[2015] UKFTT 0442 (TC)

TC04614

Appeal number: MAN/2008/0609
MAN/2008/0894
MAN/2008/0895

VAT– MTIC fraud - contra trading -denial of input tax – 52 transactions by three Appellants - common director - transactions connected with fraudulent tax losses–whether knew or should have known so connected - Kittel and Mobilx considered -– lack of commercial negotiations - lack of due diligence – basic contractual documentation - HELD – knew deals connected with fraud – appeals dismissed.

FIRST-TIER TRIBUNAL
TAX CHAMBER

Westminster Trading Limited **Appellants**
SGL International Limited
Westminster Import & Export Limited

- and -

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

TRIBUNAL: JUDGE Rachel Short
Gill Hunter (Member)

Sitting in public at 45 Bedford Square London between 15 September and 17 October 2014 and Royal Courts of Justice, the Strand London on 24 February 2015.

Mr Maninder Kohli director of each of the Appellants

Helen Malcolm QC of Three Raymond Buildings Gray's Inn and Ms Tina Ranales-Cotos of Kings Chambers Manchester, instructed by the General Counsel and Solicitor to HM Revenue and Customs, for the Respondents

DECISION

Preliminary matters

1. The circumstances of this hearing were rather unusual; the Appellants' legal representatives came off the record on 8 August 2014 and the Appellants' representative was taken ill on day three of the hearing having completed the Appellants' opening submissions but prior to any witness evidence being heard. The decision in respect of the case management issues arising from these circumstances was released on 22 October 2014 ([2014] UKFTT 985(TC)). The parties were offered and accepted an opportunity to make final written and oral submissions some time after the original hearing on 24 February 2015. The Appellants' representative was present and provided written submissions for this final day of the hearing.

Outline of appeal

2. This is an appeal against three decisions of HMRC addressed to (i) Westminster Trading Limited ("WTL") of 19 March 2008 denying a claim of input tax for the 06/06 period (ii) SGL International Limited ("SGL") of 23 June 2008 denying a claim for input tax of the 05/06 period and (iii) Westminster Import and Export Limited ("WIE") of 26 June 2008 denying a claim for input tax in the 05/06 period. The total amount of input VAT in dispute is £12.7 million. Appeals against HMRC's denial of the input tax claimed were made by WTL on 31 March 2008 and SGL and WIE on 14 July 2008.

3. The reason for refusing each of the claims was the same; that the underlying transactions were connected via a "contra-trading" scheme with fraud and the Appellants, acting through their director, Mr Kohli, knew or should have known of that fact.

Contra-trading

4. Contra-trading is a particular variation of "Missing Trader Intra-Community Fraud" ("MTIC") many examples of which have been considered by the tax tribunals. Contra-trading attempts to separate a claim for repayment of input tax in the UK from UK trades in which a trader has failed to pay output tax by interposing an apparently separate supply of goods, often of a different kind than the ones in respect of which output tax was not paid.

5. The essence of a contra-trading scheme is that standard rated goods are purchased in the UK by a broker through a chain of suppliers that has at one end a defaulting trader, a trader who had made sales in the UK but not accounted to HMRC for the correct output tax, (the "defaulter"). This part of the chain of transactions is often referred to as the "dirty chain". That trader exports those goods to the EU as zero rated supplies and acquires goods of a similar value (but not necessarily of the same type) from the EU. That trader (the "contra-trader") will have as a result input and output VAT of equal or very nearly equal amounts. These goods are then sold in the UK via an intermediary (or a series of intermediaries) to another broker. This part

of the chain of transactions is often referred to as the "clean chain". HMRC's case is that the Appellants in this appeal take the role of that UK broker. That broker then sells the goods to the EU which are also zero rated for VAT purposes and makes a claim in the UK to reclaim its input tax. The "clean chain" in this case is the purchase and sale of mobile phones of which the Appellants' deals were allegedly part. The "dirty chain" is the purchase and sale of CPUs.

6. HMRC's refusal to repay each of the Appellants' input tax for the periods in dispute is based on their argument that it is input tax which is part of such a contra - trading scheme in which the Appellants play the role of the broker and that the Appellants were, or should each have been aware, of the fact that these transactions were connected with fraudulent trades.

7. The disputed transactions carried out by each of the Appellants amount to 52 separate transactions split between WTL – 16 transactions from 20 – 27 June 2006, SGL – 20 transactions from 11 – 31 May 2006, WIE 16 transactions from 25 – 31 May 2006.

8. The grounds of appeal for each of the Appellants were very similar as set out in their appeal notices of 31 March 2008 (WTL), 14 July 2008 (SGL and WIE); that HMRC's refusal to repay input tax to the Appellants was unlawful, that none of the Appellants had knowledge of the details of the fraudulent transactions to which HMRC say their deals were connected and that HMRC had not properly proved the actual participation by any of the Appellants in the fraud.

9. The appeals were directed to be heard together by the tribunal's direction of 20 January 2009.

Background facts

The Appellants

10. WTL was incorporated on 3 June 2005 and registered for VAT on 31 July 2005. Mr Maninder Kohli and Mr Tejbir Maini were directors of WTL. Mr Maini was also company secretary. WTL's VAT1 described its business as a clothing business with an estimated turnover of £100,000. Its turnover in 2006 was £51 million.

11. SGL was incorporated on 27 September 2004 and registered for VAT on 1 August 2005. Mr Maninder Kohli was sole director of SGL. Mr Azim Zia was company secretary. Mr Zia was also secretary of Stonegalleon Plc, a company with which Mr Kohli had also previously been involved. SGL's VAT1 at the time of its registration for VAT described its business as telecommunications with an estimated turnover of £500,000. SGL's turnover was £53.6 million in 2006.

12. WIE was incorporated on 1 March 2006 and registered for VAT on 13 April 2006. Mr Maninder Kohli and Mr Tejbir Maini were directors of WIE. Mr Maini was also company secretary. WIE's VAT1 described its business as import and export and estimated its EU sales as £50,000.WIE's turnover in 2006 was £25 million.

13. The details of each transaction undertaken by each of the Appellants which are the subject of this appeal are set out in the schedule to this decision notice and are referred to by the numbers given in that schedule. Mr Kohli was a common director of all three Appellant companies and represented them at the Tribunal in the absence of legal representation.

The law

14. The relevant EU legislation which sets out a VAT registered trader's right to reclaim input tax was, in the periods concerned, the Sixth VAT Directive (77/388/EEC, the "Sixth Directive"), at Article 17. The UK legislation implementing the Directive's rules about input tax reclaims is in sections 24 to 26 Value Added Tax Act 1994. These provisions state that if a registered trader has suffered input tax which is allowable, he has a right to offset this against his output tax liability or receive a repayment if the input tax exceeds the output tax due.

15. European cases have decided that the general rule in Article 17 is subject to an exception in the following circumstances :

> " *a taxable person who knew, or should have known that, by his purchase, he was taking part in a transaction connected with the fraudulent evasion of VAT must, for the purposes of the Sixth Directive, be regarded as a participant in that fraud, irrespective of whether or not he profited by the re-sale of the goods*"
>
> *That is because in such a situation the taxable person aids the perpetrators of the fraud and becomes their accomplice.*
>
> *In addition, such an interpretation, by making it more difficult to carry out fraudulent transactions is apt to prevent them ……..*
>
> *It is for the referring court to refuse entitlement to the right to deduct where it is ascertained, having regard to objective factors, that the taxable person knew, or should have known that, by his purchase, he was participating in a transaction connected with fraudulent evasion of VAT"*
>
> *(Axel Kittel v Belgian State & Belgian State v Recolta Recycling SPRL (joined cases – C-439/04 & C- 440/04) [2006] ECR 1 – 6161).*

16. The UK's own courts have commented on the application of the *Kittel* decision in *Mobilx Limited (in liquidation) v HMRC [2010] EWCA Civ 517 ("Mobilx")* a decision of the Court of Appeal:

> "(*The test) includes those who should have known from the circumstances which surround their transactions that they were connected to a fraudulent evasion. If a trader should have known that the only reasonable explanation for the transaction in which he was involved was that it was connected with fraud and*

if it turns out that the transaction was connected with fraudulent evasion of VAT then he should have known of that fact. He may properly be regarded as a participant for the reasons explained in Kittel.

If he chooses to ignore the obvious inferences from the facts and circumstances in which he has been trading, he will not be entitled to deduct…..

Even if a trader has asked appropriate questions, he is not entitled to ignore the circumstances in which his transactions take place if the only reasonable explanation for them is that his transactions have been or will be connected with fraud".

