TC04260

Appeal number: MAN/2008/00208 & MAN/2008/00209

VALUE ADDED TAX – input tax – denials of right to deduct on grounds that the Appellants knew or should have known that the transactions were part of fraud by others – alleged MTIC – whether shown that the Appellant's transactions connected with fraudulent evasion of VAT – yes – whether Appellant knew or should have known of fraud – yes – valid refusals of right to deduct – appeals dismissed

FIRST-TIER TRIBUNAL
TAX CHAMBER

GOLD UK CONSULTING LTD **Appellants**
&
HORIZON IMPORT EXPORT LTD

- and -

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

TRIBUNAL: JUDGE JENNIFER BLEWITT
MR DEREK ROBERTSON

Sitting in public at Manchester on 20, 21 and 22 January 2014

Mr Nigel Gibbon of Nigel Gibbon & Co, for the Appellant

Mr James Puzey, Counsel instructed by HM Revenue and Customs, for the Respondents

DECISION

Introduction

1. These are appeals against HMRC's decisions dated 22 January 2008 by which HMRC denied Gold UK Consulting Limited ("Gold") and Horizon Import Export Limited ("Horizon") input tax claims in the sums of £1,680,000 and £918,750 respectively.

2. The basis of HMRC's decisions and its case before this Tribunal is, as set out in its Statement of Case, that the relevant transactions carried out by the Appellants in VAT period 06/06 were connected with the fraudulent evasion of VAT and that the Appellants, through their shared director Mr Ayub Khan, knew or should have known of this fact.

3. By Notices of Appeal dated 7 February 2008 and 13 February 2008 the Appellants appealed against HMRC's decisions. The grounds of appeal relied upon can be summarised as follows: HMRC's decisions were unreasonable, unfounded and based on assumption. The Appellants' transactions were bona fide; satisfactory checks were carried out and the Appellants acted with due diligence in respect of each of the relevant transactions. The Appellants deny any wrongdoing including involvement in, or knowledge of fraudulent activity.

Missing Trader Intra-Community Fraud: Legislation and Case law

4. The legislation governing the right to deduct is contained within Sections 24 – 26 of the Value Added Tax Act 1994 and the VAT Regulations 1995 (SI 1995/2518). If a trader has incurred input tax which is properly allowable, he is entitled to set it against his output tax liability or to receive a repayment if the input tax credit due to him exceeds that liability. Evidence is required in support of a claim (Article 18 of the Sixth Directive and regulation 29 (2) of the VAT Regulations 1995).

5. A description of Missing Trader Intra-Community Fraud, hereafter referred to as "MTIC fraud", can be found in the judgment of Roth J in *POWA (Jersey) Ltd v HMRC* [2012] UKUT 50 (TCC):

"[1] This is yet a further case of so-called missing trader or "MTIC" fraud on the system of VAT. The decision of the First-tier Tribunal ("FTT") conveniently describes the nature of a typical MTIC fraud as follows:

> *"5 … goods (almost always small but valuable items such as mobile phones and computer chips) are acquired by a registered trader in the United Kingdom from a trader in another member State, and sold to a second UK-registered trader. The goods then usually change hands several times within the UK before they are sold to an overseas trader which, if it is located in a member State of the European*

Union, is registered for VAT in that member State. Commonly the transactions all occur within a few days of the entry of the goods into the UK, sometimes even on the same day, so that goods enter the UK in the morning, pass through the hands of several UK traders during the day, and are exported again in the afternoon.

6. The first UK vendor, the acquirer from overseas, charges VAT on the consideration paid by his purchaser, but fails to account to the respondent Commissioners for that tax, and disappears. Such documentation as he may have had—if any—relating to his acquisition is never produced to the Commissioners. For the scheme to work he must be a VAT-registered trader who provides the purchaser with a genuine VAT invoice, on the strength of which the purchaser claims an input tax credit. The purchaser's own sale, and those of the other UK traders save the last in the sequence, usually generate a small profit and, consequently, a small net VAT liability, for which those traders account. The last trader, selling overseas, claims credit for the input tax he has incurred, but has no output tax liability since the sale is zero-rated. Usually this trader makes a significant profit, though that is not invariably the case; occasionally one of the antecedent traders can be shown to have made the greatest profit of all those in the chain. All of these sales and purchases, including the sale to the overseas buyer, are almost always properly documented.

[2] In the jargon that has developed to describe the various participants in such chains, the initial importer of the goods who fails to account for the output tax he has charged to his purchaser and disappears, is known as the "defaulter" or "missing trader." The trader at the end of the UK chain who sells the goods to a purchaser overseas is known as a "broker". The traders between the defaulter and broker are referred to as "buffers". In the present case, it is alleged that PJL was a broker.

[3] There are various variations and developments of this typical scheme of MTIC fraud. One of these, of which three of the transactions in the present case are said to be an example, comprises what is called "contra-trading". I again gratefully adopt the description given by the FTT:

"9 A contra-trader, a broker in one chain of transactions—again adopting the commonly used jargon, a "dirty" chain—in which a default has occurred, buys goods from a supplier in another member State, and sells them to a UK customer; after one or more further sales and purchases they are sold to a customer in another member State. The contra-trader and, usually, all the other traders in this chain account correctly for their VAT liabilities; taken by itself it is a "clean" chain. The acquirer in the clean chain has incurred a liability for

output tax which (because the values are engineered to achieve this result) matches the input tax credit due to him (or ostensibly due to him) as the broker in the dirty chain. He does not need to make a large repayment claim, attracting the Commissioners' attention, but instead makes a modest payment, or a minimal repayment claim. The same result may be achieved by undertaking a number of transactions generating an aggregate input tax credit matching the broker's output tax liability for the relevant accounting period. It is then the broker in the clean chain who has an input tax claim which, unless they can establish a link between the clean and dirty chains, the Commissioners must meet since the goods in the clean chain have not themselves been used for fraudulent purposes.""

6. This appeal involves allegations of contra-trading.

7. *Kittel v Belgium, Belgium v Recolta Recycling* SPRL (C-439/04 and C-440/04) [2006] ECR 1-6161 *("Kittel")* provided the legal basis for the denial of the right to deduct in certain circumstances:

"*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...*

56. In the same way, a taxable person who knew or should have known that, by his purchase, he was taking part in a transaction connected with fraudulent evasion of VAT must, for the purposes of the Sixth Directive, be regarded as a participant in that fraud, irrespective of whether or not he profited by the resale of the goods.

57. That is because in such a situation the taxable person aids the perpetrators of the fraud and becomes their accomplice.

58. In addition, such an interpretation, by making it more difficult to carry out fraudulent transactions, is apt to prevent them.

59. Therefore, it is for the referring court to refuse entitlement to the right to deduct where it is ascertained, having regard to objective factors, that the taxable person knew or should have known that, by his purchase, he was participating in a transaction connected with fraudulent evasion of VAT, and to do so even where the transaction in question meets the objective criteria which form the basis of the concepts of 'supply of goods effected by a taxable person acting as such' and 'economic activity'.

60. It follows from the foregoing that the answer to the questions must be that where a recipient of a supply of goods is a taxable person who did not and could not know that the transaction concerned was connected with a fraud committed by the seller, Article 17 of the Sixth Directive must be interpreted as meaning that it precludes a rule of

national law under which the fact that the contract of sale is void – by reason of a civil law provision which renders that contract incurably void as contrary to public policy for unlawful basis of the contract attributable to the seller – causes that taxable person to lose the right to deduct the VAT he has paid. It is irrelevant in this respect whether the fact that the contract is void is due to fraudulent evasion of VAT or to other fraud.

61. By contrast, where it is ascertained, having regard to objective factors, that the supply is to a taxable person who knew or should have known that, by his purchase, he was participating in a transaction connected with fraudulent evasion of VAT, it is for the national court to refuse that taxable person entitlement to the right to deduct."

8. The *Kittel* test was further clarified by Moses LJ in *Mobilx Ltd and The Commissioners for Her Majesty's Revenue and Customs, The Commissioners for Her Majesty's Revenue and Customs and Blue Sphere Global Ltd, Calltel Telecom Ltd & another and The Commissioners for Her Majesty's Revenue and Customs* [2010] EWCA Civ 517 ("*Mobilx*") at [24]:

"The scope of VAT is identified in Art. 2 of the Sixth Directive. It applies, in addition to importation, to the supply of goods or services effected for consideration within the territory of the country by a taxable person acting as such. A taxable person is defined in Art. 4.1 as a person who carries out any of the economic activities specified in Art. 4.2. Art. 5 defines the supply of goods and Art. 6 the supply of services. The scope of VAT, the transactions to which it applies and the persons liable to the tax are all defined according to objective criteria of uniform application. The application of those objective criteria are essential to achieve:-

> *"the objectives of the common system of VAT of ensuring legal certainty and facilitating the measures necessary for the application of VAT by having regard, save in exceptional circumstances, to the objective character of the transaction concerned." (Kittel para 42, citing BLP Group* [1995] ECR1/983 para 24.)

And at [30]:

"...the Court made clear that the reason why fraud vitiates a transaction is not because it makes the transaction unlawful but rather because where a person commits fraud he will not be able to establish that the objective criteria which determine the scope of VAT and the right to deduct have been met."

9. As to the issue of connection, in *Blue Sphere Global Ltd and The Commissioners for HM Revenue and Customs* [2009] EWHC 1150 (Ch) the Chancellor stated (at paragraphs 42 – 45):

"…The nature of any particular necessary connection depends on its context, for example electrical, familial, physical or logical. The relevant context in this case is the scheme for charging and recovering VAT in the member states of the EU. The process of off-setting inputs against outputs in a particular period and accounting for the difference to the relevant revenue authority can connect two or more transactions

or chains of transaction in which there is one common party whether or not the commodity sold is the same. If there is a connection in that sense it matters not which transaction or chain came first. Such a connection is entirely consistent with the dicta in Optigen and Kittel because such connection does not alter the nature of the individual transactions. Nor does it offend against any principle of legal certainty, fiscal neutrality, proportionality or freedom of movement because, by itself, it has no effect.

Given that the clean and dirty chains can be regarded as connected with one another, by the same token the clean chain is connected with any fraudulent evasion of VAT in the dirty chain because, in a case of contra-trading, the right to reclaim enjoyed by C (Infinity) in the dirty chain, which is the counterpart of the obligation of A to account for input tax paid by B, is transferred to E (BSG) in the clean chain. Such a transfer is apt…to conceal the fraud committed by A in the dirty chain in its failure to account for the input tax received from B."

10. On the issue of knowledge, Moses LJ in *Mobilx* provided the following guidance:

"4. Two essential questions arise: firstly, what the ECJ meant by "should have known" and secondly, as to the extent of the knowledge which it must be established that the taxpayer had or ought to have had: is it sufficient that the taxpayer knew or should have known that it was more likely than not that his purchase was connected to fraud or must it be established that he knew or should have known that the transactions in which he was involved were connected to fraud?

