TC02679

Appeal number: TC/2008/1164

VALUE ADDED TAX – Denial of input tax recovery as connected with fraud –whether properly denied - On facts No – Appeal allowed

FIRST-TIER TRIBUNAL
TAX CHAMBER

DYNAMIC CORNER LIMITED **Appellant**

-and –

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

TRIBUNAL: JUDGE ADRIAN SHIPWRIGHT
HARVEY ADAMS

Sitting in public at Bedford Square on 20 -21, 24-27 January 2011 and at the Royal Courts of Justice London on 11-5, 18-21 June 2012 and Bedford Square on 16 July 2012

Mark Lucraft QC and Marcus Rickard, Counsel, instructed by iTax UK LLP for the Appellant

Christian Zwart, Counsel, instructed by Howes Percival for the General Counsel and Solicitor to HM Revenue and Customs, for the Respondents

DECISION

Introduction

1. This is an appeal by the Appellant (usually referred to here as "DCL" or "the Taxpayer") against the decision of the Respondents ("HMRC") to deny DCL's claim to deduct £53,151.88 as input tax for the period 11/06. HMRC notified DCL of this decision by letter dated 24 April 2008 ("the Decision Letter"). This input tax related to CD players and concerned essentially one transaction involving two types of DVD player (Clarion and Kenwood DVD players).

2. HMRC denied the input tax claim as "... the input tax was incurred by [DCL] in a transaction connected with the fraudulent evasion of VAT and that [DCL] knew or should have known of this fact" (see the Decision Letter).

The Issue

3. The issue in this case is whether the deduction of input tax was properly denied.

4. This requires a number of questions to be considered including the following:

(a) Have HMRC proved the chain of transactions in question?

(b) Have HMRC proved a tax loss in the chain?

(c) Have HMRC proved the tax loss was caused by fraud?

This is to be done on the civil standard of proof, i.e. the balance of probability.

5. If HMRC have proved the matters set out above the question then arises did the Taxpayer know, or ought the Taxpayer to have known, from the circumstances which surrounded their transaction that they were connected to fraudulent evasion of VAT which was involved in the chain.

6. This requires us to consider whether or not the only reasonable explanation for the transaction in which the Taxpayer was involved was that it was connected to fraud and that if it turns out that the transaction was connected with fraudulent evasion of VAT then the Taxpayer should have known of that fact. In other words should DCL have concluded that the only reasonable explanation for DCL's transaction was that it was connected to fraud?

Structure of Decision

7. The structure of this decision is as follows:

Abbreviations and Dramatis Personae

8. The following abbreviations and references to persons are used in this decision but as ever are subject to the requirements of the context.

"A1 Inspections Limited"	a company incorporated in the UK employed by DCL to provide inspection services
"AFI"	the freight forwarder in France to whose premises the DVD players are accepted by the parties as having been delivered.
"AFI Logistics (UK) Limited"	a company incorporated in the UK which was the freight forwarder involved in the transaction
"Clarions"	300 Clarion VRX 746 VD In Car DVD player AM/FM DVD player LCD panel
"CMR"	a CMR Note in s standard design in a four part NCR under the Convention on the Contract for the Carriage of Goods by Road
"DCL"	Dynamic Corner Limited, the Appellant, a company incorporated in the UK
"Fairbairn"	Fairbairn Private Bank, an Isle of Man Bank
"HMRC"	Her Majesty's Revenue and Customs, the Respondents
"ICICI"	ICICI Bank UK PLC, a wholly owned subsidiary of ICICI Bank Ltd., India
"IMEI"	International Mobile Equipment Identity Number - unique electronic designation for a mobile phone and certain other electronic equipment that can be scanned electronically
"ITP"	IT Players UK Limited, a company incorporated in the UK
"Jafton"	Jafton Limited, a company incorporated in the UK
"Kenwoods"	200 Kenwood DDX 6039 In Car DVD player DVD/ VIDEO/WMA/MP3 receiver
"Lexus"	Lexus Telecom Limited, a company incorporated in the UK
"MTIC"	Missing Trader Intra Community Fraud
"Nordisk"	Nordisk Tradex ApS, a company incorporated in Denmark and carrying on business outside the UK
"PCB2"	PCB2 Limited, a company incorporated in the UK
"SPTL"	Silver Pound LPA, a company incorporated in Portugal
"STL"	STL Synergi-Tec Limited, a company incorporated in the UK
"the Taxpayer"	DCL
"TLS"	TLS UK and TLS LLP and, where appropriate, associated enterprises
"TLS LLP"	Total Logistic Solutions UK LLP
"TLS UK"	Total Logistic Solutions UK Limited
"VAT"	Value Added Tax
"VATA"	Value Added Tax Act 1994
"VIES"	VAT Information Exchange System

Course of the Hearing

9. The hearing was, broadly, in two halves separated by some 17 months or so. This was far from satisfactory.

10. It was occasioned by an officer of HMRC making comments during the "first half" whist giving evidence which related to criminal matters which had not been mentioned before and referring to documents and other evidence which DCL had not seen and which were not before the Tribunal. There was to be a criminal trial to which this evidence were related and involved a considerable number of documents. What to

do about this revelation and the making of relevant checks took time. The usual difficulties of timetabling then meant the hearing could not be resumed immediately.

11. This revelation brought into sharp focus the relationship between the criminal investigation part of HMRC and the rest of HMRC. It maybe that the position should be looked at to see what lessons can be learnt.

12. Various technical evidential and Human Rights Act matters in relation to fairness in particular came into issue especially as regards these documents of which there were a considerable number. The Tribunal not only wishes to treat all parties fairly but is under a statutory duty to provide a fair hearing. It is important that it has relevant documents to do this but the Tribunal Rules provide what is to be done not the CPR or analogies to criminal procedure. All parties interests have to be balanced and the public interest in criminal proceedings borne in mind. It also has to be borne in mind that the onus in an appeal such as this is ultimately on the taxpayer. It is not generally for the State to prove its case in tax proceedings. However, HMRC does have to show certain things in an MTIC case which can put a different slant on matters. However, ultimately it is still for the taxpayer to establish its appeal to succeed. This may be because, for example, HMRC does not show certain gateway matters.

13. In considering all of this we reminded HMRC and DCL and ourselves of Rule 2 of the Tribunal Rules which applies not just to taxpayers but to HMRC equally. It provides:

"(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".

14. Issues also arose as to the availability of documents and how promptly they were produced. In approaching this remind ourselves of two matters:

(a) This is a Tribunal hearing in the Tax Chamber not a court hearing and so is on a different basis of procedure and evidence as the Tribunal Rules apply and not the CPR;

(b) HMRC is a large organisation with many different responsibilities and issues to balance.

15. We fully accept that a Tribunal hearing has to comply with Article 6 of the Human Rights Act. However, we consider that this is achieved by complying with

the Tribunal Rules particularly in the light of Rule 2 set out above. Accordingly, we did not consider some of the arguments put to us on this issue pertinent but nonetheless have sought to take them into account. We consider the Legislature was fully cognisant of the Human Rights Act and other procedural rules when the Tribunal Rules were enacted and considered the Rules compliant with the Human Rights Act and as attaining fairness. We fully accept that and have sought to provide a fair hearing in accordance with the Rules as enacted by the legislation.

16. The obtaining of documents which the parties considered relevant was not an easy process. However, we do not consider that any of the people involved in this were doing anything other than acting properly. Each party is entitled to run its case in the way it wishes. Each party is entitled to make such applications as it thinks fit and proper within the Tribunal Rules. Merely because an application is not acceded to it does not make the application improper. Equally merely because it takes time to obtain documents that of itself does not show impropriety or anything even more serious.

17. The Tribunal was provided with sufficient evidence on which it could make a decision. We are grateful for that.

18. There were also logistical difficulties concerning papers etc. which did not speed up the process. The Tribunal is grateful for the assistance it received in this context.

The Law

Statute

19. The law in this area derives from the VAT Directive. It is currently set out in Title X of the 2006 Directive. At the time of the transaction in question by DCL it was found in Title XI of the Sixth Directive (77/338EEC).

20. The UK statutory provisions are found mainly in sections 24 to 26 VATA and Regulation 29 of the VAT Regulations 1995.

21. Section 24 VATA provides:

"24. (1) Subject to the following provisions of this section, "input tax", in relation to a taxable person, means the following tax, that is to say—

(a) VAT on the supply to him of any goods or services;

(b) VAT on the acquisition by him from another member State of any goods; and

(c) VAT paid or payable by him on the importation of any goods from a place outside the member States, being (in each case) goods or services used or to be used for the purpose of any business carried on or to be carried on by him…

(6) Regulations may provide—

(a) for VAT on the supply of goods or services to a taxable person, VAT on the acquisition of goods by a taxable person from other member States and VAT paid or payable by a taxable person on the importation of goods from places outside the member States to be treated as his input tax only if and to the extent that the charge to VAT is evidenced and quantified by reference to such documents as may be specified in the regulations or the Commissioners may direct either generally or in particular cases or classes of cases;..."