17. There are also a number of recent decisions from this tribunal which consider the same test, including *Else Refining and Recycling Limited v HMRC* ([2012] UKFTT 407(TC)) and notably *JDI Trading Limited v HMRC (*LON/2008/1179) which concluded, in a decision in favour of the taxpayer, that in order to prove that a taxpayer should have known of a connection with fraud, it is not sufficient for HMRC to establish that "*the taxpayer should have realised it was more likely than not that the transactions were connected to fraud*" in order to deny the right to deduct. HMRC must demonstrate that the only reasonable explanation for the circumstances in which the transactions took place is a connection with fraud.

18. The Appellants also referred to the *Fonecomp* case. At the time of the first part of the hearing the Court of Appeal decision in that case had not been released. They said, as part of their grounds for seeking an adjournment of the hearing, this decision was likely to contain important reasoning about the application of the *Kittel* decision in contra-trading cases such as this one. The decision of the Court of Appeal in that case was released on 3 February 2015 (*Fonecomp Limited v Commissioners for* HMRC [2015] EWCA Civ 39) and supports the *Kittel* approach: in particular that a default does not need to occur in the same chain of supply as the chain in which the disputed input tax arises.

19. The Court of Appeal in *Fonecomp* referred to the decision in *Universal Enterprises (EU) Ltd v Revenue and Customs Commissioners* ([2014] STC 1515):

"*The Appellants' argument necessarily treats "clean" as synonymous with "innocent", but a clean chain in cases of this kind – that is, one in which each of the traders accounts correctly for VAT – is not innocent; it is an integral part of the fraudulent scheme. Even if I entertained any doubt (which I do not) that as a matter of EU law there is sufficient connection between a trader in the clean chain and the default in the dirty chain, there remains an insuperable connection with the fraudulent purpose in the clean chain*".

20. The *Fonecomp* decision also made clear that the degree of knowledge required to be a participant in a fraud need not be specific, it is not necessary that a trader knows, or has the means of knowing how the fraud in question actually took place. *Fonecomp* para [51] "*He [*the trader*] has simply to know, or have the means of knowing, that fraud has occurred, or will occur, at some point in some transaction to*

which his transaction is connected. The participant does not need to know how the fraud was carried out in order to have this knowledge".

21. The onus of proof is on HMRC to demonstrate to the civil standard that the Appellant companies knew or should have known that each of the 52 transactions under appeal were connected with fraudulent tax losses and that each of the Appellants knew, or should have known of that fact.

Evidence

Witness Evidence – HMRC

22. HMRC provided extensive witness and documentary evidence, amounting to more than 100 A4 bundles including details of each of the "clean" and "dirty" chains of which they alleged the Appellants' deals were part and detailed "deal packs" including primary documents supporting each of the transactions in those chains obtained both from the Appellants and other participants in the chains of transactions.

23. In the absence of the Appellant for the majority of the hearing, it was agreed that the oral evidence to be given by HMRC's witnesses should be limited to the three officers who were responsible for verifying the VAT returns of each of the Appellant companies and HMRC's main witness dealing with the flow of money between the Appellants and other parties in the chains of transactions identified by HMRC, Mr Mendes. None of HMRC's witnesses were cross-examined by the Appellants due to Mr Kohli's absence on health grounds.

24. HMRC's officers evidence about the Appellants' co-operation with HMRC, their due diligence, the documents supporting their commercial dealings and the nature of those deals themselves was consistent; the Appellants were not co-operative, failed to produce documents to support what they said was the commercial framework of their businesses and had a less than perfect approach to due diligence and legal documentation.

25. We have not set out the full detail of all the evidence provided by each HMRC Officer but do repeat examples of what appeared to us to be illustrative of the Appellants' general course of dealing and consider in detail one deal for each Appellant.

Mrs Hudson - SGL

26. Mrs Hudson gave oral evidence to the Tribunal and provided two witness statements dated 13 March 2009 and 1 March 2010 which were taken as read. Mrs Hudson is an officer of HMRC and has been part of their MTIC team since May 2006. She was HMRC's case officer in charge of SGL.

27. Mrs Hudson's witness statement stated that for all of SGL's disputed deals, the goods were purchased from a contra-trader and the contra-trader deal chains could be traced back to a fraudulent tax loss.

SGL's communication with HMRC

28. Mrs Hudson said that in total HMRC had written 31 letters, made three visits and seven phone calls to SGL between January 2007 and May 2008. In response SGL had produced one A4 folder containing 150 pages of information about the deals being investigated by HMRC. In her view this was one of the worst levels of communication with HMRC she had come across. She told us that "*I would say the level of co-operation was very poor. They are one of the most difficult traders I have dealt with in an MTIC case*". She had received only the basic information about the transactions carried out by SGL, all of which had been included in the "deal packs" provided by HMRC, despite requesting information about what checks had been done on the goods and on suppliers and customers and other sources of information. She received responses to her requests for due diligence information only in February 2008.

29. Mrs Hudson also referred to Mr Kohli's claim for VAT input tax on an office carpet. After a number of requests to visit SGL's premises and a visit on 25 September 2006, the carpet to which the invoice related was found eventually at Mr Kohli's residence at Lennox Gardens, not in his office. The input tax claimed was therefore denied.

Documentation for deals; Example Deal 1

30. Mrs Hudson relied on evidence provided by SGL and other sources available to HMRC to produce deal packs for each of the 20 deals and used Deal 1 as an example of the deals undertaken by SGL. Deal 1 was a purchase from Globalex Limited ("Globalex") by SGL and an onward sale to Bleu Opale Technique Eurl ("Bleu Opale") in the EU. The invoices were issued on 11 May 2006.

31. For Deal 1 no terms and conditions were provided other than a purchase order between Globalex and SGL. No contracts had been provided for any purchase orders entered into by SGL. Mrs Hudson accepted that SGL's purchase order did provide details of the specification of the phones to be acquired and that they should be "shipped on hold".

32. Mrs Hudson told us that SGL had not been able to explain to her what the term "ship on hold" used in their purchase order meant. Mrs Hudson said to us

> "*I tried to get SGL to explain it but they were rather evasive of what it means. It seems to give them the right to ship the goods, usually out of the UK, and have them held somewhere on their behalf until their customer has paid them, although it is not clear who actually owned the goods at the time they are actually shipped out of the country and put on hold*".

33. Mrs Hudson confirmed that she had not seen any terms and conditions between SGL and its customer Bleu Opale. She also said that there was no clarification in the documents about who held title to the goods. Payments had been made on 24 May, some time after the invoices had been issued, but to make payment SGL had relied on a loan from Freeview Properties Limited, a third party company.

34. The phones were shipped to Germany and charged to Bleu Opale at a profit of £37 per phone, but she had not seen any evidence of negotiation on price with sellers or customers. Mr Kohli had told her that all of this had been done by phone. The pro forma invoice which was later provided by SGL gave no indication of who was paying for transportation of the goods. An SGL fax of 11 May requested a "full inspection of the goods", but the evidence suggested that only one box had been inspected. Payment for the goods had been made on 24 May, when the release note was issued, but the goods appeared to have been collected and transported on 15 May. It was unclear why a release note was required on 24 May, since the goods had already been delivered.

35. She referred to an inspection report for an inspection carried out by Verify Inspections for the goods sold in Deal 1 which had "N/A" in the box confirming whether the goods were new or not but said that the purchase order from SGL had stated that the phones had to be brand new.

SGL's due diligence

36. Mrs Hudson said that she would have expected SGL to carry out independent checks on the owners of the companies with whom it dealt, solvency checks, "Redhill checks" (a "Redhill check" is a means of obtaining confirmation from HMRC that a particular trader remains validly registered for VAT) and that SGL representatives would have visited the office premises of their suppliers and customers.

37. Mrs Hudson gave a number of examples of SGL's due diligence falling short of these expectations; the information provided by Kensai Trading Limited ("Kensai") gave no indication of the market they were in, although the VAT1 seen by HMRC said that they dealt in cosmetic and toilet articles. Equally the due diligence done on Pochard Sp Zoo ("Pochard"), (the EU customer in 7 of SGL's deals) demonstrated some discrepancies (between signatures on documents and on the director, Steve Bateman's driving licence) which had not been picked up by SGL. The situation was similar for Bleu Opale (SGL's EU customer in 8 of its disputed deals) the only due diligence information provided was a letter from its accountant and a personal bank statement from a director showing a small balance.

38. Mr Kohli had not provided any evidence of how he was introduced to the companies he dealt with or how credit risk was managed for customers who he knew were recorded as having high credit risk such as Pochard. In fact Mr Kohli had stated that no written records were kept of these aspects of SGL's dealings with customers.

