TC02292

Appeal number: TC/2010/00383

VAT – INPUT TAX – ***HMRC denied input tax claims totalling £1,048,337.50 in respect of 12 transactions of mobile phones– Was there a VAT Loss? – Yes – Was the loss fraudulent? – Yes – Were the Appellant's transactions connected with the fraud? – Yes - Did the Appellant know or should have known that its transactions were connected to fraudulent evasion of VAT? – Yes the Appellant knew – Appeal dismissed***

FIRST-TIER TRIBUNAL
TAX CHAMBER

JJ WHOLESALE LIMITED **Appellant**

- and -

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

TRIBUNAL: JUDGE MICHAEL TILDESLEY OBE
SHAHWAH SADEQUE

Sitting in public at Bedford Square London on 11 -15 June 2012 and 18-21 June 2012

The Appellant did not appear

Jonathan Kinnear QC and Howard Watkinson instructed by the General Counsel and Solicitor to HM Revenue and Customs, for HMRC

DECISION

The Appeal

1. The Appellant appeals HMRC's decision dated 20 November 2009 denying entitlement to the right to deduct input tax in the sum of £1,048,337.50 claimed on 12 transactions involving supplies of mobile phones during accounting periods 07/06 and 10/06.

2. HMRC contends that each of the Appellant's 12 transactions was connected with the fraudulent evasion of VAT and that the Appellant knew or should have known of that fact. The Appellant disagrees, arguing that there was no such connection and, if there was the Appellant did not know and could not have known that the said transactions were connected with the fraudulent evasion of VAT.

3. The Appellant was incorporated on 2 March 2003 and on 16 August 2005 changed its name to JJ Wholesale Ltd. At all times Mr Sukhvir Jaswal was the director and Mrs Baljit Jaswal the company secretary. The Tribunal is satisfied that Mr Jaswal was the controlling mind of the Appellant, and that his state of knowledge can be imputed onto the Appellant for the purposes of determining this Appeal..

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

> (1) Was there a VAT loss?
>
> (2) If so was it occasioned by fraud?
>
> (3) If so were the Appellant's transactions connected with such a fraudulent VAT loss?
>
> (4) If so did the Appellant know or should it have known of such a connection?

5. HMRC has the burden of proving on the balance of probabilities its assertion that the disputed transactions were connected with the fraudulent evasion of VAT and the Appellant knew or should have known of their connection.

6. The Appellant in a notice dated 19 July 2011 accepted that HMRC had sufficiently evidenced the following:

> (1) Fraudulent tax losses existed in all the Appellant's supply chains, except its contra trading chain.
>
> (2) Fraudulent tax losses existed at the start of all the dirty supply chains relating to the contra trader.
>
> (3) The stock purchased by the fraudulent companies was imported from other EU Member states and traded through a series of UK companies (as identified in HMRC's evidence), and was the same stock purchased by the Appellant and the contra trader.

7. The Appellant in the same notice identified the following matters in dispute:

(1) The contra-trader was fraudulent.

(2) The Appellant knew or should have known of the fraud in the supply chains for the contra-trader.

(3) The Appellant's transactions were connected to fraud having regard to the *proper* construction of the joint cases of *Axel Kittel v Belgium & Belgium v Recolta Recycling SPRL* (C-439/04 and C-440/04).

(4) The Appellant knew or should have known of the fraud in the direct tax loss chains.

Overview of the Law

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

> "167 A right of deduction shall arise at the time the deductible tax becomes charged.
>
> 168. Insofar as the goods and services are used for the purposes of the taxed transactions of a taxable person, the taxable person shall be entitled, in the Member State in which he carries out these transactions, to deduct the following from the VAT which he is liable to pay: The VAT due or paid in that Member State in respect of supplies to him of goods or services, carried out or to be carried out by another taxable person".

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

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

> "51. In the light of the foregoing, it is apparent that traders who take every precaution which could reasonably be required of them to ensure that their transactions are not connected with fraud, be it the fraudulent evasion of VAT or other fraud, must be able to rely on the legality of those transactions without the risk of losing their right to deduct the input VAT (see, to that effect, Case C-384/04 *Federation of Technological Industries and Others* [2006] ECR I-0000, paragraph 33).
>
> 52.It follows that, where a recipient of a supply of goods is a taxable person who did not and could not know that the transaction concerned was connected with a fraud committed by the seller, Article 17 of the Sixth Directive must be interpreted as meaning that it precludes a rule of national law under which the fact that the contract of sale is void, by reason of a civil law provision which renders that contract incurably void as contrary to public policy for unlawful basis of the contract

attributable to the seller, causes that taxable person to lose the right to deduct the VAT he has paid. It is irrelevant in this respect whether the fact that the contract is void is due to fraudulent evasion of VAT or to other fraud.

53. By contrast, the objective criteria which form the basis of the concepts of 'supply of goods effected by a taxable person acting as such' and 'economic activity' are not met where tax is evaded by the taxable person himself (see Case C-255/02 *Halifax and Others* [2006] ECR I-0000, paragraph 59).

54. As the Court has already observed, preventing tax evasion, avoidance and abuse is an objective recognised and encouraged by the Sixth Directive (see Joined Cases C-487/01 and C-7/02 *Gemeente Leusden and Holin Groep* [2004] ECR I-5337, paragraph 76). Community law cannot be relied on for abusive or fraudulent ends (see, inter alia, Case C-367/96 *Kefalas and Others* [1998] ECR I-2843, paragraph 20; Case C-373/97 *Diamantis* [2000] ECR I-1705, paragraph 33; and Case C-32/03 *Fini H* [2005] ECR I-1599, paragraph 32).

55. Where the tax authorities find that the right to deduct has been exercised fraudulently, they are permitted to claim repayment of the deducted sums retroactively (see, inter alia, Case 268/83 *Rompelman* [1985] ECR 655, paragraph 24; Case C-110/94 *INZO* [1996] ECR I-857, paragraph 24; and *Gabalfrisa*, paragraph 46). It is a matter for the national court to refuse to allow the right to deduct where it is established, on the basis of objective evidence, that that right is being relied on for fraudulent ends (see *Fini H*, paragraph 34).

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".

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

> "59.The test in *Kittel* is simple and should not be over-refined. It embraces not only those who know of the connection but those who "should have known". Thus it includes those who should have known from the circumstances which surround their transactions that they were connected to fraudulent evasion. If a trader should have known that the only reasonable explanation for the transaction in which he was involved was that it was connected with fraud and if it turns out that the transaction was connected with fraudulent evasion of VAT then he should have known of that fact. He may properly be regarded as a participant for the reasons explained in *Kittel*.
>
> 60. The true principle to be derived from *Kittel* does not extend to circumstances in which a taxable person should have known that by his purchase it was more likely than not that his transaction was connected with fraudulent evasion. But a trader may be regarded as a participant where he should have known that the only reasonable explanation for the circumstances in which his purchase took place was that it was a transaction connected with such fraudulent evasion."

12. The Appellant contended that the Court of Appeal in *Mobilx* had not correctly interpreted the decision of the Court of Justice in *Kittel*. The Appellant argued that *Kittel* was a case of narrow application, only to be applied in cases where the taxable person was counterparty to fraudulent transactions. The Tribunal will consider this argument when it deals with its findings on whether the Appellant's transactions were connected with fraud.

Preliminary Matters

13. On 10 December 2009, the Appellant appealed against HMRC's disputed decision of 20 November 2009. On 31 October 2011 the Tribunal notified the parties of the hearing which was to be held on 11 to 26 June 2012. On 10 May 2012 the Appellant applied to serve additional evidence which was not contested by HMRC.

14. On 7 June 2012, two working days before the hearing, the Appellant's representative, Mr Liban Ahmed of CTM Litigation and Tax Services, informed the Tribunal and HMRC that

> "Cutting to the chase, the Appellant has run out of funds, with the following consequences:
>
> 1. We are now doing work for which we have not been, and will not be paid.
>
> 2. We will not be attending the trial at any point.
>
> 3. The skeleton argument (for which we will conclude out of goodwill to the Appellant, and to assist the Tribunal) will not be served until later today.
>
> 4. Exhibits relating to the accepted late service of the Appellant's second witness statement will be served on the Respondent later today, along with the statement itself.
>
> 5. We will play no further active part in the appeal process but have agreed to remain the point of contact to assist the Tribunal should any queries arise and to receive a formal decision in due course.
>
> Further, the Appellant (*Mr Jaswal)* has stated that he simply cannot face such a daunting, complex trial without any representation. The director, although requesting that his evidence is taken into account, will not be attending the trial at any point. We accept that this is not what the Tribunal wishes to her, but the Appellant has recently sat through trials involving other MTIC appeals and does not believe he can deal with the pressure on his own. However, the Appeal will not be withdrawn".

15. At the commencement of the hearing on 11 June 2012 HMRC applied for the case to proceed in the Appellant's absence. The Tribunal granted the application. In so doing the Tribunal had regard to the wording of regulation 33 of the Tribunal Rules 2009. The Tribunal was satisfied that the Appellant had been notified of the hearing and was clearly aware of it taking place. The Tribunal considered that it was in the interests of justice to proceed because:

(1) The Appeal was over two years old and the parties were notified of the actual hearing date on 31 October 2011[1].

(2) The Appellant did not advise the Tribunal and HMRC until 7 June 2012 that it was not intending to attend the hearing.

(3) The Appellant has not withdrawn its appeal and has not requested an adjournment of the hearing.

(4) The Appellant has clearly indicated in its correspondence and through its representative that it wished the Appeal to proceed in its absence and for the

[1] The Tribunal when giving its oral decision gave the date as the 11 October 2012 rather than 31 October 2012 see line 7 page 29 trans 11.6.2012.

Tribunal to have regard to the evidence submitted on its behalf and the representations made by its representative.

(5) HMRC was in a position to proceed .

16. The Tribunal took the view that it should treat the Appeal as a full, contested hearing even though the Appellant did not attend in person to present its case. The Appellant had supplied its evidence and provided detailed arguments in support of its Appeal. There were no grounds to justify a strike out of the Appeal. HMRC had the burden of proving its assertions about the connections of the Appellant's transactions with fraud, and the Appellant's purported state of knowledge regarding the fraud. In this regard the Tribunal set aside time during the hearing to read fully the witness statements, and the accompanying exhibits, and the parties' arguments and made decisions on which witnesses should be heard in person.

17. Essentially the Tribunal decided to hear from those witnesses who were central to HMRC's case and whom the Appellant through its witness statements and its representative's skeleton had directly challenged. Thus the Tribunal received evidence in person from Miss Marva Harry, the Officer who carried out the extended verification of the disputed deals, Mr Barry Patterson, the Officer who visited the Appellant and acted as its VAT Officer at the time of the Appellant's entry into the telecommunications trade sector, and Ms Julia Danson, the Officer who analysed the date from the Appellant's FCIB account.

18. The Tribunal did not hear evidence in person from Ms Susan Okolo, Mr Peter Cameron-Watson and Nigel Humphries who dealt with the position regarding the purported contra-trader, *Famecraft (Bristol Cash and Carry)*. Although the Appellant's representative made strenuous challenges to HMRC's interpretation of the evidence of these Officers, the Appellant did not call into question the evidence itself. In those circumstances the Tribunal considered that the dispute was best dealt with by weighing up the parties' respective submissions.

19. Mr Peter Morehead and Mr Michael Downer gave evidence on the alleged fraudulent activities of the freight forwarders 1st Freight Ltd (Deal 8) and Worldwide Logistics (the destination of the goods in the Appellant's 04/06 deals.). HMRC relied on this evidence to provide background to the overall fraudulent nature of the disputed transactions. The evidence of Mr Downer had no direct relationship to the 07/06 and 10/06 periods. The Appellant did not challenge directly the evidence of these Officers because it was purportedly outside its knowledge. The Tribunal decided that the relevance of this evidence was best dealt with by evaluating the submissions.

20. Ms Farzana Malik[2] gave evidence on *Nijjers* which was one of the Appellant's trading partners in the disputed deals. HMRC relied on this evidence to demonstrate that the Appellant's relationship with *Nijjers* went beyond one with arms-length commercial characteristics. The Appellant raised no specific objections to the accuracy of Ms Malik's statement but questioned its relevance. The Tribunal again

[2] Mrs Malik was a replacement witness for Ms Joanne Gibbons who was the original Officer assigned to *Nijjers*

decided that the Appellant's contest with this evidence was best dealt with by evaluating the submissions.

21. The Tribunal Judge had dealt with the appeal by *Nijjers* against HMRC's denial of its input tax. The Judge, however, had not heard evidence relating to the substantive Appeal or made findings of fact thereon. The director for *Nijjers* had on the day of the hearing applied for the Appeal to be adjourned which after hearing representations was refused by the Tribunal. Following which the director withdrew the Appeal on legal advice.

22. The Appellant's representative contended that Mr Fletcher's evidence was generic and opinion in the main which could not possibly have been identified by the Appellant. HMRC indicated that it did not rely on Mr Fletcher's evidence for a great deal[3]. Given those circumstances the Tribunal decided that it was unnecessary to hear from Mr Fletcher in person. The Tribunal, however, required HMRC to establish the legal basis for treating Mr Fletcher as an expert witness.

23. The Appellant made no observations on the evidence of Mr Andrew Letherby who testified on the integrity of the process for extracting the information from the FCIB records. The Tribunal, therefore, agreed to receive Mr Letherby's statement without calling him in person[4].

24. The Appellant advised HMRC and the Tribunal in its notice dated 19 July 2011 that the Officers who dealt with the missing/defaulting traders[5] and Officer Stone were not required to attend the Tribunal to give their evidence. In view of the Appellant's non-attendance HMRC submitted that it was unnecessary to call the other witnesses simply to present their statements. HMRC's counsel pointed out that the witnesses had declared that their respective statements were true and correct records. Further counsel contended that the majority of the disputed matters was a matter of interpretation of the facts which could be dealt with by evaluating the respective submissions. The Tribunal assessed counsel's proposition by considering each witness statement together with the parties' skeleton arguments and arrived at the conclusions as set out in paragraphs 17-23 above as the correct way for conducting the hearing of the Appeal.

25. A full transcript of the proceedings was taken. HMRC agreed to send a copy of the transcript to the Appellant's representative at the end of each day. The Tribunal heard the Appeal over nine days, 11-15 June 2012, and 18-21 June 2012, and reserved its decision at the conclusion of the hearing.

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[3] See 11 June 2012 Trans 149 line 19

[4] See 15 June 2012 Trans page 50 – 57 where the Tribunal gives reasons for not calling specific witnesses.

[5] Namely: Officers Sarah Barker, Patricia Wilson, George Edwards, Mark Hughes, Ian Henderson, David Berry, Fiona Weldon, and Romaine Lewis.

Pleadings

26. The Appellant in its skeleton argued that HMRC could only rely upon matters that were both fairly and squarely pleaded in its statement of case and that no new issues should be permitted to be raised during the hearing. The Appellant cited the First Tier Tribunal decision in *POWA (Jersey) Limited* [2009] UKFTT 360 (TC) at paragraphs 28 & 29 and the High Court judgment in *Mobilx*[2009] STC 1107 as support for its assertion. In respect of the latter decision the Appellant referred to the views of Mr Justice Floyd at paragraph 16:

> "It is also well settled that a tribunal is not entitled to find serious allegations established against a party who calls relevant witnesses unless those allegations are clearly formulated and put in cross-examination. As Briggs J said in *Revenue and Customs Comrs v Dempster* (*t/a Boulevard*) [2008] EWHC 63 (Ch), [2008] STC 2079 at [26]:
>
> '.. it is a cardinal principle of litigation that if serious allegations, in particular allegations of dishonesty are to be made against a party who is called as a witness they must be both fairly and squarely pleaded, and fairly and squarely put to that witness in cross-examination ..."

27. At paragraph 18 of its skeleton the Appellant appeared to suggest that HMRC had only pleaded fraud in relation to the missing traders. At paragraph 59 the Appellant listed four matters which it said were not pleaded in HMRC's Statement of case:

(1) The Appellant was a fraudster, be it by cheating the Revenue or through conspiracy.

(2) The Appellant's trading partners were fraudsters.

(3) An allegation that the goods did not exist.

(4) A conspiracy between the parties in the Appellant's clean chains, with the parties in Famecraft's alleged dirty chains.

28. HMRC disagreed with the Appellant's assertion that the only fraud pleaded was that which was associated with the missing traders. HMRC contended that from the outset of the case its pleadings have made it plain that the fraud alleged went far beyond the actions of the defaulting traders and that each of the transactions in all the transaction chains had been contrived and pre-arranged as part of an overall scheme to defraud the revenue. HMRC supported its contention by reference to the decision letter dated 20 November 2009 and its Statement of Case dated 19 March 2010, and more particularised in paragraphs 4 to 8 in HMRC's closing submissions dated 20 June 2012. HMRC pointed out that the Appellant fully understood about the allegation of an overall scheme to defraud as the Appellant mentioned it specifically in its Notice of Appeal.