22. Section 25 VATA provides:

"25.(1) A taxable person shall—

(a) in respect of supplies made by him, and

(b) in respect of the acquisition by him from other member States of any goods,

account for and pay VAT by reference to such periods (in this Act referred to as "prescribed accounting periods") at such time and in such manner as may be determined by or under regulations and regulations may make different provision for different circumstances.

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

23. Section 26 VATA provides:

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

24. Regulation 29 of the VAT Regulations 1995 provides:

"29. (1) Subject to paragraph (2) below, and save as the Commissioners may otherwise allow or direct either generally or specially, a person claiming deduction of input tax under section 25(2) of the Act shall do so on a return made by him for the prescribed accounting period in which the VAT became chargeable.

(2) At the time of claiming deduction of input tax in accordance with paragraph (1) above, a person shall, if the claim is in respect of—

(a) a supply from another taxable person, hold the document which is required to be provided under regulation 13;…

provided that where the Commissioners so direct, either generally or in relation to particular cases or classes of cases, a claimant shall hold, instead of the document or invoice (as the case may require) specified in sub-paragraph (a)… above, such other documentary evidence of the charge to VAT as the Commissioners may direct".

Case Law

We were provided with copies of the decisions in a number of cases all of which we have read and carefully considered. These included the following.

(a) *Kittel v Belgium (Case C-439/04) Belgium v Recolta Recycling SPRL* (Case C-440/04) [2006] All ER (D) 69 (Jul)
(b) *HMRC v Moblix Ltd & Others* [2010] EWCA Civ 517
(c) *Optigen/Bondhouse Advocate General's Opinion*
(d) *Blue Sphere Global Ltd v RCC* [2009] EWCH 1150 (Ch)
(e) *Re Doherty* [2008] UKHL 33
(f) *In re B (Children)* [2008] UKHL 35
(g) *R (N) v Mental Health Review Tribunal (Northern Region)* [2005] EWCA Civ 1605, [2006] QB 468
(h) *HMRC v Livewire Telecom Ltd* [2009] EWHC 15 (Ch)
(i) *HMRC v Dempster (t/a Boulevard)* [2008] EWHC 63 (Ch)
(j) *Red 12 v HMRC* [2009] EWHC 2563 (Ch)

(k) *Optigen Ltd (C-354/03), Fulcrum Electronics Ltd (*C-355/03), *Bondhouse Systems Ltd* (C-484/03) *v Commissioners of Customs & Excise*
(l) *Dragon Futures Ltd v HMRC* [2005] UK VAT V19186
(m) *Brayfal v HMRC* [2010] UKFTT 99 (TC)
(n) *Livewire Telecom v HMRC* [2009] STC 643
(o) *Our Communications Ltd v HMRC* VTR 20903
(p) *Emblaze Mobility Solutions Ltd v HMRC* [2010] STC 1436
(q) *Meridian Global Funds Management Asia Ltd v Securities Commission* [1995] 3 All ER 918
(r) *Mobile Export 365 Ltd v HMRC* [2010] UKFTT 367 (TC) at 71-80
(s) *Gillex UK Ltd (In Liquidation) v HMRC* [2010] UKFTT 517 (TC) at 25-27; 37-52; 139
(t) *Masstech Ltd v HMRC* [2010] UKFTT 386 (TC) at 88
(u) *Procomm Ltd* [2010] UKFTT 561 (TC)
(v) *Xentric Ltd v HMRC* [2010] UKFTT 620 (TC) at 178-179
(w) *Megtian Limited v HMRC* [2009] EWHC 18 (Ch)
(x) *Crucial Components Ltd v HMRC UKFTT TCO1532*
(y) *Mehageben ECJ* (21 June 2012) C-80/11 C142-111

Evidence

General

25. Five volumes of agreed documents were produced. The documents were all admitted in evidence, no objection having been taken to any of the documents although certain matters were excluded in the light of the earlier difficulty leading to the split hearing mentioned above.
26. We heard oral evidence from:
    a. Officer Morgan**;**
    b. Officer Mendes;
    c. Officer Varney;
    d. Officer Ndoinjeh;
    e. Officer Sadler;
    f. Officer Wilkinson;
    g. Officer Bishop;
    h. Officer Thorpe; and
    i. Mr M Soni
    j. Mr Hobson
    k. Mr Saleem (via video link)
27. Witness Statements were produced for these witnesses and they were cross-examined.
28. Witness Statements were produced for Officers Stone and Wilkinson but these (in HMRC's words) "… were unquestioned and unchallenged by DCL". We have read them but they did not, in our view, add much but we have taken these into account in reaching our decision.
29. There was also, as had been directed, a list of agreed matters and a list of matters and issues not agreed. These would, of course, be available to any tribunal or court if the matter were to proceed further. These were of considerable use and we are grateful for the time spent in producing them.

30. We record, as we were asked to by DCL, that DCL makes no admission as to alleged fraud. Accordingly, we record this matter here.

Inferences and the evidence adduced by DCL

31. HMRC invited us to draw adverse inferences in respect of Mr Soni's evidence and DCL's decision as to what witnesses to call.

32. HMRC said:

"6. From its range of officers, DCL chose to call evidence from M Soni alone, also calling evidence from Mr Saleem as to pre-2006 events, and its advisor Mr Hobson (after his instruction) as to post-2008 events.

7. HMRC submits that the Tribunal is entitled to draw adverse inferences from the fact of DCL's choice to not call [sic] its other officers, nor S Soni, to give any evidence, and also from the fact that no officer or family member chose to support evidentially the Appellant's appeal.

8. DCL's M Soni was subject to cross-examination. In response to questions, he was hazy on certain dates but appeared by contrast to be certain about other matters. For example, he replied "I don't recall" many times (e.g. Transcript 21 June page 51 line 16, page 76 line 18;page 147 line 13) by contrast with his being certain that contemporaneous letters and conversations were in fact wrong (see Transcript 22 June 2012, page 185, lines 6-25 and page 186 lines 1-8)".

33. We note in this context that we were told that Mr Soni's baby had been taken into hospital during the second hearing.

34. On 17 June 2012 an email was sent from Mr Soni's Advisers. It read:

"Dear Judge, yesterday I was told by Mr Soni that his 8 week old son was taken to hospital and underwent tests for internal bleeding. The family were there until midnight last night and have been asked to return today for further tests. The position is, at present, uncertain but is certainly of great concern to all.

I have passed news of this development to both Counsel for the Appellant and out of courtesy to the Tribunal and all parties it has been suggested that raise we alert the Tribunal to the current position at the earliest opportunity.

Mr Lucraft has suggested that the following take place tomorrow:

- That Mr Soni be allowed to remain with his family and not attend tomorrow given the uncertainty of his son's medical condition. We would anticipate his arrival back to London on Tuesday.
- …

As ever, I am very happy to assist the Tribunal at any time.

Kind regards

Keith Hobson

Partner

iTax UK LLP"

35. The Tribunal replied by email:

"… Whilst not wanting to pre-empt anything, at first blush Mr Lucraft QC's suggestion seems a sensible one to adopt.

If the Respondents do not have any objections I would suggest that we adopt the course of action suggested in the first place. The position can be reviewed after we have heard the evidence by video link.

I am of course happy to receive any representations and suggestions".

36. Phillipa Summerlee replied on behalf of the Respondents:

"… I confirm that the Respondents agree with this approach. .. We echo your hope for a speedy recovery for Mr Soni's son.
Regards"

37. Accordingly, HMRC accepted and certainly did not dispute that Mr Soni's son was unwell. Mr Soni was cross examined whilst this was still the case.

38. We took this into account when evaluating Mr Soni's evidence as well as the fact that he gave his evidence in the Royal Courts of Justice rather than in a more informal tribunal room and that some time had elapsed between the transaction and Mr Soni giving evidence. We also carefully considered his demeanour and had he gave his answers as well as their content.

39. In the circumstances, we did not consider that Mr Soni's evidence is to be treated as different from any other evidence and is to be weighed in the usual way taking all relevant circumstances into account. We have attempted to do this.

40. How an Appellant choses to present its case is for the Appellant. The same is true for any other party. What witnesses to call is generally a matter for the party. We accept that inferences can be drawn where appropriate. However, there must be sufficient groundwork for an inference to be capable of being drawn.

