferhad Hamid has been the sole director, and his wife, Mrs Mahrukh Hamid, has been the company secretary, of the Appellant since September 2002. There have been no employees, and at all times the Appellant's business has been controlled and
40 run solely by Mr Hamid.

41. Prior to setting up the Appellant Mr Hamid worked as an IT consultant with a number of major investment banks in London. In the period March 2003 to August

2004 he worked at learning the business of trading in high-value products and establishing contacts with potential suppliers and customers. The Appellant's first significant trading transaction was the purchase of mobile telephones and their export sale to a customer in Dubai.

5 42. In addition to a wholesale trading business, the Appellant operated, from the same premises, a retail mobile telephone business.

43. According to the Appellant's quarterly VAT returns, the turnover of the Appellant's business grew very substantially over the period from September 2004 to the end of June 2006, and then rapidly declined, as follows:

10	VAT period	Net turnover (£)
	09/04	3,997
	12/04	78,986
	03/05	250,000
	06/05	1,168,560
15	09/05	9,671,290
	12/05	5,399,025
	03/06	56,936,128
	06/06	44,470,759
	09/06	7,915
20	12/06	8,677
	03/07	9,110

44. The transaction with which this appeal is concerned took place on 30 June 2006, and following the Commissioners' enquiries and refusal to repay input tax claimed by the Appellant, the Appellant ceased to trade in the mobile telephone market, so that
25 the turnover for the quarter 09/06 and subsequent quarters reflected the retail business carried on by the Appellant.

45. The Appellant's VAT return for the quarter 06/06 showed output tax on sales made totalling £7,689,234.76 and input tax on purchases totalling £7,765,294.08, thus giving rise to a net repayment due of £76,059.32. The Commissioners carried out an
30 extended verification exercise on the transactions entered into by the Appellant in that quarter as a result of which they identified one transaction where they contended that the Appellant had acted as a broker trader and in relation to that transaction the Appellant had input tax of £89,250.

46. On 19 April 2007 the Commissioners wrote to the Appellant denying it the right to deduct input tax of £89,250 claimed in respect of the transaction in question on the grounds that the transaction formed part of an overall scheme to defraud the revenue and that the Appellant knew or should have known this to be the case in that it deliberately or recklessly ignored factors which indicated that the transaction may have formed part of such an overall scheme. The letter states that the transaction can be traced back to three missing traders in the deal chain, and sets out ten other factors which comprise the grounds for denying the input tax credit. The letter identifies the transaction as follows: Purchase Order No 0303 dated 30 June 2006; Purchase Invoice No 3006-05 dated 30 June 2006; Supplier: Dualite Limited; Net amount: £510,000.

47. In the period covered by the 06/06 VAT return (1 April 2006 to 30 June 2006) the Appellant carried out fifty-five trading transactions by way of wholesale deals in mobile telephones. The Commissioners carried out investigations into each of those trading transactions, including the supply chain leading to them and subsequent transactions in the chain, working back from the invoice numbers supplied by the Appellant and information obtained from enquiries made of other traders. In relation to those fifty-five trading transactions:

(1) Seventeen of the transactions have the same supply chain to the Appellant, with a company known as C & B Trading supplying the goods to a company known as V2 UK Ltd which in turn supplies the goods to the Appellant;

(2) Twenty-three of the transactions have the same supply chain to the Appellant with a company known as RS Sales supplying the goods to a company known as Highbeam which in turn supplies the goods to the Appellant;

(3) In the supply chain for each of the fifty-five transactions (except, possibly, one) the number of mobile telephones traded remains the same throughout each deal in the supply chain, with no splitting of stock or stock brought in from suppliers outside the deal chain;

(4) In each case all the transactions in each supply chain and also the Appellant's transactions were entered into on the same date – in each deal chain they were “back-to-back” transactions;

(5) In thirty-eight of the transactions the Appellant made a profit of £0.50 per mobile telephone traded; in fourteen a profit of £0.25; in two a profit of £1.00; and in one transaction a profit of £24.50 per mobile telephone traded;

(6) In fifty-four of the fifty-five transactions the originating party in the deal chain is a defaulting or missing trader, that is, a trader owing VAT to the Commissioners who is either insolvent or who cannot be traced by the Commissioners;

(7) In fifty-four of the fifty-five transactions (those where the Appellant made a profit of £0.25, £0.50, or £1.00 profit per unit) the Appellant sold the mobile telephones to a trader registered for UK VAT purposes,

charging VAT on that supply in the normal way. In one transaction (that where the Appellant made a profit of £24.50) the Appellant sold the mobile telephones by way of export to a non-UK trader, as a zero-rated transaction. It is this transaction which is the subject of the Appellant's claim for repayment of input tax. On the same day as this transaction (30 June 2006) the Appellant sold a similar quantity of the same model of mobile telephone to a UK trader at a profit of £0.50 per unit;

(8) In the fifty-four transactions where the Appellant sold the mobile telephones to a UK trader (and where the Appellant's profit per unit was £1.00 or less), in subsequent transactions in the chain the mobile telephones were eventually sold by a broker trader by way of export at a substantially greater profit: for example:

(a) on 24 April 2006 C & B Trading Ltd (which subsequently proved to be a missing trader) sold 4,000 units of Nokia N9500 series mobile telephones to V2 UK Ltd at a price per unit of £298.25, which in turn sold the mobile telephones to the Appellant at a price per unit of £298.50, which in turn sold them to Adworks UK at a price per unit of £298.75, which in turn sold them to David Jacobs for £299, which in turn sold them to Cellular Solutions (T Wells) Ltd for £300, which in turn sold them to an overseas customer, Globalfone Communications, at a price per unit of £327;

(b) also on 24 April 2006 Midwest Communications Ltd (which subsequently proved to be a missing trader) sold 2,000 units of Nokia N7380 series mobile telephones to I H Technologies at a price per unit of £250.10, which in turn sold them to H Players (UK) Limited at a price per unit of £250.25, which in turn sold them to Xcel Solutions for £250.50, which in turn sold them to the Appellant for £251.00, which in turn sold them to Ixes UK Ltd for £251.50, which in turn sold them to an overseas customer, France Affaires Int SARL, at a price per unit of £271.60.

(9) In none of the chains of transactions were the Commissioners able to trace the supply of the goods back to a manufacturer, nor could they, in the transactions subsequent to the Appellant's sale of the goods, trace them to a retailer or end-user: thus all the transactions in the chains were in the so-called "grey market" in mobile telephones, that is, wholesale dealer to wholesale dealer transactions.

(10) Of the fifty-five transactions entered into by the Appellant in the VAT quarter ended 30 June 2006, fourteen were entered into during the two days of trading 29 and 30 June 2006, the Appellant selling mobile telephones in those two days to a value of £12,561,250.

48. In the period covered by the 03/06 VAT return (1 January 2006 to 31 March 2006) the Appellant carried out seventy-five trading transactions by way of wholesale deals in mobile telephones. The Commissioners carried out investigations into those

trading transactions and the supply chain leading to them, working back from the invoice numbers supplied by the Appellant and information obtained from enquiries made of other traders. In relation to those seventy-five trading transactions:

5 (1) In sixty-nine of the transactions the originating party in the deal chain is a defaulting or missing trader, that is, a trader owing VAT to the Commissioners who is either insolvent or who cannot be traced by the Commissioners (the Commissioners were not able to trace the remaining seven chains of transactions). Five defaulting or missing traders are the originating traders for fifty-nine of the sixty-nine chains;

10 (2) The Appellant sold the mobile telephones to a number of different UK VAT registered traders at a profit per unit ranging from £0.25 to £1.00, charging VAT on the sales in the normal way, and setting his input tax paid on purchase against the output tax charged on such sales.