39. Mr Kohli had told Mrs Hudson that he had visited another of SGL's customers, Vanprugh Communications SRL's ("Vanprugh") premises, but no documents had

been provided to support this having occurred. Mrs Hudson said that in her view there was some doubt about whether any site visit had actually been made.

40. No third party references were provided for SGL's freight forwarder All Systems Courier Worldwide Ltd ("ASC") until after deals had already been done with that entity, on 1 June 2006. The references which were provided by SGL's EU customers were all provided by the same entity Stolz Transporte GmbH ("Stolz"), but SGL did not seem concerned by this, although there was evidence that Mr Kohli was in touch with Stolz based on faxes seen dated 3 May 2006.

Mrs Tressler - WIE

41. Mrs Tressler is an officer of HMRC and has been part of their MTIC team since June 2006. She was responsible for verifying WIE's VAT returns for the periods under appeal. She provided two witness statements to the Tribunal dated 20 March 2009 and 19 February 2010 which were taken as read and gave oral evidence to the Tribunal.

42. Mrs Tressler said that WIE had been involved in 16 transactions over a 7 day period with four days of actual trading. WIE had not notified HMRC of a change in its trading activities or expected turnover after its VAT1 had been submitted, although this had clearly occurred.

43. Mrs Tressler stated that WIE purchased all of its goods directly from three contra-traders and all of that contra-trader's deals had been traced back to fraudulent tax losses.

WIE's communication with HMRC

44. HMRC had written between 30 and 40 letters to WIE and had two meetings with them, on 19 June 2006 and 6 February 2007. This high level of correspondence reflected Mr Kohli's unwillingness to meet with HMRC. Mrs Tressler described Mr Kohli as unco-operative with HMRC, saying

> "*He [Mr Kohli] wasn't very co-operative at all. He wasn't co-operative at our meeting. [of 6 February 2007] He seemed very reluctant to provide written responses to some of these issues that I was raising and my experience as a VAT assurance officer is that's quite unusual for that to happen, that level of non-cooperation*"

Mrs Tressler accepted that both of those meetings had happened after the date of the deals under appeal but said that Mr Kohli's knowledge of MTIC transactions and fraud in the mobile phone market could be inferred from his knowledge through the other companies which he was involved in; SGL and WTL. Notice 726 had been issued to the directors of those companies in November 2005, December 2005 and February 2006. That Notice, titled "Joint and Several Liability" included HMRC's guidance and the checks suggested to ascertain the integrity of a supply chain. In her view Mr Kohli would have been well aware of the high risk of fraud in the mobile phone sector.

Documentation for deals – Example Deal 13

45. Deal 13 is a purchase by WIE from Worldwide UK Import Export Limited and a sale to Pochard Sp Zoo in Poland. The invoice date is 31 May 2006.

46. Mrs Tressler confirmed that she had seen no detailed purchase orders for Deal 13. Payment was made for the goods on 20 June, when the release note was provided, but the invoice for this deal was issued on 31 May. The evidence from the inspection report at the freight forwarder done by Verify Inspections suggested that a full inspection of the goods had not been undertaken as stipulated; only one box had been physically checked.

47. For deals 1, 2, 14 and 16 in which WIE was involved Mrs Tressler also suggested that the CMRs provided could not be genuine; the number of pallets which were said to have been moved on one trailer could not physically have been done; the trailer was not large enough.

WIE's due diligence

48. Mrs Tressler explained that from the evidence she had seen, WIE had not done any of its own due diligence, but had relied on the due diligence done by its sister company, WTL.

49. Mrs Tressler said that given Mr Kohli's knowledge of fraud in this market, she would have expected him to take due diligence on his suppliers and customers seriously. According to Mrs Tressler Mr Kohli had been given "*a substantial amount of warnings*". Equally it was surprising, given that WIE was a new company (set up in March 2006) that suppliers did not do significant due diligence on it. In fact the due diligence done by WIE on its three suppliers Kensai, Worldwide and Globalex was minimal and occurred after the date when these deals were done. There was no evidence of Redhill checks having been carried out by WIE for its suppliers.

50. Mrs Tressler gave us a number of examples of information which was provided to WIE about its customers which should have put the Appellant on notice that further investigation was required. For example; WIE was told details of its customer in Deal 1, Pochard's account with First Curacao International Bank NV ("FCIB") which should have alerted Mr Kohli to the possible existence of fraud; the fact that all of his suppliers and customers had accounts at FCIB should have put Mr Kohli on notice of this risk. Mr Kohli had not provided any evidence that he had carried out a site visit to Pochard in Poland. In fact, the evidence suggested that Mr Kohli had not visited Poland despite having been advised to do so by his adviser, Vincent Curley, prior to doing business with Pochard. The trade application form which had been completed for Pochard showed that its director, Mr Stuart Bateman, was actually resident in Swansea. A site visit had been carried out at Bleu Opale, but only after deals had been done with that customer and the information provided about the site visit to Vanprugh included no evidence of when the visit was actually carried out.

51. Mrs Tressler also said that WIE's due diligence done on other customers was inadequate; Globalex provided a water bill for £11 in the name of a director. Kensai's

Experian credit reports of 22 May 2006 described them as "above average risk" and their VAT certificate seen by the Appellant described their business as "cosmetic and toilet article retailing". The due diligence on Worldwide UK included a director's mobile phone bill which was in arrears by £36.97.

52. The insurance taken out by WIE with TransPacific had not been properly executed (there were no company seals) and specific additional requirements relating to electronic equipment had not been complied with. The special dispensation given by TransPacific from some of the insurance requirements was unusual. There was no evidence that the premium to be paid had been changed to reflect this.

Mr Bond - WTL

53. Mr Bond is a higher officer of HMRC and WTL's compliance officer and was part of HMRC's MTIC team between August 2006 and 2012. Mr Bond provided a witness statement dated 21 July 2011 and gave oral evidence to the Tribunal.

54. Mr Bond told the Tribunal that all of the Appellant's deals traced to the same three contra traders, Globalex, Kensai and Worldwide and all could be traced back to fraudulent tax losses.

WTL's communication with HMRC

55. Mr Bond explained that HMRC had done a verification visit to WTL's offices on 7 December 2005, knowing that Mr Kohli and WTL were involved in the wholesale mobile phone business, in order to educate Mr Kohli about the risk of fraud in this market. Mr Bond referred to that fact that Mr Kohli had said that he had a wealth of experience in the mobile phone market through his family connection with the mobile phone trader Stonegalleon Plc and his own 30% shareholding in that company. Mr Bond had not been present at this verification visit but the notes of that visit suggested that Mr Kohli had not been very co-operative, as had also been the case when HMRC visited on 5 October 2007. WTL had, unusually, been served with a demand to produce letter in November 2007. Despite this, very few documents had been provided to HMRC.

56. Mr Bond pointed to the evidence of WTL's contrivance, through Mr Kohli, in MTIC trading; the large increase in the company's turnover, the consistent dealing with counterparties who were contra-traders, the import and export of goods which were not appropriate for the UK market, for example sales to Kensai which actually had its own UK company so should have had no need to buy from WTL and who had previously dealt directly with Monza, WTL's customer.

Documentation for deals – Example deal 15

57. Mr Bond dealt in detail with WTL's deal 15, which was a purchase from Kensai by WTL and then a sale to Monza Trading SRL for which invoices were issued on 27 June 2006. There were timing mismatches between the dates when release notes were

sent to UK freight forwarders and the time when the stock was actually transported, which in respect of deal 15, was before the release note was issued. No ordering and returns procedures were ever seen.

58. An allocation note was provided which referred to a release note dated 27 June 2006 addressed to the freight forwarder releasing the goods from Kensai to WTL. There was a second release note dated 6 July 2006 releasing the goods from WTL to Monza Trading SRL ("Monza"). Payment was not made by WTL until 6 July, more than a week after the date of the original invoice and the release note to WTL. No terms and conditions had been provided for the sale to the EU but the goods were delivered to TCF Logistique SARL ("TCF") a freight forwarder in France. Two inspections were apparently carried out; one by Verify Inspections, including only vague details and one by Global International. The reports were inconsistent in describing the condition of the goods, only one saying that they were brand new.

59. The insurance documents received by WTL from TransPacific were basic; Mr Bond compared the insurance terms to the detailed terms provided by Norwich Union Marine Cargo Insurance, of which we were shown a copy, to demonstrate this.

60. Mr Bond confirmed to the Tribunal that WTL had not recorded IMEI (International Mobile Equipment Identity) numbers for any of the phones they bought or sold.

