[2016] UKFTT 160 (TC)

TC04946

Appeal number: MAN/2008/0181

Value Added Tax – MTIC appeal –Application for adjournment – refused – substantive appeal conducted without oral evidence at request of appellant - minimal submissions from appellant - onus of proof on HMRC - whether the appellant knew or should have known that its transactions were connected with fraudulent evasion of VAT – yes - Appeal dismissed

FIRST-TIER TRIBUNAL
TAX CHAMBER

WALMLEY ASH LIMITED (formerly Balmoral Ltd) **Appellant**

- and -

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

TRIBUNAL: JUDGE ANNE SCOTT, LLB, NP
MEMBER: TERENCE BAYLISS, FFA

Sitting in public at Birmingham Magistrates Court on 2, 3 and 4 November 2015

Having heard Andrew Anthony Kelly for the Appellant

Joshua Shield, of Counsel, instructed by the General Counsel and Solicitor to HM Revenue and Customs, for the Respondents

DECISION

Introduction

1. The appellant is appealing against the decision of HMRC, which expression is used for convenience to include HMRC's predecessor, HM Customs & Excise, contained in a letter dated 18 January 2008 denying entitlement to the right to deduct input tax in relation to transactions occurring in the appellant's quarterly VAT period ending 05/06. The total tax under appeal is £1,748,587.50.

2. The grounds for the challenged decision were that HMRC considered that the appellant's transactions in which the relevant input tax was incurred were connected with the fraudulent evasion of VAT, and that the appellant knew or should have known of such a connection. HMRC consider that the fraudulent evasion is Missing Trader Intra-Community ("MTIC") fraud.

3. By Notice of Appeal dated 12 February 2008 the appellant stated that "The Commissioners claim the taxpayer had knowledge of frauds in their supply chain because of the general advice provided and of general knowledge in the trade. The taxpayer did not have knowledge of deals in their supply chain."

4. For ease of reference, since the appellant was known as Balmoral Limited at all material times, we refer throughout to the appellant as "Balmoral".

5. There is no doubt that the controlling mind and sole shareholder and director is and always has been Mr Andrew Anthony Kelly.

Preliminary Matters

Application for adjournment

6. Mr Kelly's written application for postponement, intimated just days before the hearing, had been refused, since it was opposed on arguable grounds. He was advised to be prepared for a substantive hearing and, if he so wished to reiterate his request for an adjournment at the outset of the hearing. He did.

7. It was mildly confusing that that application appeared to emanate from the fictional address of the equally fictional character "Fireman Sam". That is far from applauded, but, for the record, that apparent derivation is, indeed, disregarded.

8. He was unrepresented at the hearing. He reiterated his request for an adjournment stating that the problem was finding a source of funding.

9. We explained to him, at length, the legal framework for any application for adjournment, particularly at the last moment, in the face of numerous reminders from HMRC (including an intimation that an application would be made for wasted costs, given the lack of cooperation).

10. We also explained that the Tribunal system was designed to assist the unrepresented appellant and that we would explore all relevant issues to assist him.

The law in regard to the application

11. The Tribunal's Case Management powers are to be found at Rule 5 of the Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules 2009 ("the Rules") and, in particular, Rule 5(3)(h) which states that the Tribunal may, by direction, adjourn or postpone a hearing.

12. Rule 2 of the Rules provides the overriding objective which is to deal with cases fairly and justly:-

Rule 2.—Overriding objective and parties' obligations to co-operate with the Tribunal

(1) The overriding objective of these Rules is to enable the Tribunal to deal with cases fairly and justly.

(2) Dealing with a case fairly and justly includes—

(a) dealing with the case in ways which are proportionate to the importance of the case, the complexity of the issues, the anticipated costs and the resources of the parties;

(b) avoiding unnecessary formality and seeking flexibility in the proceedings;

(c) ensuring, so far as practicable, that the parties are able to participate fully in the proceedings;

(d) using any special expertise of the Tribunal effectively; and

(e) avoiding delay, so far as compatible with proper consideration of the issues.

(3) The Tribunal must seek to give effect to the overriding objective when it—

(a) exercises any power under these Rules; or

(b) interprets any rule or practice direction.

(4) Parties must—

(a) help the Tribunal to further the overriding objective; and

(b) co-operate with the Tribunal generally.

13. It is made quite clear in *Transport for London v Greg O'Cathail*[1] that the overarching fairness factor must be taken into account in assessing the effect of the decision as to whether or not to adjourn on **both** sides. *Terluk v Berezovsky*[2] identifies the fact that a late adjournment involves a significant loss of time and money. If this hearing were to be adjourned there would undoubtedly be a waste of scarce Tribunal time, no possibility of recovery of costs from this hearing from the appellant and a further delay in access to justice for the parties. HMRC contends that an adjournment

[1] 2013 EWCA Civ 21 at paragraph 42

[2] 2010 EWCA Civ 1345

would result in significant prejudice to HMRC, the administration of justice and the public purse.

14. Both parties are entitled to have cases dealt with fairly and justly. The appellant does not have the monopoly of the fairness factors. *Dhillon v Asiedu*[3] confirms that the decision as to whether or not to adjourn is a balancing exercise.

15. Rule 3.1(2)(b) of the Civil Procedure Rules permits a court to adjourn a hearing. Of course, we are also aware of Article 6 of the European Convention on Human Rights and the relevant part provides:-

> "In their determination of his civil rights and obligations or of any criminal charge against him, everyone is entitled to a fair and public hearing within a reasonable time by an independent and impartial tribunal established by law …".

16. In the case of *Teinaz v Wandsworth London Borough Council*[4] Gibson LJ commented on Article 6 and stated at paragraphs 21 and 22:

> "but the tribunal or court is entitled to be satisfied that the inability of the litigant … is genuine, and the onus is on the applicant for an adjournment to prove the need for such an adjournment … all must depend on the particular circumstances of the case".

17. What then are the particular circumstances of this case?

History

18. In 2006, Balmoral was originally represented in this matter by Robert Holland of Dass Solicitors. Vatease then prepared and lodged the Notice of Appeal. On 18 March 2009, Alan Rashleigh & Co intimated that they had taken over conduct of the appeal and in or about May 2012, Ferdinand Kelly, Solicitors were acting, albeit there appeared to be a period of overlap.

19. Balmoral has a history of minimal engagement in this appeal. On 7 May 2009, the Tribunal issued Directions that Balmoral should serve witness statements, with exhibits, on HMRC by 9 June 2009. Nothing happened. On 2 July 2009, HMRC sought a strike out and on 7 July 2009 the Tribunal directed that unless witness statements were served by 21 July 2009 the appellant would not be entitled to rely on witnesses at the appeal.

20. On 21 July 2009, Mr Kelly's witness statement was served by fax. It extended to a mere 11 sentences and there were no exhibits. At this Hearing the appellant's Bundle consisted of that witness statement and a further unsigned, undated witness statement with no exhibits. Even with double spacing, the 23 paragraphs extend to only nine pages. No application has ever been made for admission of that statement which has been prepared by Ferdinand Kelly.

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[3] 2012 EWCA Civ 1020

[4] 2002 ICR 1471

21. No Skeleton argument has been lodged for Balmoral and nor has Balmoral intimated any challenge to the HMRC witness statements, all as required by the Directions of the Tribunal.

22. In fairness to the appellant, we note that this appeal was struck out on 4 November 2010, as HMRC had not confirmed in writing that they were proceeding with the appeal. However, on 12 May 2011, the Tribunal Directed that the appeal be reinstated.

Recent History 2015

23. On 22 October 2015, Ferdinand Kelly, wrote to the Tribunal with copies to HMRC and Mr Kelly intimating "We are no longer representing the above company. They have no representation and the company's director (Mr Andrew Kelly) is dealing with this matter going forward".

24. On the same date, HMRC wrote to the Tribunal setting out the recent history in this appeal. On 23 July and 5, 6 and 13 August 2015, HMRC had written to Ferdinand Kelly seeking agreement to proposed Directions etc. There was no response. On 25 August 2015, HMRC contacted the Tribunal to put it on notice of the fact that there was no response. Further reminders were sent on 3 September and 21 September, the latter asking Ferdinand Kelly to confirm its agreement to the draft index of the bundles by no later than 2 October 2015. On 5 October 2015, Ferdinand Kelly responded apologising and seeking an extension of time to 9 October 2015. On 12 October 2015, in the absence of any response, HMRC wrote again to Ferdinand Kelly.

25. On 13 October 2015, Ferdinand Kelly wrote to HMRC in the following terms:-

> "We are unable to meet with our client to consider this bundle. The only instruction we have is that our client is requesting a further and final one week extension, taking us to the close of play Tuesday 20 October, 2015 to agree the index bundle.
>
> I would submit that whilst this is later than what has been ordered (and no disrespect is intended to you or the Tribunal), most of this evidence has already been served and seen by all of the parties. So the only detriment would be to our client's counsel in terms of preparation."

26. On 23 October 2015, Mr Kelly intimated to HMRC, with a copy to HMCTS, that his primary obstacle was having funding in place by 2 November 2015 for new representation and he required more time to arrange that.

27. Mr Kelly's oral arguments were entirely restricted to his problems with funding.

28. In summary, at the outset of the hearing, it was argued for the appellant that Mr Kelly had only been able to identify funding for this litigation in the period since 15 October 2015 and that he has identified a new barrister and two litigation funding organisations.

29. He said that he was stressed and had tended to leave matters to the last minute to try and avoid pressure. He offered no medical evidence.

30. Mr Kelly presented as an "innocent abroad" having left everything to his professional advisors and by implication having been left stranded.

31. The factual background proved to be radically different. We find as fact that he is, and was, very far from an innocent abroad.

32. That is also relevant to our findings on the substantive issues.

Factual background

33. We explored the factual background at some length with Mr Kelly. He stated that it was only recently that he had been able to identify a source of funding. He described a "last ditch attempt" to trawl the internet looking for sources of funding in the last few weeks. He stated that he had found two potential litigation funders, the names of which he did not know until we asked that he check his telephone.

34. We tried to explore what information he had given them and what if anything had been agreed. He was very vague, ultimately saying that he did not understand the legal issues and that he had referred the two potential funding organisations to the potential new barrister. He stated that they would only be prepared to extend funding if the barrister opined that there was a viable case. However, the barrister was not prepared to offer an opinion unless there was funding. It was put to Mr Kelly that that was a "chicken and egg" situation and that the reality was that there was no funding in place. He agreed. The only implication was that if the appeal were to be successful then any repayment of VAT would settle the fees and outlays of the litigation funder(s).

35. Counsel for HMRC drew Mr Kelly's attention to *Balmoral Limited v HMRC*[5] ("the 2005 appeal") and *Balmoral Limited v HMRC*[6] ("the 2008 appeal"), both of which had been exhibited in evidence, more than once. Balmoral Limited is, of course, the previous name of the appellant. In the 2008 appeal, *Balmoral* had appealed against an assessment and had sought a last minute postponement because the solicitors had resigned agency. Judge Bishopp refused that application and proceeded to determine the appeal with Mr Kelly acting for Balmoral.

36. The appeal against that assessment was dismissed and the assessment upheld. There is therefore outstanding a debt to HMRC of in excess of £2 million before interest.

37. Even if the appellant were to be successful in this appeal there would still be a debt outstanding to HMRC. The appellant is only maintained on the register at Companies House because of this outstanding litigation. It seems extremely unlikely that any litigation funding organisation would embark on litigation in those circumstances.

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[5] 2005 UKVAT V19233

[6] 2008 UKVAT V20677

38. At best, Mr Kelly was decidedly disingenuous when he suggested to the Tribunal that that assessment could still be appealed and those funds were not yet finally due to HMRC. He conducted that litigation in person. He was also therefore well aware of the consequences of seeking a last minute adjournment on the basis of lack of representation.

39. He later tried to argue that he could appeal the period 07/06 "assessment" in the sum of approximately £1.1 million and, if successful, funds would then be available. It would appear that that was not an assessment but rather a decision relating to disallowance of input tax on the basis of MTIC fraud. HMRC pointed out that that was not possible since no decision or assessment had ever been appealed and it was now far too late to appeal anything. We agreed. The prospects of an appeal being admitted late so many years later are almost nil particularly for an appellant who has been professionally represented until now and has experience of the appeals procedure with this being the third VAT appeal litigated. In any event it is clear from the evidence that the same arguments were in issue in that period as in this appeal.

40. We also explored the delays in recent times and put it to Mr Kelly explicitly that, in our experience, parties litigating in the expectation of a repayment, even in a minor claim, would have been pressing for resolution and we would have expected him to have done the same. In that context, he offered no explanation as to why his solicitors appeared to have been without relevant instruction for long periods.

41. On the balance of probability, we find, and Mr Kelly conceded, that there is and never has been any realistic possibility of obtaining any external funding for this litigation.

42. He ultimately confirmed that he had never paid anything to Ferdinand Kelly. He had never had funds in place, including when the last hearing was adjourned in 2014.