52. If a taxpayer has the means at his disposal of knowing that by his purchase he is participating in a transaction connected with fraudulent evasion of VAT he loses his right to deduct, not as a penalty for negligence, but because the objective criteria for the scope of that right are not met. It profits nothing to contend that, in domestic law, complicity in fraud denotes a more culpable state of mind than carelessness, in the light of the principle in Kittel. A trader who fails to deploy means of knowledge available to him does not satisfy the objective criteria which must be met before his right to deduct arises…

53. Perhaps of greater weight is the challenge based, in Mobilx and BSG, on HMRC's denial of the right to deduct on the grounds that the trader knew or should have known that it was more likely than not that transactions were connected to fraud. The question arises in those appeals as to whether that is sufficient or whether, as the Chancellor concluded in BSG, the right to deduct input tax may only be denied where the trader knows or should have known that the transaction was connected to fraud (see judgment, § 52). In short, does a trader lose his entitlement to deduct if he knew or should have known of a risk that his transaction was connected to fraudulent evasion of VAT? HMRC contends that the right to deduct may be denied if the trader merely knew or should have known that it was more likely than not that by his purchase he was participating in such a transaction. It contends that if it was necessary to show more than appreciation of a risk then the Court's decision in Kittel would not represent a development of the law and would fail to achieve the objective,

recognised in the Sixth Directive, to which the Court referred at § 54…

56. It must be remembered that the approach of the court in Kittel was to enlarge the category of participants. A trader who should have known that he was running the risk that by his purchase he might be taking part in a transaction connected with fraudulent evasion of VAT, cannot be regarded as a participant in that fraud. The highest it could be put is that he was running the risk that he might be a participant. That is not the approach of the Court in Kittel, nor is it the language it used. In those circumstances, I am of the view that it must be established that the trader knew or should have known that by his purchase he was taking part in such a transaction, as the Chancellor concluded in his judgment in BSG:-

> *"The relevant knowledge is that BSG ought to have known by its purchases it was participating in transactions which were connected with a fraudulent evasion of VAT; that such transactions might be so connected is not enough." (§ 52)…*

58. As I have endeavoured to emphasise, the essence of the approach of the court in Kittel was to provide a means of depriving those who participate in a transaction connected with fraudulent evasion of VAT by extending the category of participants and, thus, of those whose transactions do not meet the objective criteria which determine the scope of the right to deduct. The court preserved the principle of legal certainty; it did not trump it.

59. The test in Kittel is simple and should not be over-refined. It embraces not only those who know of the connection but those who "should have known". Thus it includes those who should have known from the circumstances which surround their transactions that they were connected to fraudulent evasion. If a trader should have known that the only reasonable explanation for the transaction in which he was involved was that it was connected with fraud and if it turns out that the transaction was connected with fraudulent evasion of VAT then he should have known of that fact. He may properly be regarded as a participant for the reasons explained in Kittel.

60. The true principle to be derived from Kittel does not extend to circumstances in which a taxable person should have known that by his purchase it was more likely than not that his transaction was connected with fraudulent evasion. But a trader may be regarded as a participant where he should have known that the only reasonable explanation for the circumstances in which his purchase took place was that it was a transaction connected with such fraudulent evasion.

83. We also had regard to Christopher Clarke J in *Red12 v HMRC* [2009] EWHC 2563 at [109] – [111]:

"Examining individual transactions on their merits does not, however, require them to be regarded in isolation without regard to their attendant circumstances and context. Nor does it require the tribunal to ignore compelling similarities between one transaction and another or preclude the drawing of inferences, where appropriate, from a pattern of transactions of which the individual transaction in question forms

part, as to its true nature e.g. that it is part of a fraudulent scheme. The character of an individual transaction may be discerned from material other than the bare facts of the transaction itself, including circumstantial and "similar fact" evidence. That is not to alter its character by reference to earlier or later transactions but to discern it.

To look only at the purchase in respect of which input tax was sought to be deducted would be wholly artificial. A sale of 1,000 mobile telephones may be entirely regular, or entirely regular so far as the taxpayer is (or ought to be) aware. If so, the fact that there is fraud somewhere else in the chain cannot disentitle the taxpayer to a return of input tax. The same transaction may be viewed differently if it is the fourth in line of a chain of transactions all of which have identical percentage mark ups, made by a trader who has practically no capital as part of a huge and unexplained turnover with no left over stock, and mirrored by over 40 other similar chains in all of which the taxpayer has participated and in each of which there has been a defaulting trader. A tribunal could legitimately think it unlikely that the fact that all 46 of the transactions in issue can be traced to tax losses to HMRC is a result of innocent coincidence. Similarly, three suspicious involvements may pale into insignificance if the trader has been obviously honest in thousands.

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

84. We also had regard to Briggs J in *Megtian Limited (in administration) v HMRC* [2010] EWHC 18 (Ch) at [34], [37] and [38]:

“I do not read Lewison J's analysis of the issue as to what must be shown that the broker knew or ought to have known in a contra-trading case as amounting to a rigid prescription that, as a matter of law, such an analysis must be performed in every contra-trading case, such that it will be defective unless it identifies one or other of the alternative frauds as being that which the broker knew or ought to have known...

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

Similarly, I consider that there are likely to be many cases in which facts about the transaction known to the broker are sufficient to enable it to be said that the broker ought to have known that his transaction was connected with a tax fraud, without it having to be, or even being possible for it to be, demonstrated precisely which aspects of a sophisticated multifaceted fraud he would have discovered, had he made reasonable inquiries. In my judgment, sophisticated frauds in the real world are not invariably susceptible, as a matter of law, to being carved up into self-contained

boxes even though, on the facts of particular cases, including Livewire, that may be an appropriate basis for analysis."

85. The burden of proof in this type of case rests with HMRC; per Moses LJ in *Mobilx* (paragraph 81):

"It is plain that if HMRC wishes to assert that a trader's state of knowledge was such that his purchase is outwith the scope of the right to deduct it must prove that assertion."

86. Our approach to the appeals was to recognise that, while we must consider the merits of the individual transactions, we should not view the transactions in isolation as to do so would be an artificial exercise. We were conscious to ensure that in considering the knowledge of the Appellant, through the Company officer Mr Ayub Khan, we only took account of information known to him during the relevant period. We should also note that we generic information and opinions provided by HMRC officers nor did we attach any significant weight to evidence established with the benefit of hindsight.

Issues

87. The issues to be determined in these appeals are:

(a) Was there a tax loss;

(b) If so, did this loss result from a fraudulent evasion;

(c) If so, were the Appellant's transactions which are the subject of appeal connected with that fraudulent evasion; and

(d) If so, did the Appellant know or should it have known that its transactions were so connected.

88. Mr Gibbon on behalf of the Appellant did not challenge the evidence adduced by HMRC in respect of (a), (b) and (c). However it was not expressly accepted that the evidence proved HMRC's case on those issues and we were invited to reach our own findings on the evidence.

Undisputed Background Facts

Gold

89. Gold was incorporated on 31 March 2004. The trade classification at Companies House was "wholesale of electrical household goods, wholesale of computers, computer peripheral equipment and software, wholesale of other electrical parts and equipment, other wholesale." Gold initially traded as a labour provider and from July 2005 as a wholesaler of mobile phones.

90. Mr Ayub Khan was appointed as the sole director of Gold from 9 July 2005 to date. The company secretary is Mr Khan's wife, Shahid Khan who was appointed on the same date. Gold was registered for VAT with effect from 2 June 2004.

91. Gold was subject to a pre-registration visit at which HMRC established that there was evidence of only one transaction involving the company's main declared business activity of labour provision whereby Mr Mohammad Basharat Khan (director from 31 March 2004 to 24 March 2005) had agreed to provide staff to a client for a period of 12 months. Gold had raised 4 sales invoices in 2004 relating to this service (which we should note pre-dates the period with which this appeal is concerned and Mr Ayub Khan's involvement) the VAT on which was £1,187.02. Gold failed to declare this amount to HMRC and was subsequently assessed for the sum on 23 March 2005. Mr Ayub Khan paid the outstanding liability to HMRC from the account of Horizon in lieu of a purchase fee for the company at which point he took over as director.

92. In June 2005 HMRC was notified of a change to Gold's principal place of business to Cariocca Business Park, Unit 45, Sawley Road, Manchester; the same business premises as Horizon.

93. On 9 July 2005 Companies House was informed of a change of director to Mr Ayub Khan. HMRC did not receive notification of the change.

94. Mr Khan's sole trading activity on taking over the company was the wholesale of mobile phones.

95. Gold's VAT return for period 06/06 was received by HMRC on or about 7 July 2006. The return claimed a repayment in the sum of £1,682,833.70.

96. Six transactions had been carried out by Gold during the relevant period. All related to the purchase of Nokia 8800s from Edgeskill Limited ("Edgeskill") and onward sale to MK Digital (Cyprus) Limited ("MK Digital").

97. The deal chains in each of the transactions were:

Falcon Trading International Limited ---Uni-Brand Europe Limited ----Edgeskill Ltd ---- Gold ----MK Digital

98. The goods were shipped by Gold to the Netherlands on 28 June 2006 and 30 June 2006. Gold faxed Interken Freighters (UK) Ltd on 26 July 2006 to release the goods to its customer following payment from MK Digital on 24 July 2006.

Horizon

99. Horizon was incorporated on 29 January 2003. Its trade classification at Companies House is "wholesale of clothing and footwear" and "other computer related activities."

100. Mr Khan was appointed as director on 29 January 2003. The company secretary is Mr Khan's wife, Shahid Khan, who was appointed on 29 January 2003. The shareholders are Mr Khan (99%) and Mrs Khan (1%).

101. The VAT1 stated the company's business activities as the wholesale of garments and fabric. On 14 July 2004 the principal place of business was changed to Cariocca Business Park, Unit 45, Sawley Road, Manchester.

102. HMRC officer Gellvear who gave evidence in these proceedings noted that the trading activities on the first VAT return rendered by Horizon for the period 1 November 2003 to 30 June 2004 involved some sales of garments. However the majority of the return related to the wholesale of MTIC style goods.

103. This VAT return and every subsequent return rendered by Horizon showed a repayment claim despite the VAT1 stating that the company did not anticipate being in a repayment situation.

104. From the date of registration on 1 November 2003 to 31 December 2004 Horizon's turnover was £2,348,673. In the following 12 months the turnover increased to £17,432,342 which significantly exceeded the expectation declared on the VAT1 by Mr Khan of £200,000.

105. Horizon's VAT return for 06/06 was received by HMRC on or about 7 July 2006. The return claimed a repayment in the sum of £918,750.

106. Five transactions had been carried out in the relevant period. All related to the purchase of Nokia N72 mobile phones from Edgeskill and onward sale by Horizon to MK Digital.

107. The deal chains in each of the transactions were:

Falcon Trading International Limited ---Uni-Brand Europe Limited ----Edgeskill Ltd ---- Horizon ----MK Digital

108. The goods were shipped by Horizon to the Netherlands on 12 July 2006 and released to its customer on 24 July 2006 following payment by MK Digital to Horizon on 24 July 2006. Horizon had by that point already paid its supplier two instalments on 20 and 24 July 2006.

Transactions connected to fraudulent tax losses

109. The chains of supply in respect of both Gold and Horizon were traced by HMRC via alleged contra-trader Uni-Brand to 2 defaulting traders; Mobiles 4 U Limited and Mountgale.

Mobiles 4 U Limited ("Mobiles 4 U")

110. HMRC officer Okolo provided an unchallenged witness statement regarding the trading activities of Mobiles 4 U which was incorporated on 19 July 1999 and is now in liquidation.

111. The company was registered for VAT with effect from 1 August 1999 and de-registered on 6 February 2007. The main business activity declared on the VAT1 was the wholesale and retail of mobile phones and accessories. On 24 November 2005 HMRC was notified of a change in company officers to Marc Dwaine Baptiste (director) and Dyan Shonna Louise Baptiste (company secretary).

112. On 6 February 2007 HMRC officers visited the premises of Mobiles 4 U in Middlesex. Upon arrival they found the shutters closed and no signs of trade. A lady working at a nearby kiosk told officers that the shop had not been open for a year.

113. The company had not rendered a VAT return since the change in directorship in November 2005. Paperwork obtained by HMRC showed 3rd party payment instructions issued by Mobiles 4 U to its customer R K Brothers ("RK") which was instructed to make payments into the FCIB account of a company called Diacomtech Ltd.