41. The Tribunal has to consider the evidence and decide what weight to give to it. This we have sought to do. This has to be done in the context of who has to prove what. The onus of proof of certain matters in an MTIC case (such as the chain, tax loss in the chain and that the loss was caused by fraud) is on HMRC. It is hard to see how we can draw adverse inferences in this respect from the Taxpayer's choice of witnesses. It is for HMRC to prove these matters by cogent evidence. HMRC can call such witnesses and produce such evidence as it wishes within the Tribunal Rules. How HMRC chooses to present its case is a matter for HMRC, as to how the Taxpayer presents its case is for the Taxpayer. The Tribunal has to consider and weigh the evidence presented.

42. We can see that the evidence when the onus is on the Taxpayer such as the "ought to have known" point may have to be considered in the light of HMRC's submission. However, we consider that this needs to be done in the context of each bit of evidence in a case such as this.

43. We note HMRC's contention. We have borne it in mind in considering all the evidence and what weight is to be given to it.

44. We agree that Mr Soni "…was hazy on certain dates but appeared by contrast to be certain about other matters. For example, he replied "I don't recall" many times". However, this must be judged in the particular context and of all the circumstances which includes the time between the transaction and giving evidence and that his eight week old son was in hospital. We have attempted to do just that.

45. We also note the length of time between the transaction and Mr Soni giving evidence and that Mr Soni was the main actor for DCL in the transaction and the factors mentioned above.

Findings of Fact

46. From the evidence we make the following findings of fact.

Dynamic Corner Limited

47. DCL was incorporated on 25 April 2003.

48. At the time of the transaction in question in November 2006:

a. Mr Billal Soni was the director of DCL; and
b. Mr Mohammed Soni was the company secretary.

49. DCL was registered for VAT from 3 February 2005. It submitted quarterly returns and was a repayment trader.

50. DCL's accountants were Messrs S.A. Chopdat & Co.

DCL's Business

51. DCL's started business in 2003 in local advertising. It then moved into the sale of Orange mobile telephone contracts. In addition, DCL sold "electricity and gas conversions door to door".

52. DCL did not trade between May 2004 and April 2005. Dormant company accounts were filed for that financial year.

53. In 2005 DCL commenced trading mobile telephones by purchasing small quantities from high street retailers. We were told that this methodology is known as "box breaking" and involves taking a phone and contract in the UK, dispensing with the contract and SIM and sending the telephone unit abroad. These telephones were sold to a company called Al Mashriq, based in Dubai.

54. DCL's taxable trade began in the period 11/05. It traded successfully over the period from then until the date of the transaction in question namely 29 November, 2006. It has now ceased trading.

55. There were no denials of input tax recovery to DCL with the exception of the denial which is the subject of this appeal. The repayments were made after verification by HMRC.

56. DCL obtained suppliers and customers using information obtained from designated and specialist websites. DCL's Director also visited trade fairs to make contact with potential suppliers. This was an agreed matter between the parties.

DCL Bank Accounts

57. DCL used Fairbairn in the Isle of Man for the transaction in question. It had normally banked elsewhere.

58. In November 2006 DCL had an account at ICICI. Prior to that it had banked with Barclays. DCL used a bank account with Fairbairn for the transaction which is the subject of the appeal as noted above.

59. We were told by DCL that there were difficulties for companies such as DCL with banks with mobile phones. It seems that because of MTIC fraud, banks were wary of dealing with companies that had connections. We had no direct evidence on this but it rings true. There was a suggestion that HMRC may have "leant on" the banks. There was no evidence to support this. Equally, there was no evidence that DCL was directed to use Fairbairn. We find simply find that Fairbairn was the bank used for the transactions.

60. We do not see the relevance but at HMRC's request we record that Cubic Distribution Limited made wholesale supplies of mobile phones to DCL in the VAT period 11/05. There was a common director of those companies and they used the same places of business.

DCL's Turnover

61. DCL's turnover for the period to 30, April 2006 was in excess of £1.1 million. In the following accounting period (ending 30, April 2007) after the denial of input tax recovery it fell to just over £300,000.

62. It was agreed between the parties that DCL "…declared on its VAT 1 that its intended business activity was 'Sales marketing for mobile phones and energy product canvassing door to door Gas and Electricity'". There was no mention of in car entertainment such as DVD players.

63. DCL had been a repayment trader. In the main the repayments had been made after verification. This included £42,771.29 for 02/06 and £116, 462.54 for 05 /06 which in both cases was the full amount claimed.

Visits

64. The following were agreed matters between the parties on this matter.

[a] "On 13/06/05 there was a preregistration visit made by Officer Sharp and Officer Picket .

[b] During a further interview between Mr. Sohel Soni and Mr. Mohammed Soni and Officer Sharp and Officer Foster on 16/08/05 it was confirmed that the company was supplying businesses with mobile phone contracts.

[] On 09/01/06 Officer Sharp and Officer Webster visited the premises of Mr. Chopdat, the accountant. Mr. Chopdat presented the sales invoices relating to [DCL's] previous business activity.

[d] On 15/11/06 the Appellant was visited by Officer Morgan and Officer Mitchell . The principal individuals present were Mr. Billal Soni, Mr. Mohammed and Mr. Sohel Soni. The interview took place at [the principal place of business] .

[e] During the interview on 15/11/06, Mr. Mohammed Soni was asked why there had been a reduction in trading, as witnessed by the difference in the value of sales declared in VAT return for periods 05/06 (£686,500.00) and 08/06 (£309.00). Mr. Mohammed Soni confirmed that although the Appellant Company had not traded since the end of August, it managed to survive on the profits made on previous wholesale of mobile phones and it had sufficient funds in place to survive for a while longer. Mr. Mohammed Soni stated that the initial funding came from his own savings and his family's and totalled around £50,000.

[f] The Appellant had received Notice 726 prior to the deal in question.

[g] Mr Sohel Soni had used email name "Adam Parr"".

Synergi-Tec Limited

65. STL was incorporated on 4 March 2003.

66. In the period in question (i.e. 2006) Jafton sold goods to STL. There were documents before us to show this.

67. It was agreed that "there is no documentation ... to show that Synergi-Tec purchased the goods sold [i.e. the DVD players in question] as part of the transactions [sic] under appeal from Silver Pound LDA, a Portuguese company".

68. There was no other evidence before us to show such a purchase or who the vendor to Synergi-Tec was. Accordingly, we make no finding as to who the vendor was to STL. There is insufficient evidence before us to see any pattern and so to draw any inferences as to this matter.

69. There was documentation to show that Synergi-Tec made other purchases from UK businesses including from Jafton.

PCB 2

70. There was little information about this company provided to us other than it had submitted an input tax reclaim for over £1.5m for the period 01/03/06 to 31/05/06 (not the period in question here – to 11/06) which had not been allowed.

71. This had not been appealed and the company is now in liquidation.

72. There was nothing to show DCL knew this in November 2006.

ITP

73. Again there was little information about this company provided to us. It had submitted a repayment claim for just over £1m for the period 01/0406 to 30/0606 (again not the period in question here). HMRC disallowed this claim. An appeal was lodged but withdrawn.

74. ITP was deregistered on 1 April 2008 (i.e. after the transactions in question).

75. There was nothing to show DCL knew this in November 2006.

Lexus

76. Lexus made repayment claims of £313,180.45 for the period 01/05/06 to 31/05/06 and £123,025.00 for 01/06/06 to 30/06/06 (neither being the period in question here) both of which were denied.

77. The denials were appealed. The appeal was struck out and the company is in liquidation.

78. There was nothing to show DCL knew this in November 2006.

Nordisk

79. Nordisk Tradex ApS was a company incorporated in Denmark.

80. Nordisk was the purchaser from DCL.

81. Nordisk asked for the goods to be delivered in France. It was agreed that the goods were delivered in France. It was not agreed where the goods were before then.

82. DCL checked with Redhill that Nordisk was registered for VAT outside the UK. Redhill confirmed that it was.

Total Logistics Solutions

83. There were two entities or more entities using the name Total Logistics. These were, in particular, a limited company and a limited liability partnership in the UK. They both operated from the same premises in the UK.

84. TLS UK Ltd was the freight forwarder used in the transaction under consideration. This was a UK incorporated company.

85. Total Logistics Solutions UK Limited:

a) applied for VAT registration on 13th April 2006 and on 10th August 2006;

b) was only registered for VAT on 10th August 2006; and

c) never submitted any VAT returns to HMRC; B1/15/41;

Subsequently, TLS was deregistered as a missing trader as of 7th February 2007. There was nothing to show DCL knew this in November 2006.