15 49. On 30 June 2006 the Appellant entered into the transactions for which he claims repayment of input tax, and to which this appeal relates. The following facts are established from the evidence of the Commissioners in relation to this chain of transactions (“Deal Chain 51”):

20 (1) On 30 June 2006 Heathrow Business Solutions Ltd sold 1,250 units of Nokia N8800 Black series sim card free mobile telephones to The Wireless Warehouse Ltd at a price per unit (excluding VAT) of £407.25 (total price: £509,062.50). Heathrow Business Solutions Ltd was at that time registered for VAT, and charged VAT of £89,085.94 on the sale. Heathrow Business Solutions Ltd proved to be a missing trader (see paragraph [50] below);

25 (2) Also on 30 June 2006 The Wireless Warehouse Ltd sold those 1,250 units to Exclusive Communications Ltd trading as Phone2Phone at a price per unit (excluding VAT) of £407.50 (total price: £509,375). The Wireless Warehouse Ltd was registered for VAT, and charged VAT of £89,140.63 on the sale;

30 (3) Also on 30 June 2006 Exclusive Communications Ltd sold those 1,250 units to Dualite Limited at a price per unit (excluding VAT) of £407.75 (total price: £509,687.50). Exclusive Communications Ltd was registered for VAT, and charged VAT of £89,195.31 on the sale;

35 (4) Also on 30 June 2006 Dualite Limited sold those 1,250 units to the Appellant at a price per unit (excluding VAT) of £408.00 (total price: £510,000). Dualite was registered for VAT, and charged VAT of £89,250 on the sale (this is the VAT for which the Appellant claims repayment in this appeal);

40 (5) Also on 30 June 2006 the Appellant sold those 1,250 units to Silacom Handels & Vermittlungs GmbH (“Silacom”) at a price per unit of £432.50 (total price: £540,625). Silacom’s address is Maximilianstrasse 2/C4, A-6020 Innsbruck, Austria. The sale by the Appellant was by way of zero-rated export, and no VAT was charged by the Appellant on the sale;

5 (6) The Appellant's invoice to Silacom in relation to the sale is numbered 000308 and is dated 30 June 2006. It shows Silacom as the "Customer", with address, telephone and fax number, and itemises the goods, describing them as "New Simfree never locked euro spec original packaging". It also states: "Goods are at TLS" [(TLS are freight forwarders)]. The invoice provides details of the Appellant's sterling bank account with FCIB. The invoice states the following to be the terms of sale: "1 Customers responsibility to carry out 100% inspection of these goods before purchase; 2 Full payment on receipt of invoice; 3 Goods remain property of Quality Import Export Ltd until payment received in full";

15 (7) The Nokia N8800 Black mobile telephones traded in these transactions were of central European specification. The handsets were capable of being used in the UK (and they had an English language facility alongside other European language facilities), but the battery charger included in the package with each handset was of a two plug, Continental European, design so that it could not be used in the UK without the appropriate plug adapter;

20 (8) The Appellant received payment from Silacom for the mobile telephones on 12 July 2006, on which date it paid the amount due for the mobile telephones to Dualite Limited. On that date Dualite Limited in turn paid Exclusive Communications Ltd, which in turn paid The Wireless Warehouse Ltd. All the relevant companies held bank accounts with FCIB, and payment was effected by transfers between those respective accounts;

25 (9) The Nokia N8800 Black mobile telephones traded in these transactions would have had International Mobile Equipment ("IMEI") numbers. The Appellant had no record of those numbers;

30 (10) The Appellant had no insurance cover for loss or damage in relation to the mobile telephones traded, but relied on the insurance cover maintained by the freight forwarders who had physical possession of the goods. There is no evidence that the Appellant saw the terms of any such insurance cover;

35 (11) At the time the Nokia N8800 Black mobile telephones traded in these transactions were purchased by the Appellant they were held by freight forwarders, Total Logistic Solution, to the order of Dualite Ltd. The freight forwarder gave the Appellant verbal assurance that it held the goods. At some point prior to 5 July 2006 Dualite Ltd directed the freight forwarder to allocate the mobile telephones to the Appellant. No cost of storage was paid by the Appellant;

40 (12) On 3 July 2006 the Appellant instructed Total Logistic Solution to ship the Nokia N8800 Black mobile telephones to the warehouse of a French company, A.F.I. Logistique SARL, at Charles de Gaulle Airport, Roissy, France. They were transferred on a "ship and hold" basis and on 5

July 2006 A.F.I. Logistique issued an inspection report to Silacom specifying the goods held, and identifying the “shipper” as the Appellant.

50. With regard to Heathrow Business Solutions Ltd:

5 (1) The company was registered for VAT purposes with effect from 14 October 2004, giving its business address as 72 New Bond Street London W1. In November 2005 it changed its principal place of business to 1 Martindale Road Hounslow TW4 7EW;

10 (2) Information filed at the Companies Registry shows Akbar Ali to be the director of the company and Yasar Ahmed to be the secretary of the company;

(3) The company rendered VAT returns for quarterly periods from 12/04 to 03/06. All those returns were made as nil returns on the basis that the company had not traded. No return was made for the quarter 06/06;

15 (4) A visit on 30 June 2006 by officers of the Commissioners to the Hounslow premises revealed, upon their enquiry of the landlord of the premises, that the company had never occupied the premises. Subsequent investigations revealed that the company had never occupied the New Bond Street premises;

20 (5) Subsequently the Commissioners deregistered the company for VAT purposes with effect from 30 June 2006;

25 (6) Subsequent investigations by the Commissioners in respect of other traders who had traded with the company revealed that the company had traded in mobile telephones on a substantial scale during the period up to and including 30 June 2006. As a result of these investigations the Commissioners assessed the company to VAT by a series of assessments totalling £30,637,891 in relation to undeclared sales of mobile telephones. Included in these assessments was an assessment dated 5 February 2007 for £196,665 in relation to sales made by the company to The Wireless Warehouse Limited which included the sum of £89,085.94 in relation to
30 the VAT charged by the company to The Wireless Warehouse Limited on the sale of 1,250 units of Nokia N8800 Black series mobile telephones in Deal Chain 51;

35 (7) Apart from the nil VAT returns made by the company the Commissioners have received no communication or documentation from the company or its directors, and have been unable to trace the company and its directors. The amount of VAT assessed on the company has not been paid and the company has not appealed against or otherwise challenged the assessments in question;

40 (8) An insolvent winding up order was made against the company on 10 January 2007; and

(9) On 12 July 2006 The Wireless Warehouse Ltd paid to an account in the name of Yasar Ahmed the sum of £598,148.43 (the amount due to Heathrow Business Solutions Ltd – including VAT – as specified in the

invoice issued by the company to The Wireless Warehouse Ltd on 30 June 2006 in relation to the sale of 1,250 units of Nokia N8800 Black series mobile telephones in Deal Chain 51).

51. With regard to The Wireless Warehouse Ltd:

5 (1) The company was registered for VAT purposes as at 30 June 2006 and made a VAT return for the period 06/06;

(2) No VAT has been paid in relation to that VAT return, and the sum of £1,754,700 is due to the Commissioners arising from unpaid VAT from returns made by the company and other assessments made by the
10 Commissioners following investigations by them;

(3) On 24 November 2006 the Commissioners visited the address given by the company as its principal place of business, but the company was no longer in occupation. The Commissioners have had no contact with the company since before that date.

15 52. With regard to Dualite Limited:

(1) The company was registered for VAT purposes as at 30 June 2006;

(2) The company failed to make a VAT return for the quarter 06/06;

(3) Following investigations by the Commissioners, the Commissioners have made assessments on the company in relation to sales made by the
20 company totalling £2,359,670;

(4) On 8 November 2006 the Commissioners visited the address given by the company as its principal place of business. The company was not then occupying the premises. The landlord of the premises informed the
25 Commissioners that notice given by the company to terminate the lease of the premises had expired on 31 October 2006. The Commissioners have had no contact with the company since before that date.