43. Mr Kelly has no assets and is on the point of being evicted from his home. For a number of years, until three years ago, he survived on benefits. Accordingly no award of costs could be satisfied.

Decisions on applications

44. We have refused the application for adjournment on the basis that nothing would be achieved in granting it as there is little or no prospect of any funding being obtained. Further, Mr Kelly has been aware of the funding problem for years and had done little or nothing until very recently. We do not accept that he has attempted to cooperate with the Tribunal; indeed by his own admission he had only started to look for funding on 15 October 2015. There would be considerable prejudice to HMRC if the hearing were to be adjourned, it would be a waste of scarce Court resource and it is more than probable that nothing would be any different at an adjourned hearing. The cost to the public purse would be considerable and there is no prospect of recovery of the wasted costs of this hearing.

45. With the consent of HMRC, we have deemed Mr Kelly to have made an application to admit his second witness statement in evidence and we grant that

application. We requested that he sign that witness statement and he did so on the first day of the Hearing.

The framework of the substantive appeal hearing

46. The decision on the application for adjournment was intimated verbally to Mr Kelly. We reiterated to Mr Kelly that we would do everything possible to assist him. Mr Kelly indicated that he had no wish to ask any questions of the HMRC officers who had been cited to give evidence.

47. We went on to explain to him that the burden of proof rested on HMRC. We explained that we would read all of that evidence, regardless, in order to ascertain whether or not HMRC could discharge that burden of proof.

Burden of Proof

48. There is no dispute that the burden of proof rests on HMRC. We agree with Lady Hale at paragraph 34 in *S-B Children* that the simple civil standard applies and that is on the balance of probabilities:

> "34. This issue shows quite clearly that there is no necessary connection between the seriousness of an allegation and the improbability that it has taken place. The test is the balance of probabilities, nothing more and nothing less."

49. We pointed out to Mr Kelly, that although undoubtedly the legal burden rests on HMRC to prove that the transactions were connected with fraud, we agree entirely with Judge Barlow at paragraph 48 of *Megtian v HMRC*[7] where he states:

> "48. The legal burden of proof does not alter throughout the proceedings. However, the evidential burden shifts. Once a party has produced enough evidence to satisfy the legal burden the other party is obliged, not because of any rule of law but in order to succeed in the appeal, to produce evidence to refute the other party's case so far as possible."

50. We therefore explained to Mr Kelly that he might wish to consider whether or not he wished to produce any further evidence. He declined.

HMRC's Evidence

51. We had the witness statements of the following Officers:

Andrew Siddle – broker officer – three statements dated 6 March and 24 August 2009 and 12 September 2011

Fu Sang Lam – West 1 Facilities Management Limited ("West 1") – three witness statements dated 4 March and 7 September 2009 and 31 May 2006

Matthew Lee – International Investment Services (UK) Limited dated 4 February 2010

[7] 2008 UKUAT V 20894

Ann Fyfe – FCIB 13 September 2011 (albeit referred to, it was in the bundle in error as it was superseded by Officer Ellis)

Michael Mercer – FCIB 2 August 2011

David Ellis – FCIB 27 November 2012

Andrew Letherby – FCIB dated 8 July 2011 enclosing two reports both dated 12 August 2010

Michael Clarke – Universal Mercantile Building Society ("UMBS") dated 12 September 2011

Catherine Clark – Nokia 9 May 2013

John Fletcher – Grey Market 13 July 2010

Mark Ali – Balmoral Solutions Limited 14 October 2008

Mark Ali – Balmoral Limited 17 February 2010

Graham Speight – Balmoral Solutions Limited 8 June 2010

Stephen Robinson – FX Drona Limited dated 12 July 2010

Terence Mendes – FX Drona Limited dated 12 July 2010

Roderick Stone – MTIC fraud

52. In terms of the Directions issued by the Tribunal on 17 December 2013, the appellant was directed to confirm by no later than 10 January 2014 whether or not the evidence of Officers Speight, Ali and Lee and Ms Clark were challenged. No such intimation was received. Counsel argued that no challenge had been intimated to any of the evidence and that that evidence must be assumed not to be in dispute although all of the officers were available to give evidence.

53. Mr Kelly again confirmed that he did not wish any of the Officers to attend to give oral evidence. He did not wish to ask any questions of the Officers.

54. We offered Mr Kelly time to reflect on the various points which had been raised but he declined. He confirmed that he had had the opportunity to peruse all of the bundles which had been delivered to him. We noted that the final paragraph of his second witness statement, prepared by Ferdinand Kelly, had five bullet points which were described as being "In response to comments from HMRC's witnesses...".

55. Mr Kelly confirmed that his case was simply that he had not known and could not have known about any fraud. He stood by the contents of his two witness statements and had nothing to add.

56. Counsel explained that it was his intention to cross-examine Mr Kelly and put various documents to him should Mr Kelly wish to give evidence. We made it explicit to Mr Kelly that it was entirely his choice as to whether or not he wished to give evidence and as, and when, and if, he did so he had the right to decide whether or not he wished to answer any questions.

57. We explained that we would hear Counsel's opening submission and then adjourn to read the bundles. On reconvening on Wednesday 4 November 2015, Mr Kelly would be free to intimate whether, or to what extent, he might wish to participate in the proceedings.

58. Since Mr Kelly was not represented, we had intimated that we wished to read the evidence before any decision was taken on the need, or not, for oral evidence. We did so and, having done so, intimated that we did not require the attendance of the officers.

59. On reconvening and having read the evidence in greater detail, we raised a few minor questions of detail with Counsel (such as rounding up of figures in the deal sheets) and explained the position again to Mr Kelly. He had heard HMRC's opening submission which had focussed in particular on the FCIB evidence, the evidence of fraud and Mr Kelly's alleged knowledge of MTIC fraud. He was again asked if there was any aspect of HMRC's evidence that he wished to challenge, other than whether or not he knew or should have known of the connection with fraud, and he said not.

60. He made a brief statement suggesting that period 07/06 could be appealed (see paragraph 39 above) and that that would liberate funds to enable litigation and reiterated his request for adjournment which was denied on the same basis as previously. He insisted that he did not wish to give evidence. He was offered the opportunity to make closing submissions but declined.

61. Given Mr Kelly, and therefore the appellant, in effect did not wish to participate in this appeal beyond seeking an adjournment, in those somewhat unusual circumstances and with almost no evidence being produced by or on behalf of the appellant, we decided that it was incumbent upon us to decide whether to proceed in what effectively amounted to the absence of the appellant. We had due regard to the Rules and decided that having particular regard to Rule 2 of the Rules, it was in the interests of justice to proceed. However, it is therefore appropriate to set out in full our deliberations and findings for Mr Kelly's benefit.

Authorities

62. The Authorities cited are:

Mobilx & Others v The Commissioners for HM Revenue & Customs [2010] EWCA Civ 517 ("Mobilx)

Axel Kittel v Belgium & Belgium v Recolta Recycling SPRL (C-439/04 C-440/04) [2006] All ER (D) 69 (Jul) ("Kittel")

Blue Sphere Global Limited v Revenue & Customs Commissioners (2009) STC 2239 ("Blue Sphere")

Fonecomp Limited v HMRC [2015] EWCA Civ 39 ("Fonecomp")

Calltel Telecom Limited v HMRC [2009] EWHC 1081 (Ch) ("Calltel")

Red 12 v HMRC [2009] EWHC 2563 ("Red 12")

Re B (Children) (Care Proceedings: Standard of Proof) (CAFCASS Intervening) [2008] UK HL 35, (2008) 3WLR 1

S-B (Children) [2009] UKFC 17 ("S-B Children")

MTIC fraud – a brief explanation

63. As we indicate above HMRC contend that all the transactions entered into by the appellants, on which they based their claims to deduct input tax, form part of what is described as "Missing Trader Intra-Community" ("MTIC") fraud. The "classic way" in which the fraud works was described by Christopher Clarke J in *Red 12* (at paragraphs 2 and 5) as follows:

> "2….Trader A imports goods, commonly computer chips and mobile telephones, into the United Kingdom from the European Union ("EU"). Such an importation does not require the importer to pay any VAT on the goods. A then sells the goods to B, charging VAT on the transaction. B pays the VAT to A, for which A is bound to account to HMRC. There are then a series of sales from B to C to E (or more). These sales are accounted for in the ordinary way. Thus C will pay B an amount which includes VAT. B will account to HMRC for the VAT it has received from C, but will claim to deduct (as an input tax) the output tax that A has charged to B. The same will happen, *mutatis mutandis*, as between C and D. The company at the end of the chain – E – will then export the goods to a purchaser in the EU. Exports are zero-rated for tax purposes, so trader E will receive no VAT. He will have paid input tax but because the goods have been exported he is entitled to claim it back from HMRC. The chains in question may be quite long. The deals giving rise to them may be effected within a single day. Often none of the traders themselves take delivery of the goods which are held by freight forwarders.
>
> 5. A jargon has developed to describe the participants in the fraud. The importer is known as 'the defaulter'. The intermediate traders between the defaulter and the exporter are known as 'buffers' because they serve to hide the link between the importer and the exporter, and are often numbered 'buffer 1, buffer 2 etc'. The company which exports the goods is known as 'the broker'."

64. For simplicity, but without thereby prejudging the issue, we shall adopt the same terminology of "defaulter(s)" (sometimes also known as "missing traders"), "buffers" and "brokers".

65. Some MTIC appeals involve a variation on the "classic" fraud and that is known as contra-trading. However, this appeal, does not involve contra-trading.

Substantive appeal

The Decision under appeal

66. The Return for the period 05/06 was received by HMRC on 7 June 2006 and selected for in depth verification due to the large "repayment" claim of £1,749,040.46. The decision denying the appellant entitlement to the right to deduct input tax in the sum of £1,748,687.50 was issued on 18 January 2008. The Notice of Appeal was lodged by Balmoral's then representatives on 12 February 2008. The stated ground of appeal was that Balmoral had no knowledge of the deals in the supply chain.

Overview of the Deals

67. All three deals were on 31 May 2006 and involved exactly the same parties. The chain in each case was United Traders (EU) > West 1 Facilities Management Limited (defaulter) > International Investment Services (UK) Limited (buffer) >Balmoral (broker) > Online Cellular y Multimedia SL (EU). The freight forwarder was All Systems Courier Worldwide Limited until the goods were exported to KPP International Logistics, a freight forwarder in Rotterdam.

Deal 1

68. This deal involved transactions in 6,000 Nokia 8800 telephones and the unit price went £452.25 > £452.50 > £452.75 > £490.75. The mark up for Balmoral was therefore £38.00 (8.39%) compared with £0.25 (approximately 0.05%) for the others in the chain.

Deals 2 and 3

69. These deals each involved transactions in 8,000 Nokia 8801 telephones and the unit price went £454.25 > £454.50 > £454.75 > £494.00. The mark up for Balmoral was therefore £39.25 (8.63%) compared with £0.25 (approximately 0.05%) for the others in the chain.

Parties other than Balmoral in these deals

On Line Cellular y Multimedia S.L.

70. This company ("Online") was incorporated on 17 December 1996 in Spain and registered for VAT on 14 January 1997. The Spanish Tax Authorities confirmed that they had been unable to contact it and it was deregistered for VAT on 31 January 2007. It stated that "proceedings have resulted in proven facts and strong evidence that forms part of a VAT-fraud plot in which it seems to be the conduit company". It was restored to the register on 1 February 2007 but went missing and was again removed from the register on 11 December 2009.

71. In all three disputed deals it was Balmoral's EU customer.

International Investment Services (UK) Limited

72. This company ("International") was incorporated in England on 19 October 2005 and registered for VAT on 25 October 2005. The VAT application showed an estimated turnover of £400,000 and its main business activity was stated to be Brokering European Licensing and Distribution Trade Agreements.

73. In fact, it sold what HMRC described as "vast" quantities of mobile phones in 2006 including to both Balmoral and its sister company, Balmoral Solutions Limited ("Solutions"). The Veracis report discloses that it started trading in April 2006. The sales to Solutions were in period 04/06 and Solution's records show that International traded approximately £57 million worth of telephones between 10 and 28 April 2006. Those deals were traced back to West 1 Facilities Management Limited and traced forward to Worldtech, which was the broker. Worldtech was denied input tax of £5,274,675. That has not been appealed and Worldtech entered liquidation.

74. The periods 04/06 and 07/06 for International were subject to extended verification. On 18 April 2008, decisions were issued by HMRC stating that in respect of six and four broker deals respectively, in period 04/06 extended verification has resulted in denial of input tax totalling £206,233 and in 07/06 there is a denial of £192,711. International had used two suppliers in the broker deals, which were a Canadian company.

75. The supplier for all of the remaining transactions, which were buffer deals, was West 1 Facilities Management Limited.

76. One of the directors of International, Daniel Keenan, was convicted on 3 February 2006 and sentenced to two years imprisonment for blackmail and three years imprisonment for conspiracy to defraud. He was in prison during the period that deals were done with Balmoral and Solutions. At the time HMRC were simply told that he was not available.