86. There was also a TLS presence in Dubai. This seemingly provided logistical services including insurance.

Insurance

87. An issue between the parties was, were the goods actually insured?

88. On analysis it seems that technically they were not insured as the premium had not been renewed by their insurer.

89. Mr M Soni for DCL said in giving evidence that he “didn’t want to transfer money without knowing [TLS Insurance] would receive it, so it wasn’t paid”.

90. We agree with Mr Zwart that “… there is no primary evidence of the particular sum of the premium demanded by the insurer nor that that premium was paid by anyone.” We also agree that, in consequence, payment for a particular premium sum cannot be inferred.

91. Mr M Soni confirmed that he attempted to make the insurance payment by cheque. The first cheque was returned as not being properly signed and the second was never cashed. He said in evidence DCL did not seek to ensure that payment was taken from the second cheque.

92. The premium not having been paid, the insurer would not be at risk in normal circumstances. There was nothing for us to show that DCL's attempt to pay was not genuine. We do not find that this was other than genuine.

Financial risk

93. HMRC asked us to note the absence of financial risk to DCL in the transaction.

94. Mr M Soni said in evidence that DCL "funded the VAT paid to Lexus". He asserted that the financial risk was that Lexus retained title until payment was received. Lexus released the goods conditional upon full payment.

95. We agree with HMRC and find "in fact, DCL aggregated the goods into a single invoice, and was paid a sum on 18th December 2006 and on 16th January 2007 after which it immediately paid Lexus, including with VAT."

96. We find that DCL had itself no funds with which to conclude the transaction of 29th November 2006 in the event that Nordisk had not met its contractual obligations. Despite the financial risk to DCL, and the clear terms from Lexus that DCL held no title in the goods unless and until full payment had and been made to Lexus, on 16th January 2006, DCL was paid by Nordisk and released to it the goods before the event of its having title to them from Lexus. We note that title was not to pass till payment was received.

97. It was confirmed to the Tribunal by Mr Soni that the Appellant considered the commercial risk of its transaction. Mr Soni also confirmed, that despite terms on the Lexus invoice showing that title was retained until payment in full that the Appellant released the goods to its customer before making payment to Lexus. Mr Soni's answer to this was that the goods had already been released by Lexus. However there was no documentary evidence of this produced to us. It does seem to be what happened though. The goods were delivered in France.

98. We do not find that this showed an artificial nature to the transaction or that it must have been connected to the fraudulent evasion of VAT. It could be a commercial risk the parties were prepared to take and we so find.

Due Diligence Real or Sham?

99. We find, in the words of HMRC, DCL undertook the following due diligence. "(1) In respect of Lexus Telecom UK Limited, the immediate supplier to the Appellant, … the supplier's premises were visited by the director, Mr Soni. In addition the Appellant produced photographs of the Lexus building, Redhill verifications of the supplier's VAT registration number, a supplier declaration signed by the supplier which identified it and inspection reports of A1 Inspections Limited. (2) In relation to Nordisk Tradex APS, the customer of the Appellant, the Appellant provided verification requests to Redhill to verify the VAT registration number of the customer."

100. We reject HMRC's suggestion that "the due diligence was in truth a sham process" and that "DCL was simply going through the motions…for the sake of outward appearance to HMRC rather than satisfying itself" as there is nothing before us on which we can make such a finding safely.

101.We consider that DCL did carry out third party checks and/or reports, that its supplier(s) and customer were credible, solvent businesses that would honour their trading commitments or carry out any due diligence on a freight forwarder, Total Logistic Solutions (UK) Limited

102.We do find though that DCL's freight forwarder credit application appears unsigned and without completed content and, despite visiting its own immediate supplier, and having itself visited Slough before, did not visit TLS.

103.Clearly, any information obtained by DCL after the transaction date could not have been taken into account by them in determining whether to enter into the transaction as HMRC said.

104.We find that there was no due diligence done at all on TLS by DCL.

105.[HMRC submits that the goods were not in fact present (see below)].

106.The Statement of Agreed Matters and Issues says:

"Due Diligence

[39] On 25/07/05 HMRC issued a standard letter to the Appellant advising of the procedures necessary regarding verification of the VAT registration status of any new customers or suppliers to be used with HMRC's offices at Redhill.

[40] On 13/01/06 a letter was issued to the Appellant advising that although enquiries were still continuing with aspects of the claim for VAT return 11/05, payment would be released without prejudice to any further action which might be taken.

[41] On 08/02/06 a letter was issued to the Appellant confirming a discussion held with Officer Shah on 09/01/06 reiterating the importance of due diligence checks and the use of Redhill clearance procedures.

[42] The Appellant visited Lexus Telecommunications Limited, Lexus House in mid-2006.....

[44] The Appellant carried out some due diligence on its supplier and customer. The Appellant did the following:

[44.1] Some Redhill checks in respect of the VAT status of the supplier and customer;

[44.2] Collection of company documentation from Nordisk;

[44.3] Mr Soni met with a representative of Nordisk at a trade show in Dubai in 2005."

107.We find that the Appellant carried out reasonable due diligence. It was certainly not perfect but it was not uncommercial. We also find that there was nothing as a consequence that should have alerted DCL not to trade with its supplier and/or customer. It did not show that the only reasonable explanation of the transactions was for fraud.

108.There was of course more that the Appellant could have done. Not everything in the Appendix to Notice 726 was done. However, that is a suggestion in general terms from HMRC of what might be done in the context of joint and several liability. That does not mean it is not relevant but it is not the ultimate test.

Due Diligence - Lexus

109.In 2006 the Director of DCL visited Lexus Telecom Limited. At the visit, the Director met with employees of the company and took a photograph of the premises as is documented.

110.Following telephone contact with the supplier, Lexus provided its company details to the Taxpayer on 14 November 2006.

Due Diligence - Nordisk

111.Nordisk Tradex Aps provided details to the Taxpayer on 26 October 2006, notifying of a change of name and providing company verification details.

Due Diligence - Redhill

112.On 27 November 2006, DCL checked with the VIES service as to whether the proposed supplier and customer were VAT registered.

113.On 27 November 2006, DCL contacted HMRC's Redhill office "in order to verify the supplier and customer 'officially'".

114.On 28 November 2006 (the day before the deal completed) HMRC responded to the Appellant's Redhill verification request confirming that the VAT registration details of the proposed counter-parties were valid.

A1 Inspections

115.On 22 March 2006 the Appellant engaged A1 Inspections Limited ("A1") to carry out inspections services on its behalf.

116.On 29 November 2006, the Appellant instructed A1 to carry out an inspection of the goods at their location at the TLS warehouse. Later that day notification was provided to DCL by Nicholas Haider, Operations Manager, A1 that the inspections had been carried out.

117.DCL had no reason at the time to question this or to think that the inspection had not been properly carried out. DCL were not in a position to question the validity of A1 Inspections at the relevant times. We so find.

Matched Deals

118.The question also arises whether there is anything unusual in a deal being "matched" between buyer and seller.

119.HMRC said there was.

120.We note that in *Red 12 Trading Ltd v HMRC* [2010] EWCA Civ 402, Moses LJ said "....it necessary for the fact-finder to consider each transaction in the supply chain on its own merits and the character of that transaction cannot be altered by earlier or subsequent events. Of course each transaction must be looked upon its merits, but, as the judge observed, it must also be looked at without blinkers and in the context and the background as a whole. …. It is absurd to suggest that each transaction must be considered without regard to the commercial background and context in which it was undertaken. …." We have sought to obey this injunction generally it and in particular in considering this issue.

121.HMRC submitted that the precise matching of goods as between a supplier and DCL and DCL and its own customer is unusual and indicates artificiality.

122.We do not consider that this has been shown on the information before us and the inference is that can properly be drawn from it. We do not find that the transaction showed such artificiality. Accordingly, we do not find that there was such artificiality.

CMR's

123.This matter occupied much time during the hearing.

124.The Commissioners disclosed material from the Operation Vex unused materials

125.Exhibit bag "CMRs" were also disclosed after further inquiry.

126.A1 Inspections was subject to an HMRC seizure on 12th December 2006 of "all the records and computers from [its] warehouse" (where Officer Wilkinson was in charge)

Lexus FBIB Account

127. HMRC said:

a. IT Players had an FCIB Bank Account (as was known to Lexus Telecommunications Limited by reason of its provision of the information on request to Mr Hobson).

b. On 5th September 2006, this Bank was subject to a Dutch finance investigation visit due to money laundering announced in the press on 5th October 2006.

c. Lexus must have known - by reason of IT Player's use of FCIB and the occurrence of the investigation of that Bank - of a risk to it when it transacted with IT Players on 29th November 2006;

128. This was not something that was shown to be known by DCL at the time of the transaction and we so find.

Phone call

129. Much was made by HMRC of the question "Did Officer Varney try to contact S Soni by mobile phone using a number provided for M Soni of the Appellant?" HMRC considered it relevant to the question whether DCL (i.e. Mr M Soni) was uneasy at the conclusion of deal performance after DCL had transferred funds to Lexus after the event of goods release to Nordisk.