114. As a result of the visit on 6 February 2007 and HMRC's inability to contact the company it was immediately de-registered. Mr Baptiste was notified by letter dated 6 February 2007. An assessment was raised against the company on 15 November 2007 in the sum of £2,869,310 which arose from its sales to RK in respect of which VAT returns had not been submitted. To date the assessment has not been paid or appealed.

115. Ms Okolo concluded that the tax loss identified was fraudulent on the basis that Mobiles 4 U failed to render VAT returns, instructed 3rd party payments to be made and went missing.

Mountgale Limited ("Mountgale")

116. HMRC officer Chisman provided an unchallenged witness statement detailing the trading activities of Mountgale which was incorporated on 18 August 2003. The company officers were shown on Companies House records as:

- Asif Khan (company secretary appointed on 10 November 2003);
- Abdul Khan Ghafoor (director appointed on 10 November 2003);
- Ashok Bhardwaj (Nominee secretary appointed on 18 August 2003 and resigned on 30 September 2003);
- Bhardwaj Corporate Services Ltd (appointed on 18 August 2003 and resigned on 30 September 2003).

117. HMRC received the company's VAT1 signed by the director on 23 December 2003. The trading address was given as 19 Coniston Grove, Bradford and the main business activity was declared as the "import/export general goods & clothing –

coats/jackets/jeans/leathers". By letter to the company dated 6 January 2004 HMRC requested further information regarding the company's business activities and evidence of its intention to trade.

118. On 22 September 2004 HMRC became aware that Mountgale had begun dealing in mobile phones and a letter from HMRC's Redhill unit was sent to the company advising of VAT losses within the trade sector and that future verifications of companies should be made through Redhill.

119. A repayment claim was made in Horizon's 09/04 return. HMRC officer Jones notified the company that the repayment would not be made until HMRC was satisfied in the transactions involving mobile phones and clothing that the goods had been sold abroad.

120. On 8 September 2005 HMRC wrote to Mountgale regarding the export evidence it had provided for 3 transactions which HMRC stated appeared to be false. Consequently the output tax of £299,748 claimed was deemed not due and on 5 October 2005 HMRC raised an assessment in that sum. An appeal against that assessment was withdrawn by Mountgale in January 2006.

121. On 16 April 2007 HMRC officers visited Mountgale and found that the principal place of business was deserted and had not been used as trading premises for some time. Consequently a letter requesting contact be made with HMRC was left at the director's home address.

122. Contact was made with Mr Ghafoor who told HMRC officers that he had lost money on mobile phone transactions between June and September 2004 and as a result he would no longer be trading in such goods. He stated that deals undertaken in August 2006 only involved clothing. When asked about sales of CPUs Mr Ghafoor stated that he had received strange telephone calls in October and November 2006 and believed his VAT number had been hijacked. This belief was reiterated when HMRC officers visited Mr Ghafoor on 10 September 2007; he stated he had met a man in Manchester whose name he did not recall but with whom he had considered trading in electrical goods. As a result he had opened an FCIB account but subsequently decided not to trade with the man. Mr Ghafoor did not recall if the man he had met was Mr Iqbal of Uni-Brand and continued to state that his VAT number had been hijacked.

123. Mountgale was assessed on 17 September 2007 in the sum of £1,396,150 in respect of 3 sales invoices to Uni-Brand between June and September 2006. The assessments remain unpaid. Mr Chisman of HMRC concluded that Mr Ghafoor either intentionally misled HMRC in failing to declare its sales invoices to Uni-Brand or the company's VAT number had been hijacked; either way the deals undertaken with Uni-Brand were fraudulent and led to tax losses.

Uni-Brand (Europe) Limited ("Uni-Brand")

124. HMRC officer Lam provided 4 statements detailing the trading activities of Uni-Brand. Mr Lam was not required to give evidence and the contents of his witness statements can be summarised as follows.

125. Uni-Brand is a private limited company which was incorporated on 18 December 2000 and registered for VAT with effect from the same date. The company is run by the director, Mr Mohammed Iqbal and the company secretary Mrs Shehnaz Iqbal, both of whom were appointed on 3 January 2001. The VAT1 declared the main business activity as "buying and selling a range of products to wholesalers and retailer etc." The business was run from Mr Iqbal's home address in Fulwood, Preston.

126. The turnover for the first year was approximately £46,000. In 2 years of trading as a sole proprietor Mr Iqbal submitted 8 VAT returns, 3 of which were nil returns and the highest quarterly amount of outputs submitted was for £44,799 in 11/00. A visit was carried out by HMRC to inspect the books and records in January 2001. The visit report records that Mr Iqbal had a full time job until January 2001 and that the business was carried out in his spare time, with the principal outputs being toiletries, food, drinks, clothing and children's clothing.

127. Mr and Mrs Iqbal were also involved in another VAT registered company called Globcom Limited ("Globcom") which traded in the supply of mobile phones. The companies are connected by way of common director, shareholder, premises, accountants and VAT/legal advisors. Both were under the day to day control of Mr Iqbal.

128. Mr and Mrs Iqbal are also company officials for UK registered company Uniprop (UK) Ltd which was incorporated on 2 August 2005 and registered under the classification of "buying and sell own real estate and is not registered for VAT".

129. Uni-Brand's 05/06 VAT return was received by HMRC on 29 June 2006 which showed a payment due of £55,910.34. On 14 June 2006 HMRC officers visited the company in relation to its 02/06 repayment claim and during the visit officers requested sight of Uni-Brand's schedule of transactions in relation to the 05/06 period which was produced by Uni-Brand's representative Vantis Tax Ltd ("Vantis") on 4 July 2006.

130. Mr Lam note that during period 05/06 Uni-Brand had traded in mobile phones and other products including CPUs, memory sticks, secure digital cards, Microsoft office software and other computer related products that it had not previously traded.

131. Mr Lam noted from his review of the return that there was a distinct pattern of transactions within the period of trading in that there was an almost even spread of standard rated and zero rated deals: 50.17% and 49.83% respectively. Mr Lam noted that such a pattern was consistent with contra-trading.

132. HMRC undertook verification of Uni-Brand's 05/06 return, requesting records, details of due diligence checks undertaken and clarification of the increase in turnover from £79,010 in 05/05 to £15,000,000 in 11/05 to £57,000,000 in 02/06 to £405,000,000 in 05/06.

133. Mr Lam conducted a detailed examination of 56 transactions in 05/06 in which Uni-Brand was supplied by 2 UK companies and acted as broker exporting the goods. All 56 transactions were traced back to a tax loss amounting to £35,077,174.

134. Mr Lam concluded that Uni-Brand had deliberately organised its affairs so that the outputs for the period were split evenly between standard rated and zero rated and that the value of goods acquired and subsequently sold via contra transaction chains are offset by the value of goods sold to the EU by Uni-Brand which have originated from tax loss transaction chains. Uni-Brand played a dual role by buying certain goods from UK suppliers which it sold via zero rated transactions to customers in the EU (thereby putting it in a repayment position). In a separate chain of transactions Uni-Brand acted as a UK acquirer, importing large quantities of mobile phones which were then sold on to VAT registered traders within the UK applying the standard rate of VAT. In this way Uni-Brand was able to offset its VAT liability due to HMRC incurred by acquiring goods from the EU, selling on to UK traders and thereby producing a repayment situation by selling goods purchased from other UK traders to the EU.

135. In addition to 56 broker transactions Uni-Brand also acted as a UK acquirer in 135 deals for 988,500 mobile phones from 3 suppliers in the EU for a total value of £235,821,912.50 which it then sold to UK customers for £236,384,937.50. Those customers then acted as brokers selling the goods to traders outside of the UK. Of the 135 deals, Uni-Brand sold 188,000 phones in 30 deals between 13 and 27 April 2006 to Edgeskill for £43,375,125.

136. Mr Lam noted that the profit mark-ups on the goods sold in the UK were fixed at either 50p (in 84 deals) or £1.00 (in 51 deals) irrespective of the quantity, make and model of the goods or customer involved. This uniformity led Mr Lam to conclude that the trading was contrived. In addition Mr Lam noted that the paperwork obtained by HMRC indicated that the UK traders in the tax loss chains had made 3rd party payments to parties outside the UK and who were purportedly unconnected to the supply chain. The consequence of such payments was that the first supplier would be left with insufficient funds to pay the output tax charged on its sales invoice.

137. Mr Lam noted that Uni-Brand's turnover increased from £79,010 in 08/05 to £405,000,000 in 05/06 despite the company having only 3 members of staff who were employed by Globcom and without any advertising campaigns. No formal written contracts were entered into by Uni-Brand with its trading partners and the due diligence carried out was limited.

138. Mr Lam also reviewed Uni-Brand's 08/06 return which was received by HMRC on 21 September 2006 and declared outputs of £43,000,000 and output tax of £7,920,431.51. The input tax was shown as £7,913,931.05 which resulted in a payment to HMRC of £6,500.46.

139. The pattern of transactions was similar to 05/06 in that there was an almost even spread of standard rated and zero rated deals at 49.97% and 50.03% respectively. Mr Lam concluded that Uni-Brand had again organised its affairs in such a way that the

value of goods acquired and subsequently sold via contra transaction chains were offset by the value of goods sold by Uni-Brand to the EU and which originated with tax loss transaction chains.

140. Mr Lam carried out the same type of analysis as he had for the 05/06 period and found that in 7 sample deals in which Uni-Brand was supplied by 2 UK customers and as a broker exported the goods, all 7 deals traced back to tax losses which totalled £4,265,460. The defaulters in these transaction chains included those relevant to these appeals; Mobiles 4 U and Mountgale.

141. Uni-Brand had also acted as a UK acquirer in 16 deals involving 82,989 mobile phones. Of those 16 deals Uni-Brand sold 55,000 in 10 transactions to Edgeskill on 23 June 2006 for £22,148,750. Mr Lam concluded that the pattern of trading and arrangements of specific traders in the supply chains in June and July 2006 indicated that the transactions formed part of an overall scheme to defraud the Revenue.

142. Mr Lam also considered Globcom's position. The company's turnover increased from £6,000,000 in its first quarter of trading to £85,000,000 in its second period 06/05 to £100,000,000 in 09/05 to £109,000,000 in 12/05. Uni-Brand and Globcom's combined turnover for the year ended 30 June 2006 was £890,445,838 despite having only 3 staff, combined fixed assets of less than £1,500 and combined overheads of less than £200,000.

143. Uni-Brand carried out no independent checks of its trading partners and site visits to EU suppliers took place after the company had completed its last transaction with the relevant company. No documents were produced by the company to show that due diligence had been carried out on the freight forwarder used.

144. In all of the circumstances Mr Lam concluded that the transaction chains of Uni-Brand in periods 05/06 and 08/06 formed part of a deliberate contra-trading scheme carried out with the knowledge and involvement of Uni-Brand. In periods 05/06 and 08/06 Uni-Brand's total net purchases were £446,778,400 and its sales were £446,777,100 with the company making a loss of £1,300. Mr Lam concluded that this would not occur in the course of legitimate commercial trade and it was indicative of the contrived nature of the transactions as part of a scheme to defraud the Revenue.

Findings on whether the tax loss was fraudulent and whether the Appellant's transactions connected with fraudulent VAT losses?

145. We considered the evidence in respect of the defaulting traders, contra-trader and transaction chains carefully and we should make clear that we did not simply accept the opinions expressed by the officers which we disregarded. We formed the view that we could not envisage how any serious challenge could have been made to such cogent evidence. We were wholly satisfied that HMRC had accurately traced the Appellants' chains of supply to tax losses caused by defaulting traders Mobiles 4 U and Mountgale via Uni-Brand acting as a contra-trader. We also found as a fact that Uni-Brand knowingly acted as a dishonest contra trader and that its transactions formed part of an overall scheme to defraud the Revenue.