61. In this deal 15, freight forwarders ASC were used despite WTL owing significant outstanding debts of £44,000 to other freight forwarders. ASC either did not check whether WTL had debts outstanding, or did not care. It was not clear for this deal that Mr Kohli was aware where the goods actually were (in a warehouse in Belgium) or how he could have inspected the goods.

62. Mr Bond also referred to the lack of CMRs for these import deals from the three contra-traders, none had been provided by the freight forwarders or any other parties to the transactions. Nor was there any evidence of the goods having been inspected and where inspection reports were provided, there was no evidence of where the goods were actually held. Mr Bond said that if the documents suggested that there had been no importation of the goods at all, the VAT claims made by WTL would still have been fraudulent because there would have been no UK sale.

63. According to Mr Bond, Mr Kohli did not have a clear idea of when title to the goods passed, saying only that it was "when we have paid". He said he had not seen contracts between WTL and Kensai or Globalex, two of WTL's suppliers or any of their EU customers.

WTL's Due Diligence

64. Mr Bond said that although Redhill clearances had been done for example on Muggles Consulting Company Ltd ("Muggles") in Cyprus, (an entity which WTL did not deal with directly, but which was involved elsewhere in the deal chain) the other

due diligence carried out had been minimal; the "introduction pack" supplied included a letter which was not dated. Muggles also had an FCIB bank account and had provided a reference for Pochard, another entity in the MTIC chain, as one of its customers.

65. As for WTL's due diligence on its customers (Vanprugh, Bleu Opale and Monza); taking Monza as an example, Mr Kohli had visited their offices only after deals had already been done with them and the only due diligence documents provided were an electricity bill for a small sum and a bill for a meeting room. According to Mr Bond, the due diligence documents provided seemed to have been compiled by Monza itself.

Indicators of fraud

66. In Mr Bond's view, all of the indicators of fraud were present in WTL's transactions; the phones sold were either EU or US rather than UK specification phones, all trades done were exactly matched, no retailers or producers were dealt with, all parties dealt through FCIB accounts and the profit margins made on the deals were static; each of the contra-traders made a consistent profit of 40p profit per phone, WTL made by far the largest profit margin, of up to £67.00 per phone on some types of Nokia handset.

Mr Mendes - FCIB Evidence

67. Mr Mendes gave evidence on behalf of HMRC where he has worked for 38 years. His evidence related to the records of transactions provided from servers used by First Curacao International Bank NV (FCIB) to record money flows. Mr Mendes provided four witness statements to the Tribunal dated 17 February (two) and 26 February 2010 and 15 February 2012 which were taken as read and gave oral evidence to the Tribunal. He told us that each of the Appellants had a bank account with FCIB as did other participants in the deal chains established by HMRC.

68. Mr Mendes explained that his first three witness statements were based on information which he had obtained from FCIB's own records of the flow of funds between its customers, contained in a system called "*Bankmaster Plus*" and information about the identity of customers which had been obtained by FCIB as part of its account opening procedures in a system known as "*Datastore*" and relied on information made available through an FCIB server located in Holland known as the Dutch server. At the date when he had made his final witness statement he had been able to supplement this information from a second server, located in Paris, which also provided a narrative description attached to each transfer of funds.

69. Mr Mendes provided detailed charts setting out the money flows for each of the 52 disputed transactions and the chains of deals in which they were involved in extensive detail including cross-references to the invoices identified for each deal chain.

SGL

70. The detailed FCIB evidence provided by Mr Mendes from the so-called Paris server made it clear that SGL had obtained a loan from a third party, Freeview Properties Limited, without which it would not have been able to pay for its deals. Other payments made by SGL were financed only by the repayments of input tax to the relevant traders by HMRC.

71. From the money flow charts provided by Mr Mendes he told us that he had identified six "money conduits", four of which were used to put financing into these deal chains. Once that money had been put in, other payments in the chains happened in very quick succession; for example for deal 1 for SGL on 24 May, all payments were made between 08.21 and 09.30 in the morning and all parties had the same IP address other than SGL. We were referred to the detailed explanation given for the allocation of IP addresses in the *Advent Worldwide Distribution Limited v HMRC* decision ([2014] UKFTT 249(TC)). The explanation for a common IP address is either that all participants are accessing the same physical connection, the same gateway or server and gateway or the same proxy server or mobile data connection. Mr Mendes suggested that it was extremely unlikely that the same IP address could be used by a number of different entities as mere coincidence.

72. Mr Mendes explained that Electronic Banking ("EB") numbers record a unique banking identity for each banking transaction and are allocated depending on the time when a participant logs into the bank's electronic banking system. The EB numbers were very close for all transfers in this deal, suggesting either that the numbers had been pre-booked, or that all the transfers were made by the same entity.

73. For the EB numbers to run in such a close series the deals would all have to have been done on one occasion and on a rolling basis. Only one EB number is out of the series here and that is a transaction coming from a different IP address. The chances of this pattern of payments occurring through unconnected parties, was in Mr Mendes' view, almost impossible. This must have happened as the result of pre-arrangement. Similar patterns could be seen in the other 51 deals in which the Appellants were involved.

WTL

74. Mr Mendes had analysed WTL's FCIB account for the period September 2005 to September 2006. In his view the flow of funds from WTL suggested that when WTL received its VAT repayment it was paid back through the chain of participants through their FCIB accounts. When WTL received a VAT refund on 14 February 2006 this was only partly retained by WTL.

75. Mr Mendes accepted that he could not demonstrate a complete circularity of funds for these WTL transactions but nevertheless suggested that the funds were being circulated between a small number of participants.

76. WTL's FCIB account showed that it had received three payments from a company called Freeview Properties Limited at the end of 2005 and 2006.

77. Mr Mendes used WTL's deal 19 as an example of the pattern of cash flows which he had identified for that company; Deal 19 took place on 3 July 2006 and all participants in the payment flow used the same IP address other than WTL. Six funds transfers occurred between the participants in 1 hour and 24 minutes.

WIE

78. Mr Mendes used deal 1 of 16 June 2006 as an example of the pattern of cash flows for WIE, concluding that the funds from WIE were used to fund a VAT loss transaction. In this deal the first six payments were made within 30 minutes and later the same day a further 10 payments were made within 21 minutes. Eight of the eleven participants in the payment chain had the same IP address.

79. We were also referred to the extensive reports of Mr Andrew Letherby who led the forensic investigation into the digital evidence from FCIB.

HMRC produced further detailed witness statements and exhibits which the Tribunal considered without oral evidence being given.

Mr Humphries

80. Mr Humphries provided two witness statements dated 12 March 2009 and 24 February 2014. He is a senior officer of HMRC and his evidence concerned the overall structure of the contra-trades to which the Appellants' deals were linked.

81. He told us that he had reviewed the deal sheets compiled by HMRC for all of the Appellants' trades which started from the EU and went via one of Kensai, Worldwide and Globalex through buffer traders and brokers and led to the same three defaulting traders in the UK; Woodworks UK Limited ("Woodworks"), Steven Ellison Logistics Limited ("Steven Ellison") and Only Quality Limited ("Only Quality"). In all of the deals CPUs were sold by one of the three contra-traders to the same group of EU customers as used by the brokers for their acquisition transactions, making a link between the acquisition deals and the tax loss deals.

82. He described the deals as "*a whole series of transactions contrived as an overall fraudulent scheme. Goods from the EU from a small group of 14 EU traders, 6 UK contra traders [including the 3 relevant to these deals], 29 buffers and 75 UK brokers were sold to 17 EU traders*". In his view this pattern of trading was extremely unlikely in the course of genuine arm's length transactions. The degree of control required to ensure that all elements of the transaction chain worked suggested that everyone in the chain had knowledge of the overall fraudulent scheme.

83. Mr Humphries told us that the companies involved in these linked transactions often had links through shared directors. Although there were EU traders in both groups, those EU traders never received their own goods back, which he said suggested that circularity of goods was being intentionally avoided which itself suggested that the deals were contrived.

84. Mr Humphries set out the margins which were made by each participant in the chains of deals, with the buffers in the CPU chain making 5 pence per unit, buffers in the phone chain making 25 pence per unit but the brokers in the phone chain, including the Appellants, making a much higher minimum of £7 - £9 per unit.

85. Mr Humphries said that in his view no value was being added to these deals by putting them through the UK, in most cases it would have been cheaper and more convenient for the customers to buy the goods in the EU.

86. Of the trades which Mr Humphries had considered 37 had used the same insurer; Cahan Insurance, including WTL. (Cahan had not been used for any of the deals done by WTL which were under dispute as part of this appeal).