77. International was Balmoral's supplier in all three disputed deals having purchased the phones from West 1 Facilities Management Limited. It was a buffer.

West 1 Facilities Management Limited

78. This company ("West 1") was originally incorporated as Computer Solutions Direct Limited on 7 August 2000 in England and changed its name on 6 April 2001. Turnover between 06/02 and 09/05 was in total around £200,000 but in the following year it was in excess of £1.5 billion.

79. In January, February and March 2006, West 1 was notified that deals from periods 12/05 and 01/06 had been traced back to tax losses. Solutions had made substantial purchases from West 1 in 12/05 and those deals were included in those traced back to tax loss. Balmoral also had purchased goods from West 1 in period 01/06 (see paragraph 164(o) *et seq* below).

80. In period 01/06 West 1 acted as a buffer and all of its trades (including those with Balmoral) have been traced back to Puwar (UK) Limited, a fraudulent defaulter which issued third party payment instructions and was deregistered on 15 February 2006. The debt on file is in excess of £76 million.

81. The return for period 03/06 substantially misrepresented the true extent of the trade carried on and an assessment was raised on the basis that purported supplies did not in reality take place. There was no evidence that goods physically entered or left the UK in the alleged import and export transactions.

82. West 1 made no meaningful contact with HMRC between February and October 2006 and submitted no return for period 06/06. A further large assessment was raised on the basis that the traded goods did not exist. It was deregistered in June 2006.

83. It is not disputed that West 1 is a fraudulent defaulting trader and that assessments have been raised on West 1 amounting to more than £126 million and those are unpaid. The default lost revenue in the deal with which we are concerned has been assessed and traced to that loss.

United Refrigeration and Industries

84. This is a partnership constituted in India on 28 June 1988. For the purposes of this appeal it is always known as United Traders. The partnership opened an FCIB account number 04-801-204330-01. A sub-account was opened in the name of United Traders with the number 04-801-204330-02.

85. United Traders was apparently incorporated on 13 March 2006 and registered for VAT on 14 March 2006.

86. The Portuguese Tax authorities have confirmed that it has no premises including warehouses in Portugal, that the address in Portugal was an accommodation address, that no contact had been possible and that it was believed to be a "Probable non declaring conduit company". HMRC's enquiries to ASC freight forwarders (see paragraph 88 below) had elicited the information that although United Traders was stated to be Portuguese it was believed to be based in Belgium.

SPRL Capital City

87. This company ("Capital City") was originally incorporated as SPRL Primesight on 26 March 1999 in Belgium and it changed its name on 23 March 2000. It opened an FCIB account number 04-801-202178-01 and a sub-account was thereafter opened in the name Hunzie Electronics Lda ("Hunzie") with the number 04-801-202178-03.

All Systems Courier Worldwide Limited

88. This company ("ASC") was a freight forwarder but had no commercial premises and no vehicles capable of providing the alleged service. It submitted a VAT 1 application for registration on 8 March 2006 with an estimated turnover of £750,000

but the actual turnover was in excess of £1.8 million in the first two months. It was registered for VAT from 1 February 2006 with a business activity of "courier post".

89. No incoming CMRs were produced to HMRC evidencing the import of goods and the owner of the premises where goods were alleged to have been stored denied any knowledge.

90. The owner of ASC alleged that he had purchased ASC from a former director of West 1.

Parties other than Balmoral in other deals referred to herein

Crotek Systems Limited

91. This company ("Crotek") was registered for VAT on 1 October 2004. The business activity listed for it was "pharmaceutical supplies". It had input tax denied in periods 02/06 to 05/06 inclusive of £6,531,665 and appealed unsuccessfully to the Tribunal. That decision is reported in 2011. The tax denied ultimately was £5,690,347.25.

Xchange Communications Limited

92. This company ("Xchange") was registered for VAT on 1 August 2003 and deregistered on 9 April 2008. The Director is disqualified as a Director until 19 September 2021. He is also a director of another company with which Balmoral traded in periods 11/04 to 04/05 inclusive. Both companies were placed in liquidation. The proof of tax debt in the former is £5,106,748.77 and the latter £4,479,578.62.

What must HMRC prove?

93. The matters that HMRC must prove 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 the fraudulent VAT loss?

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

94. In the Skeleton Argument HMRC stated that the appellant's position in terms of whether its transactions were connected with fraud is unclear and apparently in issue so the Tribunal is required to make findings of fact on the nature and extent of the fraud with which the appellant's transactions are concerned.

95. However, we note that after hearing arguments for both parties, the Directions of the Tribunal issued on 23 January 2013 made it clear that:

"(a) Balmoral had accepted that West 1 was guilty of fraudulent evasion of VAT as alleged by HMRC,

(b) that there was no need for evidence on that point, and

(c) there was no need for evidence to be given by HMRC as to the existence of a connection between Balmoral's purchases and the admittedly fraudulent default of West 1."

96. For the avoidance of doubt, we decided that notwithstanding that, we were required to consider HMRC's tracing exercises, in order to satisfy ourselves that the appellant's deals had all been traced to fraudulent VAT losses. We accept the very clear evidence that West 1 was a defaulting trader, that it was guilty of significant fraudulent evasion of VAT and that Balmoral's deals have been traced in connection therewith.

97. Therefore the only issue for the Tribunal was whether or not Mr Kelly, and therefore Balmoral, knew or should have known of the connection with fraud.

The law on MTIC

98. Although most readers of this decision will be very familiar with the extensive law on MTIC fraud, and we do not propose to rehearse that in this decision, the key legal principles in regard to knowledge of fraud have recently been approved by Lady Justice Arden in *Fonecomp.*

99. In summary, she stated that the question of knowledge is to be decided on the objective evidence and without reference to the trader's knowledge and she endorsed Moses LJ in *Kittel* where he stated at paragraphs 59 and 60:

"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 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."

100. She went on to endorse the test set out by Briggs J in *Megtian Ltd v HMRC*[8] at paragraph 37 and that reads:-

"37. 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

[8] [2010] EWHC 18 (Ch)

> participating is connected with that fraud, without knowing, for example, whether his chain is a clean or dirty chain, whether contra-trading is necessarily involved at all, or whether the fraud has at its heart merely a dishonest intention to abscond without paying tax, or that intention plus one or more multifarious means of achieving a cover-up while the absconding takes place."

101. Lastly she made it explicit that the case law does not require that a trader knows the details of the fraud or of the connection between its transactions and the fraudulent evasion of VAT.

102. We are required to look at all of the circumstances surrounding the transactions in question, not just at the deals done by Balmoral itself.

103. It is not enough that the circumstances of an appellant's transactions might reasonably lead an appellant to suspect a connection with a fraud and nor is it enough that an appellant should have known that it was more likely than not that the transactions were connected with fraud.

104. The test is whether on the balance of probability the *only* reasonable explanation for the circumstances in which the transactions took place is the connection with fraudulent evasion.

105. We agree with the Upper Tribunal in *GSM Export (UK) Ltd (in administration), Sprint Cellular Division Ltd (in administration) v HMRC*[9] when it confirmed that the requirement as to the taxpayer's state of mind squarely remains "knew or should have known" and that the reference to the "only reasonable explanation" is merely a way in which HMRC can demonstrate the extent of the taxpayer's knowledge, that is to say that he knew or should have known of the connection with fraud.

106. We confirm that we have looked at all of the circumstances surrounding the transactions and set out our findings below.

Background to Balmoral and Balmoral Solutions Limited

107. Balmoral was incorporated on 30 January 2002. Since January 2003, the trading address has been a residential flat with office space underneath and with no storage facilities. At all times Mr Kelly has been the sole director and shareholder of Balmoral. He is also the sole director and shareholder of three other companies, one of which is Balmoral Solutions Limited ("Solutions") which was incorporated on 6 May 2003. It too was involved in the wholesaling of mobile phones. Its pattern of trading is therefore relevant. Both businesses traded from the same address, had the same "administrative assistants" and from the date of incorporation of Solutions had the same Company Secretaries for the same periods.

108. Balmoral has had six Company Secretaries since incorporation but we note that there were two periods (11 May 2002 to 28 February 2003 and 30 November 2003 to

[9] 2014 UKUT 0529 (TCC)

4 April 2004) when there was no Company Secretary. Solutions had five as it was incorporated later.

109. It is of particular note that Mrs Beverley Tookey was Company Secretary of both companies, in the case of Balmoral from 1 March 2003, and in the case of Solutions, from incorporation on 6 May 2003 and she resigned from that position for both companies on 4 August 2003.

110. It is not known when the "administrative assistants" were employed but it is known from the record of interview on 21 September 2006 ("2006 interview") that Jackie Harris (who was at the interview) was a bookkeeper and at the time of that interview, Mr Kelly stated that Balmoral had three employees. That is consistent with his second witness statement where he stated that Jackie and Samantha did the trades after he had searched the markets to find opportunities. We can see that Samantha's signature is on some of the documentation for the disputed deals.

111. Mr Kelly told HMRC that his previous business had been Five Star Communications. HMRC ascertained that that was as a sole proprietor from 1995 dealing in retail mobile phones and contracts and then as Five Star Communications Limited from 14 April 1997 until liquidation later that year as a result of a creditors voluntary winding up. The information in Mr Kelly's witness statements is less precise (see "Mr Kelly's evidence" below).

VAT registrations

Balmoral

112. Balmoral has had two VAT registrations.

First registration

113. It was originally registered for VAT on 1 July 2002, the application having been received by HMRC on 5 July 2002. That application stated that the main business activity would be "Wholesaler and Importer of Electrical Goods".

114. The first HMRC visit was on 29 July 2002 when it was reported that no trading had taken place but that the intention was to trade primarily in the wholesale of plasma screen TVs. In the course of the interview it became evident that computers, mobile phones and batteries might also be involved. The officer was concerned about a number of issues including the lack of information about purchase prices and the stated reliance on funding by credit from potential suppliers. The officer recommended that registration be refused. Mr Kelly then provided further supporting information and registration was granted in September, backdated to July 2002.

115. The VAT Certificate states that it was registered on a trade classification "other business activities not classified". The clear inference is that the information furnished by Mr Kelly about trading did not specify mobile phones.

116. Balmoral was subsequently deregistered from VAT on 5 February 2004 (see below).

Second registration

117. Mr Kelly then submitted a new application for VAT registration dated 29 April 2004 and it was received by HMRC on 30 April 2004. That stated that the business activity was "Mobile Telecommunications Accessories". By contrast, at the HMRC visit, which followed on 28 May 2004, Mr Kelly stated that the business activity would be contract retail sales of mobile phones. He also stated that he had no need of start-up capital.

118. That VAT application stated that the estimated turnover would be £100,000 (with no EC trades) whereas in the period 6 February 2004 to 31 January 2005 the turnover was £40,337,855. (The first trades were between 17 and 20 August 2004 and those were wholesale transactions in mobile telephones worth more than £29 million and were the subject matter of the 2008 appeal.)

119. Balmoral was registered under a new number for VAT with effect from 6 February 2004, put onto monthly returns and issued with a security letter.

Solutions

120. Mr Kelly made the first application for VAT registration for Solutions on 6 February 2004 with the business activity described as "financial services". Following a visit on 19 May 2004, registration was refused, on the basis that financial services are exempt.

121. Mr Kelly signed a second application for VAT registration dated 16 February 2005. HMRC visited on 16 March 2005 and Mr Kelly advised that he had incorporated Solutions in order to keep CPU deals separate from mobile phone deals, which would be handled by Balmoral. He was told that VAT registration would be refused unless evidence of CPU deals was submitted to HMRC within 14 days. On 23 March 2005, copies of two purchase orders dated the previous day were provided.

122. Solutions was registered for VAT with effect from 22 March 2005.

123. That second application had specified estimated turnover at £1,000,000 (with no EC trades) and business activity as "IT Consultants".

124. On 24 March 2005, Officer Malik visited Solutions and the future trading activities were then described as the wholesale of computer parts.

125. However, in the first year of trading the turnover, derived almost wholly, if not exclusively, from mobile phones was at least in excess of £369,151,37. In the first VAT period alone the turnover was in excess of £24 million.

126. Furthermore, the declared business activity was not consistent with the FCIB application made earlier that year by Mr Kelly, which stated that the business was mobile phones.

Deregistration

Balmoral

The 2003 deregistration

127. During a visit on 16 January 2003 Mr Kelly was specifically advised about the incidence of MTIC fraud generally, the high level of risk associated with trading in mobile phones, the need to check VAT registrations, the other checks that could and should be carried out and that third party payments should not be made. At that stage no wholesale trades had taken place. Officer Emery orally agreed with Mr Kelly the basis on which he could trade.

128. The VAT 1 application for VAT registration had stated that the estimated turnover would be £500,000, that there would be no EC trade and that purchases would not regularly exceed sales (ie that it would not be in a repayment position). Following a period of inactivity by Balmoral, HMRC discovered that, between 21 and 25 March 2003, Balmoral had undertaken transactions to a value in excess of £10 million net.