53. With regard to Silacom:

(1) The company was registered as established in Innsbruck, Austria in June 2002;

30 (2) As at 30 June 2006 the company was registered for VAT purposes in Austria;

(3) As at 30 June 2006 the company held a pounds sterling bank account with FCIB.

54. From the records and data available from FCIB:

35 (1) All the companies involved in Deal Chain 51 (except Heathrow Business Solutions Ltd) respectively held a pounds sterling account with FCIB;

(2) On 12 July 2006 transfers were made between these respective accounts by way of payment for the 1,250 units of Nokia N8800 Black series mobile telephones traded in Deal Chain 51;

5 (3) The Wireless Warehouse Ltd, instead of paying Heathrow Business Solutions Ltd, transferred £598,148.43 (the amount due, including VAT, on its purchase of the 1,250 units of Nokia N8800 Black series mobile telephones from Heathrow Business Solutions Ltd) from its account to the pounds sterling account held by Yasar Ahmed with FCIB;

10 (4) On 12 July 2006 there were the following additional transfers between accounts with FCIB:

(a) Yasar Ahmed paid to a company based in Islamabad, Pakistan, Maks Information Technology, £595,431.25;

(b) Maks Information Technology paid to a company based in Dubai, Marxmann International FZCO, £542,500.00;

15 (c) Marxmann International FZCO paid to a company based in the Czech Republic, Kima Estates SRO, £542,500.00; and

20 (d) Kima Estates SRO paid to Silacom £541,562.50 (thereby putting Silacom's account in funds to enable it to transfer the sum of £540,625 owed to the Appellant for the purchase of the 1,250 units of Nokia N8800 Black series mobile telephones traded by the Appellant to Silacom in Deal Chain 51).

25 (5) In summary, therefore, (and subject only to the substitution of Yasar Ahmed for Heathrow Business Solutions Ltd – and Mr Ahmed was the company secretary of that company) on 12 July 2006, and in relation to the transactions in Deal Chain 51, funds moved in a circle (through respective accounts held with FCIB) commencing with a payment of £542,500.00 by Maks Information Technology to Marxmann International FZCO and ending with Maks Information Technology receiving £595,431.25. In cash terms, each party involved made a modest mark-up profit of less than
30 £1,000, except for Maks Information Technology, which made a profit of £52,931.25, and except for the Appellant, which (disregarding its entitlement to recover input VAT on the Deal Chain 51 transaction) made a loss of £58,625.

35 55. On 11 July 2006 the Appellant received in its account held with FCIB the sum of £90,000, expressed in the account narrative to be a “deposit”. That sum was transferred from an account held with FCIB by Medius Trading AG. In relation to Medius Trading AG:

40 (1) The company was registered in Zurich on 23 September 2005 (its statutes being dated 20 September 2005) with its principal place of business at Dufourstrasse 32, CH-8008, Zurich, Switzerland;

(2) The company's director and principal shareholder is Zia Khan who, in relation to the opening of the company's account with FCIB in January 2006, gave his address as being in London. In later documentation

published by the company the managing director is stated to be Daniel Hassan;

(3) The company's statutes state that "the purpose of the company is the sales abroad of individual IT components or entire systems";

5 (4) The Appellant issued "Proforma Invoice No 000298" to Medius Trading AG dated 11 July 2006 for the sale of 2,750 "Nokia 8800 new simfree never locked original packaging no logos" units at a price per unit of £327.50 (total purchase price £900,625.00). The Appellant contends that the sum of £90,000 transferred by Medius Trading AG to the account
10 of the Appellant on 11 July 2006 was by way of deposit or part payment for the goods invoiced by this document;

(5) On 3 August 2006 Mr Hamid, on behalf of the Appellant, wrote to Mr Daniel Hassan in these terms:

15 "In regards to the earlier enquiry we confirm that the specified goods have not been shipped out to Medius Trading AG.

We confirm at this stage the monies paid by Medius Trading AG to Quality Import Export Ltd as deposit PO 181 (Medius Trading AG) are still held in the FCIB account sent to. QIE Ltd has had their account in FCIB suspended so there is no access to any funds currently.

20 Regrettably at this stage we cannot give any more information, however, in case of any news we will be contacting you promptly."

(6) The Appellant has not yet delivered any goods to Medius Trading AG. Medius Trading AG has not pressed for performance of the contract nor for repayment of the sum of £90,000;

25 (7) Following the payment by the Appellant of £599,250.00 due to Dualite Ltd on 12 July 2006 the credit balance in the Appellant's account with FCIB stood at £34,109.34;

30 (8) On 29 June 2006 the Appellant issued "Invoice No 000298" to a customer Ancillary Engineering Services Ltd in relation to the sale of 4,500 Nokia N80 mobile telephone units.

56. The Appellant made successful VAT repayment claims for two VAT accounting periods prior to the 06/06 period:

35 (1) For the 12/04 period the Appellant submitted a VAT repayment claim for £8,207.31. This claim related to four zero-rated export transactions where mobile telephones had been sold to a company, New Life Trading, based in Dubai. The Appellant had purchased the mobile telephones from UK traders (the principal supplier was a Tesco supermarket). These transactions were scrutinised by the Commissioners, and the repayment was made.

40 (2) For the 12/05 period the Appellant submitted a VAT repayment claim for £7,197.80. This claim was investigated by the Commissioners (but not

5 by way of extended verification investigation), who were eventually satisfied that the Appellant was entitled to a repayment of £8,300.24, and a repayment of that amount was made. This claim related to one zero-rated export transaction on 16 November 2005 where 300 units of mobile telephones were sold to a company, Bespoke International General Trading LLC, based in Dubai. The Appellant had purchased the mobile telephones from UK traders. The Appellant's profit on the transaction was £17.50 per unit.

10 57. Each of these repayment claims prompted visits to the Appellant by the Commissioners. Miss Allen, an officer of the Commissioners working as a member of the Special Compliance MTIC Fraud Team, visited the Appellant in February 2005 and again in July 2005. The purpose of these visits was to investigate the entitlement of the Appellant to the repayment claim made for the 12/04 period, to check on the business activities of the Appellant, to obtain current information about the suppliers and customers with which the Appellant was trading, and to remind the Appellant about the Commissioners' requirements for checks on traders in the mobile telephone and computer chip wholesale trading businesses. At the July 2005 visit Miss Allen gave the Appellant a copy of the Commissioners' Notice 726 "Joint and Several Liability in the Supply of Specified Goods"; Notice 700/52 "Notice of requirement to give security to Customs and Excise", and the Commissioners' Statement of Practice on the invalid invoice measure. These documents give advice about the prevalence of MTIC fraud, the precautions which can be taken by traders, and the action which the Commissioners might take if fraud is present. In the course of her visit in July 2005 Miss Allen (together with a colleague) also conducted an interview with Mr Hamid based on a standard *aide-memoire* used as guidance by officers of the Commissioners visiting traders in business sectors where MTIC fraud is prevalent. The interview extended to 213 questions, covering the business of the Appellant, the way it conducts its trading transactions, the checks made on stock traded, the checks made on suppliers and customers, and details of specific suppliers. In the course of that interview Mr Hamid mentioned the following:

(1) The Appellant's trading transactions are self-financing, in that a supplier is not paid until the Appellant has received payment from its customer. Goods are held by a freight forwarder and are released against payment;

35 (2) The Appellant primarily uses the International Phone Traders website to seek both suppliers and customers. Established contacts are telephoned regularly to check the availability of supplies and prices. Suppliers and customers are rarely met in person;