130. We readily accept that Officer Varney considered she dialled the number of Mr S Soni's phone at the time of her call.

131. Mr M Soni cannot recall a conversation Officer Varney on 9th February 2007. His evidence was "Neither I nor anyone connected with the company can recall this conversation taking place".

132. It is unfortunate that there is no corroborative evidence here. No phone records etc. were produced. There was no evidence that there was not a misdialling. There is no evidence with whom Officer Varney actually had the conversation.

133. We find that Officer Varney sought to contact Mr Soni. We do not have sufficient evidence before us to make the findings and the inferences HMRC seek and we do not do so.

134. We decline to draw the inferences HMRC invited us to draw. We find that Officer Varney considered she dialled the number of Mr M Soni's phone at the time of her call. However, there is no sound evidence on which the premises and inferences HMRC seek to draw from which we could do so. Accordingly, we do not draw the inferences sought.

135. We find that Officer Varney tried to contact Mr S Soni by mobile phone using a number she considered was the one provided for Mr Soni. We do so on the balance of probabilities having weighed this matter very carefully particularly in the light of the importance HMRC attached to it.

Inferences

136. HMRC asked us to draw a number of inferences. These included the following:

(a) STL was the EU acquirer;

(b) SPTL the supplied STL but STL did not pay VAT by reason of fraud;

(c) The goods allocation gives the inference of artificiality;

(d) STL was "… Part of a deliberately contrived scheme in ... which [STL] intentionally failed to account for the VAT due… Not under ordinary commercial conditions, but were artificially contrived is of a scheme to defraud [HMRC]" .

(e) "By reason of DCL's purchase of the goods from Lexus Telecommunications on 29th November, and on its own subsequent dispatch of the goods to the EU mainland, DCL was connected with fraudulent evasion of VAT".

(f) The due diligence was a sham.

137.Drawing inferences is less difficult where there is a pattern of trading in particular goods. Where something has happened a number of times in the same way in a number of chains it provides a basis to infer that something happened again on the basis that it probably happened in the same way.

138.However, here there is only one chain involving goods that DCL had not dealt in before and no real evidence of any pattern. In this case it is hard to see a pattern in respect of goods not dealt in before and any evidence before us from which any inferences can be made.

139.We now turn to consider each of the inferences HMRC contends should be made.

140.We also note in this context that DCL had not had any input tax recovery denied when dealing with mobile phones.

141.HMRC considered the transaction and can be said to be "back to back".

142.We consider that this is correct in the sense of the transaction train being lined up for completion in the same way as happens with residential property. We so find.

143.The Mr M Soni for the Appellant states in his second witness statement that "in my experience, back to back deals are normal in the electronic goods trading sector, and so I do not see anything wrong with the transaction structure". This was confirmed by Mr Soni during cross examination (Transcript 22 June page 41 lines 1 - 5). At §18 he states that "This transaction took place on 29th November 2006".

144.HMRC he said "DCL's VAT 100 records the transaction date as 29th November 2006. Placing to one side their fax provenance, the transaction documents record the deal chain supply transaction occurring by reference to the single date: 29th November 2006 .There is a difference between the deal chain being set up over a number of days as opposed to the contract and its terms being concluded on a single day. Here, the documents show the latter. In *Mobilx* §111, the Court of Appeal approved the approach in *Red 12* [2009] EWHC 2563 that the "surrounding circumstances" are required to be taken into account by the Tribunal. Here, the Transaction date coincides with the date of 29th November 2006 that the faxes sent to IT Players on 15th November 2006 (see above) had pre-determined was the deal date. Whilst M Soni indicated in cross examination that the suddenness of the date was due to currency fluctuation, there is no evidence of telephone calls or emails with Nordisk showing that was a reason for that date and not another date. Rather, the precise matching of 'goods' to a customer's Purchase Order request by a supplier – Lexus- indicates pre-determination of 29th November 2006.

145.We accept that the transactions took place on the on 29 November, 2006 and so find. We find that it was preordained in the sense that being the dates that was agreed.

146.There was no evidence before us to show anything adverse in that or for us to draw any adverse inferences. We do not find anything adverse here or draw any adverse inferences.

The Chain

Introduction

147. This case is unusual in our experience in that:
(a) only one chain is involved; and
(b) it concerns DVD players for cars rather than mobile phones or CPU's.
148. For ease of understanding we set out an outline of our understanding of the chain and then a more detailed consideration of it. We have also included for convenience at the end of this section the agreed matters in respect of the chain.

The Chain in Outline

Introductory

149. The chain insofar as there is evidence starts with STL and ends would Nordisk. There is no evidence before us which shows what happened before STL or after Nordisk.
150. The chain insofar as it has been traced involves five transactions. These are as follows.
(a) STL sells to PCB 2 ;
(b) PCB 2 sells to ITP;
(c) ITP sells the Lexus;
(d) Lexus sells to DCL;
(e) DCL sells to Nordisk.
151. We have no firm evidence before us as to who supplied STL. We are asked to infer that STL acquired the goods from SPTL.
152. We have no firm evidence before us as to what Nordisk did with the goods.
153. It is common ground that the goods are to be treated as having left the UK and arrived in France.
154. There is evidence from Nordisk in Box 17 of the relevant CMRs that the goods were delivered in France.
155. The goods, until they were sent to France, and shipped on hold, were said to be held at TLS, a freight forwarder. [This has been a matter of some dispute as to precisely where the goods were. On the information before us it is hard to conclude that DCL knew or ought to have known that the goods were elsewhere than at TLS. A1 had reported on their inspection of the goods seemingly there. At the time there was nothing to indicate otherwise to DCL and we so find. We make no finding as to where the goods actually were before they left for France but find that DCL had no reason to consider that they were not act at TSL at the times in question.

STL sells to PCB 2

156. The goods in question were Clarion and Kenwood DVD players.
157. PCB 2 sent a Purchase Order dated 29 November 2006 to STL for Clarions. This required the accompanying Supplier Declaration to be returned before the order players could be processed.
158. The Purchase Order said "Stock Held at Total Logistics UK Limited".
159. PCB 2 sent a Purchase Order for Kenwood's to STL also dated 29 November, 2006. This was in the same form as the Purchase Order for Clarions.
160. STL sent a Supplier Declaration to PCB 2 dated 29 November, 2006. This confirms (inter alia) that the goods existed and have been inspected by PCB 2's agents/or freight forwarders and that PCB 2 had no reasonable grounds to suspect that VAT had not or would not be paid . It also confirmed STL was making no third party payments.

PCB 2 sells to ITP

161.PCB 2 sent a stock offer to ITP for Clarions dated 29 November, 2006.
162.ITP sent an order to PCB to which was "… Subject to the Company's a standard terms of trading". We understand the Company to be ITP. Disputes were to be resolved under English law.
163.The document said that "the accompanying Supplier Declaration MUST be signed and returned to ITPUK before the order can be processed".
164.PCB 2 sent a pro forma invoice dated 29 November, 2006. This said (inter alia) "This Pro Forma Invoice when signed and stamped constitutes a legal and binding contract between both parties".
165.The Delivery Date was "TBC".
166.PCB 2 sent ITP a Suppliers Declaration in respect of the Clarions. This was similar to the one received by PCB 2 from STL.
167.ITP sent PCB 2 a Customer Declaration dated 29 November, 2006 confirming (inter alia) that the Clarions had been allocated to ITP by PCB 2. This was stamped with a TLS stamp. This seems to have been faxed back TLS on 30 November 2006 at 12.33 from the indications on the header.
168.PCB 2 sent an Allocation Note in respect of the Clarions to TLS dated 29 November, 2006.
169.PCB 2 sent a release note to TLS dated 30 November, 2006. This requested TLS to release the goods to PCB 2. This said "release" not "ship on hold".
170.There was similar documentation between PCB 2 and ITP in respect of the Kenwoods.