129. On 25 March 2003 Officer Emery wrote to Mr Kelly in the following terms:

> "During our meeting on 16th January we discussed the high level of risk associated with your chosen trading activity and we agreed certain conditions for your future trading.
>
> One of these was to inform me before you undertook your first deal. This did not happen and I understand that you have gone ahead with another deal today.
>
> I am taking this opportunity to put our verbal agreement on a more formal footing. The points we agreed are laid out below and I look forward to receiving the details of todays transaction shortly.
>
> - Basic checks to be conducted by yourself include checking details supplied by another business match and make sense. Where appropriate you should check Companies House for directors and a personal visit is recommended where possible.
> - You are strongly advised never to deal with anybody who only gives you a mobile phone number.
> - You are strongly advised never to deal with anybody who wishes you to make, or receive, a third party payment.
> - For all new customers and suppliers the VAT number must be cleared by ourselves before trading commences. You should obtain copies of the VAT certificate, Companies House certificate and a letterheading giving the bank account details. These should be faxed to our Redhill office on 01737 734605 or to myself. You must not trade without a positive reply. The phone number of our Redhill office is 01737 734516 and you will be

able to speak to the person who answers the phone. You should repeat this check if you have not traded with somebody for a period of time.

- At the end of each days trading you should notify myself of the details of the transactions that have taken place. A suggested format has been supplied which should be faxed across but the same information can be provided by E Mail or even a phone call if you prefer."

She faxed that letter and requested that he contact her as soon as possible.

130. The following day, on 26 March 2003, Mrs Beverley Tookey telephoned Officer Emery, stating that Mr Kelly had a personal crisis and that it was she who had been conducting the deals. She provided information to HMRC. All sales were to SL Logistics. The purchases were from two other companies and she was asked how payment had been made. She confirmed that she did not have access to Balmoral's bank accounts and that SL Logistics had made third party payments.

131. On 27 March 2003, she forwarded to HMRC a copy of the sales invoices and a copy of the VAT certificate and Certificate of Incorporation both of which appeared to HMRC to have been doctored. Both of Balmoral's suppliers were hijacked traders.

132. HMRC interviewed Mrs Tookey on 31 March 2003 and she confirmed that Mr Kelly had given her no specific instructions. She agreed that she had not checked the documentation furnished by the sellers. She explained that she had been totally unable to contact Mr Kelly and because she knew that he knew the purchaser, SL Logistics, she was assisting him by conducting the deals. She knew that had made third party payments, not to Balmoral's suppliers but in both cases to Sunico, which she said that she knew was a Spanish company (it was, of course, Danish).

133. The HMRC officers noted that although she claimed total ignorance of the trade, she did appear to demonstrate a greater knowledge of the business than she claimed, particularly in regard to pricing structure.

134. Mrs Tookey told HMRC that she had been an employee of Mr Kelly when he ran Five Communications. She had seen him briefly on the evening of 19 March 2003 when, because he had a personal problem and had to leave on short notice, he had given her a key to the flat, a bank card and no specific instructions. She knew that the person behind SL Logistics, Spencer, was an old friend of Mr Kelly.

135. Mr Kelly was requested to, and had, attended an interview on 28 March 2003. At that meeting he denied any knowledge of the deals and stated that he had given no instructions or authority to Mrs Tookey who he described as somebody who worked for him in his previous retail business. He confirmed that she was an ex-employee and that he had asked her to "hold the fort" for him. He also confirmed that he had known and dealt with Spencer when he ran Five Communications.

136. Neither Mrs Tookey nor Mr Kelly told HMRC that Mrs Tookey was Company Secretary of Balmoral.

137. On 31 March 2003, HMRC wrote to Balmoral intimating the decision to deregister it for the protection of the Public Revenue.

138. W J B Chiltern, Balmoral's representative wrote to Officer Emery on 1 April 2003 indicating that firstly Mr Kelly had been absent from the business and secondly that Mrs Tookey was "unaware of the procedures to be followed in verifying the supplier's VAT registration details or to notify the details requested by Redhill office. This would therefore appear to have been a temporary lapse of the normal control procedures in place in the company". Following those representations, the VAT registration was reinstated on 30 April 2003.

139. Mr Kelly's second witness statement is at complete odds with this well documented account of events. At paragraphs 11 to 16 he stated firstly that this incident had happened in 2004 and, secondly, that his "experienced and competent administrative assistant" Mrs Tookey had done a trade with a company which lost money on their "ongoing sale" and went out of business with the result that Balmoral ended up being owed a lot of money. He stated that Officer Emery had visited Balmoral to inform it that an apparently fraudulent "missing trader" had caused SL Logistics the problem that then affected Balmoral. His suggestion was that it was because of the missing trader that HMRC "attempted to remove the VAT number". That is patently incorrect.

140. Neither of those accounts sits with a letter that Mr Kelly wrote to HMRC on 17 February 2004 when he was requesting VAT registration. He stated that:

> "Further to our conversation, this is to confirm that I do require my vat number. Unfortunatly (sic) as I explained earlier due to the theft of working capital from my business account last year, by the company secretary Beverley Tookey.
>
> As she had taken the money out of the account from abroad, I realised there was little if any change of getting it back. Never mind the reason for doing so in the first place, the event obviously depressed me for a while. I did trade within that time although I was not able to trade as hoped, due to loss of working capital.
>
> As I am now in a better frame of mind and fairly better financially, I am in a position to trade has (*sic*) intended, and know the company will trade over the vat threshold.
>
> As most of the distributors and companies I am doing business with or intend to do business with require companies to be vat registered this is also an issue, as this would affect my ability to trade.
>
> I am also aware that the industry has had problems with companies disappearing and not paying vat owed, as I trade from my home address and have been in the industry for over fifteen years of which it is my livelyhood (*sic*), it is not something that I willingly would get involved with. Companies that I deal with on a wholesale basis are checked with Redhill as requested.
>
> May I also apologise for the late returns recently and can guarantee they will be submitted on time in future.
>
> I hope this information is helpful enough as I wish to be able to trade using my vat number as soon as possible."

The 2004 deregistration

141. Following a sustained period of nil trading where it failed to make any VAT returns for the periods 09/03 to 02/04 inclusive, Balmoral was again deregistered on 5 February 2004 as it had failed to submit three consecutive returns. Again Mr Kelly requested reconsideration but that was refused on 6 April 2004. As we indicate above the next application for registration dated 29 April 2004 was accepted.

The 2008 deregistration

142. On 27 February 2008, Officer Siddle wrote to Balmoral requesting evidence of intention to trade to which there was no reply and on 5 June 2008, it was deregistered and a debt of £2,452,463.88 remains on file.

Solutions

143. There appeared to HMRC to have been no trade since 2007 and, on 23 January 2008, it was deregistered because no evidence of intent to trade was produced. A debt of £48,850.42 remains on file.

VAT Returns

Balmoral's VAT returns

144. Prior to the period under appeal, Balmoral had submitted a total of 23 monthly VAT returns on the second VAT registration number starting with the period 06/04.

145. There were three returns with minimal trade, namely for periods 06/04, 05/05 and 10/05. There were six nil returns for the periods 07/04, 09/04, 12/05 and 02/06 to 04/06 inclusive. Accordingly Balmoral was only actively trading for approximately 60 per cent of the time in question.

146. Balmoral has submitted 10 returns for periods in which, from the information provided, it bought and sold to UK traders. Therefore it was acting as a buffer. The return for period 08/04 was one of those and the resulting assessment was the subject matter of the 2008 appeal. The remaining such periods were 10/04 to 04/05 inclusive and 06/05 and 07/05.

147. In two periods, namely 08/05 and 09/05 Balmoral completed both buffer and broker deals. In period 08/05 Balmoral completed four deals with the purchases in three being from Xchange and the fourth from Solutions who had purchased the goods from Xchange. Two buffer sales were made to a UK company and two broker sales to a Hong Kong company. The UK company went on to sell the goods to the same Hong Kong company.

148. In period 09/05, in a broker deal, Balmoral again purchased from Xchange and sold on to Sunico A/S. That generated a without prejudice repayment of £17,751.18. (Sunico had been the recipient of the third party payment in the fraudulent deals in 2003).

149. In the period 11/05, Balmoral completed one deal only, and it was a broker deal, generating a without prejudice repayment of £41,561.63. The purchase was from Crotek who in turn had purchased from Xchange. HMRC have been unable to trace the deal beyond Xchange. As we indicate above both Crotek and Xchange are themselves defaulting traders.

150. The deals in period 01/06 are covered in detail below at paragraph 164(o) *et seq* but, in summary, Balmoral's three broker deals meant that the tax loss exceeded £1,094,800.

Solutions' VAT returns

151. In the first VAT period 06/05 it achieved a very large turnover of more than £24 million.

152. HMRC have traced all of the deals in the 12/05 quarter, where Solutions purchased phones from West 1 in October 2005, back to a tax loss via a contra trader and all of the onward supplies to five customers have resulted in large repayments. All repayments were made without prejudice since the period preceded the extended verification exercises. Balmoral itself did not trade in October 2005 and submitted a nil return.

153. Of 11 VAT returns, seven were submitted late and the final return never lodged, but the repayment claims in periods 03/06 and 09/06 were submitted timeously. Those repayment claims were not large.

Detail of 03/06 return for Solutions

154. There were 106 sales invoices in that period and 103 of those deals have a margin of £0.50 per unit although the deals involved differing quantities and models of phones with purchase prices ranging between £139 and £493. Of the remaining three deals one had a margin of £1 and another a loss of £0.50 per unit and the last deal of the period had a margin of £31.50 and it was the only deal with a mark up exceeding 1%. The first 105 deals were buffer deals, the last was a broker deal. It was the only export or broker deal in the period since incorporation.

155. In almost every deal the stock was sold on the same day that it was sourced, with up to 10 deals occurring on the same day.

156. Nokia 8800 phones were purchased from Phone City Limited ("Phone City") on five separate occasions in that period. In all the buffer deals the margin was £0.50 on a purchase price which varied very little and averaged £439.87 yet for the broker deal the purchase price was only £393 and the margin £31.50.

157. That deal has been traced to two defaulting traders (primary evidence of Officers Mendes and Robinson, and rehearsed by Officer Ali) and Phone City itself is a missing trader and was deregistered from VAT on 25 July 2006. The freight forwarder used by all the parties has also been deregistered as a missing trader.

158. The EU customer is also a missing trader. No due diligence on the customer has been produced notwithstanding requests from HMRC.

159. Solutions produced due diligence on Phone City from Veracis dated February 2006. That had a number of negative indicators including a report that a July 2005 deal was linked to a defaulting trader, that no financial information was available and that Veracis had been unable to meet with a Director. Crucially, it stated that "100% UK all goods are sourced from Callender Group". On 16 March 2006 HMRC issued Solutions with a veto letter stating that Callender had been deregistered with effect from 15 March 2006 yet Solutions went on to buy the goods for the broker deal from Phone City on 31 March 2006.

160. Pertinently, Solutions have never produced an original copy of the CMR. The EU customer was based in Poland but the goods were sent to Worldwide Logistics BV in the Netherlands. In the criminal investigation into that freight forwarder the controlling mind confessed in 2006 that:

> "I have done something incredibly stupid. From the beginning of February 2006 to the end of May 2006 I took care of fictitious consignments … by fictitious I mean dealing with consignments on paper which are not physically sent or where there is never any question of physical goods existing … Physical flow of goods came to a virtual standstill after December 2005. The physical flow of goods I am referring to involves electronics, in particular mobile phones … The reason for the flow of goods coming to a standstill here is that Dutch Customs became a bit stricter in relation to tax representations."

161. Every trader in the deal chain has now been deregistered as missing.

162. Solutions were denied input tax on that deal amounting to £50,205.75 and the Tribunal dismissed the appeal in 2008.

163. In addition, HMRC have identified that at least five of the UK to UK deals in the period 03/06 where Solutions acted as a buffer, have been traced back to tax losses.

Other contact with HMRC prior to 05/06

General

164. We accept the very clear evidence from HMRC that they have on many occasions drawn Balmoral's attention to the risks of MTIC fraud both in general and in relation to Balmoral's business in particular. For example, in addition to the visit on 16 January 2003, and the contact in March 2003, there was the following contact:

(a) As we indicate above Balmoral had been deregistered for VAT for the protection of the public revenue. When the registration was reinstated on 30 April 2003, HMRC provided copies of budget notices:

CE14 VAT - Extension of Security Powers,

CE15 VAT – A new joint and several liability provisions and

CE17 VAT – Evidence for input tax deduction,

and also two consultation documents:

VAT Strategy: Joint and Several Liability Consultation on reasonable checks and VAT Strategy: Input tax deduction without a valid VAT invoice consultation on draft statement of practice.

The former consultation Document is the predecessor of Notice 726 which was first issued in August 2003. At the interview in September 2006, Mr Kelly's solicitor confirmed that Mr Kelly had read Notice 726.