40 (3) The Appellant's checks on suppliers and customers comprise a check on how long they have used the IPT website; verification of their VAT registration with the Commissioners; search of the Companies Registry. In addition, suppliers are asked to sign a declaration confirming that they own the goods;

45 (4) The Appellant provides the Commissioners with a monthly "deal log" (this was a process put in place following Miss Allen's visit to the

Appellant in February 2005: subsequent investigations by Miss Allen revealed that these logs were not always comprehensive in recording all deals undertaken by the Appellant);

5 (5) The Appellant does not make “third party payments” (that is, make payment for goods to a person other than the supplier of the goods);

(6) The Appellant’s terms of business are those set out in its invoices and any purchase orders it issues – there are no further sale and purchase contractual terms;

10 (7) The Appellant’s usual mark-up on a trade is £1 per unit: the Appellant would not expect the price of traded goods to increase at each transaction in a chain over the course of the same day;

15 (8) The Appellant uses the facilities of a freight forwarder, but pays no administration or storage costs. The only insurance cover is that taken out by the freight forwarder, and the Appellant takes out no insurance cover; and

20 (9) The Appellant does not inspect goods purchased and sold, but may request the freight forwarder to make a sample inspection and confirm verbally that the stock appears to be as specified by the supplier. The Appellant does not record the IMEI numbers of mobile telephones purchased and sold (at the interview Mr Hamid was advised that it might be useful to record IMEI numbers as a precaution against trading in mobile telephones which have circulated in “carousel” transactions).

25 58. Mr William Baker, an officer of the Commissioners working as a member of the Special Compliance MTIC Fraud Team visited the Appellant on 6 February 2006. The principal purpose of the visit was to validate the documentation and figures in relation to the VAT repayment claim made for the 12/05 period. On the occasion of that visit Mr Baker reminded the Appellant of the suggested checks for traders operating in the wholesale mobile telephone and computer chip trading businesses, referring the Appellant to Notices 726 and 700/52 and the Statement of Practice on 30 the invalid invoice measure. On that occasion Mr Hamid showed Mr Baker an example of the Introduction Pack giving prospective suppliers and customers details about the Appellant and also an example of the due diligence procedures used by the Appellant to check suppliers and customers.

35 59. The Appellant carried out the following due diligence upon Dualite Ltd, its supplier in Deal Chain 51:

(1) On 25 April 2006 the Appellant called the Commissioners’ National Enquiry Helpline to verify the VAT registration number of Dualite Ltd;

40 (2) The Appellant instructed an agency, The Security People, to compile a due diligence report on Dualite Ltd. The report is dated 14 March 2006, and is stated to have been completed with the assistance of Mr Danny Brown, a director of Dualite Ltd. (According to Mr Hamid, the Appellant requested the report some time in May 2006 – the March date may indicate

that the report had been compiled previously, perhaps for another trader.)
The report included the following materials and information:

- 5 (a) The nature of Dualite Ltd's business (being wholesale trading in general electrical goods);
- (b) Contact details of Dualite Ltd and its place of business and the home contact details of its directors and company secretary;
- (c) Details of its bank accounts with HSBC bank and FCIB;
- 10 (d) Companies Registry filings, including date of incorporation (22 March 2005), current directors, filed accounts (none had been filed at the time of the report as the company had not completed its initial trading period);
- (e) The date trading commenced (April 2005) and the date of its VAT registration (1 April 2005);
- 15 (f) The names of two companies prepared to give trade references (no references were taken up by the Appellant, and subsequently in correspondence with the Commissioners the Appellant stated: "It is not company policy to take up trade reference, not until the credit terms have not been met.");
- 20 (g) A short description (and photographs) of the office premises used by Dualite Ltd;
- (h) A short description of the due diligence procedures undertaken by Dualite Ltd on its suppliers (with the statement that all due diligence is carried out by Dualite itself, and that it requires a supplier's declaration as to title to goods, VAT compliance and credibility of supplier's supplier – a pro forma of that declaration is included in the report);
- 25 (i) Verification of directors' details and identity from the electoral role, copies of driving licences and utility bills; and
- 30 (j) A credit report showing that Dualite Ltd has no credit rating as it's age is less than eighteen months, but that its estimated annual turnover is £230 million, and its estimated annual profit £280,000.

35 (3) On 30 June 2006, together with Dualite Ltd's invoice for the supply of the Nokia N8800 Black mobile telephones, Dualite Ltd provided to the Appellant a completed "Supplier's Declaration" whereby Dualite Ltd declared that it had legal title to the goods; that the goods had been inspected by its freight forwarder agents and that the goods existed; that it had no reasonable grounds to suspect that VAT had not been paid by its supplier; that both its own and its supplier's VAT registration number were then valid; and that it had carried out reasonable due diligence checks
40 on its supplier, including seeing a copy of its VAT registration certificate, its incorporation certificate and verification from the Commissioners of its VAT registration number.

60. The Appellant carried out the following due diligence upon Silacom, its customer in Deal Chain 51:

5 (1) Silacom provided the Appellant with details of its incorporation documents, showing that it was incorporated in Innsbruck on 5 June 2002; the names and addresses of its directors; its Austrian VAT registration number; its bank account held with FCIB; a short “business report” with a credit report expressing the opinion that “subject company is considered trustworthy for normal credit engagements”, and that “as the company purchases the majority of its goods abroad, we have no conclusive data
10 regarding payments. There is, however, no evidence of lawsuits or complaints”; summary balance sheets for each financial period ending respectively 31 December 2002, 2003 and 2004; and a summary of annual turnover for each of the financial periods 2003,2004, and 2005 (sales for 2005 were EUR 17 million).

15 (2) On 27 June 2006 Silacom completed and faxed to the Appellant a “trading application form” and a “credit application for a business account” (both documents were provided by the Appellant). These documents specified the contact details of Silacom; its Austrian VAT registration number; the names of its directors; its bank account details; the
20 names and contact details of two business/trade references (no references were taken up by the Appellant).

61. The Commissioners’ Notice 726 Joint and Several Liability in the Supply of Specified Goods relates principally to the application of section 77A VATA 1994 (which imposes joint and several liability for VAT unpaid on the supply of certain
25 goods, including mobile telephones – it is not argued by the Commissioners in this case that the Appellant is liable under these provisions). Section 8 of Notice 726 is headed “Dealing with other businesses – How to ensure the integrity of the supply chain”, and gives examples of commercial checks which the Commissioners recommend a trader may wish to undertake to help establish the legitimacy of his
30 customers and suppliers and the commercial viability of the trading transaction. The Commissioners supplied a copy of Notice 726 to the Appellant on the occasion of Miss Allen’s visit to the Appellant in July 2005. The examples of recommended commercial checks include the following:

- (1) The supplier’s trading history;
- 35 (2) The commerciality of arrangements for financing the goods;
- (3) The adequacy of insurance of the goods;
- (4) The commercial viability of the market for goods of the type traded;
- (5) If the price of the goods increases within the short duration of the supply chain, is that commercially justifiable?
- 40 (6) Proof of the existence of the goods and of their marketable condition;
- (7) Obtaining copies of Certificates of Incorporation and of VAT registration;

- (8) Verifying VAT registration details with the Commissioners;
- (9) Obtaining letters of introduction on headed paper;
- (10) Obtaining some form of trade reference;
- 5 (11) Obtaining credit checks or other background checks from an independent third party;
- (12) Establishing personal contact with a senior officer of the supplier;
- (13) Obtaining details of the supplier's bank account;
- (14) Verifying details provided by the supplier by checking them against other sources where available; and
- 10 (15) Using and retaining full documentation of transactions entered into for both the purchase and sale of the goods, including invoices, purchase orders, delivery notes, airway bills, allocation notification and inspection reports.