29. HMRC stated that in relation to the four matters identified by the Appellant at paragraph 59 of its skeleton that they were in effect not relying on them to prove its case. According to HMRC the Tribunal was not required to find that the Appellant was a *fraudster* in order to uphold its decision to deny the Appellant the right to

deduct on the basis that it knew or should have known that its transactions were connected with the fraudulent evasion of VAT. Equally HMRC was not required to prove that the Appellant's trading partners were *fraudsters* but in any event, it was clear from paragraphs 36-42 of its Statement of Case, that the state of knowledge of the Appellant's trading partners as to their part in the said scheme has been put in issue by HMRC pleadings. As to the non-existence of goods, HMRC was of the view that it was irrelevant to the question which they had to prove under the doctrine in *Kittel*. Finally HMRC disagreed with the Appellant's understanding of the law about the requirement to establish conspiracy in the alleged contra trade.

30. HMRC also disagreed with the Appellant on the law in relation to the amount of detail required in the pleadings, citing Lord Woolf MR in *McPhilemy v. Times Newspapers Ltd* [1999] 3 All ER 775 at 792-3:

> "The need for extensive pleadings including particulars should be reduced by the requirement that witness statements are now exchanged. In the majority of proceedings identification of the documents upon which a party relies, together with copies of that party's witness statements, will make the detail of the nature of the case the other side has to meet obvious. This reduces the need for particulars in order to avoid being taken by surprise. This does not mean that pleadings are now superfluous. Pleadings are still required to mark out the parameters of the case that is being advanced by each party. In particular they are still critical to identify the issues and the extent of the dispute between the parties. What is important is that the pleadings should make clear the general nature of the case of the pleader. This is true both under the old rules and the new rules.
>
> As well as their expense, excessive particulars can achieve directly the opposite result from that which is intended. They can obscure the issues rather than providing clarification. In addition, after disclosure and the exchange of witness statements pleadings frequently become of only historic interest."

31. The Tribunal's principal area of concern with the Appellant's submission regarding the extent of the pleadings was whether HMRC had identified in them its assertion that the Appellant's transactions were part of an overall scheme to defraud the Revenue which was a central part of its case. The Tribunal is satisfied from the analysis of the Statement of Case and decision letter that the assertion of overall scheme to defraud had been pleaded from the outset, and the Appellant clearly knew this.

32. The Tribunal considers that the Appellant's four specific issues identified in paragraph 59 of its skeleton[6] were primarily disputes about the correct interpretation of the law which will be considered by the Tribunal in the body of the decision. The Appellant's contentions about its trading partners and the existence of goods raised potential issues that may be relevant to the state of the pleadings. The Tribunal is satisfied that HMRC had put in issue the state of knowledge of the Appellant's

[6] See paragraph 27 above.

counterparties. The question of non-existence of goods only arose in the Appellant's 04/06 transactions which had in fact been mentioned in the Statement of Case and was relevant insofar as whether an inference could be drawn from that fact, if found, about the Appellant's state of knowledge[7].

33. The Tribunal agrees with HMRC's submission on the law that its Statement of Case should mark out the parameters of the case that was being advanced and identify the issues relied upon. In this instance the detail of HMRC's case has been developed by the exchange of witness statements and skeleton arguments. The Tribunal is satisfied that HMRC had fairly and squarely pleaded its case and the Appellant was clearly aware of the case against him.

34. The Tribunal notes the Appellant's reliance on Mr Justice Floyd's comments at paragraph 16 of the High Court decision in *Mobilx* which is a restatement of the fair play principle established in the House of Lords decision in *Browne v Dunn* (1894) 6 R67 namely:

> "….to put to an opponent's witness in cross-examination the nature of the case upon which it is proposed to rely in contradiction of his evidence, particularly where that case relies upon inferences to be drawn from other evidence in the proceedings".

35. In this Appeal, Mr Jaswal, the Appellant's witness, chose not to attend the hearing, and in so doing deprived HMRC of the opportunity to cross examine him on his evidence. In those circumstances the Tribunal considers that the Appellant is not entitled to complain that it was not given the chance to explain, if the Tribunal draws justified inferences from contradictions in the evidence.

Overview of the Disputed Transactions

36. The Appellant carried out 12 deals involving the wholesale of mobile phones in the 07/06 period. In 11 deals the Appellant purchased phones from a UK based trader and then exported them, which HMRC referred to as broker deals. In one deal the Appellant bought from a UK based trader and sold to a UK based trader (a buffer deal and referred to as deal 5). In the 10/06 period the Appellant carried out a single broker or export deal. HMRC's decision to deny input tax related to the broker deals transacted by the Appellant in the 07/06 and 10/06 periods, which did not include the buffer deal in 07/06 period.

37. The broker transactions in the 07/06 period took place between 29 June 2006 and 28 July 2006 and involved consignments of mobile phones, principally Nokia models but also a consignment of Sony Ericsson W900i, and one of Motorola V3i mobile phones. During this period the Appellant purchased mobile phones from six different suppliers and sold to six different customers. The buffer transaction involved a consignment of Nokia N91 mobile phones which was purchased from *NTS Telecom* and sold to *Nijjers Ltd*.

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[7] This allegation, in any event, did not figure in HMRC's case against the Appellant and not mentioned in the final submissions.

38. The transaction in the 10/06 period occurred on the 17 August 2006 involving a consignment of Nokia 6681 mobile phones bought from *Reya Limited* and sold to *Al Saqr Telecom* in the United Arab Emirates (UAE).

Was there a VAT Loss?

39. In ten of the Appellant's 11 broker deals in the 07/06 period and the single deal in the 10/06 period HMRC had traced them directly back through a chain of UK based buffer traders to a defaulting trader. In each of the deals the defaulting trader imported the mobile phones into the UK from a company based elsewhere in the EU. This purchase was, therefore, zero rated for VAT. The defaulting traders then sold the mobile phones to another UK based trader, charging VAT output tax on the invoice, which they then failed to account for, giving rise to a VAT loss. The mobile phones were then sold on to a number of other UK based traders until they were purchased by the Appellant, who in turn exported them from the UK in a sale to another EU based trader (on two occasions to traders based in the UAE). The Appellant's sales were zero rated for VAT. The Appellant sought to reclaim the input tax paid on its purchases, the denial of which by HMRC was the subject of this Appeal.

40. The Appellant accepted that a tax loss existed in its supply chains, except for deal 8 (the alleged contra-trade)

41. The Tribunal finds that the following companies/entities occasioned a VAT loss in each of the Appellant's deals, except deal 8:

(1) *Heathrow Business Solutions Ltd* (Deals 1 & 2);

(2) *Ultimate Wholesale* (Deals 3 & 4);

(3) *Sky Traders Limited* (Deal 6);

(4) *Kaymore Export Limited* (Deal 7);

(5) *Phone City Limited* (Deal 9);

(6) *ET Phones* (Deals 10,11 & 12)

(7) *Southern PhoneCare Ltd* (Deal 13, 10/06)

42. HMRC contended that the Appellant's remaining broker deal in the 07/06 period was part of a contra-trading scheme. This deal took place on the 19 July 2006 and involved the purchase of 2,350 Nokia 8800 mobile phones from *Trimax Trading International Limited* and the sale of those phones to *Alimed*, a Spanish company. HMRC stated that *Famecraft (Bristol Cash and Carry)* which supplied the phones to *Trimax* was a contra trader. According to HMRC, *Famecraft* offset its output tax liability on its supply to *Trimax* against its input tax claim on a different transaction involving the purchase and export of Gillette razor blades for the sole purpose of cheating the Revenue. HMRC have traced back the razor blade transaction to a defaulting trader which has failed to account for the VAT on its purported sale.

43. The Appellant accepted that a tax loss existed at the start of the Gillette razor blades transaction chain involving *Famecraft.*

44. The Tribunal finds that a company known as *Barato* occasioned a VAT loss in the Gillette razor blades transactions involving *Famecraft.*

Were the VAT Losses Occasioned by Fraud?

45. The Appellant did not challenge HMRC's evidence on the fraudulent activities of the defaulting traders identified in paragraph 41 above. The Appellant accepted in its notice dated 19 July 2011 that the tax losses were fraudulent. In this respect the Tribunal makes the following findings of fact on the defaulting traders.

46. *Heathrow Business Solutions Ltd* (Deals 1 & 2) was incorporated on 12 August 2004 with a business activity of labour recruitment and other software consultancy. On 1 June 2006 there was a change in its company officers which coincided with trading in large volumes of mobile phones. On 30 June 2006 HMRC visited the registered address of the company but found that it had not operated from there. On 3 July 2006 *Heathrow Business Solutions Ltd* was deregistered from VAT. Assessments were issued against it for a VAT liability of £32.5m that related solely to invoices issued in June and early July 2006 where no output tax was declared. *Heathrow Business Solutions Ltd* has not paid and not appealed against the assessments.

47. The Tribunal finds the following facts which demonstrated that *Heathrow Business Solutions Ltd* was acting as part of an overall scheme to defraud the revenue:

(1) The radical departure from its stated business activity in June and early July 2006, that by reference to its VAT returns it had never undertaken, without informing HMRC.

(2) The change of company officers immediately before the change in business activity.

(3) The volume of VAT default created by the company in just over a month.

(4) Its sudden disappearance from its premises

48. *Ultimate Wholesale Limited* was incorporated on 1 October 2005. The VAT1 declared its main business activity to be telephone accessories with an estimated annual value of ₤100,000 with no trade with the EU. *Ultimate Wholesale's* 01/06 and 04/06 VAT returns showed outputs of £17.4million and £130.4million. It failed to submit a VAT return for the 07/06 period which covered the transactions traced to the Appellant. *Ultimate Wholesale* was deregistered for VAT with effect from 29 September 2006. Its debt to HMRC of £4,112,729.77 remained outstanding.

49. The Tribunal finds the following facts which demonstrated that *Ultimate Wholesale* was acting as part of an overall scheme to defraud the revenue:

(1) The director's statements to HMRC that it would not be involved in the wholesaling of mobile telephones.

(2) The rapid increase in turnover from a standing start to £147.8m in under six months.

(3) Its repeated failure to produce its business records.

(4) The making of third party payments to *Alfa Tradezone* which appeared in the movement of monies associated with the Appellant's transactions.

(5) Its failure to declare its sales in period 07/06 leaving a large VAT default.

50. *Sky Traders Ltd* (Deal 6) was incorporated on 3 January 2005. On 16 August 2006 its director, Altaf Khan, wrote to HMRC stating that a Hasnat Ahmed had appointed himself as a director of the company and had changed the company's address without his knowledge. Mr. Khan stated that he had spoken to the fraud department of Companies House and the police. HMRC treated *Sky's* VAT registration number as having been hi-jacked. Those behind the hi-jacking of Sky's VRN used the company to amass a VAT default of £2.65million between 10 and 18 July 2006.

51. The Tribunal finds the following facts which demonstrated that the hi-jacking of *Sky's* VAT registration number was undertaken as part of an overall scheme to defraud the revenue:

(1) The hijacking occurred for a few days in July 2006

(2) The arrangement whereby millions of pounds worth of goods were sold to a single customer, that it had purchased from just two suppliers, in just over a week in July 2006.

(3) *Sky* shared the same supplier as *Phone City Ltd* and *ET Phones.com* which were also defaulting traders in the disputed .

52. *Kaymore Export Ltd* (Deal 7) was incorporated on 9 November 2000 with a business activity of the sale of motor vehicle parts. In August 2006 HMRC became aware that *Kaymore Export Ltd* was trading in mobile phones. Its director advised HMRC that an arrangement began in July 2006 between him and an ex-employee called Mr Ally whereby Mr. Ally was to be paid 10p commission on each sale of mobile phones. Between 17 and 31 July 2006 *Kaymore's* turnover was £15.2million and VAT on those sales was £2.7million.

53. The Tribunal finds the following facts which demonstrated that *Kaymore Export Ltd* was acting as part of an overall scheme to defraud the revenue:

(1) The company's sudden move into selling mobile telephones in July 2006 without declaring its activities to HMRC.

(2) The absence of *Kaymore's* initial customer Roses Motors from its claimed address.

(3) The turnover of £15.2million in two weeks in July from a standing start

(4) The payments and release of goods bypassed *Kaymore*, *SimplyConnect and Imang*, which concealed the full transaction chain and the identity of the acquiring defaulter

54. *Phone City Ltd* (Deal 9) was incorporated on 2 August 2004 with a business activity of telecommunications. On its VAT 1 registration its directors declared that its estimated turnover in the next 12 months would be £350,000 and there would be

no trade with EC companies. *Phone City's* 08/05 period return showed an increase in outputs to £102.4m from £3,683 in period 05/05. *Phone City* failed to produce any records for period its final VAT period from 1 June to 25 July 2006.

55. The Tribunal finds the following facts which demonstrated that *Phone City* was acting as part of an overall scheme to defraud the revenue:

(1) The company's sudden move into wholesaling mobile telephones and its massive increase in turnover.

(2) The directors' failure to pursue a reclaim of nearly £250,000.

(3) Its failure to provide its business records for its final period.

(4) *Phone City's* acquisition from the unknown Latvian company that supplied goods to two other defaulters in the Appellant's transaction chains in July 2006.

(5) The failure by anyone involved in the company to take responsibility for *Phone City's* trading until its director gave an undertaking in 2009 not to act as such for 12 years.

56. *ET Phones.com Ltd* (Deals 10, 11 & 12) was incorporated on 5 March 2003. Its VAT1 declared a main business activity of sales of internet phones and associated technology. On 31 May 2006 the directors for the company were changed. On 1 August 2006 HMRC received information from a freight forwarder showing that *ET Phones.com* had acquired goods from a Lativian company. HMRC found that between 3 July and 2 August 2006 *ET Phones.com* defaulted on VAT in the sum of £9,396,176 for which an assessment was issued. *ET Phones.com Ltd* did not pay the assessment and was wound up on 15 August 2007.

57. The Tribunal finds the following facts which demonstrated that *ET Phones.com* was acting as part of an overall scheme to defraud the revenue:

(1) The company's sudden move into wholesaling mobile telephones in July 2006 and its massive increase in turnover.

(2) Its failure to declare any of its sales.

(3) The creation of a VAT default of £9.4m in one month.

(4) The company's acquisition from the unknown Latvian company that supplied goods to two other defaulters in the Appellant's transaction chains in July 2006.

58. *Southern Phonecare Ltd* (Deal 13, 10/06 period) was incorporated on 8 April 1999. On 14 July 2006 there was a change in its company officers with the appointment of Ilango Tawaraja (salesperson). Mr Tawaraja had been an officer of *Verizone Ltd* that was deregistered from VAT on 13 February 2006 following nine transactions with an estimated loss to the revenue of £157,333.52. *Southern Phonecare* failed to render a VAT return for the final period of trading between 1 June and 17 August 2006 and did not declare any trading within that period. Records recovered from other traders showed that *Southern Phonecare* had begun wholesaling mobile telephones and CPUs on 20 July 2006. Between 20 July and 17 August 2006

Southern Phonecare created a VAT default of £5.9 million for which it was assessed. It did not pay nor appeal the assessment. *Southern Phonecare* was deregistered from VAT with effect from 19th August 2006.

59. The Tribunal finds the following facts which demonstrated that *Southern Phonecare* was acting as part of an overall scheme to defraud the revenue:

(1) The company's sudden move into wholesaling mobile telephones in July 2006 and its massive increase in turnover.

(2) *Southern Phonecare's* failure to declare any of its sales.

(3) The creation of a VAT default of £5.9million in one month.

(4) Mr Tawaraja's directorship of a previous missing trader.

60. The Tribunal is satisfied that the VAT losses incurred by *Heathrow Business Solutions Ltd* (Deals 1 & 2), *Ultimate Wholesale* (Deals 3 & 4), *Sky Traders Limited* (Deal 6), *Kaymore Export Limited* (Deal 7), *Phone City Limited* (Deal 9), *ET Phones* (Deals 10,11 & 12), and *Southern PhoneCare Ltd* (Deal 13, 10/06) were occasioned by fraud.

61. The Tribunal will consider the status of the loss occasioned by *Barato* (deal 8) under the next section.

Contra-Trade (Deal 8)

62. HMRC contended that the Appellant's transaction in Deal 8 had been traced to a fraudulent contra trader *Famecraft Ltd* (*Bristol Cash & Carry*) and that the defaulting trader in *Famecraft's* tax loss chains was *Barato.* HMRC considered that the only proper inference to be drawn by the Tribunal on the evidence was that Famecraft was knowingly involved in a contrived scheme to cheat the Revenue and the cover-up by Famecraft, achieved by offsetting the input tax incurred in its tax loss chains against the output tax liability in its acquisition chains, was dishonest. According to HMRC, the circumstances of Famecraft's trade permitted no other explanation than that its offsetting was done dishonestly to prevent it from having to make an input tax reclaim from HMRC that would unmask its role as a broker in fraudulent tax loss chains.