(b) HMRC wrote to the appellant on 2 October 2003 warning that security action might be taken if it continued to trade without properly verifying its supplies. It made it explicit that if Balmoral continued to trade in supply chains with businesses that represented a serious risk to the Exchequer and failed to take reasonable steps to verify the legitimacy of suppliers and customers then a security of £891,974 would be required. The HMRC Notice 700/52 specifies that checks should be made on suppliers and if not security may be required or a taxpayer deregistered and that was included with this letter.

(c) HMRC wrote to the appellant on 22 June 2004 confirming the need to verify the VAT numbers of suppliers. It was a standard "Redhill" letter the terms of which are set out at Appendix 1.

(d) On 30 November 2005, HMRC wrote to Balmoral warning about verification of the repayment claim for period 09/05 in respect of buffer deals and warning of serious revenue losses in the industry.

(e) Balmoral and Solutions have received numerous veto letters over the years from HMRC advising of the deregistration of businesses with known MTIC links.

(f) On 9 May 2005, HMRC had written to Mr Kelly at Solutions advising that trade partners should be verified through Redhill.

(g) On 8 May 2006 HMRC visited Solutions and noted that International had supplied them in April 2006 in its first month of trading. See paragraph 73 above.

Direct Phones Limited - Period 08/04

(h) On 23 August 2004, HMRC had sent a veto letter to Balmoral stating that Direct Phones Limited (Direct) had been deregistered with effect from 18 August 2004. Balmoral had purchased as many as 26 consignments of phones from Direct, which had been hijacked - that is Balmoral had dealt with someone purporting to be Direct. Balmoral claimed credit for input tax, which was allowed initially.

(i) On 20 October 2004, Balmoral was informed that it had been involved in a supply chain where a business had gone missing leaving unpaid VAT, namely Direct. On 21 October 2004, Balmoral was served with a Notice which required it to provide security pursuant to paragraph 4(2)(b), Schedule 11 VAT Act 1994 in the sum of £1,541,300.

(j) The appellant's appeal in that regard was dismissed and that is the subject matter of the 2005 appeal in which the decision was released on 25 August 2005 (see below).

(k) In the interim, on 16 March 2005, HMRC officers had visited the appellant and discussed due diligence, pointing out the many deficiencies in what the appellant had done in regard to Direct and advised far more stringent checks.

(l) On 3 October 2005 the assessment, which is the subject matter of the 2008 appeal was raised in the sum of £2,017,366. That related to the purchases from Direct and was raised on the basis that none of the invoices were valid. As we indicate above, the assessment was confirmed.

Balmoral itself hijacked

(m) On 24 August 2004, Officer Emery spoke by telephone with Mr Kelly after a suspected hijacked trader had attempted to clear Balmoral's own VAT registration through Redhill in regard to five invoices with VAT totalling £3,010,000. Mr Kelly denied that those related to Balmoral.

(n) Mr Kelly cancelled the appointment that had been arranged for the next day citing problems with his car. Officer Kelly then visited Balmoral's accountant on 25 August 2004 and crosschecked the invoices coming to the view that it was probably a hijack. Officer Emery recorded: "I later phoned Mr Kelly and advised him of today's progress. He is well aware of the MTIC problem and hijacked registrations."

SGA, Period - 01/06

(o) On 30 March 2006, HMRC wrote to Balmoral stating that Spanish Global Assistance Trade B.V. ("SGA"), a Netherland company to whom Balmoral had raised three invoices in period 01/06 had a VAT number that appeared not to have been issued by the Dutch Authorities. In response Balmoral later produced a Veracis report based on a visit on 3 April 2006 with numerous negative indicators such as the fact that SGA did no due diligence, had no VAT registration and no paperwork was available. It appeared that a draft had been sent to Balmoral on 5 April 2006.

(p) On 28 April 2006, HMRC wrote to Balmoral confirming that the three transactions with SGA in period 01/06 had commenced with defaulting traders. That letter also referred to Notice 726 and pointed out the need to "check the integrity of the supply chain". We annex at Appendix 2 the relevant extracts from Notice 726.

(q) Those transactions were on two invoices for 3,000 Nokia 8800 each and one invoice for 6,800 Nokia 8801. The tax loss exceeded £1,094,800. The customer in each case was SGA and Balmoral had purchased the goods from West 1. The defaulting trader was Puwar (UK) Limited which owes HMRC in excess of £76 million. It was deregistered on 15 February 2006, subsequently amended to 16 February 2006.

(s) HMRC made a without prejudice repayment to Balmoral of £1,095,989.13 since this was before the extended verification action.

(t) On 28 April 2006, Balmoral was issued with a warning of joint and several liability action in respect of the SGA deals.

The 2005 appeal

165. In the 2005 appeal, in which the decision was released on 25 August 2005, Judge Demack stated that having carefully considered the case for HMRC it was accepted in every detail. He recorded HMRC's reasons for the requirement for security and that reads as follows:-

> "Firstly, the Appellant had previously been involved in supply chains involving businesses that evaded substantial VAT payments and had been issued a warning letter accordingly.
>
> Secondly, the Appellant was aware that VAT had been evaded, and had been given the opportunity to address its commercial practices in order to avoid becoming involved in high risk supply chains in the future.
>
> Thirdly, the Appellant did not provide further information after the issue of the Warning letter, despite being invited to do so in the letter.
>
> Fourthly, the Appellant had entered into 26 deals with a 'missing' trader, Direct Phones Ltd, leaving a significant amount of VAT unpaid."

166. Paragraph 11 of that decision goes on to record the conditions imposed on Balmoral when it was reregistered for VAT and that reads:

> "11. Following representations by Balmoral's then VAT advisors, WJB Chiltern, HMRC agreed conditionally to reinstate its VAT registration. Reinstatement took place on 30 April 2003 subject to the following conditions: …".

The judgment then set out the terms of Officer Emery's letter of 25 March 2003 (see paragraph 129 above).

167. Judge Demack observed at paragraph 25 that: "There was not a shred of evidence, except a single telephone call to HMRC's Redhill office, that Balmoral took any steps to check that Direct was a bona fide trader." He went on to dismiss the appeal.

The Telephones

168. Balmoral has been on notice since Catherine Clark's witness statement was served in May 2013 that Solutions' apparent sale of 224,500 units of Nokia 8801 between 25 January 2006 and 28 April 2006 is simply incredible. In addition, of course, Balmoral had sold 6,800 of those phones to SGA in January 2006 and in the second and third deals with which we are concerned Balmoral apparently sold 16,000 of those phones one month later. The total number of N8801 phones, which were manufactured, was approximately 161,000.

169. Miss Clark is a solicitor in the Nokia litigation team and has no discernible interest in this litigation and her evidence is wholly credible. She states: "There are no records of any sales of the Nokia 8801 phone via any Nokia authorised distributors in the UK." She has never seen a counterfeit 8801 phone in Europe. The Nokia 8800 was destined for the European market and the 8801 was the American variant with two different

packages namely American English, Brazilian Portuguese and American Spanish for the American market and American English, American Spanish and Canadian French for the Canadian market. The phones would have had the American two pin charger.

170. She states that there were no significant thefts of those phones in that period and the phrase "EC specification" was not utilised in connection with that phone. However, all of the phones traded by Balmoral in the three deals with which we are concerned are said to be of European specification. Specifically the purchase order, pro forma and sales invoices in deals 2 and 3 describe the Nokia 8801 phones as "Euro Spec". They are not and cannot have been.

FCIB

171. Officer Fyfe initially, and then Officers Mercer and Ellis have traced all of the payments by the participants in these three transaction chains through the accounts held with the First Curaçao International Bank ("FCIB") bank. We note that Officer Ellis' analysis was independent of Officer Fyfe but came to the same conclusions.

172. Deals 2 and 3 are identical in terms of goods and quantity and the payment descriptions do not include invoice numbers so although the Officers have conflated the payments in deals 1 and 2, it could equally be a conflation of deals 1 and 3 with deal 2 standing alone. It makes no difference. The funds for the conflated two deals appear to move in tandem.

173. In each case the funds moved in a circular fashion through the known participants in the transaction chain on 31 May 2006. However, in addition in every case Hunzie introduces the funds to Online from outwith the United Kingdom.

174. In deals 1 and 2 the payments were all made within one hour. In those deals Online, which had been invoiced a total of £6,896,500 by Balmoral (zero rated), paid that sum to Balmoral at 20:09:03 having received £7,000 more than that from Hunzie three minutes earlier. Balmoral owed International £7,466,537 (inclusive of VAT) but paid only £6,896,000 at 20:12:04. International who owed West 1 £7,462,425 paid £6,896,500 at 20:15:17 and West 1 in turn then paid that sum to United Traders. Then at 21:03:13, United Traders paid more than £5 million to Hunzie and in excess of £1.5 million to a Spanish company, which ultimately remitted the funds to the USA.

175. There is therefore a shortfall in Balmoral's payments to International and indeed onward through the chain. There are no other payments through FCIB in this matter.

176. In deal 3 all payments were made within 18 minutes. The chain started at Hunzie who paid £3,956,000 to Online at 21:06:02 who paid £3,952,000 to Balmoral at 21:09:02, which sum then passed through West 1 to United Traders finishing back at Hunzie at 21:24:02. Again, because Balmoral was paid the sum due on a zero rated supply and the same sum passed through the chain, no other party was paid in full.

177. Crucially, it has been identified that all of the transactions utilised the same IP address. HMRC officers have established that there is a minimum of a three minute gap between any single transactions from an IP address (ie the refresh). That is the

gap each movement of funds except between International and West 1 where it is six minutes in both deal chains.

178. Officer Letherby furnished detailed evidence on the forensic integrity and cross-verification of the FCIB servers. In his second report he specifically addresses the situation where two or more individuals utilise the same IP address. His conclusion, having canvassed all reasonable possibilities is very clear. He states:

> "It is highly unlikely that separate users in multiple locations could coincidentally achieve the same IP address consecutively in a given set of transactions. This is because to do so, each user would need to manually release the IP address lease and the next user would need coincidentally, to be using the same Internet Service Provider, and be randomly allocated that recently released IP address."

179. Officer Ellis also traced the 03/06 deal for Solutions and established a circular movement of funds on 5 April 2006.

180. There is no evidence that Mr Kelly did any due diligence before opening the FCIB account to which he entrusted millions of pounds.

UMBS

181. Although in its two periods of VAT registration, Balmoral had indicated that it had used six different bank accounts, HMRC were never advised that it had banked with United Mercantile Building Society (UMBS). Michael Owen McGrath is a director of West 1 and also a director of UMBS. The director of ASC told HMRC that that company had been purchased from Mr McGrath for £23,000.

182. As we indicate above, there was a shortfall in the payments made by Balmoral in all three deals. Officer Siddle's third witness statement showed that on 12 July 2006, Balmoral paid in excess of £900,000 (derived from the repayment from HMRC for 01/06) into UMBS to a company which on the next day paid most of that to West 1 which in turn paid most of that to United Traders. The argument was that those payments represented that shortfall.

183. We comment thereon below but Officer Clarke's evidence was that UMBS was a fraudster's bank quoting His Honour Judge Gledhill when sentencing UMBS : "…it soon became a fraudster's bank and the evidence that the jury saw amply demonstrated that the members were using the bank for fraudulent purposes, principally carousel or missing trader intra-community frauds…carousel frauds were being done on a virtual daily basis..".

Deal packs

184. Balmoral's deal packs comprised a check list, sales invoice, purchase invoice, pro forma invoice and other supporting documentation. For these deals we had the benefit of also seeing International's and West 1's deal packs. The latter shows the stock being purchased from United Traders on 31 May 2006. The former shows that International appears to have done no due diligence on Balmoral (notwithstanding the terms of the supplier's declaration in Balmoral's deal packs).

Manner of Trading

185. We have the benefit, as did Mr Kelly, of Judge Bishopp's decision in the 2008 appeal which, at paragraph 8 describes Mr Kelly's *modus operandi* in 2004:-

> "8. The only checks he had undertaken were to examine copies of Direct Phone's VAT Registration Certificate and Certificate of Incorporation, and verify with the Commissioner's Redhill office that Direct Phones was indeed registered for VAT. He did not visit Direct Phone's premises, or ever meet Ian, and he did not inspect any of the goods, or have them inspected, on his behalf by a freight forwarder or anyone else. There are no release notes, that is instructions to freight forwarders to release consignments from one trader to another, nor any documents showing that the goods have been transported. The purchase orders add nothing to the invoices. Mr Kelly agreed that he paid for the goods by sending all of the money to a third party, contrary to the Commissioners guidance to traders in mobile phones, of which he also agreed he was aware."

186. We can also see that in these deals the purchase orders add nothing to the invoices although release notes have been produced. There is minimal information on transportation and the little that exists proves very little. There is no information about inspections and no third party payments.

187. In his second witness statement Mr Kelly described his "Method of doing deals and accompanying documentation". He stated that goods would not be held physically so all arrangements to verify and identify them and to get insurance cover for onward transit would be done through agents since typically the opportunity to buy and sell would be available for only a matter of hours.