15 These checks and actions are expressed to be not an exhaustive list, so that it is the trader who should decide what checks he needs to carry out before dealing with a supplier or customer.

The Commissioners' submissions

20 62. Miss Bevan set out for us the position in law as derived from the cases dealing with MTIC fraud. As she said, there is no material point of difference between the parties as to the legal issues and the principles to be derived from the cases. We have set out those issues and principles in paragraphs 13 to 32 above.

25 63. The first submission by the Commissioners is that the transaction entered into by the Appellant on 30 June 2006 whereby it purchased from Dualite Ltd and on-sold to Silacom 1,250 units of Nokia N8800 Black mobile telephones formed part of a transaction chain (Deal Chain 51) which was connected with fraud and formed part of an overall scheme to defraud the Commissioners. Miss Bevan argued that there was a VAT loss; that the VAT loss resulted from a fraudulent evasion; and that the transaction in question was connected with that evasion.

30 64. As to the VAT loss, Deal Chain 51 could be traced back to Heathrow Business Solutions Ltd, which had imported and then sold the mobile telephones in question, but had failed to account for the VAT it had charged on the sale. The Commissioners subsequently assessed Heathrow Business Solutions Ltd for VAT (including the VAT it had charged on this particular sale), and the VAT so assessed remained unpaid and unchallenged, proceedings for winding up the company having been commenced in
35 January 2007.

65. As to the question of whether that VAT loss resulted from a fraudulent evasion, the Commissioners argued that there was undoubted evasion by Heathrow Business Solutions Ltd: it had rendered nil VAT returns for the periods 12/04 to 03/06, stating that it was not trading. Subsequent investigations revealed that it had been trading in

10 66. Furthermore, in the Commissioners' submission, the wider circumstances of Deal Chain 51 demonstrated fraud, including the following factors: the circular flow of funds between the parties, as apparent from the evidence of Mr Mendes; the provision to the Appellant of £90,000 by Medius Trading AG at the point where it required funding to pay the VAT element of the price payable to Dualite Ltd; the pattern of trading by the Appellant during the quarters 03/06 and 06/06 (acting as a buffer trader until the Deal Chain 51 broker trader transaction); the similarity of deal chains in which the Appellant took part, with the same parties appearing in the same sequence; 15 the "back-to-back" nature of the deals entered into by the Appellant, where the exact number of units were traded, and where trades were conducted on the same day; the uniformity of profit earned by the Appellant and the other traders in the transactions and, in contrast, the substantially greater profit earned by the Appellant in the course of Deal Chain 51 on its sale to Silacom; the failure of the Appellant to inspect the goods, insure them or record their IMEI numbers; the fact that the mobile telephones traded in the course of Deal Chain 51 were not to a UK specification, and therefore relevant only to a very limited market in the UK.

25 67. As to the question of whether the relevant transactions entered into by the Appellant on 30 June 2006 were connected with the VAT loss which resulted from fraudulent evasion, this, too, is clear from the evidence, including the factors referred to in paragraph 66 above. The Appellant was an essential player in the arrangements whereby Heathrow Business Solutions Ltd evaded the payment of VAT on the sale of goods subsequently traded on the same day by the Appellant, and, as described in the 30 *Calltel* case, "by being ready, despite knowledge of the evasion of VAT, to make purchases, [made] himself an accomplice in that evasion".

35 68. The Commissioners' second submission is that the Appellant knew (or at the very least, should have known) that the transaction entered into by the Appellant on 30 June 2006 whereby it purchased from Dualite Ltd and on-sold to Silacom 1,250 units of Nokia N8800 Black mobile telephones was connected with the fraud which gave rise to the VAT loss. The Commissioners consider that, in assessing the Appellant's actual and constructive knowledge, it is relevant to consider the Deal Chain 51 transaction in the context of the Appellant's trading activities over the previous six months. They rely on the factors referred to in paragraph 66 above as evidence that 40 the Appellant must have been aware of the fraud. In particular, the Commissioners point to the profit achieved by the Appellant on the Deal Chain 51 transaction relative to the profit achieved on all its other transactions, when there was no commercial difference (other than a sale to an overseas purchaser) to justify that profit differential. They also point to the £90,000 payment received by the Appellant from Medius Trading AG on 11 July 2006, expressed as a deposit, when such a deposit could not 45

be explained commercially by reference to any documentation or pattern of trading by the Appellant. The Commissioners also questioned the commerciality of the trading terms of the parties (including the Appellant) involved in Deal Chain 51, where in relation to transactions of very substantial value, it was unclear where title to the goods lay, and where the credit risk lay – in particular, they questioned why the Appellant should ship out the goods and allocate them to an overseas customer before payment was made and title was transferred. All of these matters, they submitted, showed that Deal Chain 51 was a contrived transaction to facilitate the VAT loss by fraud, and the Appellant must have known that to be the case. The Commissioners considered that they had shown a convincing case that the Appellant knew or ought reasonably have known of the connection to the fraud, and the Appellant had not made a case showing that it did not have actual or constructive knowledge of that connection.

69. The Commissioners dismissed the Appellant’s claim that, by way of due diligence, the Appellant had done all that could reasonably be expected of it to satisfy itself that the transactions it entered into were not connected with fraud. From the visits made by Commissioners’ officers to the Appellant and from the Commissioners’ publications given to the Appellant, the Appellant had been fully apprised of the risks incurred in trading in mobile telephones and of the precautions required to ensure that there was no involvement in fraudulent transactions. The action the Appellant had taken were little more than “window dressing”, designed to show the form of due diligence without in reality attempting to discover the integrity of the deal chain. In particular, the Appellant was aware that its supplier, Dualite Ltd, with whom the Appellant had not previously traded, had been trading for just over a year, and yet no further checks were made beyond standard checks (for example, no trade references were taken up), and no attempts were made to investigate the supply chain beyond Dualite Ltd itself. The checks made on Silacom, a new customer for the Appellant, similarly did not proceed beyond the formalities, with no independent verification, and seemingly no acknowledgement by the Appellant that the transaction was significant in value to Silacom relative to its stated annual turnover.

70. For these reasons, and applying the relevant case law, the Commissioners considered that the Appellant is not entitled to repayment of the VAT in question, and that accordingly its appeal should be dismissed.

The Appellant’s submissions

71. Mr Hamid, representing the Appellant, questioned first the extent to which the Commissioners had been diligent or urgent in checking upon the activities of Heathrow Business Solutions Ltd: he asked why, without serious enquiry, they had permitted it to make nil returns over a period of six VAT return quarters and why they had not identified it as an importer from the records of freight forwarders. His view was that the Commissioners preferred the easier route of blocking repayments to traders caught up in the process along the chain, rather than seeking to halt the fraud at source.

72. He defended the commerciality of the transactions entered into by the Appellant, including the Deal Chain 51 transaction. In this respect he argued:

5 (1) That the profit margin on the sale of the Nokia N8800 Black mobile telephones to Silacom was not out of line with the profit of £17.50 which was achieved on the export sale made by the Appellant in the 12/05 quarter for which a VAT repayment was made by the Commissioners;

10 (2) That in the mobile telephone grey market the goods are normally in the possession of the freight forwarders, who carry out inspections on behalf of the various owners, and so the Appellant was aware of the goods in which it was trading. Furthermore, on the sale to Silacom, the freight forwarder expressly confirmed the arrival of the goods;

(3) “Back-to-back” deals are a normal feature of the market, since a trader will not wish to enter into a purchase contract unless he has sourced a customer for the goods in question;

15 (4) In June 2006 it was not a requirement of the Commissioners that traders should record IMEI numbers. In any event, the IMEI numbers are retained by the freight forwarders storing the goods, and so if a trader requires them for a commercial purpose they can be retrieved from the freight forwarder. A trader might also verbally request random IMEI
20 numbers from the freight forwarder to check against various databases whether they were stolen;

25 (5) The position of each trader in the chain with regard to title to the goods is clear and in line with commercial dealings: the Appellant shipped the mobile telephones to the French warehouse on a “ship-and-hold” basis, so that title did not then pass – when payment was made on 12 July 2006 Dualite Ltd released the goods to the Appellant which in turn released them to Silacom;

30 (6) Similarly the insurance arrangements followed the commercial transaction: since the Appellant had title to the goods only momentarily as payment was made by the parties, it was sensible to rely on the insurance cover maintained by the freight forwarders.