63. The Appellant disputed the characterisation of *Famecraft* as a fraudulent trader contending that the facts supported an alternative plausible explanation for its activities during the 08/06 period, namely, that the balancing of the VAT liability in disputed period was done solely for the purposes of inflating its cash flow as part of some legitimate business process.

64. As previously indicated in paragraph 18 the Appellant did not call into question the evidence of Ms Susan Okolo, Mr Peter Cameron-Watson and Nigel Humphries on the trading activities of *Famecraft.* The Appellant instead emphasised particular aspects of their evidence to support the innocent explanation advanced by the Appellant for *Famecraft's* trading.

65. The Appellant stated that *Famecraft* had been exporting razor blades to Spain for some time which was known by HMRC. Also *Famecraft* knew that its trading activities were being monitored closely by HMRC. Finally *Famecraft* presented all commercial documentation to HMRC at the end of each trading month. According to the Appellant, it was more likely than not that *Famecraft* did not know, or believe, that they could hide the fraud in their supply chains. In fact, *Famecraft* must have known that it could not. Thus *Famecraft* could not be classed as a dishonest party covering up the fraud.

66. The Tribunal makes the following findings of fact:

(1) *Famecraft* registered for VAT on 14 June 2004. The business activity was described as *letting of own property* and the turnover was estimated to be £60,000. On 23 June 2005, Famecraft advised HMRC that it was now trading as *Bristol Cash and Carry*, and that the business had moved from Peterborough to Bristol. The first trades for the company took place during the VAT quarter ending 08/05. At this time and for the months following, it acted as a warehouse/wholesale cash and carry business with little success. The company apparently over-purchased stock and had generally poor sales. The director, Paul Singh, had a background in mortgages rather than in wholesaling.

(2) *Famecraft* was fully aware of the high risk of MTIC fraud in its trade sector. On 25 and 27 April and 4 May 2006 HMRC Officers explained the risks and indicators of MTIC fraud to *Famecraft's* senior managers. Mr. Singh, the director, was specifically warned that *Famecraft's* trade showed those risks and was also given a copy of Notice 726.

(3) *Famecraft's* turnover for periods 05/05 to 02/06 was £4.89 million of which £4.4 million was accounted for in the 02/06 accounting period alone. The turnover for periods 05/06 and 08/06 increased considerably to £394.8 million.

(4) In February 2006 *Famecraft* completely changed its business, purchasing £2,040,267.33 of razor blades from a single supplier, *Flaxley*, and supplying them to either one of two UK traders, or to a single Spanish customer, *CEMSA*. The resulting VAT return submitted for the 02/06 quarter saw *Famecraft's* sales being higher than purchases for the first time in its history as a trader. HMRC allowed the repayment claim but began to monitor the activities of *Famecraft.*

(5) *Famecraft's* shift into the wholesaling of razor blades was contrary to the information it supplied to HMRC when on 3 February 2006 *Famecraft* made an unsuccessful application to submit monthly VAT returns. In that application *Famecraft* informed HMRC that it operated as a warehouse with 30 per cent UK standard rated trade and 70 per cent export trade in toiletries and soft drinks.

(6) In the 05/06 VAT period *Famecraft* undertook 148 transactions purchasing £71,466,172 worth of Gillette M Power Cartridges from *Flaxley* selling them either to eight UK customers or to *CEMSA* in Spain. *Famecraft* also made six purchases from *CRM Trading* (£1,686,847) and sold only to *CEMSA*. All the deals were traced back via *Barato* to the defaulting trader *Leeming Distribution Ltd*.

(7) On 27 November 2008 HMRC denied *Famecraft's* input tax claim in the sum of £2,990,951.61 for the 05/6 period. *Famecraft* has not appealed HMRC's decision.

(8) *Famecraft* has never adequately explained how it came to be selling razor blades to *CEMSA*, from a standing start in a sector outside its proposed remit, which was clearly beverage and snack sales. Equally there was no obvious commercial reason for *CEMSA*, supposedly an established Spanish pharmaceutical company with no need to trade within the UK for competitive prices, should strike up, immediately, strong and valuable trades in razor blades with the fledgling *Famecraft*.

(9) In its three month VAT period for June-August 2006, *Famecraft* completed 226 transactions[8] which fell into two distinct types of trade. In June and July 2006 *Famecraft* undertook 75 transactions of mobile phones which were purchased from *Sinderby Enterprises* in Cyprus and then sold onto two UK traders, *Glasgow Data* and *Trimax Trading International Ltd*. In August 2006 *Famecraft* conducted 149 sales of razor blades to a customer in Spain, *Agrupacion Iberia De Ultramar SA*, which generated a repayment claim for input tax. All of the deals involving the razor blades have been traced back from *Famecraft* to a trader named *Flaxley* and from *Flaxley* to *Barato* which purportedly sourced its goods from *Levevalour* in Portugal. *Barato* has failed to account for the output tax on its sales which has been assessed at £22,967,287.

(10) *Famecraft's* sales of mobile phones to the two UK traders generated an output tax claim which effectively matched the repayment claim connected with the trade in razor blades. The value of the razor blades closely mirrored the sale value of £154.4 million for the mobile phones. This matching meant that *Famecraft's* liability to pay output tax on the mobile phone sales (£27,296,134.67) had been effectively offset by the input tax claim in respect of the razor blade transactions (£27,291,988.93) which have been traced to a tax loss. The effect of the offsetting was that for every £1 of VAT claimed by *Famecraft* there has been a 99.9 per cent tax loss.

(11) The analysis of the deal chains for the mobile phone transactions in June and July showed that they were acquired from a single Portuguese supplier via 29 different UK traders and sold to two Spanish customers, *CEMSA* and *Agrupacion De Alimentos* (*Alimed*). The additional cost for the two Spanish customers by purchasing the mobile phones from the UK traders rather than the Portuguese supplier was £7.5 million, which made no commercial sense. Similarly there was no apparent commercial reason for *Agrupacion Iberia De Ultramar SA* to buy the razor blades in the August transactions from *Famecraft* rather than from the Portuguese supplier, *Levevalour*.

(12) *Alimed*, one of the two customers for the mobile phones, and *Agrupacion Iberia De Ultramar SA*, the customer for the razor blades were directed by the same person from the same address which provided a link between the

[8] Two deals were buffer transactions see paragraph 29 of Ms Okolo's first witness statement.

acquisition (mobile phones) and broker (razor blades) transactions undertaken by *Famecraft* in the 08/06 period.

(13) The traders in the mobile phones and razor blade deals conducted their transactions through accounts with an obscure online bank, the International Credit Bank. The traders opened their accounts with this obscure bank at around the same time in June and July 2006.

(14) In June and July 2006 *Famecraft* moved without any experience or avowed interest into the wholesale import of a completely new product: mobile telephones. This was trade in which those running *Famecraft* had no experience, and from a standing start it managed to generate enormous sales in mobile phones which would have left it with a debt of over £27 million in VAT. *Famecraft* managed to source these mobile phones from *Sinderby* based in Cyprus, with whom it had no trading history whatsoever. *Famecraft* has offered no explanation of how it came into contact with *Sinderby*. Moreover *Famecraft* carried out no genuine commercial checks on *Sinderby*

(15) In August 2006, however, *Famecraft* changed its trading pattern again reverting back to the export of razor blades but instead of trading with *CEMSA* it sold to another entirely new Spanish customer, *Agrupacion Iberia De Ultramar SA. Famecraft's* due diligence on the new Spanish company was totally inadequate.

(16) *Famecraft's* deal paperwork stated that the razor blades in the August transactions were held at a freight forwarder called *Croydon Cash and Carry.* HMRC's investigations revealed that *Croydon Cash and Carry* did not operate as a normal, active freight forwarder and had no genuine involvement in storing and freighting the supposed goods to France on *Famecraft's* behalf.

(17) *Famecraft* has not provided any due diligence checks it carried out in respect of any other associated traders in the 08/06 period which included *Flaxley, Glasgow Data, Trimax International* or its freight forwarders (*Croydon Cash and Carry* or *1st Freight*).

(18) The record of IMEI numbers for the mobile phones in the June and July 2006 transactions submitted by *Famecraft* contained obvious discrepancies. *Famecraft* purportedly obtained the record from its freight forwarder, *1st Freight.* The record included documents relating to *Famecraft's* trading partners and competitors, and details of IMEI numbers for a different Nokia model than that purportedly sold by *Famecraft* to *Glasgow Data* on 28 June 2006. The fact that *Famecraft* did not notice the discrepancies questioned the commercial authenticity of its mobile phone dealings.

67. The facts found demonstrated that *Famecraft* was not involved in legitimate trade. The only reasonable explanation for the facts found was that *Famecraft* was knowingly involved in fraudulent trading with the intention of cheating the Revenue. This conclusion was amply supported by the manner in which *Famecraft* conducted its business (no due diligence despite its knowledge of the high risk of MTIC fraud), the sudden ease in which it traded in huge quantities of new commodities and in finding customers and suppliers despite having no prior experience of the market

sector, and the rapid growth in sales resulting in a turnover which if allowed to continue would have ranked *Famecraft* as one of the biggest companies in the UK with an estimated turnover of £1.2 to £1.3 billion.

68. The facts found showed that *Famecraft's* mobile phone and razor blade transactions in period 08/06 were contrived with no commercial rationale whatsoever, and connected with each other. Both sets of transactions ultimately involved Portuguese suppliers and Spanish customers which questioned why the Spanish customers did not go straight to the suppliers, saving themselves significant sums of money. *Famecraft* had no trading pedigree in mobile phones but was able at the beginning of period 08/06 to find a UK market for mobile phones to the value of £154 million. Equally at the end of period 08/06 *Famecraft* discovered a new Spanish customer for razor blades to a value in excess of £150 million. The effect of these two sets of transactions enabled Famecraft to offset the output liability of £27,296,134.67 incurred on the mobile phones within £4,145.74 by the input tax claim on the sales of razor blades. All of *Famecraft's* 149 deals in razor blades were traced back to a tax loss by the same defaulting trader. The artificiality of the mobile phones transactions was demonstrated by the layers of UK companies acting either as buffers or brokers in the respective deal chains, and *Famecraft's* disregard of measures ensuring the bona fides of the goods sold and of its trading partners. Finally the timing of the opening and use of an obscure off-shore bank accounting facilities by the participants in both sets of transactions and the existence of a common controlling mind for the Spanish customers were indicative of the orchestrated and connected nature of the respective sets of transactions.

69. Given the above findings the Tribunal is satisfied that

> (1) At the end of August 2006 *Famecraft* knowingly traded in razor blades on which VAT had not been and would not be paid.
>
> (2) *Famecraft* triggered a repayment claim on the sale of razor blades to *Agrupacion Iberia De Ultramar SA.*
>
> (3) *Famecraft* deliberately disguised or laundered the repayment claim on the razor blades by importing mobile phones and selling them within the UK.

70. The Appellant's explanation for *Famecraft's* conduct, namely, that the balancing of the VAT liability was done solely for the purposes of inflating its cash flow as part of some legitimate business process had no basis in the evidence. The Appellant's suggestion that it made no sense for *Famecraft* to engage in dishonest concealment in view of the close supervision by HMRC of its activities was capable of another interpretation. HMRC contended that *Famecraft's* shift into contra trading was prompted by HMRC's close interest in its trading. According to HMRC, *Famecraft's* move from participation in the direct tax loss chains in the 05/05 period to contra-trading in the 08/06 period was a development of its fraudulent scheme by making it more complex and thereby more difficult for HMRC to detect the fraud. In short *Famecraft's* use of contra-trading was a logical progression of its intention to perpetuate fraud against the Revenue without detection. The Tribunal considers the facts found supported HMRC's alternative interpretation.

71. The Tribunal, therefore, holds that *Famecraft* was knowingly involved in a contrived scheme to cheat the Revenue by dishonestly offsetting in period 08/06 the input tax claim incurred in its razor blades transactions against the output tax liability in the mobile phone transactions with the intention of concealing its role as a broker in fraudulent tax loss chains. In short the Tribunal is satisfied that *Famecraft* acted as a dishonest contra-trader. The Tribunal rejects the Appellant's suggestion that it was not aware of HMRC's case in respect of *Famecraft.* The Tribunal has already expressed its view about the particularisation of pleadings in paragraphs 29 – 36 above. The Tribunal is satisfied that HMRC allegations regarding *Famecraft* were made out in the decision letter, statement of case and the witness statements of Ms Susan Okolo, Mr Peter Cameron-Watson and Nigel Humphries.

72. The Appellant accepted that *Barato* had incurred a fraudulent tax loss in the August 2006 razor blade transactions but that it did not know of and its transaction had no connection with *Barato's* fraud.

73. The Tribunal makes the following findings of fact in respect *of Barato*:

(1) The purported trade in razor blades had no connection with *Barato's* trade classification of *wholesale of soft drinks and foodstuffs* under its VAT registration dated February 2005.

(2) A massive increase in turnover in a short period of time. In the period 05/06 *Barato's* declared sales were £76 million from nil sales in period 05/05.

(3) *Barato* has not produced to HMRC its business records for the purported deals. Apparently the records were kept on a memory stick.

(4) *Barato* failed to deliver VAT returns for period 08/06 and for the final period prior to de-registration on 25 October 2006.

(5) *Barato* has not paid or appealed the assessment to the value of £22,967,287.

(6) A winding up order was made against *Barato* on 13 June 2007.

74. The Tribunal is satisfied on the facts found that the VAT losses incurred by *Barato* in the August 2006 razor blades transactions were occasioned by fraud.

Were the Appellant's transactions connected with the Fraudulent Tax Losses?

75. HMRC relied on the analysis of the deal chains carried out by Miss Harry to demonstrate that the Appellant's disputed transactions were connected with fraud. The Appellant in its Notice dated 19 July 2011 accepted that the stock purchased by the fraudulent companies was imported from other EU Member states and traded through a series of UK companies (as identified in HMRC's evidence), and was the same stock purchased by the Appellant and *Famecraft.*

76. The Appellant, however, disputed as a matter of law that its transactions were connected with fraud. The Appellant also challenged the factual connection between *Famecraft's* trades in mobile phones and razor blades in period 08/06, which

suggested that the Appellant was disputing whether its trade in deal 8 was connected with a fraudulent tax loss.

77. The Tribunal deals first with the legal argument. The Appellant contends that The Court of Justice decision in *Kittel* was of narrow application and applicable only in cases where the taxable person was a direct counterparty to the fraud. According to the Appellant, it was plain from the context of the references that the conclusion expressed by The Court of Justice in *Kittel* was confined to cases involving either the perpetrator of a fraud or the witting counterparty of such a perpetrator. The Appellant pointed out that it did not purchase any of its goods in the disputed transactions from the company that perpetrated the fraud.

78. HMRC contended that Appellant's proposition was wrong in law citing Lord Justice Moses in *Mobilx* paragraph 62

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

79. HMRC also referred to the decision of Mr Justice Roth in *Powa (Jersey) Ltd v The Commissioners for Her Majesty's Revenue & Customs* [2012] UKUT 50 (TCC) who concluded at paragraph 39:

> "…the judgment of the Court of Appeal is clear authority, binding on the Upper Tribunal, that the fact that the trader claiming credit for input tax did not deal directly with a fraudulent trader but was more remote in the chain does not preclude his being denied repayment under the rationale of *Kittel*."

80. Mr Justice Newey in *S & I Electronics PLC v The Commissioners for Her Majesty's Revenue & Customs* [2012] UKUT 87 (TCC) at paragraphs 20-30 followed Roth J's conclusions as to the law.

81. HMRC asserted that the Tribunal was bound by both the Court of Appeal's judgment in *Mobilx* and the Upper Tribunal's decisions in *Powa (Jersey) Ltd* and *S & I Electronics PLC* in that the *Kittel* judgment was not confined to perpetrator of a fraud and the witting counterparty of such a perpetrator

82. On the 21 June 2012 The Court of Justice promulgated its judgment in the combined cases of *Mahageben kft* (C-80/11) and *Peter David* (C142/ 11). At paragraph 45 of its decision The Court of Justice said:

> " In those circumstances a taxable person can be refused the benefit of the right to deduct only on the basis of the case law resulting from paragraphs 56 – 61 of *Kittel and Rocalta Recycling* according to which it must be established, on the basis of objective factors, that the

> taxable person to whom were supplied the goods or services which served as the basis on which to substantiate his right to deduct knew or ought to have known that the transaction was connected with fraud previously committed by the supplier or another trader at an earlier stage in the transaction".