188. In paragraph 21 he stated that:

> "21. In detail, the procedure which my two assistants … would follow would be:-
>
> (a) If an opportunity was found a deal pack/check list would be set up to ensure that all documents and checks were completed,
>
> (b) A full ID verification and credit check would be made on both the companies we were purchasing from and the companies we were selling to,
>
> (c) The VAT number of both supplier and purchaser would be checked on the appropriate web site,
>
> (d) An agent would check the goods were available in the location in question. He would verify the IMEI numbers in the batch concerned,
>
> (e) Freight agents would arrange and confirm insurance cover for transport of goods and would make all freighting arrangements.
>
> (f) Invoices and receipts, and terms of business orders etc would be obtained."

189. He went on to say:

> "sometimes – as for example in the instance of one of the deals now in question – the company carrying out the ID/verification/credit check would not be able to produce its written report on the day of the deal. In those cases, a representative of the company would telephone the results of the search and only later send through a written report."

190. However, we also have the evidence of the 2006 interview when he described his method of trading. That had some additional information. He stated that he used the IPT website and compared prices with the high street. He said that he had done very little market research, in that he just called suppliers and customers but he had looked at the internet. He did not prepare draft accounts or use management accounts or cash flow forecasts. The primary pressure on finances was the receipt of the input VAT from the zero rated sales. He stated that he had trained his staff in house and they were aware that the goods should be marked up with a £0.25 to £1 margin.

191. Since the evidence is not all consistent it is easier to address the steps identified in his witness statement.

Deal pack/check list

192. There are deal packs /check lists.

ID and verification –Due Diligence

193. At the 2006 interview Mr Kelly confirmed that no due diligence had been done on freight forwarders before June 2006. He stated that he did due diligence checks using Veracis and ABC and that he received verbal confirmation from the companies before a deal was done. He was clear that if a negative report was received by telephone then he would not do the deal. Balmoral sometimes met suppliers and customers as part of due diligence.

194. We have examined the due diligence in the three deals with which we are concerned.

International

195. International is Balmoral's supplier in all three deals. Solutions also traded with International in 04/06 which was International's first period of trade.

196. The due diligence provided was confirmation of the VAT number from Redhill on 4 May 2006, confirmation from the contact centre dated 31 May 2006, a supplier declaration signed 31 May 2006 and a Veracis report.

197. That Veracis report purports to have been created on 8 August 2006 following a visit on 3 August 2006, is stamped Draft and Unapproved and titled "Strictly in Draft before Peer Review and Final Checks". That report is of no value whatsoever in relation to the deals since it was drafted and delivered more than two months after the deals with which we are concerned. However, it is interesting to note that the documentation that Veracis did see was in relation to what was described as an "earlier Balmoral deal" which was in fact one of those with which we are concerned but International refused to show Veracis any supporting supplier documentation.

198. The key point is that that report makes it explicit that "…the company did not effectively commence trading until April 2006…" and no up to date financial information was available.

199. The Redhill verification was dated 4 May 2006 which was after the date of the deals but the VAT number was verified with the contact centre on 31 May 2006.

200. The Supplier Declaration for each deal is a one page document accompanied by what is described as a "Purchase Agreement" on two pages but the second page in each case relates to Solutions not Balmoral but is dated 31 May 2006 and signed for International and Solutions.

201. On 27 September 2006, HMRC wrote to Balmoral asking what checks had been done at the time of the deals. No response has ever been received. Therefore it would appear that the only checks completed before stock worth approximately £11 million was purchased were verification of the VAT number and a supplier declaration with a Purchase Agreement with Solutions.

Online

202. The due diligence amounted to a Veracis report and a Credit Safe report, both of which are dated 31 May 2006, which is the date of the three disputed deals. The Veracis visit was on the same day.

203. The Veracis report identifies that the documentation had been supplied in Spanish and Veracis had relied on interpretation by Online, third party payments are occasionally made and the trade is in commodities associated with MTIC trading. There was no storage for wholesale quantities of mobile phones. They saw a Dunn and Bradstreet credit report which showed details of the accounts to 31 December 2004 and indicated that at that stage it was low risk.

204. The Credit Safe report gives a credit limit for Online of 153,258.09 Euros (approximately £100,000 at the then exchange rate). The supplies made by Balmoral were £10,848,500. The business activity is stated to be wholesale of office equipment. Turnover in each of 2003 and 2004 (the only available data) was less than the value of these deals. No banker or auditor information was provided. The trading address in the report is not the address on the purchase order or the Veracis report but it is the address used by Balmoral. The name of the Director is given as Ramesh Arnani not Karnani.

205. There does not appear to have been any VAT registration check nor were trade references or trade applications provided.

VAT number checks

206. As can be seen VAT registrations were not always checked, such as for SGA and Online. Further it is odd that Mr Kelly should say that the checks would be on the "website", presumably Europa, when he had been repeatedly told to check with Redhill.

Freight Forwarders, IMEI numbers, inspection and insurance

207. Apart from his witness statement the only evidence about this is derived from the 2006 interview. It was less than detailed. On being asked if Balmoral had any agreements or contracts with freight forwarders he said that was down to the latter but nothing has been produced. He had no stock control mechanisms in place and no agreements with any transport companies. He did not know if the freight forwarders would be members of trade associations.

208. There is no dispute that there were no IMEI numbers collated in respect of the deals with which we are concerned.

209. Mr Kelly stated in the 2006 interview that he did not check if an inspection check had been done. He did suggest that the freight forwarders did inspections and he received any inspection check by fax "after goods have gone". He did not know if there were customs stamps on the boxes and the only purpose of inspection was to ensure the goods existed, which is consistent with his witness statement. He received no quality report unless the goods were damaged. He denied being charged by the freight forwarders for administrative costs. There is nothing in the documentation suggesting that any inspections were instructed.

210. The position in regard to insurance is less than clear. At the 2006 interview Mr Kelly stated that the freight forwarder pays to insure goods in transit and when asked who insures the goods whilst in storage Mr Kelly stated "at the far side paid by customer" but was unable to give the names of insurers.

211. The bigger problem with insurance is that Online's Purchase Orders stipulated that the price was CIF. That means "Cost, Insurance, Freight" whereby the seller must arrange and pay for both freight and insurance.

212. HMRC did interview the freight forwarder who stated that he covered the goods in the warehouse (in the UK) but insurance in transit and therefore whilst shipped on hold is up to the haulier to organise with the client. Mr Kelly was very clear in the 2006 interview that he had no contact with hauliers. We note that below the details of the consignee on the Ship on Hold and Allocation fax (not the shipping instruction fax) from Balmoral to the freight forwarders there are the words "Insurance: yes" but there is no explanation of that.

213. We note that the Veracis due diligence in relation to Phone City (the deals for Solutions in 03/06) makes it clear that although freight forwarders inspected the goods (no IMEI numbers), no insurance was arranged. Similarly, for SGA, Veracis state that there is no separate insurance policy.

Invoices and receipts and terms of business

214. Most contact with suppliers and customers was by telephone. Some of those had web sites and email and generally they had a fax.

215. Mr Kelly stated at the 2006 interview that there was no retention of title clause and the only terms of sale were that the goods were delivered to the freight warehouse. His solicitor advised that there were no written contracts with suppliers or customers although the employee who was present said that applications to trade with suppliers had terms and conditions on them.

216. That does not sit well with the purported "Purchase Agreements" produced as part of the deal packs. Those contain a provision that: "If Balmoral Solutions Limited cannot fulfil the order due to End Customer Default then the supplier MUST return the purchase amount to Balmoral Solutions Limited".

Deal Documentation generally and findings thereon

217. The deal documentation is very sparse and contains a number of anomalies.

218. As we indicate above, all the sales in deals 2 and 3 were described on the purchase order, pro forma invoice and sales invoice as "Europe Spec" or "Eurospec". However the goods in question are the N8801 which are suitable for use in North America. That makes no sense.

219. The "Purchase Agreements" produced in the deal documentation can only be described as bizarre. The wording quoted in paragraph 216 above is simply not what one would expect to find in an arm's length commercial deal. If Balmoral's customer backs out why would the supplier agree to refund the purchase price? That makes no sense unless the supplier and Balmoral are part of a contrived fraud.

220. In any event on the second page the documentation appears to be with Solutions not Balmoral and if that is the case then because it is dated 31 May 2006, it is after the event for Solution's deals in April 2006. It is certainly not signed for or on behalf of Balmoral.

221. We find the documentation in relation to Online to be odd. As we indicate, in the faxes to the freight forwarder, the address used by Balmoral is the address in the credit report. It is not the address used on the purchase order and the Veracis report makes it clear that that address is the registered office and it had not been used as a trading address since 2002. Further, the headed paper on the purchase order from Online does not even spell the name of Online correctly. We find that a prudent trader should have been concerned that the credit report identified Online as trading in a different sector and identified a different trading address from that on the headed paper and of course the spelling error is not professional.

222. All three of International's invoices were faxed to Balmoral on 8 June 2006 at 12:30 and indicate that nothing had been paid, yet payment was made on 31 May 2006.

223. The documentation in regard to freight forwarders, shipping, insurance etc is scanty at best. The only evidence of actual shipping are the CMRs and one Eurotunnel ticket. That ticket was in the documentation for deal 3 but has the registration number for the vehicle in deal 1. There is nothing for deals 2 and 3. The CMR for deal 1

purports to be signed by the recipient but the CMR for deals 2 and 3 (which appear to have been transported together) is not signed. Neither CMR has the details one would expect as to the weight or the trailer or seal numbers.

224. The address for Balmoral is given as being care of the freight forwarder but at its registered office not the location of the goods. The location of the goods is just stated as being "Feltham". The address on the CMR for delivery to the consignee in Holland is incorrect with Online being described as being care of the freight forwarder but the full name of that company is not given. The postcode utilised is not that given by either Online or Balmoral and does not match that on the stamp used by the freight forwarder itself which seems to be a different address.

225. Notwithstanding the very high value of the goods traded, the documentation appears to us to be generally lacking in any semblance of commercial reality. There is an almost complete lack of any salient information. The Purchase Orders from Online contain the greatest detail, albeit not even for the European phones do they state European Specification. They at least stipulate that the phones should be in sealed master cartons, original stock and never locked, silver colour and SIM Free. By contrast Balmoral's Purchase Orders to International and invoice to Online simply state the number, colour and that they are SIM Free Euro Spec.

226. The information in the invoices about the goods is minimal and, in deals 2 and 3, incorrect, there is no information about title to the goods, or timing of delivery. More importantly, there is no information about the detail of the specification such as language, there is nothing about the manuals, software, accessories, chargers etc. None of that information is in any of the invoices for any of the parties. The only identified trading term for Balmoral is "Payment Terms Due Immediatley (*Sic)*" on Balmoral's invoice but, of course the goods had already been released.

227. There is nothing on International's invoice. The three so called "Purchase Agreements" with International, even if it could be inferred that they relate to Balmoral are not commercial for the reasons we state above. They appear to have been produced as a smokescreen for HMRC and nor can they have been of any value for Solutions since they post-dated its transactions.

228. Online's Purchase Orders ask for delivery to Holland but stipulate no timescale. As we indicate above they do stipulate freight and insurance but there is no evidence that they sought confirmation of insurance…they just asked for the CMR to be faxed to them. That is not what would be expected in an arm's length transaction.

229. In summary we find that the documentation in the deal packs and generally is seriously deficient and decidedly superficial. It is completely inadequate in the general commercial world but is particularly valueless in a market rife with fraud. If Balmoral had been an innocent trader, it would have been hideously exposed to risk. As Judge Demack pointed out in 2005, Balmoral had paid no heed to the warnings and had not changed its commercial practices. That does not appear to have changed. It appears to have ignored the circumstances in which its transactions took place and at very best turned a "blind eye".

Conclusion

230. We have set out the evidence in comprehensive detail since we had no real indication as to any argument that might have been run by or for the appellant. In their Skeleton Argument, HMRC argue that Balmoral's case rests on Mr Kelly's credibility which is in part correct but, given the lack of representation and evidence, we have considered other possible arguments advanced in MTIC cases such as whether there were a succession of coincidences or whether Balmoral was an innocent dupe.

231. Before we rehearse our findings in regard to HMRC's evidence it is appropriate to comment on Mr Kelly's evidence since it is germane.

Mr Kelly's evidence

232. Mr Kelly's first witness statement dated 22 July 2009 is decidedly misleading as it states at paragraph one that "the company has been registered for VAT purposes since 22 March 2005 …. The company trades as IT consultants and supplies mobile telephones by wholesale." In point of fact, in the period between the second VAT registration on 6 February 2004 and 22 March 2005 Balmoral had submitted nine monthly returns showing almost £44 million worth of sales and the period 08/04 was the subject matter of the 2008 appeal. Further he omits to mention the trading during the first VAT registration.

233. There is no evidence that Balmoral has ever made supplies of IT Consultancy.

234. In paragraph two he states that he has been involved in "such businesses for over 20 years" but no wholesale activities had ever been declared to HMRC. It was only on investigation of VAT returns that that became apparent. Further, as we indicate above his experience in mobile phones started only in 1995.