35 73. The Appellant submitted that no particular significance should be attributed to the fact that the Appellant, Silacom and Dualite Ltd each held an account with FCIB through which payments were made in the transaction in question: the context which needs to be understood is that all the UK clearing banks refused to operate accounts for mobile telephone traders, and so such traders were forced to open accounts with foreign banks. FCIB spotted this opportunity and advertised its services on the IPT website, and so was both well-known (and well-used) throughout the business.

40 74. In relation to the questioning by the Commissioners of the commerciality of the transaction and the banking arrangements of the parties, the Appellant referred to the following paragraph in the decision of the tribunal in the case of *Olympia Technology Limited v The Commissioners of Her Majesty’s Revenue and Customs*:

5 “44 We consider that some of the indicators relied on by Mr Moser
[counsel for the Commissioners] relate to the trade in general and are
not relevant in assessing whether the Appellant ought to have known
of the fraud in the deal chains in which we have found fraud. If
10 something is normal in the trade then it is not likely to excite suspicion.
Mr Stone [witness for the Commissioners] would no doubt say that it is
only normal because 95 per cent of the trade is fraudulent but we have
already stated that we start from the view that something that appears
to be commercial is commercial, and if Customs say it is fraudulent,
15 that is something that needs to be proved by evidence. We include the
following: quick back-to-back same-day deals with any stock being
held to order until payments are made; dealings usually in the same
quantities of goods in the chain; mark-ups in whole pounds (in one
case 50p); many of the companies banking with FCIB when UK high
street banks would not allow mobile phone traders to have accounts.”

20 75. The Appellant further submitted that its due diligence checks on its supplier and
customer were in accordance with the checks and actions recommended by the
Commissioners in Notice 726, and that, therefore, the Appellant had taken every
precaution which could reasonably be required of it to ensure that the transactions it
entered into were not connected with fraud. Therefore the Appellant should, as
specified in *Kittel*, be entitled to rely on the legality of those transactions without the
risk of losing its right to deduct the input VAT. The Appellant is entitled to the input
tax claimed by way of repayment in respect of the transactions it entered into on 30
June 2006, and the Appellant’s appeal should be allowed.

25 *Decision*

30 76. To decide this appeal we must first reach a decision as to whether there has been
fraudulent evasion of VAT resulting in a loss to the revenue. It is agreed that the
Commissioners have to prove this on the balance of probability test. This issue was
not contested by the Appellant, but nevertheless the Commissioners, quite properly,
fully argued their case on the evidence on the point they put before us.

35 77. We are concerned with a single transaction which is the purchase and sale by the
Appellant of 1,250 units of Nokia N8800 Black mobile telephone handsets which
took place on 30 June 2006, with payment made on 12 July 2006. The evidence
before us showed that, on the same day, that number of units of that model of
telephone was traded though a chain of previous transactions until it reached Dualite
Ltd, the supplier to the Appellant. The evidence also showed that payments were
made on 12 July 2006 according to the respective invoices rendered by the parties in
the chain (except in relation to Heathrow Business Solutions Ltd – payment of the
40 invoice it rendered was made to a Mr Yasar Ahmed (someone of that name was then
the company secretary of Heathrow Business Solutions Ltd)).

78. Of those parties, Heathrow Business Solutions Ltd failed to file a VAT return for
the quarterly period in which it entered into the transaction and The Wireless
Warehouse Ltd filed a VAT return for that quarterly period, but paid no VAT; Dualite
Ltd also failed to make a VAT return for that quarterly period. Subsequently the

Commissioners assessed Heathrow Business Solutions Ltd for an amount of VAT including that which it charged to its customer (The Wireless Warehouse Ltd) in relation to the supply of the Nokia N8800 Black mobile telephones. That assessment has not been challenged by Heathrow Business Solutions Ltd, nor has it been paid, and the company has now been wound up owing this amount (and a great deal more - £30,637,891 in total) to the Commissioners.

79. Similarly with regard to Dualite Ltd, assessments have been made by the Commissioners to include the VAT it charged on the supply of the Nokia N8800 Black mobile telephones to its customer, the Appellant, and those assessments remain unpaid. In the case of The Wireless Warehouse Ltd, where a return was made covering this particular transaction, the VAT assessed in the return remains unpaid.

80. We have no hesitation in deciding, in these circumstances, that there is a loss to the revenue by reason of the failure of those companies to comply with their VAT obligations. It would appear that Dualite Ltd and The Wireless Warehouse Ltd were “buffer” traders in Deal Chain 51, so that the loss to the revenue is, in effect, the VAT on their margin. Heathrow Business Solutions Ltd, however, was the importer of the mobile telephones in question, and therefore the loss relates to the entirety of the VAT it charged on its supply of those goods, namely £89,085.94.

81. Similarly, we have no hesitation in deciding that the loss to the revenue resulted from fraudulent evasion: Heathrow Business Solutions Ltd made the supply in question on 30 June 2006 and charged VAT on that supply in accordance with the invoice it rendered to The Wireless Warehouse Ltd. It both failed to make a return in relation to that supply and failed to account to the Commissioners for the VAT it charged; when the Commissioners later rendered their own assessment covering this VAT liability, it went unpaid. There has been no attempt to explain or justify such failure on the part of Heathrow Business Solutions Ltd. Upon investigation it was found that the company had never operated from the addresses it gave to the Commissioners as its principal place of business. The only conclusion is that Heathrow Business Solutions Ltd deliberately chose not to make the VAT returns it was required to make and deliberately chose not to pay the VAT it owed to the Commissioners, which is fraudulent evasion. Miss Bevan asked us to take account of certain features of Deal Chain 51 as further evidence of the fraudulent and orchestrated nature of the loss of revenue, in particular the circularity of funds as shown in the respective bank accounts held parties with FCIB. We agree that this supports the point, but it is not necessary to our decision to look beyond the actions – or failings – of Heathrow Business Solutions Ltd itself to reach our decision on this issue.

82. The next issue to be decided is whether the Appellant’s transactions, the purchase and sale of the Nokia N8800 Black mobile handsets on 30 June 2006, is connected with the fraud, as that concept is to be understood from the case law. As discussed in paragraph 24 above, it is not necessary that the person denied the repayment – the person in the Appellant’s position – should be in a contractual relationship with the party committing the fraud. It is sufficient if the transactions giving rise to the repayment are part of a chain of transactions in the course of which the fraud is

perpetrated. This issue was examined in the *Calltel* case, where the appellant in that case argued that a purchaser several links down a chain of transactions was so remote from the fraudulent transaction at the commencement of the chain that it could not be said that he participated in a fraud that had been committed prior to his entering into his transactions. This argument was rejected by both the tribunal and the High Court on appeal for reasons expressed in these terms by Floyd J at paragraph [81] of his decision:

“It will be recalled that the rationale in *Kittel* for refusing repayment where the purchaser knows that he was taking part in a transaction connected with fraudulent evasion of VAT was that he “aids the perpetrators of the fraud and becomes their accomplice”. 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 ready, despite knowledge of the evasion of VAT, to make purchases, the purchaser makes himself an accomplice in that evasion.”