146. In those circumstances we were satisfied that HMRC had proved to the requisite standard that the Appellants' transactions were connected to fraudulent tax losses.

Did the Appellant know, or should it have known that the transactions in this appeal were connected to fraud?

147. The evidence we heard related mainly to this principal issue. Given the volume of evidence before us, both oral and documentary, the following is intended as a summary of the points raised however we should make clear that all of the evidence was carefully considered.

148. HMRC relied on a numbers of factors as indicators that the Appellants knew or should have known that their transactions were connected to fraud.

The Appellants and Awareness of MTIC fraud

149. Both Gold and Horizon were sent a number of letters by HMRC in which the prevalence of fraud in the mobile phone industry was outlined. Ms Gellvear of HMRC exhibited the correspondence as part of her evidence which included the following:

- Letter to Horizon dated 9 August 2004 which stated that "HMRC hold serious concerns that the requested move to monthly returns would have the consequence that the Commissioners may be at risk of a higher volume of transactions by those persons intending to abuse the VAT system";

- Letter to Horizon dated 10 March 2005 in which HMRC refused the company's request to move to monthly returns as: *"following the extended verification exercise conducted in relation to your trading activity to date, the Commissioners have identified transactions involving goods that originated from UK traders, who have raised invoices charging an amount shown as VAT, but who have defaulted in their responsibility to discharge the amounts to Customs and Excise. The VAT, which remains unpaid by the persons at present, amounts to approximately £11.4m"*;

- By letter dated 3 August 2005 HMRC notified the Appellant that goods had been traced along a supply chain in which some transactions caused concern and led HMRC to conclude that tax had been lost;

- A letter dated 14 July 2004 from Redhill outlining the problems experienced by HMRC in the Appellant's trade sector;

- A letter dated 28 July 2004 outlining problems with MTIC trade;

- A letter dated 4 May 2005 notifying Horizon that it had been involved in trade *"where transactions have led to underpaid VAT";*

- A letter from Redhill to Gold dated 16 August 2005 requesting that it verify the VAT numbers of trading partners prior to a deal and outlining concerns regarding MTIC fraud;

- A letter dated 7 September 2005 reiterating the need to conduct due diligence on all business transactions and the need to verify VAT numbers at Redhill;

- A letter dated 30 September 2005 in which Gold was notified of tax losses connected to its 08/05 transactions. The supplier to Gold in these deals had been Globcom. Ms Gellvear noted that Horizon went on to trade with Globcom on 16 and 20 December 2005 after the letter had been sent;

- Letter dated 8 February 2006 which stated: *"following the extended verification exercise conducted in relation to your client's trading activity in the 06/05 and 12/05 VAT periods the Commissioners have identified transactions involving UK traders who have defaulted in their responsibility to pay the VAT to HMRC. The VAT, which remains unpaid by these persons, amounts to approximately £787,587. This is 44% of input tax claimed by your client for these periods"*.

150. In addition to correspondence sent to the Appellants by HMRC, a number of visits were also carried out to the companies, the most relevant being:

- On 18 February 2004 Horizon was visited prior to its VAT registration from which Ms Gellvear inferred that MTIC fraud had been one of the topics discussed;

- At a visit on 27 July 2004 HMRC left Horizon with all relevant MTIC Notices;

- On 6 September 2005 Ms Gellvear visited the Appellant. At the visit she discussed the potential problems of MTIC style trade and reiterated the importance of verifying VAT numbers with Redhill prior to transactions. Public Notices regarding Joint and Several Liability, Notices of Requirement to give Security and HMRC's Statement of Practice relating to invalid invoices were given to Mr Khan.

151. Mr Khan's written evidence set out how in February 2003 Mr Khan had been a taxi driver and how he subsequently came to acquire 2 companies which traded in the same manner and same goods. He explained that Horizon was purchased off the shelf for approximately £150. Prior to this he had run a retail shop trading as "Top Fashion" and had been director of Ishtar Trading Limited which was a wholesaler of textiles. Ishtar Trading Limited had achieved a turnover of almost 500,000 in the year ended 31 May 1996. Horizon started trading in textiles in February 2003; the company's first sale was on 24 February 2003 for goods valued at £6,115. The textile business was not good and an opportunity in mobile phones presented itself through Mr Suhail who was a director of Farouk and Suhail Trading LLC based in Dubai. Mr Suhail was a longstanding friend. Throughout 2004 Mr Suhail offered to help and became the company's main customer. In order to conduct research and source stock Mr Khan looked at mobile magazines and various websites. In oral evidence Mr Khan stated:

"A. I know Suhail from Pakistan…

Q. And what happened…?

A. Then I don't remember if he said to me or I said to him – I said to him, you know – he said, "why not come into the mobile phone business?", you know, and I said to him, "where do you buy it?" He said, "Buy from the UK as well" and he said to me, "If you can source the goods"…he said to me, "I buy it from the UK as well" and I said, "Well, if I source the goods can you buy?" He said to me, "If the price is right.""

(Transcript 22 January 2014 page 26)

152. In cross examination Mr Khan was asked:

Q. Why did he suggest that a man who dealt in clothing would be a suitable wholesaler of mobile phones?

A. I had retail experience. I have also experience…I did business for long time. For me to change one commodity other commodity is no problem.

Q. What was your expertise in mobile phones?...

A. I made the research.

Q. By buying a magazine from WHSmith?

A. Well, magazine give you quite a lot of information."

(Transcript 22 January 2014 page 66 – 67)

153. Mr Khan noted that the Company's annual return dated 12 January 2006 made it clear that Horizon was involved in, inter alia, the wholesaling of mobile phones.

154. Mr Khan was aware of Gold as its former director was a relative of his wife. However he was unaware of an unpaid liability in the sum of £1,207 to HMRC until approximately July 2005. As Mr Khan hoped to engage in retail as well as wholesale, his accountant advised that it was preferable to have two separate trading vehicles. The retail outlet never came to fruition as the right premises could not be found.

155. Mr Khan could not explain why his accountant, in a meeting with Ms Gellvear on 6 September 2005 had stated that the reason for two companies was to keep turnover below a certain level. Mr Khan stated that he had arrived at the meeting later and was unaware this had been said. Mr Khan denied having confirmed the accountant's comment to Ms Gellvear as recorded in the visit report.

156. Mr Khan confirmed in oral evidence that he was aware of the prevalence of fraud in the mobile phone industry and he had received warnings from HMRC. As regards warnings given by HMRC to Mr Khan that his transactions prior to those in these appeals were connected to tax losses and in which Globcom was the supplier Mr Khan stated:

"Q. This letter told you that two of your transactions had been linked to tax losses exceeding £326,000…you knew that these particular deals involved you being supplied by Globcom…as a result of receiving this letter you spoke to Mr Iqbal…?

A. I went…there, he wasn't there, so I met his manager. Then he called me couple of times…They gave me the assurance that that will never happen again and they gave me the assurance that they stopped trading to his supplier who supplied these Nokia 7610.

Q. And you believed him?

A. I did believe him.

Q. Did you ask for that assurance in writing?

A. No.

Q. Why not?

A. I trust him, believe him, and what he say.

Q. Because he is somebody you had dealt with on a number of occasions.

A. It's not that. It's just…

Q. What caused you to trust him and believe him then?

A. Well, I just believe him. You know, talk to me seriously, called me a few times and say he's spoken to his suppliers…and the suppliers say they don't know anything about this…"

Commercial Checks

157. Ms Gellvear set out the due diligence documents provided by the Appellants. She noted that a due diligence report on its freight forwarder Interken was carried out by a company called Veracis almost one year before the relevant transactions.

158. The Appellants also produced a report by Veracis on its supplier Edgeskill. The report was dated 18 April 2006, 2 months prior to the first of the deals in this appeal. No negative indicators are flagged up by the report but Ms Gellvear noted that Veracis acted as a VAT advisor to Edgeskill. Two trade references were also produced by way of due diligence on Edgeskill. The references came from The Export Company ("TEC") and Globcom, although Ms Gellvear queried why there was a reference from TEC when the trade reference form offered Globcom and Our Communications Ltd as references. Ms Gellvear noted that the reference from TEC was poorly worded and referred to Edgeskill as *"Edgeskills"*. The reference by Globcom states that they have *"known the director of Horizon Import Export for over 18 months"* but no mention is made of Globcom's relationship with Edgeskill. The Redhill VAT verification undertaken by the Appellants on Edgeskill post dated the

June transactions although a Europa check had been carried out on 27 June 2006; the date of the transaction and Mr Khan had telephoned HMRC's National Advice Service to validate the VAT numbers of both Edgeskill and MK Digital on 27 and 28 June 2006. A positive Checksure report was also produced by Mr Khan which pre-dated the June deals. Ms Gellvear noted that Edgeskill had indicated on the supplier declarations supplied by Horizon that the goods were not being sold at current market value. Edgeskill had deleted the comment on the document *"These goods are supplied to you at the current market price."* Edgeskill subsequently stated that this had been done in error. The oral evidence of Ms Gellvear was:

"Q. ...if we just leave the circumstances of Edgeskill, Horizon and Gold to one side, if goods that a business holds drop in price or drop in value I should say, and they have to be sold at a loss, would you agree that in general terms the price that they are being sold at would now be the market value?

A. Yes."

(Transcript 21 January 2014 page 73)

159. Mr Khan stated that initial contact was made to Edgeskill via telephone; he believed he obtained the company's details from the IPT website. Edgeskill sent its company details on 5 October 2004 and Horizon sought verification of its VAT number through Redhill on 6 October 2004. Mr Khan also visited Edgeskill at its London address in May 2006 and its head office in Rochdale in June 2006. Various documents were obtained from the company director Mr Adeel Rashid such as passport, driving licence and office bills. Mr Khan also checked the company's annual accounts for the year ended 30 June 2005 in addition to the Checksure credit check and Veracis report. He clarified that the Globcom reference was submitted in error.

160. Prior to undertaking the transaction with Edgeskill Mr Khan faxed Redhill on 23 June 2006. Further faxes were sent on 27 June 2006 (the day of the deal) and 12 July 2006; no response was received until July 2006.

161. A due diligence pack on M K Digital was provided which was dated 2004. Ms Gellvear queried the value of the information contained therein given it pre-dated the deals by 2 years. A credit scoring agency called @rating considered MK Digital as above average risk in 2004 and a Dun and Bradstreet report dated 7 July 2006 (which post dates the June deals) assessed the company as fair risk (slightly greater than average). Two Europa validations were provided; one pre-dated the June deal and one was the same date as the deal. A Redhill response dated 13 July 2006 stated that it could not confirm that the registration was valid. MK Digital completed a trade application form which provided Edgeskill as a reference. Ms Gellvear queried how Horizon was able to participate in transactions when its supplier and customer were known to each other to such a degree that Edgeskill was offered as a reference. There is also no evidence that Mr Khan queried the relationship between MK Digital and its accountant which was stated on the trade application form to be *"other than through normal business relations."* In oral evidence Mr Khan could not recall whether he had noticed the comment or queried it. HMRC also highlighted the fact that PwC who had

provided a reference had failed to complete questions as to whether MK Digital was up to date with its accounts. Mr Khan stated that he had spoken to them by telephone:

"We did ring them and ask them and they gave us some information. They said, "Oh, we will forget about this", that's what they explained to us.