235. It was entirely inaccurate to state as he did at paragraph two that there had been "no undue problems" with VAT over a period of 20 years as we indicate above. Two unsuccessful litigations seem to be a reasonably substantive problem.

236. In paragraph three he states that Balmoral generally purchases goods from within the EU. However, from the date of second registration for VAT until period 03/06 a total of 23 returns were submitted declaring total acquisitions from the EC as nil.

237. In paragraphs four and five he states:

> "Most of the businesses with which we have traded have been known to us for many years or else due diligence checks have been undertaken
>
> We have, where appropriate undertaken due diligence using a firm called 'Vericus' (sic), who produced written reports. We have only undertaken transactions on the basis of a positive report."

238. Officer Siddle made most of these points in his second witness statement dated 24 August 2009 and notwithstanding that, Mr Kelly's second witness statement did not clarify matters.

239. Indeed, in Mr Kelly's second witness statement, he stated that he had been in the mobile phone business for 22 or 23 years and that he had "traded" Five Star Communications since the "early 1990's". That is not consistent.

240. We comment in greater detail on the actual process and due diligence for the deals elsewhere but the key finding in relation to Mr Kelly's witness statements is that even although his witness statements can only be described as minimalist, he has not made fair, full or accurate disclosure because:

(a) In point of fact, International was only incorporated less than eight months before these deals and as the Veracis report makes clear, it only commenced trading in April before these deals in May 2006. Further the deals in April were with Solutions.

(b) The due diligence reports on International and SGA were obtained more than two months after the deals were completed.

(c) In the 2006 interview, in the presence of his solicitor, he said that he used two companies for due diligence, Veracis and ABC and if he got a negative report on the telephone he did not do the deal. As can be seen the Veracis reports on Online, International, Phone City and SGA are, in our view, negative for the reasons we state,

(d) At the 2006 interview he stated that "No checks done on numbers" but they would set up a database in future. They had no records as at the date of interview in September yet his second witness statement states that they were obtained after July 2006. Therefore one of the statements about IMEI numbers is wrong. That is not material in itself for this appeal other than as a matter of credibility.

(e) In his second witness statement he distinguishes in paragraph 21(d) between "an agent" in regard to who was responsible for arranging inspections and in paragraph 21(e) "a freight agent" who would arrange insurance for, and transport of, goods. Yet in the 2006 interview he said that the freight forwarder arranged the inspection and only some insurance, Balmoral did not always pay the cost of insurance and storage and the customer would pay for storage "at the far side". He did not know the identity of the insurers. That is not consistent.

(f) In his second witness statement, his evidence in regard to Mrs Tookey and the fraudulent deals in 2003 is neither consistent with his own earlier accounts, accurate or credible (see paras 139 and 140 above). He patently lied about Mrs Tookey.

Essentially, in the very little that he has said, he is inconsistent and when preparing the second witness statement and when attending the 2006 interview he was professionally advised. We do not find his evidence credible.

241. Whether or not we find Mr Kelly credible is certainly not the primary question. The question is whether or not as controlling mind of the appellant he knew or ought to have known of a connection with fraud.

Was there a tax loss as a result of fraud and if so was there a connection between the appellant's deals and that fraud?

242. The connection between deals and tax losses is a question of fact and is established simply by the tracing of the deals. In this case there is absolutely no doubt that these deals have been traced to tax losses as we indicate at length above. Furthermore, those tax losses undoubtedly result from a contrived arrangement for the fraudulent evasion of VAT. That is indicated very clearly by the FCIB tracing.

243. In summary, the compelling evidence in regard to fraud comes from the witness statements of Officers Mercer and Ellis. They proved conclusively that payments were made in relation to the three transactions and those funds passed in two circular money flows with one circuit being completed in 57 minutes and the second commencing three minutes after the first was completed and that was completed in exactly 18 minutes. The outcome was that West 1 paid the VAT for which it should have accounted to HMRC, to an offshore company, United Traders who then paid Hunzie.

244. HMRC's tracing of the payments by analysing the FCIB bank details, particularly those on its Paris server demonstrated unequivocally that the payment chains were circular, not only in regard to the deals with which we are concerned, but also in regard to the cited example for Solutions. We agree with HMRC that undoubtedly these deals were fraudulent. We agree with HMRC that it is highly improbable that the mastermind organising the transactions will have relied on mere coincidence or some form of manipulation to ensure that the exporting broker actually buys and sells and thus receives and makes payment in a precise fashion to ensure the circularity. The natural inference is that the exporting broker must have known of the fraudulent planning.

245. The use of the same IP address demonstrates that the payments must have been made either by use of the same computer or by computers using the same router, regardless of the fact that several of the companies making payments were ostensibly based in different countries. As can be seen from our findings in regard to the FCIB tracing the timescales involved in these deals are tiny and so that is simply not possible. That makes it even more likely that this was fraud. Accordingly not only do we accept Officer Letherby's conclusion but we find that the evidence that all of the parties in these deals utilised the same IP address, taken with the circularity and timing of the money flows is conclusive evidence that this was a contrived fraud and it was connected with the three deals.

Did Mr Kelly, and therefore Balmoral, know or should he have known that the transactions were connected with fraud?

246. However, the Officers' evidence did not assist us in determining the issue of whether the appellant knew that the transactions were connected with fraud.

247. We do accept that it is more than probable that Mr Kelly did not know the full details of the fraud.

248. The evidence of Officers Stone and Fletcher is generic and did not assist us in determining the issues specific to the appellant.

249. We have dealt with FCIB evidence.

250. Undoubtedly there is no direct evidence as to knowledge and in fact rarely would there be any such direct evidence. It is inevitable that direct evidence of an appellant's knowledge is almost never, if ever going to be available. Nevertheless the combination of individual factors made together can give rise to a clear inference that the appellant had, or ought to have had, knowledge of a connection with fraud. The starting point is knowledge of MTIC fraud.

Knowledge of MTIC fraud

251. We have no hesitation in finding that

(a) Mr Kelly has known about the incidence and extent of MTIC fraud from the outset. Indeed, in his letter of 17 February 2004 he says as much. In fact he must have been painfully aware of it following the fraudulent deals in 2003.

(b) It is plain, indeed we regard the evidence as overwhelming, that before and during the period concerned in the appeal Mr Kelly knew that there was fraud in the wholesale mobile phone industry, and that the fraud involved an importer defaulting on its VAT liability on selling the phones to another UK trader. He also knew that MTIC fraud was fed by the sale of phones in a chain of transactions within the UK and by the export by brokers such as the appellant. He was further aware of the possibility that their purchases could be connected to a fraud committed by a trader who was the appellant's immediate supplier. He had been repeatedly informed that MTIC fraud was widespread and involved very large sums of money.

(c) As Judge Demack made clear, Balmoral was one of the parties in ***R v Federation of Technological Industries***[10] which was an application for Judicial review in the context of VAT fraud.

(d) Given that Balmoral was aware of the serious impact of MTIC fraud it should have been under a duty to mitigate the risk of entering into transactions tainted by such fraud. It could reasonably be expected to conduct commercial checks on its business partners whether suppliers or customers. Indeed the VAT

[10] [2004] STC 1008

Notice 726, section 8 suggests a number of potential checks. That is explicitly not mandatory or comprehensive.

(e) His solicitor had confirmed that he had read Notice 726.

(f) When the Veto letter for Direct was issued on Monday 23 August 2004, and Balmoral had completed the deals with that company on the preceding Tuesday and Friday, Mr Kelly should have been extremely concerned.

(g) The two letters in regard to Security Notices and the 2005 appeal should have made him acutely aware of the issues.

(h) Judge Demack's repetition of the precise requirements in regard to trade in mobile phones should have reminded Mr Kelly very clearly of the risks and what was expected of him.

(i) The letter dated 28 April 2006 in relation to SGA should have made him very wary indeed.

(j) His acknowledged use of the IPT website should have ensured that he would have been very well aware of the risks in the trade sector.

252. As far as UMBS is concerned, we unequivocally accept Officer Clarke's evidence, quoting His Honour Judge Gledhill that it was a fraudster's bank. We do find that Officer Siddle established that Balmoral used the bank and deposited a sum that was only £483.50 less than the £893,187 which it had underpaid International. (That shortfall was identified as long ago as 2011 in Officer Fyfe's witness statement but was not addressed by Mr Kelly.) Whilst funds certainly flowed from Balmoral ultimately to United Traders and it is very close to the amount of the shortfall, we do not consider that HMRC have proved, on the balance of probabilities, that it is the shortfall.

253. However, what is quite clear is that although International was significantly underpaid, as was everyone else in the chain, Online seem to have obtained the goods, title appears to have passed and no one seems to have complained. That makes no commercial sense whatsoever. The clear inference is that the shortfall did not matter because it was a contrived fraud. Further, in the absence of any explanation and having withheld information that an account had been set up, the use of a "fraudsters' bank" based offshore and deeply enmeshed in MTIC fraud on a daily basis is suggestive of a knowledge of fraud on the part of Mr Kelly.

254. We found the evidence of the HMRC Officers compelling in relation to other matters. We bore in mind that in some instances they had relied on the work of others but we were satisfied that there was no basis on which to doubt the evidence before us. We noted that the exhibits annexed to their statements supported the facts put forward and that the evidence of the witnesses accurately reflected the contents of documents such as visit reports and contemporaneous notes of the conversations with the appellant in respect of which there was no contradictory evidence such as would have undermined their evidence.

255. HMRC's case on knowledge is based on drawing inferences from a wide range of facts to establish the position that Mr Kelly must have known of the involvement with fraud. Their alternative case is that he should have done so.

256. HMRC are not required to prove that the appellant knew the identity of any of the other parties in any overall fraudulent scheme.

257. There is nothing before us to show that Balmoral was aware of the actual tax losses when it entered into its transactions which were traced to those losses and we so find.

Circumstances surrounding the deals and other deals to which we were referred

258. We find that Mr Kelly deliberately manipulated the information given to HMRC in regard to registration for VAT for both companies in order to obscure the fact that he was wholesale trading in mobile phones in both companies.

259. Although he stated in the 2006 interview that he separated out the trade in mobile phones between Balmoral and Solutions when the trade in CPUs stopped, in reality Solutions had never really traded in CPUs. Stating that it would trade in CPUs was a device to obtain registration. There is absolutely no explanation as to why Balmoral and Solutions both traded in wholesale mobile phones, with the same suppliers and indeed transacted with each other, other than the explanation in the 2006 interview when he states that he had exports in one company and UK deals in the other so that he could continue to trade while waiting for a VAT repayment. In any event that was not wholly true in that Balmoral did both types of deal and on one occasion Solutions exported.

260. We find that the sole export deal for Solutions in period 03/06 was deliberately engineered on the last day of the period to transform a payment to HMRC of £44,580.42 into a repayment of £5,625.33. Although the documentation was all dated 31 March 2006, the shipment, if any, and payment were not achieved until 5 April 2006. We find that no reasonable businessman, having read the Veracis report would, or should, have taken the risk of purchasing from Phone City given the Veto letter about Callender.

261. The margin achieved in that isolated deal is simply incredible and given the detail set out above, we find that Solutions, through Mr Kelly, should undoubtedly have known that the deal was connected with fraud.

262. When we considered the deals in the period 05/06 and the previous history of Balmoral we find that the background to each deal completed in 05/06 is not dissimilar to the 18 deals completed in period 01/03 where HMRC advised Balmoral of the tax loss in excess of £1.7 million and also the deals in 01/06 where there was a tax loss exceeding £1 million. All of the deals carried out in these periods involved back-to-back wholesale purchase and sale of goods commonly associated with MTIC fraud. Balmoral never took delivery of the goods which were all retained at the freight forwarder rather than the suppliers.

263. There is no cogent explanation as to why one company traded at times whilst the other did not. We find that there was a deliberate strategy to try and mask the trading activities.

264. We find that the information that Mrs Tookey was the Company Secretary was deliberately withheld from HMRC and that there was a deliberate attempt to suggest that she was an ex-employee helping out in an emergency yet she had been made Company Secretary three weeks previously. It is simply incredible that she was appointed Company Secretary of Solutions slightly more than one month later if there were any issues with her conduct from Mr Kelly's perspective. As we indicate above Mr Kelly has patently lied to HMRC in regard to Mrs Tookey.

265. In that regard he had successfully argued through his representatives that it was Mrs Tookey who had let him down and it was she who had "done the deals". He attempted the same argument in regard to these deals stating at the 2006 interview that it was his employees who had done those deals. Whether or not he was involved and, in our view, he was, because he and only he had access to the FCIB bank account through which the payments were processed, he knew or should have known that he was responsible for the actions of his staff. Indeed he stated that he had trained them. The 2003 fraud should have impressed that on him rather powerfully.

266. The trading pattern for Balmoral is very odd. Prior to the period 05/06, from the date of the second VAT registration, a total of 23 VAT returns were submitted and nine of those showed nil or absolutely minimal trading yet other periods such as 09/05 and 11/05 generated comparatively large repayments. The three months prior to 05/06 were nil returns yet 05/06, with only three deals on the last day of the month, generated a repayment claim of in excess of £1.7 million. That is not a credible trading pattern.