83. At paragraph 49 The Court of Justice repeated the formulation that "*the transaction was connected with fraud previously committed by the supplier or another trader at an earlier stage in the transaction"*.

84. The Tribunal agrees with HMRC's understanding of the law that HMRC is required to establish on the balance of probabilities that the Appellant's transactions were connected with fraudulent evasion. It matters not whether that fraud was occasioned by the Appellant's immediate counterparties or by some other trader provided HMRC can show a connection between the Appellant's transactions and fraud. HMRC's understanding is based on The Court of Appeal decision in *Mobilx* which is binding on this Tribunal. There is an inference in the Appellant's submission that the Tribunal can somehow depart from the Court of Appeal if it considers that its decision in *Mobilx* is inconsistent with The Court of Justice decision in *Kittel.* In the Tribunal's view this proposition has no traction and been put to bed by the judgments of The Court of Justice in *Mahageben kft* (C-80/11) and *Peter David* (C142/ 11).

85. In respect of the factual dispute regarding deal 8, the Tribunal finds that the Appellant's transaction which took place on 19 July 2006 and involved mobile phones was traced back to *Trimax* and then to *Famecraft.* This transaction formed part of a series of mobile phone transactions which was used by *Famecraft* in an attempt to conceal the fraudulent tax losses in the razor blades transactions[9]. The Tribunal is satisfied that the Appellant's transaction in deal 8 was connected with the dishonest contra-trader, *Famecraft* and thereby with the fraud.

86. The Appellant raised separate legal issues about the required state of knowledge where an allegation of contra-trading was involved, which will be dealt with later. At this juncture the Tribunal is solely concerned with whether there was a factual connection between deal 8 and a fraud.

87. The Tribunal concludes from the analysis of the deal chains presented in evidence which has not been challenged by the Appellant in respect of the direct tax losses that the Appellant's transactions in deals 1-4, 6 and 7, and 9–13 were connected with fraudulent VAT evasion. The Tribunal decides on the facts found that the Appellant's transaction in deal 8 was also connected with fraudulent VAT evasion.

Did the Appellant know or should have known?

Introduction

88. The burden was upon HMRC to prove on the balance of probabilities that the Appellant knew or should have known at the time of entering the disputed

[9] See the Tribunals findings at paragraphs 66 – 71 above.

transactions that they were connected with the fraudulent evasion of VAT. In this Appeal it was Mr Jaswal's state of knowledge at the relevant time which was the question in issue.

89. HMRC's primary case was that the Appellant had actual knowledge of its transactions being connected with fraud. The Appellant submitted that when actual knowledge was pleaded, the Tribunal must be satisfied that the Appellant knew that its transactions were connected with fraud. In this respect the Appellant stated the Tribunal would have to find that the Appellant was so directed by fraudulent controlling minds and that the Appellant knew without doubt that its transactions were for fraudulent purposes. In short, the Appellant's director was a fraudster and part of a conspiracy to defraud the Revenue.

90. HMRC disagreed with the Appellant's understanding of the law in relation to the requisite state of knowledge. HMRC argued that there was no requirement for it to prove that *"the Appellant was a fraudster."* The test for the Tribunal is whether at the time of entering the transactions the Appellant knew or should have known of the connection between its transactions and the fraudulent evasion of VAT. If that test is met then the Appellant's transactions fall outwith the scope of VAT. HMRC relied on *Mobilx* where Lord Justice Moses at paragraph 41 said:

> "Kittel did represent a development of the law because it enlarged the category of participants to those who themselves had no intention of committing fraud but who, by virtue of the fact that they knew or should have known that the transaction was connected with fraud, were to be treated as participants. Once such traders were treated as participants their transactions did not meet the objective criteria determining the scope of the right to deduct."

91. The Tribunal agrees with HMRC's submissions on the requisite state of knowledge. The Court of Appeal in *Mobilx* emphasised that the test in *Kittel* was simple and should not be over-refined. The Tribunal, therefore, has to be satisfied on the balance of probabilities that the Appellant knew or should have known at the time of entering the disputed transactions that they were connected with the fraudulent evasion of VAT.

92. The Appellant contended in respect of deal 8 which concerned contra-trading that HMRC had to prove a conspiracy to commit fraud between all parties in both chains and that there were problems when the clean chains were conducted before any specific dirty chains may have even been planned. The implication being that the test in relation to the Appellant's state of knowledge was somewhat different in a contra-trading situation from that involving a direct tax loss chain.

93. HMRC disagreed, arguing that the test in relation to the Appellant's state of knowledge remained the same whether the transaction chain involved contra-trading or a simple tax loss chain. HMRC cited in support the decision of Mr Justice Briggs in *Megtian Limited (in Administration) v The Commissioners for HMRC* [2010] EWHC 18 (Ch) which at paragraphs 37 and 38 he said:

> "In my judgment there are likely to be many cases in which a participant in a sophisticated fraud is shown to have actual or blind-eye knowledge that the transaction in which he is participating is connected with that fraud, without knowing, for example, whether his chain is a clean or dirty chain, whether contra-trading is necessarily involved at all, or whether the fraud has at its heart merely a dishonest intention to abscond without paying tax, or that intention plus one or more multifarious means of achieving a cover-up while the absconding took place.
>
> Similarly, I consider that there are likely to be many cases in which facts about the transaction known to the broker are sufficient to enable it to be said that the broker ought to have known that his transaction was connected with a tax fraud, without it having to be, or even being possible for it to be demonstrated precisely which aspects of a sophisticated multi-faceted fraud he would have discovered, had he made reasonable inquiries. In my judgment sophisticated frauds in the real world are not, invariably susceptible as a matter of law, to being carved up into self-contained boxes even though, on the facts of particular cases including Livewire that might be an appropriate basis for analysis".

94. Mr Justice Roth in *Powa (Jersey) Ltd* agreed with Mr Justice Briggs concluding at paragraph 53:

> "In any event, it is clear from the Court of Appeal judgment in Mobilx, where one of the three cases under appeal was Blue Sphere Global, that no special approach is required in a case involved in contra-trading. The correct test as regards knowledge is always the same. It is the test derived from Kittel as set out in para [59] of Moses LJs judgment:…"

95. HMRC also pointed out the fact that *Famecraft's* mobile phone transactions preceded the razor blade transactions with the tax loss did not have a bearing on the legal test to be applied which was confirmed by Lord Justice Moses in *Mobilx* at paragraph 62:

> "If the circumstances of that purchase are such that a person knows or should know that his purchase is or will be connected with fraudulent evasion, it cannot matter a jot that that evasion precedes or follows that purchase."

96. The Tribunal agrees with HMRC's submission that the question of whether the Appellant knew or ought to have known of a connection between its transactions and a fraud did not depend upon knowledge of a particular aspect of the fraud. The test is the same regardless of the type of fraud committed. HMRC must prove that the Appellant knew or should have known that its transactions were connected with the fraudulent evasion of VAT.

97. The Tribunal is required to consider all the available and relevant evidence when determining the Appellant's state of knowledge, otherwise termed as the big picture approach. The authority for this proposition is derived from Lord Justice

Moses' endorsement[10] of Mr Justice Christopher Clarke's dicta in Red12 v HMRC [2009] EWHC 2563:

> "109 Examining individual transactions on their merits do not, however, require them to be regarded in isolation without regard to their attendant circumstances and context. Nor does it require the tribunal to ignore compelling similarities between one transaction and another or preclude the drawing of inferences, where appropriate, from a pattern of transactions of which the individual transaction in question forms part, as to its true nature e.g. that it is part of a fraudulent scheme. The character of an individual transaction may be discerned from material other than the bare facts of the transaction itself, including circumstantial and "similar fact" evidence. That is not to alter its character by reference to earlier or later transactions but to discern it.
>
> 110 To look only at the purchase in respect of which input tax was sought to be deducted would be wholly artificial. A sale of 1,000 mobile telephones may be entirely regular, or entirely regular so far as the taxpayer is (or ought to be) aware. If so, the fact that there is fraud somewhere else in the chain cannot disentitle the taxpayer to a return of input tax. The same transaction may be viewed differently if it is the fourth in line of a chain of transactions all of which have identical percentage mark ups, made by a trader who has practically no capital as part of a huge and unexplained turnover with no left over stock, and mirrored by over 40 other similar chains in all of which the taxpayer has participated and in each of which there has been a defaulting trader. A tribunal could legitimately think it unlikely that the fact that all 46 of the transactions in issue can be traced to tax losses to HMRC is a result of innocent coincidence. Similarly, three suspicious involvements may pale into insignificance if the trader has been obviously honest in thousands.
>
> 111 Further in determining what it was that the taxpayer knew or ought to have known the tribunal is entitled to look at the totality of the deals effected by the taxpayer (and their characteristics), and at what the taxpayer did or omitted to do, and what it could have done, together with the surrounding circumstances in respect of all of them."

98. The Appellant proposed that the Tribunal should focus on the circumstances of the purchase when determining knowledge. Further that the Tribunal must only consider what the Appellant knew at the time of entering into its transactions based on the material actually available at that time and not material subsequently disclosed in the course of the Appeal.

99. The Tribunal considers that the Appellant's focus on the circumstances of the purchase has overlooked the Court of Appeal's endorsement of the big picture approach, namely, the attendant circumstances and context of the disputed transactions should be examined when determining the requisite state of knowledge.

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[10] See *Mobilx para. 83.*

100. The Tribunal agrees with the Appellant that the correct legal test is the Appellant's state of knowledge at the time it entered the disputed transactions. This, however, does not mean that the Tribunal ignores the big picture in deciding whether that test is met in respect of each of the disputed transactions. Moreover the Tribunal is entitled to examine evidence which has come to light regarding the transactions as a result of HMRC's investigation. In respect of the latter the Tribunal accepts that hindsight cannot be applied to determine the Appellant's state of knowledge. It is, however, inherent in the alleged fraudulent nature of the transactions, that aspects of them would be hidden and only be uncovered after a thorough investigation. The acid test for evidence later coming to light is whether it is relevant to the Tribunal's determination about what the Appellant knew at the time it entered the transactions.

101.HMRC's case against the Appellant on the issue of knowledge was that in respect of each of the 12 transactions, the transaction chain was contrived as part of an overall scheme to defraud the Revenue, and that each party in the chain including the Appellant knew that they were contrived for that purpose. In HMRC's view the true inference to be drawn from the Appellant's appearance in the pivotal role of broker in contrived transactions was that it knew of the connection between the transactions and the fraudulent evasion of VAT.

102. HMRC argued that the above submission on the inference to be drawn from the Appellant's appearance in the contrived chains of transactions can be tested by reference to the evidence of:

(1) What the Appellant, on the face of its own documents, knew at the time of entering into the transactions.

(2) The credibility of the evidence given by Mr. Jaswal on the Appellant's behalf.

(3) The Appellant's conduct since the transactions and the production of documents after the event

103. HMRC contended that it was entirely consistent with Mr Justice Christopher Clarke's dictum in *Red 12* as cited in paragraph 98 above for the Tribunal to ascertain the wider circumstances of the Appellant's transactions before examining what the Appellant must have known from the transaction documentation generated between it and its immediate counterparty. Such an approach has, in HMRC's view been endorsed by Newey J in *Regent Commodities Limited v HMRC* [2011] UKUT 259 (TCC) at paragraph 46. At that paragraph of the judgment Newey J was dealing with two types of evidence of the wider circumstances to that Appellant's transactions, both of which are present in the instant case (i) documentation that proved an overall contra-scheme and (ii) evidence of circularity of funds within the FCIB. Newey J stated:

> "To my mind, it was open to the Tribunal to take the view that each of the matters mentioned in sub-paragraphs (i) to (xi) of paragraph 43 above suggested actual knowledge on the part of Regent. I should have thought, moreover, that, in the circumstances of the present case, the evidence given by Mr Humphries and Mr Mendes (as to which, see paragraphs 17-31 above) would of itself have

> sufficed to entitle the Tribunal to make a finding of actual knowledge. As already mentioned, the Tribunal considered (with justification, in my judgment) that that evidence indicated that Regent knew to whom it was supposed to sell."

104. The Appellant's case was that it did not know of the fraud in the supply chains and had no way of identifying the fraud. The Appellant asserted that it was so far removed from the alleged defaulting traders that it would not have any means of identifying the alleged fraud.

105. The Tribunal's examination of the facts follows the approach advocated by HMRC. The Tribunal considers first whether the 12 transactions were contrived as part of an overall scheme to defraud the Revenue, and if they were, to determine on the evidence whether the Appellant knew that they were connected with fraud at the time the Appellant entered into them.

Were the Appellant's transactions contrived and part of an overall scheme to defraud?

The links between the Appellant, Mr Bedesha and Nijjers

106. HMRC asserted that the Appellant's movement into the wholesaling of mobile telephones was inextricably linked to the activities of two other individuals, Mr. Pardip Nijjer and Mr. Jasbinder "Jack" Bedesha.

107. The Tribunal makes the following findings of fact

(1) The Appellant was originally known as *Artefacts By Design* and registered for VAT on 18 March 2003. The VAT1 declared that the Appellant's main business activity was *retailer of furniture and wooden artefacts.* The Appellant ran its business from a concession within a department store. On 16 August 2005 the Appellant changed its name to the current one. On 19 August 2005 Mr. Jaswal advised HMRC that the name change had come about as the Appellant had decided to start trading in electronic goods and requested a change to monthly VAT returns as it would be exporting inside and out of the European Union.

(2) Pardip Nijjer was appointed a director of Nijjers on 9 April 2003. Nijjers was registered for VAT on 25 July 2003 with a declared business activity of running a *Subway* sandwich bar. On 28 July 2005, Nijjers informed HMRC of its intention to begin wholesaling electronic goods.

(3) Mr Bedesha was Mr. Jaswal's brother-in-law and had lent him £26,350 at the time the Appellant was set up under the name of *Artefacts by Design.* Mr Jaswal, the Appellant's director, was related to Pardip Nijjer on his wife's side.

(4) Mr Nijjer and Mr Bedesha supplied references on 21 and 22 November 2005 respectively in support of the Appellant's application to open an account with FCIB. Mr Nijjer and Mr Bedesha stated in the references that they had known Mr Jaswal for 10 years. Mr Jaswal in turn supplied a reference for Pardip Nijjer in respect of *Nijjer's* application for a FCIB bank account.

(5) Mr Nijjer had connections with Mr Bedesha through his company called Rawlings Voigt Ltd. A director of that company, Mr Hasu Patel, was also the company secretary and accountant for one of Mr Nijjer's companies, *Python Trading.*

(6) In the summer of 2005, the time at which both the Appellant and *Nijjers* began wholesaling mobile telephones, Mr Bedesha was operating a company called *Anisha Brokers LLC* wholesaling mobile telephones as part of a criminal conspiracy to cheat the revenue. On 16 December 2010 Mr. Bedesha was convicted of conspiring to cheat the public revenue and money laundering and sentenced to 7 ½ years imprisonment. The opening note for the prosecution of Mr. Bedesha and others demonstrated his central role in the conspiracy. *Anisha Brokers* received several third party payments in the course of the fraud. Those third party payments were the method employed by Mr Bedesha and the other fraudsters to move the VAT monies out of the jurisdiction to Dubai

(7) *Nijjers* was the Appellant's supplier in four of the 12 disputed transactions. The Appellant in turn supplied *Nijjer* in deal 5 (the buffer transaction). The customer, *Blue Star Telecom* was the same in deals 3 and 5 where *Nijjers* and the Appellant took it in turns to be the supplier to each other. In 07/06 *Nijjers* transacted ten mobile phone deals as a broker. All the deals have been traced back to a fraudulent tax loss. The trading patterns for *Nijjers* and the Appellant in the 07/06 period shared many similarities. They had common suppliers in *Data Solutions Northern, NTS Telecom* and *Trimax Trading.* They had common customers in *Compucell BV, Blue Star Telecom APS* and *Alimed.* They used the same freight forwarders: *Pauls Freight, ASR Logistics, Central Solutions* and *1st Freight.* There were also common defaulters in the deal chains, *Phone City* and *Kaymore Export.*

(8) *Nijjers* and the Appellant entered the *Famecraft* contra trading scheme on the same date. They also used newly opened ICB bank accounts with consecutive account numbers in respect of the deals connected with *Famecraft.*

(9) *Nijjers* and the Appellant both made use of the same *due diligence* company *Pro-Intell.* Mr. Nijjer was connected with the director of *Pro-Intell*, Ms Gill, in that they shared a mortgage on a residential property in Coventry.

(10) After the mobile telephone wholesaling business of both the Appellant and *Nijjers* had ceased the relationship between those behind the two companies remained. On 19 December 2007 Kamaldip Nijjer, the company secretary for *Nijjers*, Mr. Jaswal and Baljit Jaswal were appointed company officers of Warner Leisure Ltd.