Mr Corkery

87. Mr Corkery gave expert evidence to the Tribunal concerning the operation of the so called "grey market" in mobile phones and provided a witness statement dated 27 August 2014. Mr Corkery is a partner at Ernst and Young.

88. He explained the main features of the "grey market" which he defined as "*the exchange of goods through routes which are unofficial or unintended by the original manufacturer*" in mobile phones setting out the market opportunities which the grey market exploits, being (i) volume shortages in particular types of handsets (ii) "box breaking" to free up networks (iii) dumping which arises when there is an over rather than under supply of handsets and (iv) transactions exploiting changes in the value of the currency in which the goods are traded. He told us that all of these relied on the ability to verify the specific type of phones which were being bought and sold and the needed for a detailed specification of stock held. In his view the market would only allow intermediaries to play a role such as this if they were adding value through specialisation or some other value was being added.

Contra-traders

Mr Patterson and Mr Bycroft for Worldwide (UK) Import Export Limited

89. Mr Patterson produced two witness statements dated 5 March 2009 and 20 July 2011. Mr Patterson was the HMRC officer in charge of verifying the deals done by Worldwide for UK VAT purposes. Unfortunately by the time of the hearing in 2014 Mr Patterson had died and his witness evidence was adopted by Mr Bycroft in his place and who produced his own witness statement. He told us that 97% of that company's deals for January to July 2006 had been traced back to a fraudulent tax loss and to one of Woodworks, Steven Ellison or Only Quality. The company's VAT registration was cancelled on 1 June 2007 and its last deals were done on 20 June 2006.

Mr Saul for Kensai Trading Limited

90. Mr Saul produced a witness statement dated 20 March 2009. Mr Saul was the officer in charge of dealing with Kensai's VAT from 03/06. He told us that the majority of its trades for the periods from March to June 2006 could be traced to defaulting traders (154 out of a total 161 deals) and that the company was generating only a negligible difference between the input tax it suffered and the output tax it charged so that very small amounts were paid to or re-claimed from HMRC. The majority of its EU sales could be traced back to two defaulting companies Steven Ellison and Only Quality.

Mr Phillips for Globalex Limited

91. Mr Phillips produced a witness statement of 20 March 2009. Mr Phillips was responsible for Globalex's VAT from May 2006. He told us that the company had no storage facilities and only two employees and a turnover from August 2005 to June 2006 of £1,080,899,649. Of the 344 deals undertaken in that period 336 traced back to fraudulent tax losses. It also generated only a small difference between its input and output VAT from February 2006 to June 2006 with input tax of £83,441,180.71 and output tax of £83,537,081.92

*Defaulter*s

Mr McCaskell – Steven Ellison Logistics Limited

92. Mr McCaskell provided a witness statement dated 11 March 2009. He was the HMRC officer allocated to Steven Ellison. He visited the principal place of business in March 2006 which turned out to be a private address on a council estate. The company had never made any VAT returns but Mr McCaskell said that from evidence provided by its customers, its turnover in March 2006 was £404,944,684.80. The company had been registered for VAT on 20 January 2006 and its business was described as delivering aircraft wings to British Airways and Saudi Airlines. It has significant VAT debts owing to HMRC.

Mr Mandalia for Woodworks UK Limited

93. Mr Mandalia produced a witness statement dated 12 March 2009 and was the HMRC officer for Woodworks. He explained that two visits had been undertaken to the company's premises but the directors had never been present. Their business was described as "joiner and cabinet makers". From details which HMRC had of deals done with its customers they had established that Woodworks had a total debt due to HMRC of £84,042,421. The company had gone into liquidation on 27 April 2006 and the VAT remained unpaid.

Mr Wald for Only Quality Limited

94. Mr Wald provided a witness statement of 31 July 2013. Mr Wald is a higher officer of HMRC and told us that Only Quality was registered for VAT on 10 February 2006 and described its business as "general trading". When its principal place of business was visited it was occupied by a different company. HMRC had information about trades done with customers in June and July 2006 in respect of

which £36,786,214,24 of VAT was outstanding on a total value of sales of £959 million. Only Quality had not accounted for any VAT.

Mr Downer for Freight Forwarder Worldwide Logistics

95. Mr James Downer produced a witness statement of 11 February 2010. Mr Downer told us that he had obtained information from Dutch fiscal authorities that they had visited the premises of Worldwide Logistics in Holland and spoken to the director of the company Mr Monster. They had established that the company had produced and stamped customs documentation (CMRs) for goods which did not exist including for transactions involving Kensai and other participants in these deal chains.

Witness Evidence - Appellants

Mr Kohli

96. Mr Kohli is a director of each of the Appellant companies. Mr Kohli provided a statement of case to the Tribunal on 17 September 2014 and gave oral evidence to the tribunal before being taken ill on 25 September. He was not cross-examined by HMRC. Mr Kohli struck us as a clever but not entirely straightforward witness.

Involvement with the Appellants

97. Mr Kohli explained that he had agreed with Mr Maini in August 2005 that he would become involved with WTL. WTL's business model was changed and an FCIB account was opened in August 2005.

98. Mr Kohli became a director of WIE on 25 May 2006. An FCIB account was opened for that entity on 8 May 2006 and the company changed its business from trading shoes to trading mobile phones after 28 April 2006.

99. SGL was set up in 2004 and Mr Kohli had always been its sole director. It was set up to deal in telecommunications.

100. Mr Kohli described the role of each of the Appellants in these transactions as a broker and said that they were not in a position to import goods directly from Europe themselves and that was why an intermediary was used. They would not have got such a good price if they had attempted to deal directly with European suppliers.

Dealing with HMRC

101. Counter to what HMRC suggested, Mr Kohli said that the Appellants had provided HMRC with what they said they required by way of documentation and pointed out that much of the delay in moving the issues forward was as a result of delays at HMRC's end. For example, documents had been provided to Mrs Tressler for WIE in February 2007 but no response had been received until June that year. Similarly for SGL there had been a significant delay in communications with HMRC from September 2006 until July 2007.

Documentation

102. According to Mr Kohli much of his dealing on behalf of the Appellant companies was done by telephone, hence the lack of documentation to provide to HMRC, including a lack of detailed terms and conditions. Mr Kohli said that he did have terms and conditions for his suppliers and this is where he thought the risk of fraud was. Mr Kohli accepted that there was some lack of detail on purchase orders from the Appellants' EU customers. Mr Kohli said that he did not keep records of how suppliers and customers were contacted. Terms and conditions were discussed in meetings and by phone.

103. In Mr Kohli's view, the fact that the phones dealt in by the Appellants were not appropriate for the UK market should not be taken as significant. The role of the Appellants in these deals was that of a broker, who just wanted to make money. It was not relevant to the broker what type of phones were imported; if a customer wanted them, the Appellant would buy them in order to make a deal. At the end of the day the Appellants were exporting to the EU which explained the need for EU specification phones. Mr Kohli said *"if our customers want a particular type of specification of phone and we can source and make a profit, and it is a free market, there is nothing incorrect with it"*. He explained that there was a price arbitrage to be made by importing US phones because these could easily be adapted for the EU market with the purchase of a different adapter.

104. Mr Kohli explained that he ensured that his sales and purchase orders matched by either decreasing demand or increasing the available quantity of phones. There was no evidence of this aspect of the transactions because this would have been done by telephone. In response to HMRC's comments about the lack of details contained in his purchase orders with his customers he said that he did not consider it his role to vet the documents provided by his purchasers. If the purchase documents were not precise, that was his purchaser's problem, not his.

105. Mr Kohli stressed that his purchase orders from his UK suppliers did contain details of phone specifications and other details which he described as comprehensive and indicative of the Appellants acting as diligent companies knowing that the most important thing was to ensure the integrity of their supply chain in the UK.

Due diligence

106. Mr Kohli defended the amount of due diligence which was carried out on his UK suppliers, saying that he was buying from them, not offering them credit, so he was not concerned about credit risk. While the documents which he relied on (such as utility bills) might not have been for large amounts of money, their purpose was to validate the identity and address of the company and they were sufficient for that. As long as he had control of the stock which he was buying and selling, he was merely taking a risk on the insurance and freight costs of the goods, which he was happy to do.

107. Mr Kohli pointed out that HMRC were well aware of the due diligence which the Appellants were carrying out and had not raised any issues with the level of due diligence done, in fact SGL had been complimented by HMRC on its due diligence. He referred to a number of entities on which due diligence had been carried out, including Redhill checks, and with whom the Appellants had decided not to deal as a result, such as Muggles.