267. We find it inherently unlikely that all of the parties would make such an error in description of the Nokia 8801 and even if there was a genuine trade in those phones it would have been important to specify the language package. No party in the deal chains did so.

268. Further, given that Mr Kelly claimed that he was experienced in the mobile phone market, the fact that the Nokia 8801 were not designed for the market into which he was selling should have at least given him pause for thought.

269. There has never been any suggestion that there was a change in the chargers so those phones would never have been for use in Europe. They were also SIM free.

270. On the balance of probability if the freight forwarders had arranged insurance or inspected the goods (beyond ascertaining their physical existence) some evidence would have been produced, particularly in light of the 2005 and 2008 appeals where Judges Demack and Bishopp highlighted the difficulties posed by the lack of evidence produced by Balmoral. Despite numerous requests by HMRC to both Balmoral and Solutions nothing has been produced. Even if direct evidence was not available, we would have expected to have seen bills from the freight forwarders showing the

disbursements for these items. Mr Kelly and his advisers have been in possession of HMRC's evidence in this case for years and nothing has been produced. We infer that there is no evidence. We find that the probability is that, just as in 2004, there were arrangements for neither insurance nor inspections (in the sense of detailed inspections) in place.

271. The almost complete lack of care and attention, not just to minor detail but to basic commercial imperatives such as documentation and insurance and assessment of risk go very, very far beyond any possible naivety and point to either knowledge or means of knowledge of fraud.

272. We find that Mr Kelly had repeatedly been warned by HMRC that making third party payments in this sector was dangerous and viewed as an indicator of fraud. In part, the 2005 appeal had been triggered by third party payments, as also the 2008 appeal. In his second witness statement, he confirmed that he did sometimes make third party payments and alleged that that was not unusual. It seems inherently unlikely that Balmoral had materially changed any of its trading practices over the years.

273. Balmoral purchased directly from West 1 in period 01/06 and therefore it is difficult to understand why it should have dealt with International, with whom it had never dealt (albeit Solutions had done so in the previous month), rather than with West 1. Had it purchased from West 1 it is evident that the price would have been lower. (Incidentally, Solutions also traded with West 1 in 10/05 and HMRC have traced all of those deals back to tax losses.)

274. We were satisfied that the limited due diligence, obtained by Balmoral provided insufficient information from which Balmoral could meaningfully assess the financial viability of its trading partners and was carried out to meet some of the standards set out in Notice 726 rather than for Balmoral to satisfy itself as to the veracity of its customer and supplier. For the reasons set out above, it can be summarised as "too little" and generally "too late" and in our view it too is a smokescreen produced for HMRC rather than for Balmoral's benefit.

275. We find it incomprehensible that a prudent trader, could possibly consider that there had been anything like an appropriate assessment of the potential risk factors, let alone in relation to easily transported goods of such high value. It is particularly noteworthy that no stock was ever seen. It does not suffice to say that in regard to the purchases the stock was at the freight forwarder. The fact that Mr Kelly did not even make any relevant checks about the freight forwarder and saw no need to do so was indicative of just how little Balmoral knew. Its willingness to enter into such high value transactions on the basis of such limited knowledge was indicative, in our view, of Balmoral's knowledge that the deals were contrived. There are many, many other inquiries that a prudent trader, engaged in an arm's length transaction would be expected to have pursued. Balmoral has done exceptionally little.

276. There is much in the factual context which, in our view, should have alerted any prudent businessman to the possibility that there was a likelihood of fraud. In every

export deal cited to us, including those where Balmoral or Solutions were buffers and not brokers, the exporting broker, be it Balmoral or any other company, made substantial profits in transactions that appear to have fallen into their laps, that involved no provision of added value and that involved nothing other than the preparation of fairly poor documentation with no sight of the product whatsoever.

277. Balmoral made a mark-up on the deals which are the subject matter of this appeal of 8.93% and 8.63%. The mark-up for the traders was tiny in comparison. Their mark-ups were 25p per unit whereas Balmoral made £38 and £39.25.

278. Balmoral's profit margins are simply "too good to be true" in the context of the market on that day.

279. We agreed with and had regard to the comments of Judge Bishopp in *Calltel Telecom Ltd v HMRC*[11]*:*

"(52)…it is, we think, possible that a trader could have the means of knowing that, by his participation, he is assisting a fraud. Much will depend on the facts, but an obvious example might be the offer of an easy purchase and sale generating a conspicuously generous profit for no evident reason. A trader receiving such an offer would be well advised to ask why it had been made; if he did not he would be likely to fail the test set out at paragraph 51 of the judgment in Kittel*".*

That is precisely the position in which the appellant found itself yet it proceeded with the deals.

280. We do not accept Mr Kelly's assertion when he responds to "comments from HMRC's witnesses" stating that significant increase in turnover is to be expected and "really significant money could be made quickly". He argued that businesses can achieve high turnover without large staff numbers or big offices. We agree with HMRC that the possibility of this phenomenal "overnight" yet sporadic growth in what purported to be a competitive open market in a situation where there are few employees, no assets and no financial backing seems far too good to be true.

281. At the 2006 interview, Mr Kelly suggested that it was simply "coincidence" that in each period goods were always sourced from the same supplier. We do not accept that, just as we do not accept that it is a coincidence that every deal that HMRC have looked at in detail for both Solutions and Balmoral over a period of three years has been traced to tax losses and defaulting traders. That stretches credulity too far.

282. For the reasons set out above, we reject the implicit submission that Balmoral was an innocent dupe in the scheme and in the absence of any alternative reasonable explanation for the appellant's involvement we were wholly satisfied that the appellant, through Mr Kelly had the knowledge and, at the very least, the means to conclude that its transactions were connected to fraud.

283. For the avoidance of doubt, we confirm that we found that some reasons carried more weight than others and we did not base our decision solely on one reason but

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rather the cumulative effect of our findings viewed in totality. We have specifically weighed in the balance the information which was known, could have been known, should have been known and/or was ignored by Balmoral in May 2006.

284. In our view Balmoral can only have played its role in the middle of these plainly pre-planned transactions if it had known precisely what it was doing. Simply put the only reasonable explanation is that it must have known that it was participating in pre-planned transactions connected to VAT frauds.

285. We did not focus unduly on the issue of due diligence, and we took into account all of the surrounding circumstances in reaching our decision that Balmoral knew that all three of its transactions were part of an artificial scheme.

286. We concluded that the appellant, through Mr Kelly, had actual knowledge that the transactions were connected to fraud and that, by its purchases, it was taking part in transactions connected with the fraudulent evasion of VAT. We were also satisfied that the factors identified above would also support a finding of means of knowledge. It is quite clear that from the date of first registration for VAT Balmoral has ignored every warning given. Judge Demack in 2005 made it absolutely explicit that Balmoral had been given the opportunity to address its commercial practises in order to avoid becoming involved in high risk supply chains in the future. In our view it did not. Accordingly we take the view that the circumstances are so clear that Balmoral must have known of the connection to fraudulent transaction. If that were not so it certainly ought to have so known.

Decision

287. HMRC has proved that the appellant's means of knowledge was such that the transactions fell outside the scope of the right to deduct input tax. Accordingly we found that the decision of HMRC to deny the appellant's input tax was correct and is upheld.

Costs

288. On 12 May 2011, Judge Demack issued clear directions on costs. Rule 29 of the Value Added Tax Tribunal Rules 1986 (Awards and directions as to costs) is applied to these proceedings pursuant to paragraph 7(3)(a) of Schedule 3 to the Transfer of Tribunal Functions and Revenue and Customs Appeals Order 2009 (S.I.2009/56, "the Transitional Provisions"); and Rule 10(1)(c) of the 2009 Rules shall be disapplied to these proceedings, pursuant to paragraph (7)(3)(b) of Schedule 3 to the Transitional Provisions.

289. Accordingly since we see no reason why costs should not follow the event we therefore direct that Balmoral is to pay to HMRC the costs of, incidental to and consequent upon this appeal, to be the subject of detailed assessment if not agreed.

290. 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.

ANNE SCOTT
TRIBUNAL JUDGE

RELEASE DATE: 7 MARCH 2016

APPENDIX 1

Dear Sir/Madam

Missing Trader Intra-Community (MTIC) VAT fraud constitutes one of the most costly current forms of VAT fraud within the EU. It is a serious problem for the UK and is Customs' top VAT fraud priority. As you may be aware I am a Tax Operations Manager with responsibility for this area of work.

Amongst the commodities involved are computer equipment, mobile phones, ancillary items and any other goods. The current estimate of the VAT loss from this type of fraud in the UK alone is between £1.7 and £2.6 billion per annum.

Customs and Excise are still experiencing certain problems with businesses in your trade sector offering commodities regularly involved in Missing Grader Intra Community (MTIC) VAT fraud. As part of our local controls you may previously have been verifying the VAT status of new or potential Customers/Suppliers with your local office.

However, with effect from today's date, verification of the VAT status of new Customers/Suppliers should instead be faxed to **Redhill VAT Office**. However, if you do not have fax facility please contact us by telephone or E-Mail: Marie.Haynesperks@hmce.gsi.gov.uk

The fax numbers at Redhill VAT Office are: 01737 734605 or 01737 734600. The telephone number at Redhill is 01737 734612.

If know, the information provided should include the following:

- The name of the new or potential Customer/Supplier.
- Their VAT registration number.
- Their contact numbers (including telephone number, fax number, e-mail address and mobile numbers if known).
- The Directors and/or responsible members.
- Whether they are buying or selling goods.
- The nature of the goods.
- The quantities of the goods.
- The value of the goods.
- Their bank sort code and account number.
- We would also require you to continue forwarding, on a monthly basis, a purchase and sales listing with the identifying VAT Registration Numbers against the suppliers/customers to Redhill Vat office."

I look forward to your continued assistance in this matter.

Yours

APPENDIX 2

EXCERPTS FROM NOTICE 726

2.3 MTIC fraud is a systematic criminal attack on the VAT system which has been detected in many EU states. In its simplest form the fraud which costs the Exchequer between £1.7 to £2.7 billion in 2001/2002 involves a fraudster obtaining a VAT registration number in the UK for the purposes of purchasing goods free from VAT in another EU Member State, selling them at a VAT inclusive purchase price in the UK and then going missing without paying the output tax due to Customs & Excise.
The fraud relies heavily on the ability of fraudulent businesses to undertake trade in goods with other businesses that may either be complicit in the fraud, turn a blind eye, or are not sufficiently circumspect about their trading connections.

8. <u>Dealing with other businesses – How to ensure the integrity of your supply chain</u>

8.1 Checks you can undertake to help ensure the integrity of your supply chain

The following are examples of checks you may wish to undertake to help establish the integrity of your supply chain.

(1) Undertaking reasonable commercial checks to consider the legitimacy of customers or suppliers. For example:

- What is the supplier's history in the trade?
- Are the normal commercial arrangements in place for the financing of the goods?
- Are the goods adequately insured?
- What recourse is there if the goods are not as described?

(2) Undertaking reasonable checks to ensure the commercial viability of the transaction. For example:

- Is there a market for this type of goods – such as superseded or outdated mobile phone models?
- Is it commercially viable for the price of the goods to increase within the short duration of the supply chain?
- Have normal commercial practices been adopted in negotiating prices?
- Is there a commercial reason for any third party payments?

(1) Undertaking reasonable checks to ensure the goods will be as described by your supplier. For example:

- Do the goods exist?
- Have they been previously supplied to you?

- Are they in good condition and not damaged?

We recommend that sufficient checks be carried out in each of the above categories to ensure that you are not caught in a fraudulent supply chain.

8.2 Checks carried out by existing businesses

The following are examples of specific checks carried out by existing businesses. These may also help you to decide what checks you should carry out, but this list is not exhaustive and you should decide what checks you need to carry out before dealing with a supplier or customer.

- obtain copies of Certificates of Incorporation and VAT registration certificates;
- verify VAT registration details with Customs and Excise;
- obtain letters of introduction on headed paper;
- obtain some form of trade reference, either written or verbal;
- obtain credit checks or other background checks from an independent third party;
- insist on personal contact with a senior officer of the prospective supplier, making an initial visit to their premises whenever possible;
- obtain the prospective supplier's bank details, to check whether:

  (a) payments would be made to a third party; and

  (b) that in the case of import, the supplier and their bank shared the same country of residence.

- check details provided against other sources, eg website, letterheads, BT landline records.

Paperwork in addition to invoices may be received in relation to the supplies you purchase and sell. We believe that this documentation should be kept as evidence of a transaction's legitimacy. The following are examples of additional paperwork that some businesses retain:

- purchase orders;
- pro-forma invoices;
- delivery notes;
- CMRs (Convention Merchandises Routiers) or airway bills;
- Allocation notification;
- Inspection reports.

Again this is not an exhaustive list, but does show some of the more common subsidiary documentation.