The *Calltel* case concerned an appellant who, it was found, had actual knowledge of the fraud and the resulting loss, but the reasoning holds good where the purchaser in the chain ought to have known of the fraudulent evasion of VAT.

83. The evidence presented by the Commissioners clearly established the chain of transactions commencing with the sale of the relevant mobile telephones by the missing trader, Heathrow Business Solutions Ltd, and proceeding through to the Appellant’s purchase of those mobile telephones from Dualite Ltd and their sale on to Silacom. The evidence comprised invoices rendered at each point in the chain identifying the goods, and specifying the price, and, additionally, we saw copies of the bank account statements identifying respective payments of those invoices (the “final” payment being to the company secretary of Heathrow Business Solutions Ltd, rather than to that company itself). All the transactions were entered into on the same day, 30 June 2006, and all the payments were made on 12 July 2006.

84. We therefore decide that the Appellant’s transactions in respect of which it claims a repayment of VAT are connected with the fraud which gave rise to the VAT loss. For the sake of completeness we mention that, as discussed above, Dualite Ltd, the supplier of the mobile telephones to the Appellant, also acted fraudulently, so that the Appellant’s transactions are directly connected with that fraud, too.

85. The final issue, and the real point of dispute between the parties in this case, is whether the Appellant knew or should have known that the purchase and sale of the Nokia N8800 Black mobile handsets which it entered into on 30 June 2006, was so connected with the fraud which gave rise to the VAT loss.

86. As discussed, it is for the Commissioners to make out an answerable case, but if that case is established, it is for the Appellant to show, on the balance of probabilities, that it did not know and could not reasonably be expected to have known, of that

connection with the fraud. In this case, where the Appellant is controlled solely by Mr Hamid, we are concerned with his knowledge and with what he ought to have known, applying the objective test of what a competent trader engaged in transactions of this kind should be expected to have known (see paragraph 25 above).

5 87. The Commissioners invited us to look at the pattern of the Appellant's trading in addition to the particular chain of transactions, Deal Chain 51, giving rise to the fraud and the Appellant's repayment claim. To that end they provided evidence of every transaction entered into by the Appellant for the six months ending with the date of Deal Chain 51. We accept that it is legitimate to look in this way beyond the
10 immediate transaction under scrutiny as part of the process of establishing what the Appellant knew or ought to have known in relation to the connection of that transaction with fraud.

15 88. Our findings in relation to the Appellant's trades during this six month period are set out in paragraphs 47 and 48 above. The Appellant traded goods to a substantial value (over £100 million during the period) in 130 trades, and should therefore be regarded as experienced in this particular market. Of those 130 trading transactions, nearly all were part of a chain involving a missing trader. In all but one of those transactions the Appellant was a buffer trader, selling to a UK VAT registered customer, and only in the transaction with which we are directly concerned, the 30
20 June 2006 transaction in Deal Chain 51, did the Appellant sell to an overseas customer. In relation to overseas customers it should be noted that the Appellant had traded only infrequently with overseas companies (the five sales in quarters 12/04 and 12/05 to two Dubai companies: see paragraph 56 above).

25 89. It is a striking feature of the trading transactions in the 06/06 period in particular that so many were part of identical deal chains: whereas it might be expected that the Appellant would deal with a number of suppliers on a regular basis, in genuine market conditions it seems unlikely that the entire deal chain would be frequently replicated in this manner.

30 90. The commercial genuineness of the transactions entered into by the Appellant is also called into question by the fact that every deal chain (except, possibly, one) relates to the same number of units of mobile telephones – following the chain through, the self-same goods were exported as were imported, with no trader “splitting” stock or “aggregating” stock along the way: putting the point differently, every trader was fortunate enough to find a customer requiring exactly the stock
35 which that trader's supplier was offering the trader in the market on that occasion.

91. It is also the case that with respect to each of the 130 trading transactions the entire deal chains were entered into on the same day, as “back-to-back” transactions, suggesting a degree of co-ordination between the parties beyond what would be expected in a commercial and competitive market.

40 92. In challenging the commerciality of the trading transactions generally of the Appellant the Commissioners referred to the fact that, notwithstanding the very substantial value of goods traded in each transaction, the Appellant had taken out no

5 93. Mr Hamid had some response to these points arising from the Appellant's pattern
and conduct of trade: he explained that the Appellant would itself buy and sell only on
a "back-to-back" basis as it was not prepared to risk exposure in the market and was
not financed to hold stock; he explained that the Appellant relied on the insurance
cover maintained by the freight forwarder, since the Appellant did not hold stock and
10 had title only fleetingly because of the "back-to-back" nature of its deals (but he was
unable to say whether he had asked for details of any such insurance cover held by a
freight forwarder, so he was not aware whether such cover existed, or if it did, on
what terms it applied). He explained that the freight forwarders gave verbal reports
confirming the stock and also kept records of IMEI numbers which would have been
15 available to him had he requested them.

94. Whilst we agree that there are, arising from the pattern of transactions entered into
by the Appellant in the first half of 2006, questions as to whether those transactions
were commercially genuine, there are a number of factors, mainly relating to Deal
Chain 51 and the Appellant's part in that deal chain, which together lead us to infer
20 that the Appellant knew that the transactions it entered into in the course of that deal
chain were co-ordinated and also connected with the fraud carried out by Heathrow
Business Solutions Ltd.

95. First, we note that of the fifty-five trading transactions carried out by the
Appellant in its VAT quarter 06/06, the only trade where it acted as broker (the sale to
25 Silacom) was carried out on the last day of the quarter. This, no doubt, was to
minimise the period for which the Appellant would be out of pocket before (as it
hoped) the repayment claim was settled. As such it may be regarded as sensible VAT
planning. But it also suggests a wider orchestration of events, whereby the Appellant
chose the timing of this particular transaction, not because, by the operation of the
30 market, an offer made by a supplier coincided with request made by an overseas
customer, but because that was the most advantageous date on which the only zero-
rated supply which the Appellant was to make in that quarter could be made.

96. Secondly, of the fifty-five transactions entered into by the Appellant in the VAT
quarter 06/06, fourteen were entered into during the two days of trading 29 and 30
35 June 2006, the Appellant selling mobile telephones in those two days to a value of
£12,561,250. Furthermore, each of those fourteen transactions was part of a deal
chain where every other party in that deal chain entered into its respective transactions
on 29, or, as the case may be, 30 June, since they were all "back-to-back"
transactions. That, too, suggests a wider orchestration of events, and not merely the
40 coming together, through market processes, of a series of independent trades.

97. Thirdly, and more significantly, there is the question of the profit or margin
achieved by the Appellant on the sale of the mobile telephones to Silacom, and its
relativity to the margin achieved by the Appellant in other trades and by other traders

in Deal Chain 51. In trades of this kind the profit is measured by reference to the unit of mobile telephones traded. In 129 of the 130 trades made by the Appellant in the first half of 2006 its margin per unit never exceeded £1.00, and more usually was £0.50 or £0.25. When the Appellant sold the 1,250 units of Nokia N8800 Black mobile telephones to Silacom its margin was £24.50 per unit. In relation to Deal Chain 51, all the other traders made a margin of £0.25.