108. Mr Kohli referred to the Redhill check carried out for SGL's deal 1, which was carried out on 11 May, the date when the deal was entered into. In his view it was perfectly legitimate for him to rely on this and expect HMRC to notify him if there were any issues with the company he was dealing with. The Appellants used National Advice Service ("NAS") checks done on the day of the transaction as a check against the Redhill verifications.

109. Mr Kohli also gave details of the due diligence done on Kensai, including attempting to obtain references from freight forwarders, accountants and Kensai's bank. He also met Mr Butt, director of Kensai. Mr Kohli pointed out a number of instances in which HMRC had omitted documents from their list of due diligence material which he said existed, for example in SGL's deal 1, the instructions given by SGL to Verify Inspections and the insurance certificate and instructions were missing from HMRC's deal pack.

110. In response to HMRC's suggestion that little due diligence was done on the Appellants' freight forwarders, Mr Kohli insisted that he did do physical inspections at freight forwarders. He confirmed that he had visited the freight forwarder ASC's premises. He said that he did not consider it his role to carry out due diligence on his customers' freight forwarders in Europe; it was their obligation to undertake that due diligence. He had attempted to obtain due diligence documentation from both Global and ASC but had not received any response to his enquiries.

111. Mr Kohli made clear that the Appellants did not care where stock was held. Wherever it was held the Appellants would have control of the stock at the freight forwarders when it was held in a "cage", designated for holding the goods of that Appellant, operating in a way similar to a "nostro account" at a clearing bank.

112. He explained that in the normal process two inspections were done when goods were held at a freight forwarder; one on behalf of the seller and one by the freight forwarder itself and HMRC's evidence on this was confused. Mr Kohli also explained the reference in the Appellants' purchase orders to "no IMEI" numbers and "no labels" on pallets (which he said referred to the shrink wrapped pallets themselves not to labels on the individual boxes of phones).

113. Mr Kohli spent some time responding to HMRC's suggestion that CMR documentation or Eurotunnel tickets were fraudulent (for WTL deal 12). Concerning the amount of time taken to travel from Dover to Heathrow and back and Eurotunnel ticket times; he proffered several alternative explanations for the apparent discrepancy in the timings; an incorrect vehicle registration number was entered onto the CMR, a lorry broke down and was replaced with a different one, the wrong trailer attached to

the lorry, or a different trailer was used to take the goods to France. In his view HMRC had ignored obvious explanations and were suggesting that Eurotunnel had been involved in creating false documents which was not credible. This was a good example of HMRC twisting documentation to fit into their interpretation of the facts. There was no independent evidence to suggest that the Eurotunnel document was false.

114. Mr Kohli was clear that credit was not given by the Appellants to their customers; in no circumstances would goods be released prior to payment. Their terms were that payment had to be made by customers after inspection at their freight forwarder. That meant that the only risks which the Appellants carried were the costs of shipping and insurance. If the customer did not pay when the goods were delivered, they would simply be recalled. He also said that the Appellants did not receive credit from their suppliers, the suppliers merely allowed the Appellants to move goods "on hold", until and unless the Appellants paid for the goods, they would not be released to the Appellants. Since he was not giving credit to his customers, he was not overly concerned with due diligence reports which suggested that customers were a high credit risk.

Knowledge of fraud

115. Mr Kohli accepted that from the information which had been supplied to the Appellants by HMRC they, through him and the other directors, did have a general awareness of fraud in the mobile phone market. However he was adamant that the Appellants did not have specific knowledge that the deals which HMRC were disputing were connected with fraud.

Insurance

116. The insurance entered into with TransPacific was described by Mr Kohli as it was by Mr Ibrahim as a "credit based insurance policy".

We also considered some additional brief Appellant witness statements but were informed that none of the Appellants' witnesses other than Mr Kohli were available to give oral evidence to the Tribunal.

Mr Tejbir Maini

117. Mr Maini was a director of WTL and WIE. Mr Maini provided two witness statements both undated, one in relation to WTL and one in relation to WIE. In response to the HMRC's request that Mr Maini be made available in the absence of Mr Kohli, we were told that it was not feasible for Mr Maini to give evidence.

118. Mr Maini supported Mr Kohli's accounts of his meetings with HMRC to discuss WIE and WTL, saying that information had been provided as requested by HMRC. He also told us that it was he who carried out due diligence on WTL's client Monza, visiting their offices in Milan in December 2005. He stressed that HMRC had complimented the companies on the due diligence which they were carrying out.

119. Mr Maini told us something about the way in which WIE became involved in the mobile phone trade;

> *"Only a few deals were entered into selling shoes. Then in early May 2006, Mr Kohli, who knew of the company, asked if he could use it for mobile phone trading. As WTL was doing well and had recently received a payment of VAT credits, it was agreed that the business activity of the company [WIE] would be changed"*

120. Mr Maini said that WIE undertook NAS clearances for every deal entered into. In response to HMRC's points about Mr Bateman and doubts about his links with Poland, Mr Maini said that WIE had no reason to suspect that Mr Bateman was not based in Poland, all phone calls and faxes with him were through a Polish number.

Mr Azeem Ibrahim

121. We were told that Mr Ibrahim was abroad and could not be contacted to give oral evidence to the Tribunal. Mr Ibrahim was the director of the entity providing insurance to each of the Appellant companies for the disputed deals, TransPacific. He provided a witness statement dated 22 October 2009. He told us that TransPacific was regulated by the authorities in Anjouan. It had been made clear to all of the Appellants that the insurance contracts provided were "credit based". Clients would usually be given 14 or even 30 days to pay. TransPacific would issue special dispensations against their standard requirements, if, as here, it had carried out background checks on the clients. Mr Ibrahim told us that contrary to what was said by HMRC, Mr Bateman was not a director of TransPacific, but had provided the website used by them.

HMRC's arguments

122. In order to deny the Appellants' input tax for the periods under appeal HMRC has to demonstrate that (i) a tax loss has arisen (ii) that tax loss resulted from the fraudulent evasion of VAT (iii) the Appellants' deals were connected with that fraudulent evasion (iv) the Appellants knew or should have known that each of the 52 disputed deals were so connected.

123. HMRC pointed out that the overall VAT input tax claim amounted to £12.7 million claimed by the three Appellants all of which Mr Kohli is a director of. Mr Kohli's knowledge could therefore be treated as the knowledge of the three Appellant companies.

124. Despite the statements made by the Appellants' advisers that all issues were disputed, the only aspect of HMRC's case not effectively accepted by the Appellants is whether they knew or should have known that the disputed transactions were connected with fraud. Ms Malcolm pointed out that the Appellants had not challenged HMRC's evidence on any of issues (i), (ii) or (iii).

125. Despite what was said by Mr Kohli, Ms Malcolm stressed that HMRC need only to establish to the civil standard of proof that each of the Appellants, acting through Mr Kohli, knew or should have known that each of these transactions was connected with fraud. HMRC's primary case is that the Appellants were each knowingly part of a fraudulent scheme, their secondary case is that the Appellants, acting through their director Mr Kohli, should have known that each of these 52 disputed transactions was connected with fraudulent evasion.

Tax losses linked to fraud

126. That tax losses had arisen was demonstrated by the fact that all 52 deals had been traced back by HMRC to the same three defaulting traders, Only Quality, Steven Ellison and Woodworks via three contra-traders; Globalex, Kensai and Worldwide. All three of the defaulting companies had been compulsorily wound up and VAT assessments totally £294 million had been made against them, none of which had been paid.

127. There was ample evidence of fraud carried out by each of the three defaulters on the evidence provided by the relevant HMRC officers; all had been involved in similar patterns of trading which included making third party payments; all had significantly changed the nature of their business and the level of their turn over since initial registration and submission of their VAT1. Only Quality had made no VAT returns and its company officials had criminal convictions for dishonesty; Steven Ellison claimed to be producing aircraft wings from a council estate and had generated a turnover of £400 million in 18 days; Woodworks was stated to be a cabinet maker but had had its VAT registration cancelled and an assessment of £84 million of VAT after it had failed to make any VAT returns.

128. All of these defaults by the three defaulting entities were attributable to fraud, and were linked to contra-traders Kensai, Globalex and Worldwide in the "dirty chain" with CPUs being sold via UK buffers to those three entities. On the basis of the evidence of officers Mendes and Humphries, all of Worldwide, Globalex and Kensai, having originally registered for VAT and given turnover estimates of less than £250 thousand had actually achieved turnover of more than £1 billion up to 2006 through trades in CPUs which could be traced back to the three defaulters, while accounting for only a small amount of VAT in the UK on the difference between their input and output VAT, which was carefully balanced.