Q. I see. So, did you ask them for a replacement reference?

A. I did. I did send them, sir. I did send them that letter then.

Q. Did they send it back to you completed?

A. No. I don't think the letter came back. We called them back and they said the letter – they didn't receive the letter, then called them back. They said, "we posted the letter"…"

(Transcript 22 January 2014 page 130 – 131)

162. Mr Khan's written evidence stated that he had visited MK Digital in Cyprus in 2006 when he was provided with documents such as the director's identification, utility bills and a Dun and Bradstreet report which pre-dated the release of the goods. Mr Khan also checked the company's VAT number via the Europa website on 18 May 2006, 23 and 27 June 2006 and 13 July 2006. Letters were also sent to Redhill but no response received until 5 September 2006. However validation of the VAT number was also provided by the National Advice Service on 27 and 28 June 2006.

163. Goods in transit were insured through Interken Logistics based in Dubai under a Marine Open Policy dated 27 June 2006 for £9,900,000. Ms Gellvear concluded that the terms of the insurance policy had been breached in that the policy required goods to be packed in neutral boxes and consignment shrink wrapped however the inspection report shows that the stock was in its original packaging and there was no evidence that Mr Khan arranged for the goods to be shrink wrapped. Furthermore the policy states that CMRs should not indicate that the goods are mobile phones however the documents provided by Gold do state that the goods are mobile phones.

164. Mr Khan asserted that despite having been told by Ms Gellvear that there was no legal requirement for due diligence on freight forwarders, he nevertheless visited Interken on many occasions and obtained verbal trade references from other mobile phone traders.

165. Ms Gellvear concluded the due diligence was perfunctory in nature and did not appear to be genuine attempts to test the credibility of suppliers or customers. She denied ever having told Mr Khan that the Appellants' due diligence was "*more than enough*".

Nature of trading

166. Mr Khan's written evidence on behalf of Horizon stated that he received a written request for stock from MK Digital. Thereafter he telephoned potential

suppliers and advertised for stock on the IPT website. He noted down a number of offers he received but did not retain these records. On 23 June 2006 he was contacted by Sandeep from Edgeskill. Although he had previously spoken to Sandeep, the companies had not traded. Negotiations over stock took place over the course of a few days as Mr Khan believed the price given by Edgeskill was too high and better prices had been received from other traders. On or about 26 June 2006 Sandeep agreed to match the offers received and also stated that the stock was available immediately which was critical as other traders had a lead time of 4 – 6 weeks. Mr Khan's written evidence stated that he was not aware that Edgeskill made a loss on the transactions; he believed that the goods were being purchased at market value as a similar price was offered by other potential traders. As regards the supplier declarations completed by Edgeskill, Mr Khan stated that he contacted the company upon receipt and was told by Sandeep that a mistake had been made in crossing out the sentence *"these goods are supplied to you at the current market rate"*. Mr Khan's written evidence also stated that he *"knew that Edgeskill had paid more for the goods than they were going to charge us – Sandeep told me this when we were negotiating the price."* In a subsequent written statement in respect of Gold, Mr Khan stated: *"The company had no knowledge of the price which Edgeskill paid for the stock."* In his third witness statement Mr Khan accepted the contradiction, stating: *"I was aware that Edgeskill were sending the goods at a loss. I was not aware of the quantum of the loss."* In oral evidence it was stated:

"Q. Now, as far as you were concerned and your purchase from Edgeskill, did you think that the price you were paying was the market price, below the market price or above the market price?

A. It was the market prices because I had been after goods, simple prices."

(Transcript 22 January 2014 page 35)

167. Ms Gellvear highlighted the back to back nature of the transactions and the fact that quantities of goods were matched without any delay or excess stock left over.

168. Two inspection reports prepared by Aberdale Inspections Limited ("Aberdale") were produced by the Appellant. The reports were dated 28 June 2006 (21,000 Nokia 8800s) and 30 June 2006 (9,000 Nokia 8800s). The reports declare that Aberdale had carried out a 100% physical inspection of the goods although Ms Gellvear noted that there was no evidence to show that anything other than an external examination had been carried out. Ms Gellvear queried Mr Khan's assertion that he requested that Aberdale inspect the stock on 27 June 2006 as records obtained from Interken indicated that 30,000 Nokia 8800s did not arrive in the UK until 30 June 2006. This raised a further query in that the CMRs provided by Mr Khan purported to show that the bulk of the goods were exported on 28 June 2006:

"Q. …Do you think it is possible that Inteken have mistakenly put the wrong date for the goods in in this ledger?

A. It's possible, yes.

Q. Mr Khan has told me that he thinks from his visit to Interken that there may be a laxity in recording goods in if they are going out very quickly. Do you have any knowledge of Interken that you could agree or disagree with that?

A. I don't, but isn't that part of Mr Khan's due diligence? If he thought they were going to be lax, why was he using Interken as a freight forwarder?"

(Transcript 21 January 2014 page 86 – 87)

169. On the same issue Mr Khan stated:

"I had been told Sandeep the phones are at Interken.

Q. And did you have any reason to think that was untrue?

A. No, I believed it.

Q. Now, we know that some of the goods didn't go out from Interken until much later. Could you tell the Tribunal, please, a little bit about what you know or what you were told as to the reason for the delay?

A. I called many times to Interken and they gave me a few reasons. They say it's holiday, they're very busy, the manager, the export manager is not well. So that's the three reasons they gave me."

(Transcript 22 January 2014 page 37)

170. Mr Khan denied in oral evidence that he had been manipulated by others:

"Q. …Do you remember Mr Gibbon using the word "patsy" yesterday?...Somebody who is used by others?

A. Nobody used me.

Q. Nobody used you. You were not anybody's patsy then?

A. No...

Q. …We know that there was fraud…and it appears that it was your old friend, Mr Iqbal, who was right in the thick of it…

A. Mr Iqbal, I had no relationship with him personally…

Q. You told Mrs Gellvear on 6 September 2005 that he was your personal friend.

A. No…I reject that submission…Obviously I traded with his company. Personal friend is that you go out for dinner, you go out your house, you see each other, you drink together…but what I did, I traded with his company.

Q. 19 transaction chains which your company, Horizon, features in, Mr Iqbal's companies supplied you directly on eight occasions. Almost half of them.

A. So what does it make different…

Q. Where is Mr Iqbal?

A. I don't know. Nothing to do with me where's Mr Iqbal.

Q. When did you last speak to him or have contact with him?

A. I think long time ago.

Q. When?

A. Probably 2006.

Q. You have not spoken to him since these deals?

A. No.

Q. No contact with him at all?

A. I don't think I have had."

(Transcript 22 January 2014 page 56 - 63)

171. Records obtained by HMRC from Interken indicate that 25,000 Nokia N72s were not received by the freight forwarder until 11 July 2006 which may explain the delay in Horizon shipping the goods which took place on 12 and 24 July 2006. Ms Gellvear queried why Mr Khan did not know the whereabouts of the goods at the time he entered into the transaction.

172. As to where the N72s were when purchased, Mr Khan stated in oral evidence that he had *"no idea"*; he thought he may have asked Sandeep a Edgeskill but was told to call Interken, which worried him. Mr Khan had then called Interken; in cross-examination Mr Khan initially stated that he did not recall being told that the goods had not arrived but later stated he thought he was told.

173. Ms Gellvear highlighted a letter from Aberdale to Mr Khan dated 15 February 2008 in which it stated that where IMEI numbers had been requested but not obtained, the reason would have been time constraints at the time of the inspection. Ms Gellvear noted that Gold did not in fact ship the goods until 28 and 30 June 2006 and did not release those goods until 26 July 2006. In oral evidence Ms Gellvear confirmed in respect of IMEI numbers for previous transactions exhibited to Mr Khan's third witness statement in May 2011 that the numbers had not previously been provided to her nor was there any information provided with the lists of numbers which would enable them to be matched up with a particular consignment or particular date. The evidence went on:

"Q. …Mr Khan says: "I kept the IMEIs for each transaction the company entered into, checked against them when entering into a new transaction to ensure that the company did not buy the same stock on more than one occasion…I was asked by Miss Gellvear to provide IMEIs. I provided them…" Is that correct?

A. No, it's not.

Q. As far as you are concerned, were you ever supplied with IMEI numbers?

A. Not that I'm aware of, no….

Q. …In order to be any use to Mr Khan, what would he have to do with these numbers?

A. Mr Khan would have had to keep a record of the mobile phone IMEI numbers that he had bought, to see if he had bought them in the past and be able to check them against.

Q. From the information that you have seen in this file, is it apparent to you how he could achieve that?

A. No."

(Transcript 21 January 2014 page 44 – 45)

174. Mr Khan's written evidence explained that he instructed Aberdale to conduct 100% external box checks and 10% internal box checks. Aberdale was also instructed to check that the seals had not been broken and to scan the IMEI numbers. Mr Khan stated that he "*kept the IMEIs for each transaction the Company entered into, checked against them when entering into a new transaction to ensure that the Company did not buy the same stock on more than one occasion. A couple of times I was asked by Ms Gellvear to provide IMEIs. I provided them but she subsequently indicated that she had been too busy to check them."* He clarified that where Aberdale had informed him that there was insufficient time to scan the IMEI numbers, in the last few transactions Mr Khan did not have time to arrange a scan. Mr Khan stated he had paid the inspection company for conducting an IMEI scan even though it was not in fact carried out.

175. Ms Gellvear queried what value the Appellant added to the supply chain given the fact that the Appellant and its supplier claimed to find customers through websites on which traders advertised stock.

176. HMRC also relied on the lack of written terms and conditions as an indicator of knowledge or means of knowledge on the part of the Appellants. Ms Gellvear highlighted the fact that neither the Appellants nor their trading partners had written contracts other than purchase orders and invoices. There was, therefore, no written record of agreement on commercial issues such as shipping terms, insurance, date and method of payment or responsibility for faulty goods. In oral evidence Mr Khan was asked when he was due to pay Edgeskill:

"Q. …What was agreed between you as to when you paid them?

A. After the inspection of the customer.

Q. And where does it say that?

A. Discuss with them "ship on hold" basis.

Q. It doesn't say on any of these documents when you were due to pay Edgeskill, does it?

A. No, it doesn't say, sir.

Q. Why wouldn't Edgeskill make it a contractual term as to when they were going to be paid?

A. That was the normal practice for the ship on hold basis in the mobile phone industry, sir…

Q. Edgeskill's terms of sale agreement…There is actually a term as to when payment is to be made in clause 6: "Full payment must be made at the time the stock is allocated to the customer." This stock was allocated to you…on 27 June but you didn't make payment then did you?

A. No

Q. Why not?

A. They agree with me, "ship on hold" basis…

Q. You signed these terms…didn't you?

A. Yes.

Q. So when did you come to this verbal agreement?

A. On the 27th, sir…"

(Transcript 22 January 2014 page 147 - 149)

177. As regards the issue of faulty goods, Mr Khan stated in his written evidence that if the customer returned to the retailer who is warranted by the manufacturer, e.g. Nokia, the retailer would pass on the claim to a Nokia authorised service company for repair as all Nokia phones are subject to warranty.

178. Ms Gellvear noted the significant increase in turnover of both Appellant companies within a short period of trading. Taken together with Mr Khan's lack of technical knowledge about the products he traded and lack of experience in the trade sector, Ms Gellvear concluded that the Appellants trading fell far short of that expected of a legitimate company.

179. Mr Khan set out the turnover figures for Horizon, which he considered as *"standard for this type of commodity trading"* as follows:

- £109,221 for y/e 31/3/04
- £3,027,374 for y/e 31/3/05
- £16,702,182 for y/e 31/3/06
- £5,400,000 for y/e 31/3/07

180. It was noted that all of the traders in the chains of supply held accounts with the FCIB which was used by many MTIC traders prior to the arrest of the principal shareholder.