ITP sells the Lexus

171.ITP sent a stock offer to Lexus in respect of the Clarions dated 29 November, 2006.
172.Lexus faxed an order for the Clarions to ITP on 29 November, 2006.
173.ITP provided Lexus with a pro forma invoice dated 29 November, 2006. This said (inter alia)? 2/451
174.Lexus was provided with a supplier declaration by ITP in respect of the Clarions dated 29 November, 2006.
175.Lexis provided ITP with a customer declaration dated 29 November 2006.
176.ITP sent an allocation Note to TLS dated 29 November, 2006. This read "on behalf of ITPUK I request you to allocate ownership on the whole basis of the following goods currently in your possession to…" Lexus. The goods were the Clarions.
177.This was stamped with a TLS stamp and faxed back at 12.33 on 30 November, 2006.
178.ITP sent a release note to TLS dated 10 January, 2007. This requested TLS to release the Clarions to Lexus.
179.There were similar documentation between ITP and lexis in respect of the Kenwoods. The Release Note to TLS for the Kenwoods though was dated 31 January, 2007.

Lexus sells to DCL

180.There was not much documentation before us covering this stage.
181.DCL sent a Purchase Order dated 29 November, 2006 to Lexus.
182.DCL sent a Sales Order dated 29 November, 2006 for Clarions to Lexus. The top left hand corner marking suggested this was faxed at 09:56 on 30 November, 2006.

183. The document stated "All good to remain the property of Lexus Telecoms Ltd till paid in full". In also said "Goods to be released from TLS".

184. There was also an invoice of the same date for the same goods. It had the same provisions as to property etc. as the sales order.

185. There was a similar Sales Order and Invoice for Kenwoods.

186. There were faxes from Fairbairn and confirming instructions to pay Lexus and payment made dated 19.11.06 and 17.1.07.

DCL sells to Nordisk

187. Again there was not much documentation before us covering this stage.

188. Nordisk sent DCL a purchase order for Clarions and Kenwoods which said "Purchase Order date 29-11-2006".

189. There was a nine figure against the heading "VAT number".

190. TLS invoiced DCL on 1/12/2006 for road freight and inspection for Kenwoods. This provided that the consignee was Nordisk Tradex. TLS invoiced in similar form for Clarions on 12/12/2006.

191. They were Marine Cargo Insurance Service Invoices from TLS in the UAE.

192. It was common ground that the goods had been delivered in France.

193. The Fairbairn bank statement showed transfers received from "Capital Conservator" and to Lexus.

194. *Agreed Matters in respect of the Deals*

195. The following matters were agreed between the parties in respect of the deals and were set out in the list of agreed matters in issues. For convenience we set them out here.

> "[25] The deal in question took place during VAT accounting period 01/09/06-30/11/06. On 29 November, 2011 the appellant purchased 300 Clarion VRX 746 VD In Car DVD player AM/FM DVD player LCD panel and 200 Kenwood DDX 6039 In Car DVD player DVD/ VIDEO/WMA/MP3 receiver from Lexus Telecom Limited and sold the goods to Nordic Tradex ApS.
>
> [26] The Appellant's purchases orders and sales invoices are dated on the same day as where its customers and suppliers. The purchases and sales were in the same quantities.
>
> [27] The Appellant chose Total Logistics Solutions UK Ltd. ("Total Logistics"),… of… Slough to act as their freight forwarder. Total Logistics Solutions UK Ltd. was registered for VAT on 10/08/06 and was deregistered six months later with effect from 07/02/07.
>
> [28] The goods were sent to the customer as "ship on hold".
>
> [29] No written contract existed between the appellant and or supplier Lexus telecom limited or their customer Nordiques Tradex ApS and Denmark other than in the terms on invoices or supplier tax declarations.
>
> [30] The Appellant did not take physical possession of the goods.
>
> [31] The Appellant asked Total Logistics to insure the goods on its behalf.
>
> [32] Total Logistics did not cash any cheque sent by the Appellant in relation to this deal.
>
> [33] The Appellant asked Total Logistics to send the completed CMR. Total Logistics did not send the Appellant the completed CMR for this deal. At the time of the request it had been uplifted by HMRC in December 2006.
>
> [34] Payment was made for the goods as follows:

[34.1] Item –Clarion car DVD –the customer, Nordisk Tradex ApS, paid Dynamic Corner Limited in full on 18/12/06 and one day later on 19/12/06 Dynamic Corner Limited paid the supplier, Lexus Telecom Limited in full.

[34.2] Item – Kenwoods car DVD – the customer, Nordisk Tradex ApS paid Dynamic Corner Limited in full on 16/01/07 and one day later on 17/01/07 Dynamic Corner Limited paid the supplier, Lexus Telecom Limited in full

[35] Mr. Chopdat, the Accountant acting on behalf of the appellant wrote to HMRC on 14/12/07 regarding payment for the deal.

[36] Serial numbers would not recorded.

[37] Inspection of the goods was carried out on the consignments by A1 Inspections of Greenford Middlesex at the freight forwarders premises. Prior deals had been inspected by the Appellant itself.

[38] The Appellant's invoices relating to this deal are the only deal in this tax period".

Submissions of the Parties

The Taxpayer`s submissions in outline

196.In essence, DCL argued that it was not concerned in a fraudulent transaction or one which it ought to have known was connected to fraud. Accordingly, the denial of input tax was not properly made.

197.DCL submitted that on the basis of *Mobilx* for the denial of input tax to be proper the Tribunal must be satisfied that in the light of the factual circumstances and on the basis of cogent evidence, that at the time DCL entered its deal it either knew that there was a connection between those transactions and the fraud or that the only reasonable explanation for the transactions in question was that they were connected with fraud. The threshold is a high one and deliberately set by the Court of Appeal, if input tax recovery is to be denied. HMRC have not met this.

198.Further this does not even need to be considered because HMRC have not established that the goods which are the subject of this appeal are connected to a tax loss. HMRC seek to rely on the drawing of an inference that STL (the alleged defaulter) was the acquirer of these goods. The Appellants submit that this is not a safe inference for this Tribunal to make in this case on this vital issue.

199.It was contended that the UK trading evidence of STL that is, 4 invoices from Jafton Limited, balances and therefore neutralizes the acquisition evidence offered by HMRC as the basis for the drawing of an inference that these goods were acquired from Silver Pound.

200.It is contended that since HMRC have the burden of providing that these goods were the subject of a tax loss and, despite having the benefit of unlimited resources and time (in excess of four years has passed since the transaction) HMRC have not been able to identify any evidence to link these goods to an acquisition leading to a failure to account for output tax other than to contend for the drawing of an inference based on the weakest of evidence.

201.Further, HMRC have failed to identify any features of this transaction which were known to DCL at the time which were capable of informing it in any way at all of the likelihood of an alleged fraud taking place or likely to take place.

202.HMRC have failed to demonstrate that DCL decided to participate in any transaction connected with fraud, nor have HMRC demonstrated that, at the time of

entering into the transaction in question DCL was making an informed choice to do so. In short, HMRC have not begun to establish that DCL was by its purchase directly and knowingly involved in the fraudulent evasion of VAT.

203. For these reasons, DCL invited the Tribunal to conclude that HMRC are unable to discharge the burden of proof and satisfy the high test that must be met and to allow repayment to DCL of the input tax it paid to its suppliers in VAT Accounting Periods 11/06.

204. Even if the Tribunal considers that HMRC had shown a tax loss caused by fraud in the chain the Tribunal could not conclude that the only reasonable explanation for the transaction was fraud on the evidence before it.

205. Accordingly the appeal must be allowed.

HMRC`s submissions in outline

General

206. In essence HMRC argued that the evidence showed that the transaction was connected with the fraudulent evasion of VAT which DCL knew or ought to have known. In broad terms, HMRC argued that the input tax recovery was properly denied. This was because "… the input tax was incurred by the Appellant in a transaction connected with fraudulent evasion of VAT and the Appellant knew or should have known of this fact".

207. In more detail HMRC argued:

(1) The chain could be traced back to a defaulting trader STL;

(2) Accordingly there was a tax loss in the chain courts by fraud as STL had not accounted for its VAT;

(3) DCL knew or should have known of the risks of MTIC fraud generally and as regards its own business;

(4) HMRC were entitled to expect "… the Appellant to take every precaution which could reasonably be required of it to ensure that its transactions were not connected with fraud. This high standard means that the Appellant is under a positive duty to take precautions, which includes carrying out due diligence to check on suppliers and customers where the indicators of risk were presented to it";

(5) DCL did not meet the standard in what it did and failed to do;

(6) DCL did nothing to confirm by third party checks and/or reports that its supplier and customer were credible, solvent businesses able to meet their trading commitments and failed to carry out due diligence on its freight forwarder;

(7) The transactions were on a Back-to-Back basis and left DCL with no stock;

(8) Although the customer is located in Denmark the goods were delivered to France;

(9) The Appellant did not retain the serial numbers of the goods or carry out IMEI checks or their equivalent;

(10) DCL was not required to pay its supplier until it had been paid in full by its paying customer;

(11) DCL said the goods were insured from the time they were held in the UK freight forwarders until delivered to the final destination. As the premium was not made this cannot be the case;

(12) On the basis of this and all the other relevant circumstances the Tribunal must be satisfied on the civil burden of proof that the transaction formed part of a transaction chain which was connected with the fraudulent evasion of VAT and the Appellant knew or should have known of this.