98. Mr Hamid could give no explanation for this enormous differential. He told us that he and other traders use the IPT website and other websites to source deals, but could not explain why Silacom, a new customer, should have come to the Appellant when, had they sourced the goods direct through such a website they could have purchased them for considerably less. Correspondingly, he was not able to explain why another supplier in the chain, say Dualite Ltd, had not instead taken the opportunity to make a substantial profit on an export sale. He was not able to show that a sale to an overseas customer resulted in significant additional cost to a trader such as the Appellant, such as would otherwise justify in the market a significant mark-up in the price for an export sale – he thought that the Appellant had paid the costs of shipping the goods to France on the Silacom deal, but had no evidence of that, and his recollection was that the costs of shipping would be no more than £1.00 per mobile telephone. In cross-examination he did suggest that the Nokia N8800 Black model of mobile telephone was something of a special commodity, but if that were the case the other traders trading in those goods on 30 June 2006 would have reflected the fact in their prices. His point is further undermined by the fact that on the same day the Appellant sold 1,000 units of the same model of mobile telephone to a UK customer for a price which was £27.50 per unit less than the price charged to Silacom (the Appellant achieving a margin on that deal of £0.50 per unit).

99. Mr Hamid's only significant response to this point was to refer to the export transaction by the Appellant in November 2005, where the Appellant had achieved a margin of £17.50 in a transaction which the Commissioners had examined, and for which they had agreed a VAT repayment. Mr Nevin told us that that transaction had not been subjected to an extended verification process by the Commissioners (that process was introduced later, when action was stepped up in response to the growth in MTIC fraud cases), so that the examination had been limited to checking the purchase and sale and export shipping documentation. In those circumstances the Commissioners were not prepared to concede that the November 2005 transaction was itself a genuine commercial transaction free from the taint of fraud somewhere in a chain of transactions of which it formed part. In any event, without further evidence (of which there was none) as to why as a matter of genuine commerce export deals inherently carry a margin so much greater than UK deals, we do not consider that the existence of this transaction substantiates to any material extent the commerciality of the very large profit achieved on the sale to Silacom.

100. Again, therefore, we see this as convincing evidence that leads us to the inference that the Appellant was, in entering into these transactions, taking part in a planned and organised series or chain of transactions relating to the VAT fraud carried out by the missing trader in the chain.

101. Fourthly, we have regard to the compelling evidence of Mr Mendes with respect to the circularity of funds moving between the parties in Deal Chain 51 on 12 July 2006 as demonstrated by the entries in their respective bank accounts held with FCIB. The details are set out in paragraph 54 above. Such a train of events could have been achieved only by careful pre-arrangement and with the complicity of all the parties.

102. Finally, and most telling of all, there is the payment of £90,000 by Medius Trading AG to the Appellant on 11 July 2006. Without that payment the Appellant would not have been able to pay the following day what it owed to Dualite Ltd. It is a necessary payment which facilitates the entire chain of circular payments made on 12 July 2006. The payment is virtually equal to the VAT (£89,250) due from the Appellant to Dualite Ltd and which the Appellant could not recover from its zero-rated supply to Silacom. Mr Hamid acknowledged that the payment was required for this purpose. His explanation was that he had negotiated a deal with Medius Trading AG whereby he agreed to sell a large consignment of mobile telephones at some future date for £900,000, with Medius Trading AG agreeing to pay a deposit of ten per cent of the price against future payment of the purchase price.

103. We do not accept Mr Hamid's evidence on this matter. It is contrary to any commercial logic or practice, and it is not credible that an independent overseas company, new to dealings with the Appellant, would have entered into such an arrangement as a commercial deal. It is also contrary to the conduct of the Appellant's own trade. Thus:

(1) Medius Trading AG was asked to make a deposit payment to a company based in a different jurisdiction with which it had not previously traded, and whose credit-worthiness would not justify such an unsecured payment;

(2) There was nothing special about the mobile telephones offered by the Appellant to Medius Trading AG so as to indicate why Medius Trading AG would enter into such an arrangement at its commercial risk rather than buying them on conventional terms from another trader;

(3) There was no documentation, beyond a simple invoice, to record the terms of such an unusual transaction – for example relating to delivery, transfer of title, or refund of the deposit if failure to deliver;

(4) The Appellant had never before entered into a transaction of this kind;

(5) Mr Hamid told us, in another context (that of title to the goods the Appellant traded in, and insurance cover) that the Appellant always traded on a "back-to-back" basis, selling on the same day goods which it purchased that day, and that it achieved its mark-up to secure its profit. In the case of Medius Trading AG the Appellant was at risk that it would not be able to source what it had agreed to sell, or, if it could source them, that it could do so at a price which did not result in a loss.

104. We also note that there is no evidence that Medius Trading AG has pressed for repayment of the sum in question or for the Appellant to complete its deal and deliver

the mobile telephones. Nor is there evidence that the Appellant has attempted to buy the mobile telephones which would enable it to complete the deal. All that has happened is that in August 2006 the Appellant wrote to Medius Trading AG to state (wrongly) that the funds were still held in the Appellant's bank account.

5 105. We further note that when the Commissioners eventually asked for a copy of the invoice issued to Medius Trading AG by the Appellant, the Appellant produced an invoice with a number identical to that used on an invoice previously issued to another customer. Mr Hamid explained that as an administrative error.

10 106. Taking all these matters of evidence together we conclude that the only reasonable inference is that the arrangements comprising Deal Chain 51, and the arrangements beyond Deal Chain 51 which resulted in the circular transfer of funds between the parties (including the arrangements involving Medius Trading AG) were co-ordinated so as to accomplish the VAT fraud carried out by Heathrow Business Solutions Ltd. Those arrangements could not have been so co-ordinated without the
15 active participation and knowledge of the Appellant.

107. We therefore conclude that the Appellant knew that the transactions it entered into with Dualite Ltd as its supplier and Silacom as its customer for the purchase and sale of 1,250 units of Nokia N8800 Black mobile telephones on 30 June 2006 were connected with the VAT fraud in question.

20 108. The Appellant placed much reliance on the due diligence it carried out with respect to both Dualite Ltd and Silacom, arguing that it had, in the *Kittel* phrase, "taken every precaution reasonably required of [it] to ensure that [its] transactions are not connected with fraud," and therefore should be entitled to recover its input tax. However, the formality of due diligence checks counts for nothing where, as we have
25 found, the taxpayer knew that its transactions were connected with the fraud. In such a case the due diligence checks are no more than a sham, and it is our decision that in this case such checks as the Appellant carried out were a sham.

109. For the reasons given we decide that the Appellant is not entitled to repayment of the input VAT in question, and we therefore dismiss the Appellant's appeal.

30 *Costs*

110. The parties asked us to leave open the question of costs, and therefore we make no order as to costs. The parties are at liberty to apply for a costs order.

Appellant's right to appeal.

35 111. The Appellant has a right to apply for permission to appeal against this decision pursuant to Rule 39 of The Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules 2009. 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.

5

EDWARD SADLER

TRIBUNAL JUDGE

10

RELEASE DATE: 28 January 2010

Authorities referred to in skeletons and not referred to in the decision:

- 15 *Total Network SL v HMRC* [2008] UKHL 19
Optigen Ltd v Customs and Excise Commissioners (C354/03); *Bond House Systems Ltd v Customs and Excise Commissioners* (C484/03); *Fulcrum Electronics Ltd v Customs and Excise Commissioners* (C355/03) [2006] STC 419
Just Fabulous (UK) Limited [2007] EWHC 521 (Admin)
- 20 *Blue Sphere Global Limited v HMRC* [2008] UK VAT 20901
Hall (Inspector of Taxes) v Lorimer [1994] 1 WLR 209
Softwarecore Ltd v Pathan [2005] EWHC 1845 (Ch)
Dragon Futures Limited v HMRC [2006] UK VAT 19831
Honefone Limited v HMRC [2008] UK VAT 20667
- 25 *HMRC v Brayfal Ltd* (Unreported VAT Tribunal decision, released 22 August 2008)
HMRC v Blue Sphere Global Ltd [2009] EWHC 1150 (Ch)