181. HMRC highlighted the lack of documentation to support Mr Khan's assertion that negotiations took place on price nor has he provided any explanation as to how figures were arrived at. Mr Khan contended that he did have handwritten notes but they have been lost over the years.

182. Mr Khan could not explain why MK Digital and Edgeskill did not trade directly when the evidence showed that the parties were known to each other. In oral evidence he made the following analogy:

"Let me put it to you this way. I was trading mobile phones. If somebody come to me asking something and I was there to source the goods, you know. Another example: if somebody go into Marks and Spencer, buy something, Marks and Spencer, they will say "Why do you come to us, why do you not go to Tesco."

(Transcript 22 January 2014 page 111)

183. Mr Khan went on to explain that the delivery date arranged with MK Digital was "as soon as possible" but he could not say whether this meant days, weeks or months. The lack of details contained on the inspection reports was put to Mr Khan:

Q. As regards their specification for the phones, this was as detailed as it got, was it?

A. Yes.

Q. No other details specified as to what sort of phones they wanted, for example, what colour the N72s were to be.

A. I think I say on inspection report black…

Q. But I think actually with regard to the inspection report, this document does not say what they wanted, what colour.

A. Yes…he told me…black…

Q. We do not see that written here. You have written "Silver 8800s"…This document does not specify a central European specification, does it?

A. No, it doesn't.

Q. It does not specify what accessories they want.

A. Accessory would come with the mobile phone.

Q. What software.

A. I'm sure everybody aware of software…"

(Transcript 22 January 2014 page 113 – 115)

184. The goods were shipped on hold and not released to a customer until payment made:

"A. "Ship on hold" meant both – he agreed with both parties, customer and supplier, whoever at that time is your supplier – ask them to allow to ship the goods on hold and when – if the suppliers agree then you ship the goods to wherever your customer's destination is and the customer check the mobile and inspect it. After the inspections, they make 100% payment. When they receive the payment, our action "forward payment to supplier". Action: Horizon and Gold release note, you know, and the supplier releases the goods with this notice…

Mr Robertson: So, there are two release notes, one from your supplier and one from you?

A. It depends how many in the chain. Yes, so, you know, I don't know entirely but my concern…

Mr Robertson: Are you saying there could be lots of release notes if there are other suppliers down the chain?

A.Yes

Mr Robertson: So, there may be four, five or six release notes?

A.I don't know. That's something I can't talk about."

(Transcript 22 January 2014 page 47 – 49)

185. Ms Gellvear noted the assertion by Mr Khan that goods were shipped on hold to MK Digital which. HMRC submitted, highlights a high level of trust between the parties who had previously not traded with each other.

186. Mr Khan was cross-examined about legal title to the goods. It was noted that the Appellant's terms and conditions specified that *"The goods shall remain the property of Gold UK Consulting Ltd until payment is received."* When asked if the Appellant

owned the goods when the invoice was issued, Mr Khan explained that they were allocated to the Appellants and the title remained with the supplier until the supplier was paid in full:

"Q. So, when you said they remained the property of Gold UK Consulting, they weren't your property at all.

A.They were my property but the goods were allocated to them.

Q. That doesn't give you property though does it? It doesn't give you title, to use your word, does it?

A. Well, I mean, English is my second language.

Q. You used the word "title". You must know what it means. I didn't introduce that.

A. I did it to the best of…language. I am not a solicitor or a lawyer. I can't do better than them and I didn't know I was going to end up in a court…I'm just saying these phones were allocated to Horizon and Gold. When Horizon and Gold received the payment from the supplier, then we hand over all payment to the supplier and the supplier releases the note and we release the note."

(Transcript 22 January 2014 page 137)

187. In respect of earlier repayments made by HMRC Ms Gellvear confirmed that each claim had been paid on a *"without prejudice"* basis and at no time had Mr Khan been told that HMRC was satisfied with his method of trading. She added in oral evidence:

"…I think at that time I had no legal recourse to stop his repayments.

Q. I am struggling with this as to what the difference is between the legal recourse in…March 06 and June 06…

A. Yes, it was the departmental policy that at that time we would release those repayments, then come June 06 the departmental policy was that we would stop them if there was tax losses within the deals…"

(Transcript 21 January 2014 page 47 – 48)

188. Mr John Fletcher, a director of KPMG LLP ("KPMG") provided the Tribunal with a detailed report about the grey market for UK based distributors of mobile handsets in 2006. He has over 15 years' experience in the telecoms industry and has held positions in audit, accounting, corporate finance and international business development.

189. Mr Fletcher's witness statement covered a number of generic topics, which can be summarised as follows:

- General background to the mobile phone handset market;
- The characteristics of the authorised mobile phone handset distribution market in the UK and abroad;
- Alternative trading opportunities: the grey market;
- Conclusions

190. The statement of Mr Fletcher was unchallenged. Due to the generic nature of its contents we will summarise the principle points.

191. The grey mobile phone handset distribution market arises from the failure of the authorised mobile phone handset distribution market to meet fully the needs of certain participants in that market. There are two categories of market failures in the distribution market: price-related market failures and volume-related market failures.

192. Price related market failures give rise to two forms of market opportunities; arbitrage and box-braking. Arbitrage takes advantage of the opportunity created by differentials in the gross price between countries, and box-breaking takes advantage of differences between gross and net prices.

193. The volume-related opportunity occurs as a result of over or under-stocking by the AD or the retailer. When a retailer under-stocks, volume shortages arise, and when the AD overstocks, the dumping (i.e. sale of old stock which is now surplus to current requirements) opportunity arises.

194. The presence of the following negative indicators would be sufficient to conclude that a trader is extremely unlikely to be exploiting rational arbitrage opportunities:

- Trading in Nokia stock excludes traders from pursuing arbitrage opportunities as Nokia sets homogenous pricing for its customers across all territories. The absence of price differences fails to meet the basic criteria for arbitrage;
- Taking an unreasonable volume of specific handsets that represent an unrealistic market share of the total volume sold through non-OEM-sourced distribution channels in Europe;
- Generic product descriptions documented on purchase orders and invoices which as a minimum must include information regarding the warranty, battery, charger, languages and any auxiliary software;
- Traders not sourcing stock from OEMs or Ads and additional suppliers in the chain;
- 100% of the trades being successful 100% of the time;

- Purchasing mostly from suppliers other than OEMs or Ads despite trading sufficient volumes to secure those supply relationships with such parties;

- Permitting additional traders to enter the deal chain.

195. The presence of the following negative indicators would be sufficient to conclude that a trader is extremely unlikely to be exploiting rational volume shortage opportunities:

- Clear and detailed descriptions of handsets;

- Lack of own stock or rapid access to the exact stock required;

- Trading an unreasonable volume of specific handsets that represent an unrealistic market share of the total volume sold through non-OEM-sourced distribution channels in Europe;

- Purchasing from suppliers other than OEMs or Ads despite having sufficient volumes to secure those relationships and supply chains.

196. The presence of the following negative indicators would be sufficient to conclude that a trader is extremely unlikely to be exploiting dumping opportunities:

- Trades initiated by customer request;

- Trading an unreasonable volume of specific handsets that represent an unrealistic market share of the total volume sold through non-OEM-sourced distribution channels in Europe;

- Lack of own stock;

- Purchasing from suppliers other than OEMs or Ads despite having sufficient volumes to secure those relationships and supply chains;

- Generic product descriptions documented on purchase orders and invoices.

197. Mr Fletcher concluded that within the mobile phone handset market there is an authorised market and a grey market. The presence of any of the negative indicators set out above would indicate that a distributor is extremely unlikely to be exploiting a rational grey market opportunity.

198. In oral examination Mr Khan stated that he had not read Mr Fletcher's evidence in full as it was an opinion. In Mr Khan's view the inspection provided all product information, although he accepted by the time of those reports he had already bought and sold the goods. Mr Khan explained that further information about the products was available online and the availability of phones was a result of "dumping" surplus stock. In respect of specification Mr Khan was unsure whether there were any other European specifications other than Central European, although he believed there must be.

199. HMRC adduced evidence from Officers Letherby, Everett and Ellis which demonstrated that a number of participants in the Appellants' transaction chains made payments between FCIB accounts using the same IP addresses. By way of example:

Date	Payment From	Payment To	Time	IP Address
22 July 2006	Call Back Trading	Link Maze Trading	18:30:03	83.110.197.89
22 July 2006	Link Maze Trading	Regent Sp z.o.o	18:39:04	83.110.197.89
22 July 2006	Regent Sp z.o.o	Neo Abaco	18:42:05	202.134.185.31
22 July 2006	Neo Abaco	MK Digital	18:45:02	202.134.185.31
22 July 2006	MK Digital	Gold	18:51:08	83.110.197.89
22 July 2006	Gold	Edgeskill	19:18:03	82.23.81.149
22 July 2006	Edgeskill	Uni-Brand	19:36:07	217.135.181.64
22 July 2006	Uni-Brand	Falcon Trading International	19:54:01	83.110.197.89
22 July 2006	Falcon Trading International	Artlons Trading Ltd	19:57:09	83.110.197.89
22 July 2006	Artlons Trading Ltd	Wall Street General Trading	20:15:03	87.228.133.78
22 July 2006	Wall Street General Trading	Call Back Trading	20:21:08	83.110.197.89

200. We should note that the Appellants did not share an IP address with other traders. HMRC relied on this as evidence of not only contrivance in the chain but also, on the basis that payment were made within relatively short periods of time and profit margins were consistent, of knowledge on the part of the participants of the chains who, HMRC submitted, must know when and to whom to make payments.

201. Mr Khan stated that he used the FCIB as it offered a 24 hour internet service which made it possible to complete deals within minutes; no other bank offered such a service. In oral evidence Mr Khan could not comment on other traders' shared IP

addresses; a fact he stated he was wholly unaware of until the evidence was served by HMRC.

Submissions

202. On behalf of HMRC Mr Puzey submitted the following features of these appeals indicated knowledge or means of knowledge on the part of the Appellants through Mr Khan:

- The circumstances in which Mr Khan purchased Horizon for £150 and took over Gold from a relative having previously been a wholesaler and market trader of clothing and a taxi driver whose knowledge of the mobile phone industry was attained from reading magazines purchased from WH Smith;

- The significant turnover achieved by the Appellant despite no previous experience in the industry;

- The unchallenged evidence of Ms Gellvear that every one of the Appellants' transactions that could be traced was found to lead back to a tax loss;

- The fact that Mr Khan was fully aware of the prevalence of MTIC fraud when viewed against his evasive answers on this issue in cross-examination and generally unconvincing evidence;

- The lack of any action taken by Mr Khan to change his methods of trading despite receiving three notifications of tax losses in his transaction chains;

- Mr Khan's implausible explanation that the availability of mobile phones may have been a result of the dumping of excess stock; evidence which is rebutted by the unchallenged evidence of Mr Fletcher;

- The unchallenged evidence of Mr Fletcher that the Appellant's business model of looking at websites and calling up other grey market traders was not consistent with genuine grey market trading;

- The lack of clear and detailed specification on the purchase orders and invoices taken together with the Appellant's lack of record keeping and uncertainty in evidence regarding the difference between European and Central specification phones;

- The questioned raised by references provided, in particular in respect of MK Digital, which remained unanswered and were not chased by Mr Khan,

- The splitting of loads purportedly to facilitate the movement of the goods out of the UK when viewed against Mr Khan's inability to explain how such movement would be facilitated by the split;

- Mr Khan's inability to explain the statement on his invoices that the goods were the property of either Gold or Horizon when each participant in the chain purported to retain title;

- Mr Khan's willingness to export £15,000,000 worth of goods without knowledge of their destination and before payment was received;

- The anomalies in the inspection reports, in respect of IMEI numbers and Interken's records as to when goods arrived at their warehouse;

- The fact that Mr Khan had no idea where the N72 phones were when he bought them and his unconvincing evidence on the matter under cross-examination;

- The circularity of payments within short time scales;

- The earlier repayments to the Appellant in 2005 and early 2006 do not affect the information that was available to the Appellant at the relevant time and were, in any event, made on a *"without prejudice"* basis and therefore cannot be relied upon as an assurance that the Appellants' trading was not connected to fraud.