(11) HMRC denied *Nijjers*' input tax claims in the sums of £583,583.19 and £1,068,444 for periods 04/06 and 07/06 on the basis that the transactions were connected with fraud and that *Nijjers* knew or should have known of that connection. All of *Nijjers*' denied transactions have been traced to the fraudulent evasion of VAT. *Nijjers* appealed HMRC's decisions but Mr. Nijjer stated that he was not prepared to give evidence and ultimately withdrew his appeal. *Nijjers* was wound up on 7 July 2011.

The Other Parties in the Appellant's Deals

108. HMRC asserted that the buffer traders and the customers in the Appellant's deals, together with the freight forwarder 1st Freight in the contra-trade (deal 8) were knowing participants in an overall scheme to defraud the Revenue. According to HMRC, the transactions involving the Appellant were not frauds solely attributable to the missing trader at the end of the fraud.

109. The Tribunal finds the following in respect of the buffer traders:

(1) *Gemini Technology Ltd* (Deals 1, 2, 9 and 12): the deals were completed after *Gemini* had been deregistered from VAT on 19 May 2006. Its director, Mr Ahmed, disregarded HMRC's advice given in person on due diligence. A cursory check of Companies House and VAT certificate information in relation to the company, *Heathrow Business Solutions*, that *Gemini* purchased from in deals 1 and 2 would have revealed that the company had no business wholesaling mobile telephones as it was an IT recruitment and software company.

(2) *Data Solutions Northern Ltd* (Deals 1, 2, and 12): On 17 May 2006 HMRC informed *Data Solutions* that everyone of its 100 sales in period 05/06 had been traced to a defaulting trader resulting in a tax loss exceeding £12,800,110. Despite the warning, *Data Solutions* continued with its activities demonstrated by its appearance in the Appellant's and *Nijjers'* deal chains in June and July 2006. Mr Keith Thelwell, director, was made the subject of a 14 year-long director's disqualification order by the Companies Court on 4 February 2009. The unfit conduct found against Mr. Thelwell included that he had caused *Data Solutions* to enter into transactions resulting in claims for more than £22.7million in VAT.

(3) *AB International Trading Ltd* (Deal 4): On 19 April 2006 HMRC informed *AB International Trading* that one of its transactions in December 2005 had been traced to a fraudulent trader. *AB International Trading*, however, continued trading. On 25 June 2008 HMRC denied input tax in the sum of about £850,000 for VAT periods 06/06 and 09/06. HMRC's decision letter recorded that *AB International Trading* did not retain IMEI numbers; did not insure its goods, had poor due diligence and had an extraordinary turnover in 2006 of £19.5million despite employing no staff.

(4) *NTS Telecom.net Ltd* (Deals 5, 6 & 13): The company used *Pro-Intell* as its *due diligence* company. HMRC investigations revealed that *NTS Telecom.net Ltd* ignored the information provided in the due diligence reports. On 14 December 2009 Mr. Rashid, the director gave an undertaking that he would not act as a company director for a period of 12 years. The unfit conduct listed in the schedule to Mr. Rashid's undertaking was stated to be: "*NTS Telecom.net Ltd made sales of wholesale mobile telephones and computer components of at least £19.6million between periods 10/05 and 10/06, Mr. Rashid failed to ensure that checks were undertaken on its counterparties*". HMRC assessed *NTS Telecom.net Ltd* for £672,925. Further HMRC disallowed its input tax in relation to a sale to Dubai in period 10/06 that was deemed to be connected with fraud.

(5) *Talking Digital Ltd* (Deal 5): Its trade in mobile phone wholesaling was inconsistent with its stated business of *retail sale of electrical household appliances and radio and television goods*. Its director, Bhabdeep Singh Chahal, was disqualified from being a director for six years from 7 July 2008.

(6) *Reya Ltd* (Deals 6 and 13): HMRC denied *Reya's* input tax claim for period 03/06 on the ground that its mobile phone transaction was connected with fraud. The decision letter pointed out that *Reya* had not inspected the goods or retained any IMEI numbers and had carried out barely any due diligence. A further input tax denial letter was issued to Reya in relation to two of its purchases in periods 06/06 and 09/06.

(7) *Simply Connect Ltd* (Deal 7): Mr Shahzad Hussain, the company secretary, confirmed that the wholesale part of the business started trading on 14 July 2006 and ended on 11 August 2006 when HMRC instructed *Simply Connect* to cease. *Simply Connect* was to receive commission on deals conducted and money due on their sales was to be routed through to *Kaymore* but that no payments had yet been received from *Kaymore.*

(8) *Imang Ltd* (Deal 7): Mr Vimal Patel, company secretary, stated that the wholesale deals started in July 2006 and were only done for one month. The supplier was *Simply Connect Ltd* and the customer was *Ultimate Wholesale Ltd.* Imang was to receive a commission and the customer was going to make the rest of the payment directly to the supplier.

(9) *H Communications Ltd* (Deals 7 and 9): HMRC denied an input tax claim of *H Communications Ltd* in the sum of £104,119.89 incurred on the purchase of 3,000 mobile telephones in period 09/05. *H Communications* was linked to the buffer *Talking Digital* (which changed its name to *Chahal Trading*) by a common director/company secretary.

(10) *Trimax Trading International Ltd* (Deal 8): HMRC denied *Trimax Trading's* input tax claims exceeding £13 million on the purchases of mobile telephones between March to June 2006.

(11) *Star Express Ltd* (Deals 9, 10, 11): HMRC denied *Star Express'* claim for input tax of £249,725.25 on the purchase of computer chips in VAT period 08/06 on the basis that the two transactions involved had been traced to fraudulent tax losses and that *Star Express* knew or should have known of that connection.

(12) *Sky Pro 2020 Ltd* (Deal 13): *Sky Pro* only started trading in mobile telephones on 17 August 2006 and had no previous experience in the business. Its director confirmed that he neither inspected nor insured the goods.

(13) *Regal Portfolio Ltd* (Deal 13): On 10 May 2010 the Companies Court disqualified the director of Regal Portfolio Ltd for a period for 14 years from 10 May 2010. The unfit conduct leading to the disqualification included: making sales of at least £206m, issuing payment instructions for third parties to be paid monies owed to Regal of about £3.5million, materially contributing to the liquidation of six of its suppliers due to the use of third party payment instructions,

ignoring failed VRN verification checks and failing to maintain, preserve and deliver up accounting records to the Official Receiver.

(14) *Vital Tec Ltd* (Deal 13): failed to submit complete business records or VAT returns for periods 01/06, 04/06 and 07/06 to HMRC. Redhill blocked the company's VRN from 13 July 2006.

110. The Tribunal finds the following in respect of the Appellant's customers:

(1) *Goldphone SL* (Deal 1): The Spanish Authorities reported its conclusions on *Goldphone* to HMRC stating that

> "Evidence has been found, designed to pretend carrying out a real business activity. However, from the way it operates, and because the clients do not pay in VAT, the tax office has serious doubts on whether the company is effectively carrying out these operations. The only sure thing is that a VAT fraud is being committed."

(2) *Agrupacion De Alimentos Mediterraneos SL ("Alimed")* (Deal 8): The Spanish Authorities reported its conclusions on *Alimed* to HMRC stating that

> "Enough facts and evidence have been gathered to argue that Alimed takes part in a VAT carousel fraud scheme within the mobile phone sector. It acts as conduit company located in a different member state than that of the supplier and the end recipient of the goods, so these never enter Spanish territory (as the company's administrator himself has confirmed)."

(3) *Compucell BV* (Deal 12): The Netherlands authorities informed HMRC that: the director of Compucell since 2 June 2005 was a Mr. Amonker, an Indian national, who had no address in the Netherlands. *Compucell's* Vat Registration Number had been withdrawn from 30 September 2006. The VAT returns rendered by *Compucell* did not match the purchase and sales invoices found and that criminal proceedings would be started against the company.

(4) There were clear links between *Compucell*, *Blue Star* (deals 3,4, 5 & 9), *Blue Alfa* (deals 6,7,10 & 11) and *Al-Saqr* (deal 13). The Directors of *Compucell* and *Blue Star* had both previously worked for *Cellucom*. *Blue Star* provided *Compucell* with a reference for its application to open an account with FCIB. The personal addresses of the Directors of *Blue Star* and *Blue Alfa* were the same flat in Dubai, 522 Hamad Khamis Al Ghuwaid Building. *Compucell* provided *Blue Alfa* with a reference for its application to open an account with FCIB. Finally *Al Saqr* provided *Blue Alfa* with a reference for its application to open an account with FCIB.

111. The Tribunal is satisfied that *1st Freight*, the freight forwarder, which purportedly inspected and transported the goods of the *Appellant* and *Nijjer* in the split contra deal of which the Appellant's deal 8 formed a part, was a participant in the fraud. This conclusion was supported by the facts:

(1) *1st Freight's* warehouse was too small to contain the number of telephones claimed on deal documentation to be present there on certain dates.

(2) The vehicle registrations on the CMRs produced by *1st Freight* were found to relate to vehicles which did not carry out the declared purported journeys.

(3) The IMEI numbers provided by *1st Freight* contained the same pattern running through all of them whereby the penultimate digit of the number ran continuously from 0 – 9 and the IMEI numbers followed on in batches from those provided to other traders. Thus *1st Freight* did not scan IMEI numbers for its customers but merely provided them from a list that been illicitly obtained.

The Defaulting Traders and Famecraft's Supplier in the Contra Acquisition Chain

112. HMRC contended that the sudden appearance and disappearance of the fraudulent defaulting traders from the deal chains showed that those orchestrating the fraudulent defaults had a pool of valid VAT registration numbers which could be used to create VAT defaults for a short period and stay ahead of HMRC's investigations. The Tribunal considers that the facts speak for themselves which were summarised at paragraph 102 of HMRC's opening submissions dated 22 May 2012. The Tribunal decides that the inference of an available pool of VAT registration numbers to perpetuate the fraud is justified on the facts.

113. *Sinderby Enterprises*, the Cypriot supplier to *Famecraft* in deal 8 had no business establishment and no employees in Cyprus. Its bank account was never used. *Sinderby* traded only for 40 days, during which time it made sales totalling over 130 million Cyprus pounds. The Tribunal is satisfied that *Sinderby* was solely set up to facilitate MTIC fraud.

The Deal Chains and Movement of Goods

114. HMRC argued that the pattern and structure of the deal chains including the contra trade showed that they had no commercial function. The Tribunal finds the following facts:

(1) The length of the direct tax loss deal chains in each of the disputed transactions ranged from six to ten traders. The membership of those chains was remarkably consistent which appeared to be organised in blocks. *Nijjers, The Fones Centre, Gemini Technology, Blue Star Telecom* and *Blue Alfa com* appeared at least four times in the Appellant's direct chains. *ET Phones, Star Express* and *Data Solutions Northern Ltd* appeared three times in the Appellant's chains.

(2) The mobile phones in the acquisition chain of the contra-trade found their way from a single Portuguese supplier via 29 different UK traders of which the Appellant was one, to the same two Spanish customers.

(3) Each deal chain was traced to a fraudulent tax loss[11].

(4) The traders in the deal chains did not add any value to the mobile phones transacted. None of the traders in the chains were manufacturers or authorised

[11] Deal 8 was traced to a fraudulent tax loss by the offsetting undertaken by *Famecraft.*

distributors. The mobile phones were sold again and again without ever reaching an end user or consumer. The deal chains showed no signs of a commercial hierarchy with wholesalers selling large amounts and their customers selling smaller numbers to retailers.

(5) All the Appellant's transactions were completed on a back-to-back basis. In each deal the Appellant's supplier held the exact stock in the exact quantity that was required by its customer or vice-versa. There was no evidence that the Appellant was holding stock to take advantage of market fluctuations in price.

(6) The mobile phone consignments for each deal were bought from a country outside the UK passed through various UK companies and then exported by the Appellant to a trader outside the UK. With most of the deals the consignments passed through the hands of companies based in several different EU countries all on the same day. For example, in deal 6 the Appellant was involved in a transaction in which the phones were purportedly traded between companies based in Belgium and passed through six UK traders before being exported to Denmark and then to Spain.

(7) In deals 3, 4, and 12 the mobile phone consignments were carouselled in and out of the UK.

(8) There was a high degree of consistency in the level of the mark ups through the chains with the initial buffer traders receiving mark-ups of around 25 pence per phone and later buffers from £0.50-£1.50 per phone. The Appellant's mark up as a broker was much more substantial ranging from £5 to £30 per phone. This pattern was repeated in deal 5 where the Appellant as a buffer made a £1 mark up, whereas its customer (Nijjers), the broker, made a mark up of £22.50.

(9) The mobile phones traded had an EU specification with a two pin plug, which meant that the phones ostensibly had no market within the UK.

The Money Flows and the Banking Evidence

115. HMRC asserted the evidence on the analysis of the FCIB data demonstrated that the transactions except deals 8 and 13[12] were characterised by circular money flows which could have only happened if every trader in the respective chain knew who to sell to and buy from and at what price. Further the wider banking evidence highlighted the contrived nature of the transactions.

116. The Tribunal finds the following findings:

(1) There was a true circularity of funds in deals 6,9,10 and 11 whereby the funds in large part returned to the company with whom they originated.

(2) Deals 1, 2, 3, 4, 6 and 12 were characterised by a wider circularity of funds where the money circulated in and out of the UK (UK/EU/UK/EU/UK) through a small and well defined group of traders, comprising *Silus, Alfa Tradezone, Imanse, Blue Alfa Com, Compucell* and *Blue Star.*

[12] Deals 8 and 13 did not involve FCIB but other internet banks

(3) Funds from deal 10 financed the broker purchase in deal 11.

(4) The widespread use of references from other traders in the deal chains in support of applications to open FCIB accounts.[13]

(5) All of the Appellant's suppliers and customers each banked with FCIB. The customers were from five different countries.

(6) Pounds sterling was the currency used in each and every money movement regardless of the country in which the company making or receiving the payment.

(7) In deal 8 the Appellant used an account with the International Credit Bank (ICB). The Appellant's payment from that account to fund the purchase happened on the same day as the account was opened. All of the other companies involved in the *Famecraft* contra trade of which HMRC have evidence banked with ICB with the accounts being opened in a very short period of time and having very close account numbers.

(8) In deal 13 the Appellant used a third obscure offshore account with the Universal Mercantile Building Society (UMBS), purportedly based in Sweden but utilising the clearing facilities of Banco Portugese de Negocios in Portugal. At least two other companies in the deal chain *Reya*, the Appellant's supplier and *NTS Telecom* were also using accounts with UMBS.

(9) The Appellant held other bank accounts with UK High Street Banks: Barclays and HSBC which were in place before it opened the accounts with the offshore banks.

Grey Market

117. HMRC contended that the Appellant did not exhibit the characteristics of a business trading in the legitimate grey market in mobile phones.

118. Mr. Fletcher set out in his witness statement the trading opportunities in the grey distribution market for mobile telephones and the characteristics of a business seeking to make use of such opportunities. Mr. Fletcher identified four grey market opportunity scenarios: box breaking, arbitrage, volume shortages and dumping.

119. The Appellant contended that Mr Fletcher's evidence was generic and derived from research conducted after the disputed transactions took place. The Appellant stated that Mr Fletcher's evidence has been found unreliable and outdated by many Tribunals. The Appellant cited the decision in *Emblaze Limited* (TC 00680) where at paragraphs 225-226 the Tribunal stated :

> "We accept the submission of Mr Patchett-Joyce that there was no need for Global to know the reasons of its customers for their purchases and what market opportunity they were addressing. From a

[13] See paragraphs 107 (4) & 110(4) above. Further examples include *Silus & Gemini & Jos (UK) LTD & Label Clothing. ET Phones & Heathrow Business* both obtained references from Norton Peskett.

> commercial viewpoint all that Global needed to know was that a customer was willing to pay a price which gave Global a profit. While the type of analysis of market opportunities which Mr Fletcher envisages might be a useful marketing tool in some types of business, it does not seem to us that such analysis was to be expected in grey market transactions in mobile phones. It is to be remembered that Global had a considerable business in mobiles in the domestic market which has not been questioned which was also on the grey market.
>
> We regard Mr Fletcher's evidence as to the size of the total retail European market (paragraphs 135 and 136 above) with reservation, particularly in the light of Vodaphone's 8.52 million new customers in 2006-07 in Italy. In any event there was no evidence that Mr Drinkwater or Global were aware that their sales were out of line with those of the market as a whole."

120. The Appellant argued that Mr Fletcher's evidence principally appeared to be opinion and should be treated with caution.

121. HMRC argued that Mr Fletcher was an expert. His evidence was relevant and should be admitted. HMRC disagreed with the Appellant's assertion of many Tribunal decisions finding Mr Fletcher's evidence unreliable. HMRC had identified 14 First Tier Tribunal decisions which had admitted Mr Fletcher's evidence. HMRC had only found one appeal, *HT Purser Limited* [2011] UKFTT 860 (TC), where there was substantial criticism of Mr Fletcher's evidence by the Tribunal. In that case the Tribunal decided that Mr Fletcher could not be regarded as an expert because his employers, KPMG, had acted in accountancy matters for Nokia.