129. HMRC argued that the contra-traders' offsetting input and output tax created the connection between the Appellants' deals and the fraudulent defaulters higher up the chain. The fact that the contra-traders bought and sold CPUs but the Appellants bought and sold mobile phones is not relevant. Nor is it relevant whether the Appellants knew specific details about the clean and dirty chains of which their deals formed part. This was made clear by Briggs J in the *Megtian* case:

> "*There are likely to be many cases in which facts about the transaction known to the broker are sufficient for it to be said that the broker ought to have known that his trade is connected with a tax fraud; without it having to be, or even*

being possible for it to be demonstrated precisely which aspects of a sophisticated multifaceted fraud he would have discovered had he made reasonable enquiries" [*Megtian Limited (in administration) v HMRC* [2010] EWHC 18 (Ch)].

130. The Appellants' transactions were connected with these fraudulent deals as demonstrated by the deal packs provided by HMRC's officers for each of WTL, SGL and WIE. It was not necessary for HMRC to show that any of WTL, WIE or SGL dealt directly with one of the defaulting traders, but only that their deals were connected through a chain of transactions. The deal packs provided for each of the 52 deals by HMRC's officers show an actual connection with the defaulters via the contra-traders and the Appellants have produced no real challenge to this evidence.

131. Ms Malcolm stated that it must be more than coincidental that all of the 52 disputed transactions could be traced to tax losses made by three fraudulent traders (Only Quality, Woodworks and Steven Ellison) and three contra-traders (Globalex, Kensai and Worldwide). All of these deals were interconnected; e.g. in all 52 deals a standard mark up of 40p is made by each contra trader. As stated by Clarke J in *Red 12 Trading Limited* v *HMRC* ([2009] EWHC 2563(Ch)) *"a trader could legitimately think it unlikely that the fact that all 46 transactions in issue can be traced back to tax losses by HMRC is a result of innocent coincidence"*. It is not necessary for HMRC to establish that the Appellant knew or should have known the precise nature of the fraud.

Evidence of orchestration

132. HMRC pointed out that none of the deals done by any of the Appellant companies could be traced back to an authorised distributor or manufacturer or forward to a legitimate retailer or end user, despite the fact than an estimated addition of £9 million has been added to the cost of the phones as a result of them being put through the UK for just the month in question. There was no evidence that there was a single legitimate sale of a Nokia 8801 in the whole of Europe during May and June 2006; they were not in general commercial circulation in Europe at this time. However, several (10) of the Appellants' deals were with this model of phone.

133. The clean and dirty chains of which the Appellants' deals were part were heavily engineered; happening within very short time periods and through the same IP address and the Appellants' deals fitted into this framework; they were contrived and connected.

134. Ms Malcolm stressed that the Appellants had not dealt directly with significant aspects of HMRC's case; including the FCIB evidence which suggested either that (i) the Appellants were knowing participants or (ii) if they did not know about the whole structure, they knew about their part in it (iii) if they did not know about anything other than their own deals, they must have been directed very specifically who to buy and sell from or (iv) it was coincidence that the Appellants were able to conclude exactly the right transactions on 52 occasions which fitted within the overall structure precisely.

135. It is telling according to HMRC, that the Appellants did not, in any of these 52 deals, make a sale outside the contra-trading framework of buyers and sellers and always did their deals within the small time window which allowed the rest of the chains to operate correctly, despite the fact that there was no time for payment stipulated in their deal documentation; the Appellants must at least have known that they needed to undertake their part of each of the deals in a particular way at a particular time, (e.g. Deal 1 for SGL in which all components were completed between 8.21 am and 9.06 am).

136. The deals entered into made a non-commercial profit of £8,371,798 over 14 days for 52 deals. The level of profit available should have suggested a non-legitimate source for the deals. The deals represented such a large profit for such small companies with so little resource that they cannot have been commercially realistic. The Appellants had no capital to support large deals of this size but did not question why they were being entrusted with such valuable stock with no upfront payment. No deals ever went wrong.

137. The lack of commerciality in the mobile phone chains is evidence of the connection between these clean chains and the dirty CPU chains; there is no commercial explanation for these transactions at all other than to hide the fraud and distance the VAT reclaims from the dirty chains. Other aspects of the structure of these deals was non-commercial, for example SGL sold to customers in France, Poland and Spain but goods were physically delivered to Germany (for the French and Polish customers) and France (for the Spanish customer).

138. The stock bought and sold in each of the 52 deals were EU and US phones, which would not be sold in the UK and which there was no reason to import into the UK. (e.g. Nokia 8801).

139. This is supported by the FCIB evidence for which HMRC used deal 1 of SGL as an example. In this deal the cash started and finished with the same company, Finasol. The goods followed the money. All payments were made between 08.21 and 09.06 on 24 May. EB numbers for the bank transfers were incredibly close chronologically; in HMRC's view this was evidence of contrivance, suggesting either that the EB numbers are pre-booked or at least very closely co-ordinated indicating orchestration and knowledge of the order in which payments were to be made. All payments were made from the same IP address other than SGL's.

140. HMRC said that these deals could only work on the basis that SGL bought from and sold to a set person; otherwise the chain would be broken. Either Mr Kohli knew about each of these stages or, at least, he was making payments on the basis of instructions and he was willing to do this because he knew that these payments were part of a dishonest scheme.

141. HMRC pointed out that there was a shortfall in the payment which SGL had to make for this deal. It received £1.396m but had to pay out £1.466m; this gap was closed by an intercompany loan from another company controlled by Mr Kohli, Freeview Properties Limited. There was no legitimate business reason for this loan to

have been made. This was the money which was used to pay the VAT due by SGL. The same company made funds available to WTL for its VAT payments in June 2006.

Lack of due diligence

142. In HMRC's view the Appellants' due diligence was poor or non-existent despite the very large sums of money involved. There was a lack of clarity about who actually owned the goods at any point in the transaction chain. There was no evidence of any written documentation between the parties dealt with by the Appellants as either buyers or sellers. Existing invoices and terms and conditions (with suppliers) were deficient. Only one due diligence file had been produced for all 6 suppliers and customers by SGL. The checks which were done on customers were not appropriate for the levels of payment being made; for example sales of £12.4 million were made to Bleu Opale based on a letter from that company's French accountant stating that he was looking forward to doing business with Bleu Opale. The Appellants seemed to pay no attention to the risks of passing high value phones to customers on whom they had done very little financial due diligence through freight forwarders over whom they had little control.

143. Although the goods were insured this was not with a well recognised company (TransPacific in Anjouan) and the terms of the contract included non-commercial waivers of the standard policy. There was no evidence that Mr Kohli made any checks on TransPacific before he dealt with them and failed to comply with any of the standard terms of its insurance document.

144. Ms Malcolm suggested that when considering the due diligence undertaken by these Appellants the Tribunal should look at all the circumstances of the case and not focus unduly on what due diligence was or could have been done in each case.

Discrepancies in documentation

145. HMRC pointed out that the freight forwarders could not produce CMRs and that in some instances the vehicles on which the goods were supposed to be transported did not have sufficient capacity to carry all of the pallets which would have been required. There was also a significant discrepancy in some of the documentation produced by the freight forwarders; for example on 28 June goods were said to be collected in vehicle GK52KYE. This vehicle checked in at Eurotunnel Folkestone at 21.37 UK time. It was recorded as leaving Dunkirk at 20.00 French time on a ferry to Dover. Assuming it would have docked in Dover 21.00 UK time, it is impossible for it to have got to Heathrow, loaded with 11 pallets of Nokia 8800 phones and back to Eurotunnel by 21.37 UK time. There must be some inaccuracy in these transport documents.

146. HMRC also suggested that one of the French freight forwarders used in these transactions, TCF Logistique, did not trade and was registered at a residential address in Paris with a director who was a Czech national.

147. HMRC concentrated on deal 1 carried out by SGL which was used as an example of all of the trades, which were said to be very similar to this one. Deal 1

was invoiced on 11 May 2006. An EU supplier, Muggles, sold to Globalex in the UK who sold to SGL. SGL on sold to Bleu Opale in the EU.

The following document shortcomings were pointed out by HMRC;

(i) The purchase order between the suppliers further up the chain, to Muggles from Globalex, included only very limited terms and conditions and provided no details of the phone type required.

(ii) Release instructions were given from Muggles to ASC (freight forwarder) to release to Globalex in UK. It was not clear from these documents where the goods actually were at this stage.