203. On behalf of the Appellant Mr Gibbon submitted that HMRC have failed to establish knowledge on the part of the Appellant. Furthermore it cannot be said that they should have known that *"the only reasonable explanation"* (see Moses LJ in *Mobilx* at [60]) was that the Appellants transactions were connected to fraud.

204. It was submitted that it would have been impossible for Mr Khan to discover anything, including the identity of suppliers further up his chains of transactions and even if Mr Khan had been able to conduct full due diligence on the suppliers in the Appellants' chains, no tax losses would have been discovered.

205. The evidence adduced by HMRC regarding the grey market is obtained with the benefit of hindsight and it would be unjust to judge a trader by knowledge acquired in later years. By way of example Mr Gibbon referred us to Mr Fletcher's report at paragraph 1.1.4 which relies on many source materials from 2007 and onwards, which post date the periods with which these appeals are concerned. Similarly the evidence of Mr Ellis was obtained so late that it was served within a week of the hearing.

206. It was submitted that HMRC's primary case is knowledge and that means of knowledge is a subsidiary allegation put almost as an aside.

207. Mr Gibbon submitted that the evidence of Mr Khan was straightforward and honest. The Tribunal should accept the evidence which withheld scrutiny under robust cross-examination. In response to the factors relied on by HMRC in support of its case on knowledge the Appellant submitted:

- The observation regarding the increase in turnover over a short period is made with the benefit of hindsight over 7 years after the event. This was not a fact

which was necessarily obvious to a small businessman in 2006 or even HMRC who consistently made repayments to traders until June 2006;

- HMRC's actions in making repayment would cause a trader to perceive that his transactions were not linked to fraud;

- HMRC did not suggest that the Appellants' businesses were involved in a wholly contrived market and it is unreasonable to suggest that the Appellants' level of trading is evidence of knowledge of fraud;

- Mr Khan's evidence regarding the purchase of Gold as a retail outlet was compelling;

- The fact that the chains of transactions that could be traced by Ms Gellvear (including those which do not form part of these appeals) led back to tax losses is not surprising with the information now available as to the prevalence of fraud;

- Combining both Appellants' transactions pre-June 2006, there were 12 purchases were from Globcom, 1 from Uni-Brand and 9 from unrelated suppliers. Although Globcom was an important supplier, it does not merit HMRC's description as "supplier of choice";

- There is evidence of commercial trading by the Appellants in that no transactions were undertaken in 03/06 as the VAT element of deals could not be funded until repayments made by HMRC. Had the Appellants been knowingly involved in a contrived scheme it is likely that loans would have been provided to enable the Appellants to trade;

- Mr Iqbal at Uni-Brand was not a personal friend of Mr Khan's. This allegation was buried in the minutiae of a visit report and made for the first time in HMRC's skeleton argument. Denial of this allegation was not put to Ms Gellvear in cross-examination as a result of the Appellants' representative being instructed late in proceedings and mistakenly over-looking the point for which the Appellant should not be penalised. Mr Iqbal was no more than a business acquaintance/colleague and it was submitted that Ms Gellvear was mistaken on the point;

- Ms Gellvear was also mistaken in her visit report in asserting that Mr Khan was personal friends with Farouk of Farouk and Suhail, the company in Dubai who suggested that Mr Khan start trading in mobile phones. Mr Khan was in fact friends with Suhail. It should be borne in mind that Ms Gellvear had also been inaccurate about Mr Khan's earlier employment commenting that he emptied bins, a statement which she later withdrew;

- Mr Khan took action when informed that tax losses had been found in his transaction chains where goods were purchased from Globcom; he attempted

to see Mr Iqbal in London without success but spoke to him and accepted Mr Iqbal's word that he would not trade with the particular suppliers again;

- The notifications sent by HMRC regarding transactions traced back to tax losses did not specify the transactions in question nor the proportion that led to tax losses. Taken together with the repayments made by HMRC to the Appellants, Mr Khan was reasonably entitled to continue to trade;

- It is unreasonable to assert that success in trading is evidence of knowledge;

- It can be inferred from the insertion of Horizon into deal chains between Edgeskill and MK Digital who knew each other that those traders sought to add an innocent trader into transactions;

- Although Mr Fletcher's evidence rebuts the suggestion that "dumping" explained the circumstances of the Appellants' transactions, that evidence was not known in 2006. Furthermore Mr Fletcher's evidence supports the assertion that "dumping" did occur;

- In any event, Mr Fletcher's opinions are irrelevant to the issue of knowledge;

- Precise specifications of the goods were recorded by the inspection company Aberdale. Furthermore, Mr Khan explained that full specifications were available online;

- The fact that the Appellants were able to source and match goods does not indicate contrivance nor knowledge, if such contrivance existed, on the part of the Appellants;

- The Appellants did not share IP addresses with others in the chains of transactions which supports the submission that the Appellants were unaware of the contrived nature of the deals;

- It is accepted that certain parts of due diligence were not followed up however the inference to be drawn by HMRC highlighting these small points is that there is little to criticise in relation to the remainder of the due diligence;

- Mr Khan's evidence that splitting a load into smaller parcels to allow the freight forwarder flexibility in transport was compelling and reasonable;

- The argument that the Appellant exported £15,000,000 worth of phones abroad prior to payment misses the point that the goods were shipped on hold until release. Presumably the same action was taken by Edgeskill;

- The error on 11 supplier declarations by Edgeskill was, in reality, 1 error made on 11 documents. Furthermore Mr Khan accepted that he knew Edgeskill was selling at a loss (although he did not know how much but suggested £1 per unit) in which case the price was market price;

- It is obvious that, with the exception of the deposit paid, the Appellants must have agreed to pay Edgeskill when they were paid by MK Digital despite there being no record of that verbal agreement;

- The anomalies in the inspection report fax dates are explained by the fact that Mr Khan received verbal reports by telephone on the day of the inspections;

- Mr Khan accepted Aberdale's explanation that they had insufficient time to carry out IMEI checks and he was aware that inspections were carried out as close to the shipping date as possible. Furthermore, Mr Khan had ensured that IMEI checks were carried out on earlier deals and therefore the absence of such scans would stand out; if the deals were contrived he would surely have remedied this by ensuring IMEI checks were done;

- The anomaly in respect of Interken's stock records for arrival and shipping of the goods is clearly a mistake and takes the issue of knowledge no further;

- Mr Khan's lack of knowledge as to where the goods were when he purchased them posed no risk as he did not make payment until the goods were inspected;

- The payments made within short time periods is explicable by reference to the fact that quick payments are necessary in order that traders can give the appropriate release instructions to the freight forwarder as Mr Khan explained in evidence;

- That the Appellants' payments were not made using an IP address shared by other traders in the chain cannot sensibly be suggested as evidence of contrivance. To the contrary, it is suggestive of the fact that the Appellants were not closely connected to the other traders;

- HMRC did not inform the Appellants that Europa checks may be unreliable and in circumstances where Redhill responses were delayed Mr Khan took reasonable alternative steps such as the Europa site and National Advice Centre to validate the VAT numbers of those he traded with;

- HMRC gave no indication that the Appellants' methods of trading were in any way deficient which meant that Mr Khan's state of knowledge was such that he believed his trading did not point to participation in fraud. In those circumstances it cannot be said that the only reasonable explanation for the circumstances in which the transactions took place was that they were connected to fraud.

The Decision

Findings of fact on whether the Appellant knew, or should have known, that its transactions were connected to fraud.

208.We considered the law, oral and written evidence and submissions of both parties carefully in reaching our conclusions.

209.We should note at the outset that we found Ms Gellvear to be a credible and convincing witness and we were satisfied that minor inaccuracies in her evidence did not undermine the quality of it overall. We found Mr Khan to be less convincing; his evidence was vague and at times he appeared determined to avoid answering questions in cross-examination.

210.We were satisfied that the Appellants, through Mr Khan, were aware of the existence, prevalence and characteristics of MTIC fraud within the mobile phone trade sector and we assessed the nature of the companies' trading against this background.

211.The circumstances in which Mr Khan began trading in mobile phones was vague; as a result of his friendship with Mr Suhail, joining mobile phone web forums and conducting research through magazines, Mr Khan was able to achieve a significant turnover in a short period of time with no prior experience of the industry. There was no detailed evidence as to the understanding he had of the market, in fact to the contrary we found Mr Khan's evidence that *"…for me to change one commodity other commodity is no problem"* was indicative of his lack of any meaningful knowledge of the trade sector.

212.We concluded that the Appellants' turnover figures were, on any view, significant. We did not accept the Appellants' submission that the observation is made with the benefit of hindsight 7 years after the event; in our view any reasonable businessman would be aware of his turnover, at the very least in general terms, and we were satisfied that the rapid growth would have been obvious to Mr Khan as director.

213.We considered Mr Khan's evidence as to why he required two companies to trade. Whilst it may have been Mr Khan's intention to establish one company for retail and one for wholesale, we noted that there was no evidence to support this assertion such as a business plan. Even accepting that this was the case and no suitable premises could be found for the retail outlet, we queried why in those circumstances Mr Khan chose to trade through both companies in wholesaling mobile phones, for which no explanation was provided.

214. We noted the letter dated 30 September 2005 in which Gold was notified of tax losses connected to its 08/05 transactions and in which the supplier was Globcom. That Horizon subsequently went on to trade with Globcom in December 2005 was in our view indicative of knowledge or means of knowledge on the Appellants' part. We found Mr Khan's evidence vague and unconvincing; he provided no reasonable explanation as to why he simply believed Mr Iqbal who stated he had changed suppliers particularly given Mr Khan's adamant assertion that Mr Iqbal was not a personal friend. Taken together with the total of three notifications about connection to tax losses, in our view any reasonable businessman seeking to protect himself from involvement or connection to fraud would have taken more active steps to change his

method of trading. We concluded that either Mr Khan had attempted to minimise his relationship with Mr Iqbal or he was content to conduct business without questions; either way we were satisfied that this supported the case for HMRC.

215.We queried what the Appellants added to the transactions such as would explain their participation. The Appellants did not alter the products and their trading partners were already known to each other. There was no evidence to demonstrate that the Appellant added value or provided anything beyond identifying a buyer and seller, yet significant mark ups were achieved. There was no explanation as to why the Appellant was able to achieve such profits, there being no identifiable addition made to the transactions. We found as a fact that this was indicative of the contrived nature of the transactions; a fact of which the Appellant must have been aware. Our view was reinforced by the contradictory evidence given by Mr Khan in respect of the loss made by Edgeskill in one of the deals and the supplier declaration on which Edgeskill had crossed out the statement *"these are supplied at market rate."* We considered the Appellant's submission, supported by a letter from Edgeskill, that the deletion had been no more than an error, albeit one repeated 11 times and we accepted that this was feasible. Mr Khan's evidence did not clarify matters for us; he stated that he knew that Edgeskill were selling at a loss but did not know the quantum. Mr Khan was then able to sell the goods at a profit. We accepted Mr Gibbon's submission that selling the goods at a loss does not necessarily mean that the price was not market rate however we queried how Mr Khan was then immediately able to sell at a profit if the market rate had forced Edgeskill to sustain a loss. Putting aside the minutiae of the deal, the fact is that Mr Khan did not query the peculiar nature of this scenario; either why Edgeskill had been forced to sell at a loss or why he was able to make a profit.