122. HMRC referred to the First Tier Tribunal decision in *Atlantic Electronics Ltd* [2011] UKFTT 314 (TC) which was given by Judge Wallace, who had been the Judge in the earlier decision of *Emblaze*. Judge Wallace said in *Atlantic* at paragraph 48:

> "However notwithstanding my own reservations of the value of Mr Fletcher's evidence, I recognise that others may take a different view. This is an important and complex appeal. It is inevitable that the Tribunal will have to consider the grey market if only because the Appellant relies on it. Mr Fletcher's evidence was served in 2009 without any objection until this year. I do not grant the application that it be excluded".

123. HMRC relied on the judgment of Sir Andrew Park in *Mobile Export Ltd v Revenue and Customs Commissioners* [2009] EWHC 797(Ch) which dealt with the evidence of a Mr Taylor on the market in mobile phones. Mr Taylor was also an employee of KPMG and described by HMRC as Mr Fletcher's predecessor. Sir Andrew Park ruled that Mr Taylor's evidence was relevant and admissible stating that

> "If HMRC wish to adduce in evidence a competent and informative analysis of a sector of business and of an appellant's activities within it, rule 28(1)[14], in my judgment, enables them to do that without having

[14] Rule 28 referred to the previous 1986 Tribunal Rules. Rule 15 of the 2009 Tribunal Rules is expressed in similar terms to rule 28 giving the Tribunal discretion to admit evidence.

> to meet technical arguments about whether the witness does or does not strictly rank as an expert".

124. HMRC's principal contention was that the Appellant had not actually challenged the admissibility of Mr Fletcher's evidence. The Appellant's objection appeared to be one of weight. According to HMRC, Mr Fletcher's evidence was relevant, in that it dealt with the grey market and how that market operated. Mr Fletcher's evidence was that a grey market existed but limited in respect of its range to four opportunities. HMRC submitted that what Mr Fletcher described as a grey market did not apply to the disputed deal chains, which was also corroborated by other evidence adduced by HMRC, particularly the existence of circular money flows.

125. The Tribunal decides that Mr Fletcher's evidence on the operation of the grey market was a relevant issue in this Appeal, particularly as the Appellant was a relatively new entrant in the mobile phone sector and Mr Jaswal's assertion that he had fully researched the market prior to the Appellant's trades. In the Tribunal's view Mr Fletcher held the necessary credentials for giving this evidence. He was a chartered accountant with a Masters in Business Administration from the London Business School. He had over 15 years experience in the telecoms industry, holding positions in audit, accounting, corporate finance and international business development. More recently he has worked as a strategic adviser to participants and investors in the industry. The Tribunal also considers that a dispute on general business practices in a specific market sector should be determined on the evidence and not on presumed specialist expertise on the Tribunal's part. In this respect the Tribunal considers that the step taken by HMRC to obtain a witness statement from an expert in the telecoms industry was appropriate and necessary.

126. The Appellant's principal challenges to Mr Fletcher's evidence were that it was compiled after the event, his analysis was not readily accessible and had no real relevance to an ordinary wholesaler who was simply interested in making a profit. The Tribunal considers that the Appellant's challenge had missed the point on the evidential value of Mr Fletcher's testimony and at the same time exaggerated its importance. In the Tribunal's view, Mr Fletcher's identification of the various characteristics of grey market opportunities provided a helpful reference point with which to assess the Appellant's trading but was just a part of the overall case presented by HMRC and not determinative on its own of the Appellant's state of knowledge.

127. The Tribunal decides that the Appellant's submissions did not undermine Mr Fletcher's analysis of the grey market in the mobile phone trade sector.

128. The Tribunal finds that the Appellant dealt almost exclusively with Nokia models which did not originate in the UK. Further the Appellant did not have a significant workforce, had no storage or warehouse facilities and held no stock. The Appellant also did not source stock from authorised distributors and used generalised product descriptions on its purchase orders and sales invoices. These features corresponded with the negative characteristics for each of the four grey market opportunity scenarios identified by Mr Fletcher. The Tribunal is satisfied that the

Appellant's transactions did not exhibit the characteristics of a business trading in the legitimate grey market in the mobile phones.

The Tribunal's Conclusions on Overall Scheme to Defraud

129. The Tribunal concludes on the big picture that the Appellant's transactions were part of a highly orchestrated web of transactions wholly bereft of a commercial rationale and carried out for the sole purpose of attracting a charge for UK VAT.

130. The structure and the length of the deal chains including the contra trade ran contrary to the profit maximising behaviour expected in commercial transactions. The back to back nature of the transactions indicated the absence of negotiation and bargaining on the part of the companies involved in the deal chains. The established and close relationship between some of the parties undermined the suggestion that they were acting at arms length. The circular money flows demonstrated that the transactions as a whole carried no commercial risk. The dealings in mobile phones with EU specifications questioned the involvement of UK companies in the chains. Finally there was no evidence of genuine grey market trading associated with the transactions. These findings on the lack of commercial rationale were amplified by the Appellant's dealings with *Nijjers*. It made no commercial sense for them to supply each other when they knew of overseas customers from whom they could secure significant profits far exceeding the meagre mark ups on the sales to each other.

131. The highly orchestrated nature of the big picture was supported by the findings on the use of an available pool of VAT registration numbers, the introduction of straw companies in the chains as buffers, the creation of a company to facilitate fraud, the consistent mark ups in the chains, the use of common offshore banking facilities, the opening of accounts with ICB, the existence of a small and well defined group of traders controlling the financing of the deals and the close co-operation between the traders in respect of providing references for each other. The orchestrated nature of the big picture was typified by the findings on the entry of the Appellant and *Nijjers* into the mobile phone trade sector and their close relationship, which questioned the independence of their decision making and whether they operated at arms length.

132. The findings on the movement of the mobile phones consignments in and out of the UK in a short space of time, the existence of carousels in some of the deals, the use of pound sterling as the common currency, and the illogical behaviour of overseas companies paying higher prices to UK companies for goods which could be obtained much cheaper on the continent led to the conclusion that the sole purpose of the transactions was to attract a UK VAT charge.

133. The Tribunal in reaching the above conclusions had regard to Mr Jaswal's witness statements and the Appellant's submissions. Mr Jaswal's contribution was minimal. His stance generally was that he had no knowledge of the big picture and that he saw nothing questionable in back to back trading, trading in EU specification mobile phones and his dealings in the grey market. Mr Jaswal studiously avoided commenting on Mr Bedesha and the opening of the ICB bank account.

134. Mr Jaswal's evidence on *Nijjers* was unconvincing and contradictory. At paragraph 55 of his first witness statement he questioned the relevance of the close relationship between the two companies, acknowledging at the same time he had a close business relationship with *Nijjers* and that *Pardip Nijjers* was related to his wife. Mr Jaswal's assertions at paragraph 55 were undermined somewhat by his comment at paragraph 32 of his statement that he found *Nijjers* on the International Phone Traders' website. Mr Jaswal's witness statement, however, was contradicted by the evidence of the respective references given by Mr Jaswal and Mr Nijjer for each other in respect of the opening of the FCIB accounts. In the references they both declared that they had known each other for over ten years. HMRC stated that the evidence of the references and the background connection between Mr Nijjer, Mr Jaswal and Mr Bedesha clearly showed that Mr Jaswal had lied about his relationship with Mr Nijjer and *Nijjers* in his statement. The Tribunal agrees with HMRC.

135. The Appellant's submissions on the big picture focussed on selected issues rather than on the overall fraudulent scheme as alleged by HMRC. The Appellant argued that there was no paper and no witness evidence to substantiate any allegation made by overseas authorities and no evidence before the Tribunal to suggest that any customer was still not a healthy, legitimate trading company. The Tribunal considers the submission inaccurate, overlooking the evidence of Miss Harry and Ms Danson on the status and connections of the Appellant's customers (see paragraph 110 above).

136. The Appellant's submissions on the FCIB and banking evidence were limited. The Appellant referred to the First Tier Tribunal decisions in *G Comms Limited* and *Blada Limited* which found that circularity of funds only substantiated an allegation of should have known not actual knowledge. Next the Appellant asserted that it opened three legitimate bank accounts and was unaware of who else opened up accounts and on what day. The Tribunal considers that the appeals by *G Comms Limited* and *Blada Limited* were decided on their own facts and have no significant bearing on the facts of this Appeal. The Appellant's assertion of three legitimate banks did not address the points made by HMRC about the rationale for using these offshore banks and in particular the switch to ICB and its close connection with deal 8. Finally the Tribunal observes that the Appellant knew about *Nijjers* opening an account with FCIB by the stint of the reference given by Mr Jaswal.

137. The Appellant denied knowledge of what other traders were paid in the supply chain and of the composition of those chains. The Appellant questioned HMRC's conclusions on EU specified mobile phones and back to back trading arguing that retailers and box breakers routinely changed plugs and there was nothing wrong with back-to-back trading. The Tribunal decides that the Appellant's assertions were unsubstantiated.

138. It follows from the Tribunal's conclusion on the Appellant's transactions in paragraph 129 that they were part of an overall scheme to defraud the Revenue. The fraudulent nature of the overall scheme was reinforced by the Tribunal's findings on the other parties in paragraphs 109 to 111. The existence of an overall scheme to defraud implied that the success of the scheme depended upon each participant buying from and selling to persons designated by those orchestrating the scheme.

139. HMRC argued that the true inference to be drawn from the Appellant's appearance in the pivotal role of broker in the contrived transaction chains for which it received the lion's share of the profits, was that the Appellant knew of the connection between its transactions and the fraudulent evasion of VAT. The Appellant denied that it knew of such connection. The Tribunal now tests this inference against those matters that the Appellant stated were within its knowledge.

Knowledge of MTIC Fraud

140. HMRC contended that the Appellant was fully aware of high risk of missing trader fraud in the mobile phone trade sector.

141. Mr Jaswal disagreed, stating that he knew there was risk of fraud but that Officer Patterson gave him the belief that the risk was not great. Mr Jaswal pointed out that he had only received one visit in October 2005 from HMRC prior to the commencement of the Appellant's trading in the mobile phone sector. At the October meeting Mr Jaswal accepted that Officer Patterson informed him about the existence of fraud but that he could avoid it if he carried out effective due diligence on the Appellant's suppliers. Mr Jaswal also accepted he received copies of Public Notice 726.

142. Mr Jaswal pointed out that after the October 2005 meeting he had no further personal contact from HMRC until October 2006 except for one brief telephone conversation with Mr Patterson. Mr Jaswal e-mailed Mr Patterson full details of the Appellant's transactions every month without any response. HMRC did not inform him about tax losses in the Appellant's transactions until September 2006 which was after the dates of the disputed transactions. At the October 2006 meeting Mr Jaswal stated that Officer Lewis informed him that his paperwork and due diligence were very good. Also Mr Jaswal alleged that the Officers told him that it was unnecessary for him to keep IMEI numbers.

143. Mr Jaswal argued that HMRC was very quick to say that it gave sufficient warnings of fraud, and by doing so HMRC accepted responsibility to impart such warnings. According to Mr Jaswal, he had good reason to believe that the Appellant was trading in an industry that was genuine in view of the praise that HMRC gave him.

144. HMRC accepted that there was only one visit of the Appellant prior to and during the period of the disputed transactions, and that Mr Jaswal complied with Mr Patterson's request to provide him with monthly reports of transactions made. HMRC also acknowledged that it made an administrative error in making the repayment on the Appellant's 04/06 VAT return and that the first time it informed the Appellant of tax losses in its deal chains was in September 2006.

145. HMRC disagreed with Mr Jaswal's recollection of his conversation with Mr Patterson at the October 2005 meeting and that HMRC Officers would have praised the quality of the Appellant's due diligence. Mr Patterson asserted in his evidence that he was an experienced Officer and would have been explicit about the risks of fraud

in the mobile phone sector. Mr Patterson pointed out that the visit in October 2005 was not pre-arranged and that at the time the Appellant had not carried out any deals. He, therefore, would not have been in a position in October 2005 to praise the Appellant for the quality of its paperwork because there was nothing to see. Mr Patterson referred to the 30 August 2006 entry on the VAT Audit Report for the Appellant on which he commented that the Appellant's due diligence was poor. Miss Harry examined a copy of the Officer's notebook for the 10 October 2006 visit and found no reference to the quality or standard of the Appellant's due diligence and paperwork.

146. In some respects Mr Jaswal's comments on what HMRC did in the Appellant's first nine months of trading in mobile phones was not wholly relevant to the issue of the extent of his knowledge of fraud in the trade sector. At the beginning of 2006 HMRC was under considerable pressure with the escalation in mobile phone trading following the release of the *Bondhouse* decision. Mr Patterson stated that in January 2006 there were just two members of staff in his office dealing with repayment claims in this sector which was increased to 15 members of staff by April 2006. Given those circumstances the Tribunal considers it unsurprising that HMRC was unable to maintain a close eye on every trader's activities during this period. The fact that HMRC was unable to advise the Appellant of tax losses in its deal chains until September 2006 did not lead to the inference that HMRC had given tacit endorsement of what the Appellant had done in the preceding nine months. An unscrupulous trader may have viewed HMRC's inability to catch up with dubious trades as an opportunity to continue with his questionable activities.

147. Mr Jaswal accepted that prior to and during the Appellant's trades he had received copies of Notice 726 which made it clear that it was the trader's responsibility not that of HMRC to verify the integrity of the supply chains. On 13 October 2005 and 3 July 2006 HMRC sent the Appellant letters highlighting the serious problems of MTIC fraud in the mobile phone trade sector. On 5 and 20 January, 9 February, 9 March, 26 and 30 May 2006 HMRC Redhill sent veto letters to the Appellant informing it that a number of traders had been deregistered from VAT. The Tribunal accepts Mr Patterson's account of his meeting with Mr Jaswal on 13 October 2005, namely that he informed Mr Jaswal of the significant fraud risk in the mobile phone sector. Mr Patterson was an experienced Officer who had worked on a daily basis in the MTIC area for five years. Mr Patterson's version was supported by his contemporaneous notes and tested on oath.

148. The Tribunal is satisfied on the above facts that HMRC informed Mr Jaswal of the high risk of fraud in the mobile phone trade sector and of his responsibilities to mitigate the risk prior to and during the Appellant's mobile phone venture. The due diligence documentation produced by the Appellant demonstrated that Mr Jaswal fully understood those risks and responsibilities. The *Pro-Intell* report for the Appellant stated that *Mr Jaswal and Mr Kazmi (an employee) appeared very knowledgeable of HMRC regulations procedures and gave concise answers to all of our questions.* The Appellant's pro-forma documents[15] supplied to traders before

[15] See EX2-59-63 and 19 June 2012 Transcript page 5 21-25 & page 8-10 7-6.

trading with them revealed Mr Jaswal's high degree of understanding of the risks associated with missing traders, and of the steps expected by HMRC to combat the fraud. The Tribunal decides that Mr Jaswal understated his true understanding of the prevalence of fraud when he asserted that the risk was not great.

The Level and Pattern of Trading

149. HMRC asserted that the value of the Appellant's trade in mobile phones was simply too good to be true. The Appellant's rapid increase in turnover and its sporadic trading pattern defied the normal commercial expectations of a new entrant into the market.

150. The Appellant saw nothing untoward in its increased turnover and sporadic trading pattern. Mr Jaswal asserted that in 1998 he started wholesaling in furniture which involved the import and export of goods and travelling to trade fairs in the UK and the Far East building up business contacts. Mr Jaswal stated that at the start of 2005 he noticed a slowdown in the furniture market and decided to look elsewhere for business opportunities. Mr Jaswal had always been interested in mobile phones and accessories which had become more accessible to small traders. According to Mr Jaswal, during 2005 he conducted a lot of homework into the mobile phone sector and met many traders mostly at Trade shows. Mr Jaswal also subscribed to various trade websites, including Phonetrade.com and Worldtrade.com. The implication of Mr Jaswal's assertions was that the Appellant's success in mobile phones was due to his experience in wholesaling and his extensive market research.

151. The Tribunal makes the following findings of fact:

(1) The Appellant's first two deals in mobile phones in January 2006 were worth in excess of £800,000 from a standing start.

(2) Over the next eight months the Appellant turned over in excess of £12 million, trading on just 14 days. This level of turnover was far in excess of and out of all proportion with what the Appellant achieved as a furniture wholesaler and retailer.

(3) In the VAT period covering the May, June and July 2006, the Appellant did not trade at all in May. In June the Appellant only traded on 29 June 2006. In July the Appellant traded in two blocks: from 3 to 5 July, and 21 to 28 July with two single days trading in between on 13 and 19 July.