208. Accordingly, the appeal should be dismissed.

Discussion

Introduction

209. We set out at the beginning of this decision what we considered to be the issue and some of the question to be considered in deciding the issue. These questions included:

(a) Have HMRC proved the chain of transactions in question?

(b) Have HMRC proved a tax loss in the chain?

(c) Have HMRC proved the tax loss was caused by fraud?

210. If these matters are shown by HMRC then the question of "ought to have known" arises. This is a matter where the onus is on the Taxpayer. We consider that the relevant question here is "whether [DCL] should have known that the only reasonable explanation for the circumstances in which his transaction took place was that it was connected to fraudulent evasion of VAT"?

211. However, in considering these matters it is important to bear the decisions of the higher courts in mind. Accordingly, we will consider this first and then consider the questions set out above.

Case Law

212. We have found the Court of Appeal decision in *Mobilx Ltd (in Administration) v HMRC* [2010] EWCA Civ 517 most useful in our consideration of this appeal. We have sought to keep in the forefront of our minds in reaching our decision.

213. The main judgement was given by Moses LJ (with whom Carnwath LJ and Sir John Chadwick agreed). References to paragraphs of *Mobilx* are to paragraphs of his judgement. We gratefully adopt it.

214. Some helpful comments on the right to deduct are found at paragraphs 25 - 28 where it is said:

"[25] The principle of legal certainty requires that the application of Community legislation is foreseeable by those subject to it (see, egg, the Advocate General's opinion in *Optigen*, para 42). The principle demands that when a taxable person enters into a transaction he should know that the transaction is within the scope of VAT and that his liability will be limited to the amount by which the output tax on his supply exceeds the input tax he has paid. In *Optigen* the court set out the criteria which identify the scope of VAT (see paras 38 – 41). It emphasised the importance of the objective nature of those criteria (paras 44 – 46). Once a transaction meets those criteria, it follows that the right to deduct for which art 17 provides must be recognised (paras 52-53).

[26] The right to deduct input tax is integral to the system of VAT. It may not "in principle" be limited (para 53). It is integral to the system because it ensures the principle of fiscal neutrality which lies at the heart of the system of VAT.

[27] It is necessary to recall the importance of that principle since it explains why the jurisprudence of the ECJ has been so resistant to attempts to combat fraud by encroaching upon the right to deduct in the case of traders who are not themselves participants in the fraud.

[28] Since the right to deduct is fundamental to the system of VAT because it ensures that the charge is limited to the value added at each stage of the supply and because it ensures fiscal neutrality, it may not, in principle, be limited; any derogation from the principle of the right to deduct tax must be interpreted strictly (see Case C-414/07

Magoora [2008] ECR I-000). Moreover, the right must be exercisable immediately in respect of all taxes charged on input transactions. Since the right arises immediately the taxable person pays tax (input tax) to his supplier, the principle of legal certainty demands that he knows when he enters into the transaction that it is within the scope of the tax and that his liability will be limited to the amount by which any output tax he may be liable to pay, on making a supply, exceeds the input tax he has paid. The objective criteria determine both the scope of the tax and the circumstances in which the right to deduct arises".

215.Help is also provided as to the ECJ decision in *Kittel*. It was said of *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".

216.We note in particular paragraph 75 on the issue of "ought to have known" where it is said:

"[75] The ultimate question is not whether the trader exercised due diligence but rather *whether he should have known that the only reasonable explanation for the circumstances in which his transaction took place was that it was connected to fraudulent evasion of VAT*. The tribunal might have concluded that Mr Peters should have known that the transactions into which he entered were connected with fraud, by reference to the unconventional nature of those circumstances (a finding it came close to making at para 228). But it was not the only decision within the bounds of reasonable conclusion". [emphasis supplied].

217.The Court expanded on this at paragraph 77 where it is said:

"[77] There remains only the case of Mobilx. For the reasons I have given, both the tribunal and Floyd J applied the wrong test. The question was not whether Mobilx should have known that its transactions were more likely than not to be connected with fraud (the test applied by the tribunal at para 108 and by Floyd J at para 88). The correct question is whether it should have known that its transactions were connected with fraud. That, as I have said, could be established by demonstrating that it ought to have known that the only reasonable explanation for the circumstances in which the transactions in question were undertaken was that they were connected with fraud. In my judgement, although the tribunal applied the wrong test, the primary facts found by the tribunal did establish that the only reasonable explanation for the transactions in respect of which Mobilx claimed repayment of input tax, in their returns between April and June 2006, was their connection with fraudulent evasion of VAT".

218.We also note what was said at paragraph 84 of *Mobilx*:

[84] "Such circumstantial evidence…, will often indicate that a trader has chosen to ignore the obvious explanation as to why he was presented with the opportunity to reap a large and predictable reward over a short space of time. In Mobilx, Floyd J concluded that it was not open to the tribunal to rely upon such large rewards because the issue had not been properly put to the witnesses. It is to be hoped that no such failure on the part of HMRC will occur in the future.

His Lordship noted "...[85] the warning given in HMRC's Public Notice 726 in relation to the introduction of joint and several liability. In that Notice traders were

warned that the imposition of joint and several liability was aimed at businesses who "know who is carrying out the frauds, or choose to turn a blind eye" (3.3). They were warned to take heed of any indications that VAT may go unpaid (4.9). A trader who chooses to ignore circumstances which can only reasonably be explained by virtue of the connection between his transactions and fraudulent evasion of VAT, participates in that fraud and, by his own choice, deprives himself of the right to deduct input tax".

219.We also note what Moses LJ said in *Red 12*

"8. I turn to the second ground, which contends that the findings of fact made adverse to *Red 12* were based upon presumptions, as it is called; in other words, assumptions by the tribunal which the taxpayer was in no position to rebut. It is perfectly true that there was evidence of which *Red 12* had no direct knowledge and no basis for rebutting. But, in my judgment, to suggest that everything the Customs has to prove to prove the fraud is confined to facts which *Red 12* is in a position to rebut is to misread the decision on which reliance is placed, namely FTI [2006] ECR 1/4191. Of course the Tribunal must not assume that there has been fraud or, to put it another way, must not rely upon presumptions; but, if there is good evidence of the fraud and of the way it was carried out, it would almost be inevitable that the trader claiming input tax, who is alleged to have knowledge of the fraud, will not have knowledge of every detail of it. That is a trite proposition in relation to conspiracy in crime, in conspiracy in civil law, and in relation to alleged frauds such as in a case like this. There must be evidence, and good evidence, upon which it is proper for the tribunal to rely...."

220.We also note in relation to our fact finding the consideration of "... a dictum in the Advocate General's opinion in *Optigen Ltd v Customs and Excise Commissioners* at paragraph 27; that is: it necessary for the fact-finder to consider each transaction in the supply chain on its own merits and the character of that transaction cannot be altered by earlier or subsequent events. Again, it is important not to misunderstand what the Advocate General said as endorsed by the court at paragraph 47 of its judgment. Of course each transaction must be looked upon its merits, but, as the judge observed, it must also be looked at without blinkers and in the context and the background as a whole. The evidence as to what had gone on was stronger in relation to some deals than the others, but that inevitably coloured, as it does in all of these cases, the transaction and the state of *Red 12*'s knowledge in relation to those other transactions. It is absurd to suggest that each transaction must be considered without regard to the commercial background and context in which it was undertaken. As I observed in argument, these transactions take place with usually one phone call, often from a completely anonymous caller using the name of a company that varies almost from day to day, quite often plucked out of the air, asking the particular trader whether he is willing to go through the particular transaction, and it is usually all over in one telephone call. The idea that any fact-finder, be it a criminal court or a VAT Tribunal, has to disregard what is going on daily seems, as I have said, to be quite unarguable and absurd and I reject [it]...."

Questions to consider?

221.With the caselaw in mind we now turn to consider the questions raised we consider as being important in determining this case. These were:

(a) Have HMRC proved the chain of transactions in question?

(b) Have HMRC proved a tax loss in the chain?

(c) Have HMRC proved the tax loss was caused by fraud?

222.We then need to consider the issue of "ought to have known" if these three matters are established. In other words "whether [the Taxpayer] should have known that the only reasonable explanation for the circumstances in which his transaction took place was that it was connected to fraudulent evasion of VAT"?

Has the chain been proved? To where?