216. The transactions took place on a back to back basis and there was no documentary evidence to show that Appellant was ever left with unsold stock. That said, we could not be satisfied that this fact, of itself, was sufficient to indicate that the Appellant knew or should have known that the transactions were contrived.

217. We noted HMRC's reliance on the Appellant's use of the FCIB in which all accounts were suspended by the Dutch authorities in the autumn of 2006. There was no evidence to demonstrate that users of the FCIB or the public generally were aware of any such problems during the period with which we are concerned and we were not satisfied that this indicated knowledge or means of knowledge on the part of the Appellant.

218.Mr Khan highlighted in evidence that there was no legal requirement to retain IMEI numbers and we accepted that to be the case. However we found Mr Khan's evidence on the subject of IMEI numbers generally was vague and unconvincing. He stated that he had previously kept IMEI numbers but his evidence was unclear as to who had carried out checks of those numbers and how any such system worked. The lists of IMEI numbers relating to earlier transactions produced by Mr Khan were adduced late in proceedings and did not help clarify this issue for us, there being no identifiable way in which those numbers would have been used in subsequent deals. Furthermore we found the evidence that Mr Khan had paid for IMEI numbers to be scanned yet the service was not provided was a matter that any reasonable

businessman would have queried. We considered Mr Khan's evidence that he was told that time constraints had meant that the numbers could not be recorded, but this did not in our view explain why Mr Khan paid for the service or he simply seemed content to accept the excuse. We concluded that Mr Khan was attempting to minimise the Appellants' responsibility to conduct the type of efficient checks we would have expected of any legitimate trader seeking to avoid connection to fraud.

219.The evidence of Mr Fletcher was not challenged and we preferred the evidence of Mr Fletcher as to grey market opportunities to that of the Appellant, whose evidence that "dumping" of surplus stock provided the explanation as to why he could readily access large quantities of mobiles phones. That said, we agreed with Mr Gibbon that the statement of Mr Fletcher is generic and compiled with the benefit of hindsight. In those circumstances we found that although Mr Fletcher's evidence supported our view that the Appellants were not taking advantage of rational grey market opportunities, this did not assist us in determining the issue of knowledge or means of knowledge on the part of the Appellants. We should note that Mr Fletcher highlighted generic product descriptions documented on purchase orders and invoices as indicative that a distributor is extremely unlikely to be exploiting a rational grey market opportunity. Disregarding the view of Mr Fletcher, the lack of details such as colour and specification of phone on the Appellants' paperwork and those of its trading partners was clear. We found Mr Khan's explanation that details were easily obtained off the internet lacked credibility; in our view any trader would ensure that the details of his purchase and sale were recorded in order to guard against receiving goods or having goods returned as incorrect. We concluded that the absence of such details between the parties was indicative of knowledge that the deals were contrived.

220.Mr Khan's evidence regarding legal title to the goods and how goods were released was confused and unpersuasive. We considered that this is an issue which any reasonable trader would find crucial business to ensure it was clear which party held legal title to the goods and at what stage that title passed. The Appellants paperwork indicated that they held title but in fact this was not true; as Mr Khan stated in evidence title remained with the supplier until the supplier was paid in full. However upon further cross-examination it was apparent to us that this was also inaccurate as Mr Khan conceded that there could be a number of release notes depending on how many participants were in the chain. We inferred from this that it was clear to Mr Khan that title may have been held by his supplier's supplier or even beyond. We concluded that in such circumstances Mr Khan's explanation of goods being *"allocated"* to the Appellants had little practical effect as the Appellants' supplier may not have had title to allocate; a fact which Mr Khan did not question. We found as a fact that the conspicuous lack of clarity or formal record on this issue was indicative of the fact that such legalities did not matter to the parties as they knew that the transactions were contrived and legal title would never be an issue.

221.There was no evidence that Mr Khan agreed to important terms when entering into transactions, for example regarding dates of payments, prices or return of faulty goods. In evidence Mr Khan stated that such matters were verbally agreed however the deal documentation either makes no reference to these agreements or, where terms did exist they bore no reality to what happened in practice (for instance Edgeskill's

terms of sale agreement). There was no evidence of emails, letters or at the very least a note made by Mr Khan dealing with the practicalities one would expect to find in significant commercial transactions, such as offers, counter-offers or any discussions about delivery, payment, shipping, inspection and release. We should note that the documents presented by Mr Khan on the last day of evidence purported to show notes kept in respect of transactions which took place prior to the deals with which we are concerned. Given the fact that the records did not relate to the deals in this appeal and their very late production we attached no weight to them. We concluded that this manner of trading lacked commerciality and given the risks inherent in this type of trading we were satisfied that this issue indicated knowledge on the part of the Appellants.

222. The due diligence carried out by the Appellants lacked any meaningful substance and we concluded that Mr Khan had failed to look beyond or analyse the documentation obtained which was inadequate for the purpose of ensuring that his trading partners were legitimate. We took into account that Redhill checks had been undertaken along with Europa checks where Redhill responses were delayed and that trading references and other documents were obtained. However in our view, upon closer inspection the documents obtained told Mr Khan very little from which he could feel assured that the transactions were legitimate. To highlight a few examples, the report on Edgeskill completed by Veracis could not be said to be independent given that the company acted as VAT advisors to Edgeskill – even accepting that Veracis was engaged as a professional service there is no evidence that Mr Khan queried this apparent connection to ensure independence, that Edgeskill was put forward as a reference for MK Digital was also left unquestioned and the credit reports for MK Digital highlighted risk – the extent of which was seemingly left unascertained by Mr Khan. Looking beyond the documentation, we found Mr Khan's evidence as to his business relationships with his supplier and customer vague. We considered that the real commercial risk in the Appellants' transactions was posed by its customers, the most obvious risk being whether they would be able to pay for the goods. On the evidence before us we were not satisfied that Mr Khan took any real steps to measure that risk in circumstances of high value transactions. We concluded that the absence of any meaningful checks and action taken to follow up or query the results of those checks was indicative of knowledge on the Appellants' part and the fact that Mr Khan knew that the transactions posed no real risk.

223. As regards the inspection reports we accepted that the discrepancy when compared with the dates contained on Interken's stock records may have been an error. However we found the other anomalies highlighted in evidence raised questions which remained unanswered. By way of example we would have expected any reasonable trader to have retained a record of the verbal report provided by Interken prior to receipt of the written report yet there was no evidence of any such records nor any evidence that Mr Khan had even considered the scenario that the written report may wholly differ from the verbal communication, the absence of evidence showing the customer chasing the Appellant where there was delay in shipping goods in circumstances where Mr Khan had highlighted his customer's urgent need for goods – that being the reason Mr Khan told us for purchasing from Edgeskill and the willingness of Mr Khan to purchase goods despite not knowing where they were,

together with the fact that neither Sandeep or Interken seemed willing or able to clarify this, which is not the actions of a reasonable and prudent trader.

224.The Appellants were not recorded as sharing IP addresses with other traders in the chains of transactions and we concluded that this supported the Appellants' case that they did not know of the connection with fraud. We also took into account that there was no evidence that Mr Khan had any knowledge of the traders in the chains other than his trading partners or the short time in which those other traders made payments. We found that this evidence demonstrated that the Appellants' transactions were part of a contrived scheme to defraud the Revenue but we did not find that the evidence pointed towards knowledge or means of knowledge on the Appellants' part.

225.Mr Khan made much of the fact that HMRC had made repayments relating to his earlier transactions and it was submitted on his behalf that the making of repayments had left Mr Khan with the perception that his methods of trading were not connected to fraud. We did not accept this submission; all of the earlier repayments were made on a without prejudice basis which would have left Mr Khan in no doubt that that HMRC was in no way guaranteeing the veracity of his transactions. Combined with the three notifications that his transactions had been traced back to tax losses and the repeated warnings about MTIC fraud given by HMRC prior to and throughout the relevant period we were wholly satisfied that any such perception as that asserted by Mr Khan was both misplaced and unreasonable.

226. We found the structure of the transactions; in particular the delays in shipping and ship on hold arrangement were indicative that the deals were not legitimate commercial deals. By way of example the shipping of goods prior to payment, even taking into account the ship on hold arrangement, reduced the Appellant's control over the goods and had the potential to cause difficulty and expense to the Appellant if there was subsequently a problem with the deal. Furthermore delay in completing the deal – such as delay in payment – posed the risk that the value of the goods might change and payment may not be made. The illogicality of these factors indicated to us that the deals were clearly not genuine commercial transactions but were contrived transactions which the Appellant knew were connected with the fraudulent evasion of VAT.

227.We considered whether, irrespective of his denial, Mr Khan had been manipulated by other traders and used as what is commonly referred to as a "patsy". In doing so and in order to reach our decision on the issues of knowledge or means of knowledge we bore in mind the questions posed by Moses LJ in *Mobilx* at [72]:

"(1) Why was…a relatively small company with comparatively little history of dealing in mobile phones, approached with offers to buy and sell very substantial quantities of such phones?

(2) How likely in ordinary commercial circumstances would it be for a company in [the Appellant's] position to be requested to supply large quantities of particular types of mobile phone and to be able to find without difficulty a supplier able to provide exactly that type and quantity of phone?

(3) Was [the supplier] already making supplies direct to other EC countries? If so, he could have asked why [the supplier] was not making supplies direct, rather than selling to UK traders who in turn would sell to such other countries.

(4) Why are various people encouraging [the Appellant] to become involved in these transactions? What benefit might they be deriving by persuading [the Appellant] to do so? Why should they be inviting [the Appellant] to join in when they could do so instead and take the profit for themselves?"

228. We have based our decision on the totality of the evidence and we were careful not to focus unduly on the issue of due diligence or judge the evidence with the benefit of hindsight. We were wholly satisfied that the actions and inactions of Mr Khan when viewed against the circumstances of the Appellants' transactions as a whole indicated that he had actual knowledge that the transactions were connected to fraud. We found that some reasons carried more weight than others and we did not base our decision solely on one reason but rather the cumulative effect of our findings viewed in totality.

229. The factors identified above, from which we inferred the Appellant's actual knowledge, would in our view also support a finding of means of knowledge. The deals at the time were quite clearly "too good to be true"; something which we were satisfied would have been obvious to Mr Khan, for example the profits made, the little amount of work done to earn those profits, the ease of implementing the deal, the casual way the business was conducted without contractual terms and the basic rather than investigative due diligence which was unlikely to assist in determining whether fraud has occurred to name only a few.

Conclusion

230. We were satisfied HMRC had established fraudulent tax losses and that there was an orchestrated scheme for the fraudulent evasion of VAT connected with the transactions which form the subject of this appeal.

231. We concluded that in respect of the periods under appeal the Appellants knew, through Mr Khan, that the transactions were connected with the fraudulent evasion of VAT or that the factors set out above would at the very least support a finding of means of knowledge.

232. The appeal is dismissed.

Costs

233. We direct that the Appellant is to pay HMRC costs of, incidental to and consequent upon the appeal, to be the subject of detailed assessment if not agreed.

234. This document contains full findings of fact and reasons for the decision. Any party dissatisfied with this decision has a right to apply for permission to appeal against it pursuant to Rule 39 of the Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules 2009. The application must be received by this Tribunal not later

than 56 days after this decision is sent to that party. The parties are referred to "Guidance to accompany a Decision from the First-tier Tribunal (Tax Chamber)" which accompanies and forms part of this decision notice.

JENNIFER BLEWITT
TRIBUNAL JUDGE

RELEASE DATE: 30 January 2015