(4) Under the 12 deals under Appeal, the Appellant would have made a gross profit of £415,235.

(5) The Appellant's trading activities were confined to making phone calls and producing purchase and sale documentation. The Appellant did not add value to the mobile phones being transacted. As already found the Appellant's activities did not fit with the identified trading opportunities in the grey market.

(6) The Appellant adduced no documentary evidence to corroborate Mr Jaswal's assertions about attendance at trade fairs and his comprehensive market research except a copy of *Key Note Market Report 2005* entitled *Mobile*

Phones[16] which was produced just two days before the hearing. Mr Jaswal stated that the production of the *Report* clearly demonstrated his long term interest in mobile phones.

(7) The contents of the *Key Note Market Report 2005* did not deal with the wholesale distribution of mobile phones but was about the sale of airtime. The *Report,* however, gave details of the number of companies engaged in the overall telecommunications market: in 2004 the number was 5,895 down on the 6,945 companies in the previous year. The *Report* added that almost two thirds of the companies engaged had annual turnovers of less than £250,000 and that barriers to entry were high for new entrants.

152. The Tribunal agrees with HMRC that there was no rational commercial explanation for the Appellant's immediate success in the mobile phone trade sector. The Appellant's level of turnover and the high expected profits from mobile phone trading were out of all proportion to Mr Jaswal's wholesaling experience in furniture, and that in itself should have raised questions about the bona fides of the mobile phones deals. Mr Jaswal's insistence that the Appellant's success was due to his extensive trade contacts and market research was not borne out by the evidence. The *Key Note Market Report 2005* which told Mr Jaswal very little about the wholesaling of mobile phones but gave an overview of the companies involved in the overall telecommunications market. If Mr Jaswal had read the overview he would have known that the Appellant's success and that of its trading partners were wholly unrealistic.

The Funding Arrangements

153. HMRC asserted that the Appellant's funding arrangements for its mobile phone trading were highly suspect and organised in such a manner that the deals carried no commercial risk.

154. Mr Jaswal disputed the absence of commercial risk, arguing that a customer could have rejected the stock before paying for them. Further Mr Jaswal contended that the Appellant was financed with own money through savings and borrowings from friends and relatives.

155. On 31 May 2006 HMRC requested the Appellant to provide statements of all bank accounts held in 2006. HMRC had in its possession a limited number of the Appellant's bank statements but required a complete set to establish the truth of Mr Jaswal's assertion on the Appellant's funding. The Appellant's representative responded on 7 June 2006 by stating that the Appellant had no requested material to disclose, albeit they certainly existed at some point.

156. The Tribunal finds the following on the analysis of the bank statements in HMRC's possession[17]:

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[16] Sixth Edition February 2005 Edited by Jenny Baxter

[17] See Appendix 8 of Core Bundle A1: Summary of Payments

(1) The Appellant paid its suppliers after receiving funds from its customers in deals 1-9 (including the buffer deal 5 which is not subject to appeal) and 12.

(2) The Appellant was unable to pay in full its suppliers for deals 10, 11 and 13, although the deals still went ahead.

(3) There were five unexplained deposits totalling £641,979 in the Appellant's bank account from 9 May 2006 to 10 August 2006.

157. HMRC fully explained why it requested details of the Appellant's bank statements which was to assess the truthfulness of Mr Jaswal's assertions regarding the financing of the Appellant's trading. The Appellant failed to meet that request and has not provided any documentary evidence to substantiate Mr Jaswal's assertions. The Tribunal concludes from the analysis of the banking information and its earlier findings on the Appellant's questionable banking arrangements and circular money flows that the Appellant's funding arrangements were far removed from those for legitimate commercial enterprises. The Appellant did not risk its own monies or capital in the transactions but awaited payment from its customers before satisfying the debt with suppliers. When the Appellant did not have sufficient funds to discharge the payment due to its suppliers, it underpaid them without repercussions to either itself or the deal. The Tribunal infers from the unexplained deposits that the Appellant was being financed by a third party to cover the VAT differential between its purchases and supplies. The Tribunal's inference is reinforced by its findings on circular money flows and the existence of a small group of companies which appeared in the majority of the money movements connected with the disputed deals

An Enterprise not being run on Commercial Lines

158. HMRC relied on a series of indicators for its proposition that the Appellant was not being run on ordinary commercial lines. The Appellant's riposte was to urge the Tribunal not to be drawn into HMRC's trap of believing that everything which was not text book business practice must in some away arouse suspicion.

159. The Tribunal makes the following findings of fact:

(1) The Appellant was dealing in volume high value transactions where the expectation would be complete and accurate transaction documentation. In respect of the disputed deals there were no purchase orders in the transaction packs for deals 1, 2, 6, 7, 8, 10 and 11. Further the Appellant failed to record detailed descriptions of the specifications of the mobile phones purchased and sold. In deal 9 the specification stated in the invoice was *1,000 Nokia N72, sim free new.* No mention was made of the colour, software specification, manual and keypad language, accessories and charger type for the goods.

(2) There were no release notes in the transaction packs for deals 1, 2, 4, 6, 8, 9, 10 and 11 which begged the question: on whose authority the freight forwarder acted when it released the goods to the Appellant's customer? In deal 3 where there was a release note, the Appellant authorised release of its goods two days before being paid for them by its customer, which was contrary to Mr Jaswal's assertion that he would not release stock to the customer until they had

examined the goods and payment had been received. Similarly the Appellant's suppliers, *Trimax* (deal 8) and *Star Express* (deals 10 & 11), released goods before payment which was contrary to the suppliers stated business practices.

(3) *Nijjers* was the Appellant's supplier in four of the disputed transactions, *Nijjers*' supplier declaration for each deal stated that it did not own the goods. The Appellant still went ahead with the purchase despite the seller not owning the mobile phones.

(4) The freight forwarder deal documentation for deals 2 and 3 differed greatly in the weights shown for identical quantities of same model mobile phones. There was no evidence that the Appellant enquired of the freight forwarder or the supplier the reason for the weight anomaly.

(5) In deal 6 the Appellant received a faxed invoice not from its customer, *Blue Alfa* but from another company, *Auditum LDA*, with a different telephone number.

(6) Mr Jaswal stated that he would ask formally the freight forwarder to inspect the goods[18]. In ten deals there was no inspection request produced by the Appellant. In deal 5 (the buffer deal) there was no inspection at all despite there being a request. In deals 10 and 11 there was an inspection report from *Central Solutions* produced by the Appellant but the Appellant has not been charged for the same on the *Central Solutions* invoice, despite other such invoices recording a charge for inspection.

(7) Mr Jaswal insisted that the Appellant insured the goods to the full sale value (the customer invoice amount) from the point they left the freight forwarder. The facts painted a different picture[19]. No insurance documents have been produced for Deal 1. Deals 6-13 were not insured to the customer sales invoice amount as claimed. In Deals 2-4 the goods were apparently double insured because Paul's Freight had stamped the Appellant's pro-forma invoices with confirmation that they were insuring the goods as well.

(8) In his witness statement of 25 November 2010 Mr Jaswal stated that the Appellant ensured that its suppliers and customers signed an eight page agreement form. The Appellant did not, however, produce copies of contracts with five suppliers and three customers for the disputed deals[20]. The terms of the contract were not reflected in the reality of the transactions. No delivery date was specified in the purchase order. No delivery notes were supplied. The Appellant had 28 days to pay its supplier which was not taken advantage of except in deal 13. The Tribunal will deal later with the question of the contracts' authenticity.

(9) The Appellant kept no record of IMEI numbers. Notice 726 advised traders to check whether they had previously purchased the goods they were trading in. The only way to carry out this check was to record the IMEI numbers. The

[18] See Core Bundle A1 Appendix 5

[19] See Core Bundle A1 Appendix 6

[20] See Schedule of VAT Checks and Contracts.

Appellant knew that several of its counterparties referred to IMEI clearance on their documents and that its freight forwarders and inspection agencies provided the scanning service.

160. HMRC's assessment of the Appellant's business practices was not against some amorphous and universal standard for text book commercial enterprises as alleged by the Appellant but against those practices firmly rooted in the exploitation of the grey market opportunities in the mobile phone sector and more particularly those practices claimed by the Appellant.

161. The reality of the Appellant's mobile phone business was that it was dealing in values of goods which far exceeded those traded in its previous enterprise of furniture wholesaling and retailing. The Appellant knew that fraud was rife in the mobile phone sector. The Appellant did not hold the goods which were kept with a freight forwarder. Mr Jaswal did not personally inspect the goods. The Appellant's business activities comprised the negotiation of the deals, and the completion of the necessary paperwork to progress the transactions, and evidence the agreement reached. The risks involved in such an enterprise were disputes about the product specification, non-payment by the customer, and goods lost in transit.

162. Mr Jaswal stated that a deal would start with a request from a customer and once he had secured an order for goods he would go out to his suppliers and match the stock offer with the stock order. Mr Jaswal instructed the freight forwarder formally to inspect the goods and arrange insurance for the full value of the goods. The Appellant operated ship on hold which meant that the goods would not be released until it had received payment from its customer.

163. The facts found showed that the Appellant did not comply with its own stated business practices. The Appellant failed to substantiate its assertion that it made formal requests of the freight forwarder to inspect the goods. The Appellant did not in the majority of the disputed deals insure the goods to the value paid by the customer. The Appellant did not have written contracts for the majority of its suppliers and two customers. The Appellant supplied no copies of purchase orders and release notes for most of the disputed transactions. The release note for deal 3 showed that the Appellant released the mobile phone consignment before payment from its customer. The Appellant did not protect itself by keeping records of IMEI numbers. The Appellant took risks with the transactions by ignoring the weight anomalies in deals 2 and 3, and purchasing goods from *Nijjers* despite its declaration that it did not own the mobile phones supplied. Finally the Appellant did not appear to query why *Trimax* and *Star Express* were prepared to release goods without payment in direct contravention of their terms and conditions.

164. The picture built up from the above findings was that the Appellant did not operate its trading in such a way to ensure the integrity of the deals struck and to

minimise the commercial risks[21] associated with the wholesaling of mobile phones when the stock was held elsewhere.

Due Diligence

165. HMRC contended that the examination of the Appellant's evidence on due diligence revealed that most of the due diligence material had been recently fabricated in an attempt to bolster the Appellant's case. Further it was also clear that even if the Appellant had in its possession all of the documentation dated before the dates of the deals the Appellant knew next to nothing about its counterparties before entering into the transactions. HMRC concluded that the Appellant made no proper enquiries into its counterparties because it knew that the transactions had all been orchestrated and pre-arranged, and therefore carried no risk.

166. Mr Jaswal disagreed, arguing that the Appellant's due diligence was thorough and consistent throughout. Mr Jaswal insisted that he conducted due diligence on the Appellant's suppliers and customers before trading and then continued to enhance it as the business relationship developed. Mr Jaswal did not trade with any supplier if he was not satisfied that the supplier was not a good company to trade with, had a good level of experience in the industry and good product knowledge. Mr Jaswal asserted that he reviewed information provided and did not treat it as a paper exercise. Mr Jaswal listed in his first witness statement the due diligence material kept by the Appellant for each customer and supplier for the disputed deals. Mr Jaswal concluded that the Appellant's due diligence was very strong and that he did not see one indicator of fraud when dealing with either suppliers or customers.

167. The Appellant did not produce the bulk of its due diligence material relied upon to HMRC and the Tribunal until 7 June 2012 just before the commencement of the hearing on 11 June 2012. HMRC expressed its strong disapproval of the late delivery of the documentation but did not object to its admission. Mr Jaswal urged the Tribunal to examine the material submitted which it did in open Tribunal[22]. The Tribunal sets out below its findings on the Appellant's due diligence. The Tribunal will consider later HMRC's allegation that the majority of the Appellant's documentation was produced after the event.

168. Mr Jaswal asserted that the Appellant would not trade with a company that was not cleared through HMRC at Redhill. The Schedule of VAT Checks and Contracts revealed that the Redhill checks were dated after the first deals with *AB International, H Communications, Goldphone* and *Bluestar*. Thus the Appellant did not obtain Redhill clearance prior to dealing with a third of the companies[23] traded with in the disputed transactions.

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[21] See paragraph 161 above

[22] See Transcript dated 19 June 2012.

[23] 14 companies were traded with during this period. 12 of those companies were covered by Redhill checks. The final two companies were based in UAE.

169. The Appellant produced a *Due Diligence Report* prepared by *Pro-Intell (UK) Limited* for all its suppliers except *Trimax.* The Appellant adduced no documentary evidence to substantiate its assertion that it commissioned the reports from *Pro-Intell* or even paid for its services. The independent status of *Pro-Intell* was brought into doubt by the evidence that the director of *Pro-Intell* was connected with *Nijjers'* director. Pro-Intell was only incorporated on 22 May 2006 and its director from the date of incorporation was Jagjot Kaur Gill. At the time of Pro-Intell's incorporation Jagjot Gill had no apparent experience in undertaking due diligence enquiries into companies and was a director of a pharmaceutical company called KMJ Corporation Ltd The *Pro-Intell (UK)* reports for the suppliers except *Star Express* and *Data Solutions* were dated after the date of the Appellant's first deal with them. The Appellant also included a copy of a *Pro-Intell* report carried out on it.

170. The Tribunal's examination of the *Pro-Intell* reports revealed that they followed the same format repeating similar phrasing across the complete range of reports, for example, the owners of the various companies *were very knowledgeable about HMRC regulations & procedures and gave concise answers to all our questions* and the wording for the source of goods. It was evident from the examination that the reports were cut and paste jobs. The reports on *Nijjers* and *Star Express* contained references to *Letting Solutions Ltd* rather than the names of the companies for whom the reports were being prepared. *Letting Solutions Ltd* appeared as a buffer trader in deal 5 and as a supplier to *Nijjers.* The Tribunal formed the view that the *Pro-Intel* reports gave no assurance to the Appellant and were in fact being churned out for the UK participants in the disputed transactions with the implication that the reports were produced for the purposes of covering up the fraudulent activities.

171. The Appellant supplied in some instances *Due Diligence Reports* from *Veracis* but no evidence of a contract with or payments made to *Veracis.* Mr Jaswal acknowledged that the *Veracis* reports for *Nijjers* and *H Communications* were handed to him by those companies. The reports for those companies were incomplete, and could not be relied upon since they were not commissioned by the Appellant.

172. The Appellant purportedly ordered the *Veracis* report on *Goldphone* which stated that the *owner had previously traded in Limited Company format but because of issues over a VAT repayment, he made a decision last year to trade in SLU format as a sole director and shareholder.* The report also identified as a negative factor that no financial information was available. Given that information the Tribunal was surprised that the Appellant proceeded with a deal in excess of £300,000 with *Goldphone*

173. The Appellant supplied incomplete *Veracis* reports on *Blue Star* and *Compucell.* The extract for *Blue Star* did not include the page on negative indicators. The Tribunal considers that even on the information provided the Appellant should have been reluctant to enter into deals with *Blue Star* to the value of £1 million. The report indicated that no financial information was available because the company was relatively new. The company's turnover, however, was recorded as £5 to £6 million per month. The director's experience was described as working within the telephone

industry in India as a telecoms engineer. The report also expressed doubts about the director's claim of customers worldwide. The Tribunal suggests that a new company with a claimed annual turnover of £60 - £72 million run by a person with no wholesaling experience should have raised immediate questions in Mr Jaswal's mind about the legitimacy of the company's trading.

174. The incomplete Veracis report for *Compucell* identified five negative factors which included sales to the UK, lower than average Dun & Bradstreet rating and trading from a small basic office in the owner's apartment. The Tribunal considers these negative factors were clear indicators of *Compucell*'s potential involvement in fraudulent trading. The Tribunal also questions the Appellant's business sense of selling goods to the value of £461,000 to a company with a tangible net worth of 2,723 Euros.

175. The Appellant required its suppliers and customers to complete a trade application form, which required them to provide information about the company, banking arrangements and their understanding of HMRC requirements. Mr Jaswal indicated that he completed the forms when he visited some of the Appellant's trading partners. The table below sets out the respective dates for the site visit, the completed trading application form and the Appellant's first deal with the partner.