223.It was common ground the chain from Nordisk to STL had been proved.

224.There was no evidence before us which proved conclusively that STL had acquired the DVDs in question from a particular company or supplier.

225.HMRC invited us to infer that the DVD players had been acquired from SPT, a Portuguese Company.

226.The evidence for this according to HMRC was provided by Officer Mendez.

227.Officer Mendez said in his witness statement:

"On 29th November 2006 an Officer of HM Revenue and Customs Lydia Ndoinjeh visited a freight forwarder by the name of AFI Logistics (UK) Ltd as part of the MTIC strategy to identify goods that had been sent from the European Union and were being acquired within warehouses in the UK by companies registered for VAT in the UK. The goods identified by the officers were those which they believed to be acquired by potential defaulting traders would be inspected and the paperwork audited to enable the acquirer to be identified. During the visit the officer identified goods which she believed may be tainted by MTIC fraud. An inspection of the relevant paperwork showed that in four transaction chains Synergi-Tec Ltd were acquiring goods from Silver Pound Trading LDA. A copy of the officer's report I produce as "TM-1". Silver Pound Trading LDA is a company based in Portugal, Lydia Ndoinjeh contacted a gentleman from Synergi-Tec Ltd who said he was Kadir and confirmed that Synergi-Tec Ltd were acquiring the goods in the warehouse and had purchased the goods from Silver Pound Trading LDA. A copy of the summary of the telephone conversation that was captured to the Electronic Folder system of HM Revenue and Customs I produce as "TM-2"."

228.We note that Officer Mendez refers to four transactions all of which related to mobile phones rather than DVD's.

229.We were only provided with the documentation relating to one of those four chains and not for the other three chains. The chain for which documents were provided was a broken chain.

230.On the evidence and documentation in front of us, namely one broken chain for different goods, it is hard to discern a pattern of dealing in DVD players on which to base an inference.

231.We do not consider that it has been shown that it is more likely than not yet alone more probable than not that STL acquired the DVD's from SPL. We consider that it is as likely that the DVD players were acquired from Jafton.

232.We find that STL acquired the DVD's but we cannot make a finding who from as there was no direct evidence and no pattern of dealing as there was only one DVD transaction before us and the only other evidence was from Officer Mendes as to one broken chain concerning mobile phones.

233.We make these findings bearing in mind particularly what was said in *Mobilx* and *Red 12.*

Was there a tax loss proved?

234.The tax loss we were invited to concentrate on by HMRC was in respect of STL.

235.STL had been deregistered

236.The amount of output tax for STL was shown. We did not have any evidence as to what input tax would have been allowed.

237.We find that on the balance of probabilities the full amount of VAT was not accounted for by STL.

238.Accordingly, we consider that a tax loss has been proved.

Was that tax loss caused by fraud?

239.We then have to consider whether it has been shown that the tax loss was caused by fraud.

240.There was no direct evidence that it was caused by fraud. The evidence showed that HMRC had not received the amount of output tax.

241.We were invited to infer that there was fraud in this chain of transactions.

242.In considering this we note:

(a) The amount of the VAT not accounted for has not been shown. In particular, the amount of input tax if any has not been shown. This makes it harder to conclude that any tax losses caused by fraud.

(b) The chain above STL has not been proved. The DVD players could have been acquired from SPTL, Jafton or some other person.

243.We do not consider that there was any direct evidence before us that the Tax Loss was caused by fraud.

244.The question then is whether we should infer that it was caused by fraud. We accept that it could have been caused by fraud but there is nothing before us on which to base this in respect of the one chain concerning these goods. It would have been easier in our view to do so if it had been shown that the goods had been acquired from abroad. We found this a difficult aspect of the case but concluded there was not sufficient material before us to infer that the cause of the tax loss was fraud. We do not find that it was so caused. We do not consider that fraud as the cause of loss has been shown by direct evidence. We do not consider that there is cogent evidence before us which would allow us properly to draw the inference of causation by fraud.

245.We do not make the inference that the loss was caused by fraud.

246.We find that HMRC have not established a loss caused by fraud in the chain on the basis of the evidence before us and what we can reasonably infer from it. The fact that there was only one chain makes it hard to see patterns and make inferences.

"Ought to have known"

247.On what we have found so far the question then does not arises whether DCL should have known that the only reasonable explanation for the circumstances in which his transaction took place was that it was connected to fraudulent evasion of VAT?

248.However, for the sake of completeness and in case this decision is appealed we will now consider this question.

249. On the material before us, we do not consider that the only reasonable explanation was connection to fraudulent evasion of VAT. It is as plausible that this was a good commercial opportunity as that it was a chain with fraud in it. We find that the circumstances and evidence here are not such that the only reasonable explanation was connection to fraud. This was not an unbelievable transaction or one that was too good to be true. The level of profit was not outrageous.

250.There was nothing obvious in the sale and purchase involving DCL to put it on notice of fraud. The way the transactions were carried out may not have been ideal. However, that is not the test. In answer to the question, was connection to fraud the only reasonable explanation for the transaction, our answer is that fraud was not the only reasonable explanation and we so find.

General

251.HMRC's arguments start from the premise that there was an MTIC fraud. This is not the correct starting point in our view. This is a matter for HMRC to prove which it has not done here.

252.We accept that the chain could be traced back to STL. We also accept that STL did not account for the full amount of VAT that it should have done.

253.It does not follow that "Accordingly there was a tax loss in the chain courts by fraud". This has been discussed above.

254.It is accepted that DCL knew or should have known of the risks of MTIC fraud generally and as regards its own business.

255.We accept that a taxpayer should take the precautions which could reasonably be required of it to ensure that its transactions were not connected with fraud. We also accept that this is a high standard. The Notice 726 suggestions though were for a different purpose but provide interesting general guidance though are not conclusive in any particular case.

256.However, the issue here is not whether DCL took every precaution but whether the only reasonable explanation for DCL's transaction was that it was connected to DCL did not meet the standard in what DCL did.

257.HMRC said DCL did nothing to confirm by a third party checks there and/or reports that its supplier and customer were the credible, solvent business that would fail to honour their trading commitments and failed to carry out due diligence on its freight forwarder.

258.HMRC argue that the transactions are on the Back-to-Back cases and left no stock and so were artificial and only explicable on the basis of fraud..

We do not consider that this of itself makes the chain fraudulent nor did the fact that the customer was located in Denmark but the goods were delivered to France.

259.We agree that it would have been prudent for the Appellant to retain the serial numbers of the goods. However, in the circumstances of this case alone or otherwise it does not show fraud as the only explanation for the transactions.

That DCL was not required to pay its supplier until it had been paid in full by its own customer does not of itself show that the transactions were part of a fraudulent chain nor that the only explanation was fraud.

260.We accept that DCL said the goods were insured from the time they were held in the UK freight forwarders until delivered to a final destination. As the premium was not made this cannot be the case. Again this alone or otherwise does not show fraud as the only explanation for the transactions.

261. HMRC said that on the basis of this [set of facts] and all the other relevant circumstances the Tribunal must be satisfied on the civil burden of proof that the transaction formed part of a transaction chain which was connected with the fraudulent evasion of VAT and the Appellant knew or should have known of this.

262. We are not so satisfied and so find.

Costs

263. The Tribunal (Judge Roger Berner) directed on 18 November 2009 that Rule 29 VAT Tribunal Rules should apply and Rule 10 Tax Chambers Rule be disapplied.

264. It was further directed no direction be made with respect to the allocation of this appeal to one of the categories in Rule 23(2) of the Tax Chamber Rules.

265. As set out in the Summary Reasons for the Direction the significance of the earlier rules applying it that the Tribunal has the ability to make an award of costs.

266. Consequently, the question of costs has to be considered in this case.

267. One would expect costs to follow the event unless there is a reason why this should not be the case. We do not see any reason why costs should not follow the event.

268. Accordingly, the appeal is not only allowed but allowed with costs.

269. If the parties are unable to agree the amount of costs within six weeks of the release of this decision then either party shall be at liberty to apply to the Tribunal for a direction in respect of costs.

Conclusion

270. We have found that there was:

a. a chain established from STL to Nordisk;
b. not established who supplied STL nor whether it was from the UK or abroad;
c. a loss in the chain in that STL did not account for VAT but the amount of this loss was not established;
d. a tax loss but how it was caused was not established and certainly not that it was established that it was caused by fraud, directly or by inference;
e. a transaction for which fraud was not the only reasonable explanation.

271. Accordingly, the appeal is allowed and allowed with costs

272. 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.

ADRIAN SHIPWRIGHT
TRIBUNAL JUDGE

RELEASE DATE: 29 April 2013