Trader	**Date of First Deal**	**Date of Trading Application**	**Date of Site Visit**	**Comments**
Nijjers	20 January 06	8 June 06/15 August 06/14 September 06		3 separate sets of the trade application documentation.
A B International	4 July 06	14 July 06	14 July 06	The visit was apparently to an address which *AB* only moved into on 7 August 06[24]
H Communications	13 & 21 July 06	26 July 06	25 July 06	
Trimax	19 July 06	17 & 21 July 06	22 July 06	2 separate sets of the trade application documentation
Star Express	28 July 06	26 June & 18 July 06		2 separate sets of the trade application documentation
Data Solutions	28 July 06	14 July 06		
Reya	17 August 06	5 September 06	2 August 06	

[24] 19 June 2012 Transcript 58/59 21-3

Trader	Date of First Deal	Date of Trading Application	Date of Site Visit	Comments
Goldphone	29 June 06	29 August 06		
GNJ General Trading	3 July 06	16 May 06	16 May 06	GNJ's Introduction letter dated 3 July 06 implies that it did not know the Appellant
Blue Star	20 January 06	14/15 August 06	19 June 06	
Blue Alfa	13 & 28 July 06	4 September 06	25 July 06	The visit took place on the same day as that for *H Communications*
Alimed	19 July 06	24 July & 16 August 06	24 July 06	2 separate sets of the trade application documentation
Compucell	28 July 06	8 August 06	8 August 06	
Al Saqr (Zenith)	17 August 06	7 November 06	13 April (May) 06	Date of visit altered to May. Site visit to *Zenith Al Saqr* did not change its name until 15 July 06

176. The above analysis on the dates for completion of the Appellant's trade application documentation and site visits showed that the information for most of the Appellant's trading partners were collected after the dates of the first deals with them, and, therefore, of limited use for assessing the bona fides of the transactions and of the partners.

177. The analysis also questioned whether the site visits by the Appellant took place. The Appellant produced no documentary evidence, such as flight tickets or payment records, to corroborate the visits. No photographs of Mr Jaswal with the directors or owners of the companies visited were supplied by the Appellant. More significantly there were inherent contradictions with some of the visits. Apparently the Appellant visited *H Communications* in Birmingham and *Blue Alfa* in Portugal on the same day, 25 July 2006. The Appellant completed information on *Zenith* at a site visit on either 13 April or 13 May 2006 which happened two or three months before *Al Saqr* changed its name by resolution to *Zenith* on 15 July 2006. Finally the Appellant saw *AB International* three weeks in its new offices before it moved into them.

178. Finally the analysis revealed that the Appellant had produced multiple sets of signed trade application documentation for various companies where the only difference between the respective documentation for each company was the dates of the signatures. The Appellant has offered no explanation for the multiple sets. The existence of multiple sets of the same completed documentation suggested that the

Appellant was not considering the information provided on the forms, and simply going through the motions to give the appearance of due diligence on its trading partners.

179. The Appellant's evidence on due diligence included various reports on the financial standing of its trading partners. The Tribunal's overall finding on those reports was that the credit limits for the companies involved were either very small or non-existent with many of those companies being either new or dormant ones. In the Tribunal's view, the Appellant took on unacceptable commercial risk in transacting with these companies for values well in excess of £250,000.

180. The *Busibody* credit opinion on *Nijjers* dated 21 January 2006 stated that *there is a deficit in both capital employed and shareholders' funds. A maximum risk company. All credit transactions should be supported by a director's guarantee…"*. There were no credit ratings for *H Communications* (risk of business failure high), *Star Express* (dormant), *Data Solutions* (new) and *Reya* (new). *AB International* had a credit rating of £1,500, whilst *Trimax* had the best credit rating of the Appellant's suppliers of £12,800.

181. The Tribunal has already made findings on the financial standings of *Goldphone, Compucell* and *Blue Star* in paragraphs 172–174. The Appellant submitted no credit checks on the other customers as part of its due diligence.

182. The Appellant stated that it placed weight on the references received, in particular the one supplied by *Brindley's* for *Nijjers.* The Tribunal disagreed with the value attached by the Appellant to the references. The *Brindley's* one was addressed to *Whom it may concern* and, therefore, generic which could be copied and sent to anybody.

183. The Appellant's partners in several instances gave names of companies which were involved in some capacity with the disputed transactions and or the names of their suppliers and customers as trade referees. *A B International* named *Red Trading* and *Compucell* as referees; *Trimax* gave *Glasgow Data* and *Sapphire; Data Solutions* named *Star Express,* whilst *Reya* cited *Mike* from *Nijjers* as a referee. *Blue Alfa* provided the names of *Silus BV* and *Al-Saqr*. *Silus* appeared at one end of the transaction chain in deals 10 and 11 despatching the mobile phones to the defaulting trader, whilst *Blue Alfa* appeared at the other end as the Appellant's customer, which begged the question that as they knew each other why did they not trade directly and miss out all the intervening traders.

184. The Tribunal considers that its finding on the references supplied, particularly the names of the trade referees were typical of the standard of the Appellant's due diligence. Rather than providing the reassurance as asserted by the Appellant, they indicated real concerns about the bona fides of its trading partners and of the ensuing transactions. The readiness of traders to give names of other players in the market defied commercial logic especially in a sector which was said to be highly competitive and where traders were apparently unwilling to disclose their suppliers and customers. Moreover, the Appellant must have recognised that some of the trade referees appeared as counterparties in its

disputed transactions, which should have raised questions in the Appellant's mind about whether the transactions were connected and not at arms length.

185. The Tribunal observes from the due diligence documentation that the Appellant was prepared to trade with companies with little or no experience in the wholesaling of mobile phones. The trade classification of *Data Solutions* was advertising activities, whilst the introductory letter for *Star Express* emphasised its roles as a hardware consultancy company and as an independent business mobile provider for achieving the best mobile business rates. It would also appear that the Appellant failed to note that the letters of introduction for *Compucell*, *Blue Star* and *Al Saqr* were identical in their wording.

186. The remaining documents included in the Appellant's due diligence identified the directors of the various companies, gave details of bank accounts and VAT registrations, and confirmed that the companies had a presence in the addresses from which they were trading. Some of the documents for the overseas companies were not translated into English. The details of the bank accounts revealed that most companies held accounts with more than one bank but always an account with FCIB. The trading addresses comprised a motley collection of rooms in the directors/owners residence, small offices above shops, hired spaces in serviced office accommodation and dedicated office suites. The Tribunal considers that even this most basic of information raised issues about the commercial viability of some companies, their banking choices and the need for translating services which the Appellant apparently ignored.

187. The Tribunal's findings on the Appellant's due diligence demonstrated that it was wanting in every respect and fell considerably below Mr Jaswal's exalted claims of being very strong and not showing one indicator of fraud amongst the Appellant's suppliers and customers. The Appellant's reliance on the reports of due diligence companies was highly questionable. There was no evidence that the Appellant had actually commissioned the companies involved to produce reports on its behalf. The independent status of *Pro-Intell* and its competence to conduct due diligence were severely compromised by the close connection of its director with *Nijjer's* director and by the poor quality of its reporting which was self evident from the number of mistakes and the standard wording in the reports. The Appellant took no heed of the warnings in the *Veracis* reports, the majority of which were incomplete which suggested that Mr Jaswal had obtained the extracts from other traders in an attempt to bolster his exaggerated claims on due diligence.

188. The theme of the Appellant disregarding information that brought into question the bona fides of its trading partners was a recurrent one throughout the Appellant's due diligence. The Appellant ignored the questionable financial standings of all the companies involved, the connections between its trading partners as revealed by the trade referees, the trading classification of some of the companies, and the suitability of the office accommodation for companies purportedly dealing in high value transactions.

189. The Tribunal's findings on due diligence, however, were more damaging in respect of Mr Jaswal's credibility. They revealed the lies to Mr Jaswal's assertions of

always obtaining a Redhill clearance before embarking on a trade, and of reviewing the information provided and not treating the due diligence as a paper exercise.

190. The findings also showed that the Appellant had created documentation after the event, which applied equally to the copies of the contracts supplied by the Appellant. The Appellant supplied the bulk of its due diligence documentation including copies of the contracts just before the hearing. The fact that the Appellant's original disclosure of due diligence material was non existent for *H Communications* and *Trimax* and extremely sparse for each of the Appellant's customers questioned the authenticity of the later material. The facts that the later material contained anomalies, particularly the separate sets of trade application forms with different dates for the same company, the inconsistencies with the site visits to *Blue Alfa, H Communications, AB International* and *Al Saqr* (*Zenith*), no evidence of commissioning the due diligence companies and the inclusion of the *Pro-Intel* report on the Appellant were compelling evidence that the material had been compiled after the event.

191. The Tribunal reaches the same conclusion of creation after the event in respect of the contracts for the following reasons:

(1) The Appellant has not supplied a copy of a contract for each of its trading partners contrary to Mr Jaswal's assertion that all of them signed binding eight page trade agreement forms.

(2) The Appellant claimed that the contracts were drafted by *Buss Murton* solicitors but has not produced any document or record evidencing payment to them.

(3) The Appellant response to HMRC's disclosure request for: "*All documentation, including invoices, that passed between the Appellant and Buss Murton Solicitors regarding the drafting of the disclaimer, trade form and 8-page contract*" was that it had no requested material to disclose.

(4) The contracts themselves purport to have been made in the main on the dates of the transactions but they bear no fax headers indicating that they have been transmitted between any parties whilst almost all the deal documentation bore fax headers.

(5) Not a single piece of other transaction documentation from the Appellant such as a purchase order or sales invoice referred to what were in essence the Appellant's purported standard terms and conditions which suggests that the "contracts" did not exist at the time of the transactions;

(6) Multiple contracts have been purportedly signed between the Appellant and *Nijjers*, with one dated 21 January 2006 and a further contract dated 29 June 2006. The terms of the contract showed that there was no need for a new contract to be drawn for each subsequent transaction between the same parties. The fact that the Appellant has, on its own account had the contracts signed twice by *Nijjers* showed that it had no regard to their contents.

(7) There were further terms of the contract that have not been reflected in the reality of the transactions. Clause 5.2 of the supplier contract stated that the delivery date would be specified in the order or if unspecified would taken place within 28 days of the order. The Appellant's purchase orders did not specify the dates of delivery and accordingly the Appellant could not be satisfied that it would be able to sell the goods to its customers and deliver them because they had not stated the delivery date in their own purchase order; this despite time of delivery being "of the essence" according to Clause 5.5. Clause 5.4 of the supplier contract stated that the seller was to accompany each delivery with a delivery note. No such notes have ever been produced in evidence. The payment clause at 8.1 of the supplier contract gave the Appellant 28 days to pay its supplier. In all but Deal 13 the Appellant did not take advantage of the time available to it in the payment clause.

192. The Tribunal holds that the Appellant with its creation of material after the event was seeking to mislead HMRC and the Tribunal about the strength of its case, which strongly indicated that it had something to hide about its involvement in the disputed transactions.

Overall Findings on Knowledge

193. The Tribunal summarises its findings on the question of the Appellant's knowledge as follows:

(1) The Appellant's transactions were part of a highly orchestrated web of transactions wholly bereft of a commercial rationale and carried out for the sole purpose of attracting a charge for UK VAT. They were, therefore, part of an overall scheme to defraud the revenue.

(2) The existence of an overall scheme to defraud required each party in the scheme to play its role to ensure the success of the fraud. Each party had to buy from and sell to persons designated by those orchestrating the scheme.

(3) The Appellant occupied the pivotal role of broker in the disputed transactions. The position of broker was critical to the effectiveness of the overall scheme to defraud. The broker made the claim for the VAT which was the very object of the fraud, and as a result carried the greatest risk of investigation for which it was amply rewarded with a significant proportion of the ill gotten gains. The Appellant's mark up from the disputed transactions was much more substantial than the other traders in the respective deal chains.

(4) The Appellant's role within the overall scheme was typified by its relationship with *Nijjers*, which had no commercial rationale and had all the characteristics of being contrived. Their appearance as brokers on the same date in the *Famecraft* contra scheme was beyond coincidence. Mr Jaswal lied about the extent of his relationship with Mr Nijjers.

(5) The Appellant's active involvement in the overall fraudulent scheme was demonstrated by its appearance in commercially inexplicable circular fund structure and its use of off-shore banking facilities in pounds sterling. The

circumstances surrounding the opening of the ICB account which was critical to the execution of the fraud perpetrated by *Famecraft* demanded an explanation from Mr Jaswal but none was forthcoming.

(6) The disputed transactions exhibited no characteristics of a business trading in the legitimate grey market in mobile phones.

(7) At the time of entering the disputed transactions Mr Jaswal understood the high risk of fraud in the mobile phone trade sector and of the steps the Appellant was expected to take to ensure that its transactions were not tainted with fraud.

(8) There was no rational commercial explanation for the Appellant's immediate success in the mobile phone sector.

(9) The Appellant's funding arrangements for its mobile phone business were far removed from those for legitimate commercial enterprises.

(10) The Appellant did not operate its trading in the disputed transactions in such a way to ensure the integrity of the deals struck and to minimise the commercial risks associated with the wholesaling of mobile phones when stock was held elsewhere. The Appellant did not adhere to its own stated business practices.

(11) The Appellant's due diligence was found wanting in every respect and fell considerably below Mr Jaswal's exalted claims of being very strong and not showing one indicator of fraud amongst the Appellant's suppliers and customers.

(12) The Appellant created documentation after the event with the intention of misleading the Tribunal and HMRC about the strength of its case which strongly indicated that it had something to hide.

194. The above findings paint on objective criteria a compelling and cogent picture of the Appellant having actual knowledge at the time of entering the disputed transactions of their connection with the fraudulent evasion of VAT. The Tribunal is, therefore, satisfied that the Appellant knew at the time of entering the disputed transactions that each of those transactions was connected with the fraudulent evasion of VAT.

Additional Legal Arguments

195. The Appellant submitted that it was not proportionate to deny it input tax after making virtually no attempt to recover the input tax from the defaulter or from those companies which purchased the goods from the defaulter. Moses LJ in *Mobilx* at paragraph 66 rejected the proportionality argument:

> "It is not arguable that the principles of fiscal neutrality, legal certainty, free movement of goods and proportionality were infringed by the Court itself, when they were at pains to preserve those principles (see §§ 39-50). By enlarging the category of participation by reference to a trader's state of knowledge before he chooses to enter into a

> transaction, the Court's decision remained compliant with those principles."

196. Closely allied with its argument on proportionality, the Appellant asserted that its treatment was inequitable and discriminatory when other traders in the disputed deal chains were allowed their right to deduct VAT. The argument of non discrimination was rejected by Roth J in *Powa (Jersey)* at paragraph 60 and Newey J in *S & I Electronics PLC* at paragraphs 33-37. Roth J stated at paragraph 60:

> "As to non-discrimination, this Appeal concerns the decision by HMRC that the objective criteria determining the right to deduct input tax were not met as regards these claims for repayment by PJL. If that is the case, PJL were not entitled to such repayments, irrespective of the position of anyone else. ……Furthermore whether HMRC could have applied a similar approach to the traders who served as buffers in the chains (who would generally not be making a repayment claim to HMRC but simply crediting the input tax against the output tax received) does not affect that conclusion; and whether HMRC should have pursued those traders for an account of the output tax received is a question of policy regarding the effective enforcement of the VAT regime, with no doubt limited resources. Accordingly, I consider that the principle of non-discrimination is not engaged".

197. The final legal argument was that Appellant should have received credit for the difference between the total amount of repayments claimed and the missing VAT. Again Moses LJ in *Mobilx* at paragraph 65 dismissed the validity of the Appellant's proposition:

> "The Kittel principle is not concerned with penalty. It is true that there may well be no correlation between the amount of output tax of which the fraudulent trader has defrauded HMRC and the amount of input tax which another trader has been denied. But the principle is concerned with identifying the objective criteria which must be met before the right to deduct input tax arises. Those criteria are not met, as I have emphasised, where the trader is regarded as a participant in the fraud. No penalty is imposed; his transaction falls outwith the scope of VAT and, accordingly, he is denied the right to deduct input tax by reason of his participation."

198. The Tribunal concludes there was no substance to the Appellant's further legal arguments. The Tribunal also adds that it would lead to gross injustice if the Appellant was able to claim the benefit of another Community right in respect of actions where it has been shown on objective criteria that the Appellant has abused Community law. In effect the Appellant's arguments amount to an endorsement of allowing Community law to be used for fraudulent ends.

Decision

199. The Tribunal finds the following:

(1) There was a VAT loss in each of the Appellant's disputed transactions.

(2) The loss in each of the Appellant's disputed transactions was occasioned by fraud.

(3) Each of the disputed transactions was connected with the fraudulent evasion of VAT.

(4) The Appellant knew at the time of entering the disputed transactions that each of those transactions was connected with the fraudulent evasion of VAT.

200. The Tribunal, therefore, dismisses the Appeal and confirms HMRC's denial of input tax in the sum of £1,048,337.50 claimed on 12 transactions involving supplies of mobile phones during accounting periods 07/06 and 10/06.

201. This Appeal was re-categorised as complex on 21 April 2010. In those circumstances the Tribunal grants HMRC's application for costs, and orders the Appellant to pay those costs. Leave is given to the parties to apply to the Tribunal for a determination of the amount of costs if not agreed between the parties.

202. 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.

MICHAEL TILDESLEY OBE
TRIBUNAL JUDGE

RELEASE DATE: 19 September 2012