(iii) The purchase order from SGL to Globalex, given at 5.05pm on 11 May did contain more details of the phones required; central European specification, multi-lingual manual, lithium batteries, two pin stock and the requirement that "all pallets to be neutral for labels". It was not clear why European specification phones would have been required by a UK based trader. The requirement to have pallets free of labels suggested that the Appellant wanted to make sure that these goods had not previously been checked by Customs. There was also a requirement that the phones be delivered on 11 May, despite the fact that these instructions were sent very close to the end of business hours on the 11th.

(iv) SGL's terms and conditions asked for confirmation of full legal title, confirmation that inspection of the goods had been carried out and confirmation that due diligence checks had been done on the supplier. However, it was not clear how full legal title could be confirmed in the absence of clear terms and conditions or of payment for the goods. Nor was it clear how full inspection could be carried out at this time of the day (late in the afternoon on 11 May) if the goods had been shipped from Belgium

(v) Payment was not made through SGL's FCIB account until 24 May, many days after the invoices were issued.

(vi) The purchase order from Bleu Opale dated 11 May was for shipping to Germany (to Stolz). A profit of £37 per phone was made on the basis of the sale price to Bleu Opale but there was no evidence of any negotiation about this. No specific delivery terms were provided, all that was known was the destination.

(vii) There was a request for inspection from SGL to ASC the freight forwarder, plus a request to "ship on hold" and do not release until release note faxed. The inspection report of 12 May by Verify Inspections demonstrated that only one box of phones was actually checked despite the request for a full count and check of the stock.

(viii) SGL sent its release note to ASC on 24 May, this was the date of payment, not the date when the stock was released, which was earlier, on the 16 May (when the phones were delivered to Stolz in Germany).

Communications with HMRC

148. HMRC also referred to the Appellants' lack of co-operation with HMRC, mainly through Mr Kohli and Mr Kohli's lack of honesty in another claim, namely the false VAT invoice for an office carpet; which they suggested indicated the character of Mr Kohli. He had lied to HMRC about a VAT reclaim for an office carpet which he said had been fitted at SGL's principal place of business in Coventry. When HMRC asked to see the office carpet to which the claim related they were shown a tatty carpet which did not look as if it had been recently bought. It transpired that the carpet for which input tax had been reclaimed had actually been fitted at Mr Kohli's home address in London. Mr Kohli had produced a false invoice for this carpet which was clearly not an office expense.

Grey market trading

149. In reliance on the expert evidence of Mr Corkery, HMRC suggested that the Appellants' deals showed none of the features which were common to the grey market in mobile phones. There was no evidence of any value which had been added by the Appellants in any of these deals, in particular given the type of handsets dealt in (mainly Nokia) which were not generally susceptible to price driven arbitrage. Nor was there evidence that the Appellants had been involved in box breaking or that they were profiting from short term volume shortages in the mobile phone market. The characteristics of the Appellants' trades made it very unlikely that they were trading in the legitimate grey market.

Conclusion

150. The Appellants (through Mr Kohli) had chosen to ignore obvious inferences from the facts and circumstances in which they were trading and knew or should have known that their transactions were connected with fraud

Appellants' Arguments

151. Mr Kohli stressed that it was for HMRC to prove their case beyond the ordinary balance of probabilities, the standard of proof in this case being "the heightened civil proof". He said that HMRC had not presented a fair view of the case; the sample deals which they relied on had incomplete documents and produced a skewed view of the transactions.

Tax losses linked to fraud

152. In the Appellants' view HMRC have not proved their case; in particular that the Appellants knew at the relevant time that their deals were connected to fraud. HMRC were applying a retrospective test by reference to what their officers have established after considerable time and employing considerable resources. HMRC's evidence had not made clear when the fraud which they say the Appellants' deals were connected to occurred, in particular it had not been made clear that the fraud had been carried out before the Appellants had entered into their deals.

153. The test of knowledge is at the time when the transactions were carried out; the Appellants had no actual knowledge of the fraud at this time and could not have known at the time that they were connected to fraud. No reasonable person could have known at the time what HMRC are now arguing. The Appellants had no knowledge of the wider framework of these transactions, they only had knowledge of the deals in which they were involved. The Appellants knew nothing about the contra-trades with CPUs; they were completely separate deals. The Appellants knew nothing about the defaulting traders; they did not deal directly with any of them.

154. In order to deny the Appellants' input tax HMRC have to demonstrate more than the Appellants' general, unspecified awareness of fraud, they have to demonstrate actual participation by the Appellants in the fraud.

Documentation

155. Mr Kohli explained that all of the Appellants' dealing was done by phone and that is why no written evidence could be provided to HMRC. Just because deals were done on a back to back basis did not make them fraudulent. A lack of commerciality also does not indicate fraud. A lack of contractual documents does not necessarily mean that the deals were contrived.

156. The Appellants' purchase orders to their suppliers did contain detailed specifications of the phones to be purchased and included on the back terms and conditions which had to be signed by the supplier before a deal would be agreed.

157. HMRC's points about the Appellants not having ownership or control of the goods are incorrect; the Appellants did have control of the goods at the freight forwarders and had control under the "ship on hold" process.

Orchestration

158. Mr Kohli described the Appellants as acting as brokers who had no need to establish what it was that the end customer required. Their job was to match trades. The fact that the goods were not suitable for sale in the UK was irrelevant. The stock acquired by the Appellants had been pre-sold and so they were taking no risk on movements in market price. The fact that there were no sales to retail customers reflected the nature of the Appellants' broker role in what Mr Kohli referred to as the grey or parallel market.

159. The fact that the Appellants' payments came from a different IP address than all the other payments in each of the clean and dirty chains demonstrates their innocence. This could not have been an intentional ploy since this significance of the IP addresses in fraudulent chains of dealing was not known until several years later.

Due diligence

160. Mr Kohli's arguments concentrated on pointing out gaps in HMRC's lists of due diligence documents which had been provided and responding to detailed specific points made by HMRC. He did not consider the bigger picture of the level of due

diligence done by each of the Appellants for each of their suppliers and customers or attempt to draw any conclusions from this.

161. Mr Kohli said that HMRC had made repayments to the Appellants in the same year, despite now claiming that those suppliers to which the repayments relate are contra-traders. HMRC did not point out to the Appellants what they should have done in addition to avoid being involved in fraud; in fact HMRC's site visits suggested to the Appellants that nothing further was required

162. The Appellants had done due diligence in the form of obtaining Redhill clearances by telephone at the time of all actual trades carried out. They had also employed a third party firm, the Due Diligence Exchange, in the person of Mr Vincent Curley, to carry out commercial checks for them.

163. Mr Kohli said that the Appellants had considered recording IMEI numbers but had concluded that this was both expensive and risky; he was aware of HMRC challenging IMEI numbers as being incorrect.

164. The Appellants also made a number of detailed points concerning allegations of fraud made by HMRC which they said had not been proven and to which they had not had the opportunity to respond. (i) In WTL's deal 12, the alleged discrepancies in the ferry docket times and the freight forwarder's journey time; HMRC had ignored obvious explanations for this, (ii) Mr Mendes evidence which the Appellants did not get an opportunity to cross-examine and (iii) the deal chains evidenced by HMRC were disputed but as a result of Mr Kohli's ill health the Appellants have been prevented from making their arguments on these issues.

HMRC's administration – Discrimination and disproportionality

165. It is the Appellants' view that HMRC intentionally delayed issuing decision notices in an attempt to force the Appellants out of business and stop the appeals. HMRC delayed their decision process by asking for documents in a piecemeal fashion. HMRC were disingenuous and inconsistent between officers and were actually employing a blanket delaying strategy. HMRC were careless and inefficient.

166. It is unlawful for HMRC to penalise these Appellants and not penalise other traders; this is disproportionate and contrary to the fundamental principles of European law, that taxpayers should have legal certainty, the principle of neutrality and Human Rights. There was no basis on which HMRC could take account of a separate chain of transactions when determining the fiscal consequences of the Appellants' own deals.

Facts Found

167. On the basis of the evidence provided to the Tribunal we make the following findings of fact:

168. The trading history of each of the Appellant companies suggest a significant change in nature and profitability of each of their businesses leading up to and including the periods for which input tax is in dispute. All three entities achieved a significant increase in turnover and a consistently high margin was made on all 52 deals with very little resource. We saw no evidence that any of the Appellants employed large numbers of staff.

169. The change of business model by WIE and WTL, their move into the mobile phone business and the opening by those two companies of an FCIB bank account coincided with Mr Kohli becoming a director of those companies.

170. Each of the Appellants had a history of contact with HMRC before and during these investigations and had knowledge of fraud in the mobile phone market and were aware of the levels of due diligence required in order to guard against being unwittingly involved in these fraudulent activities including the guidance set out in Notice 726.

171. Mr Kohli had knowledge of this industry prior to his involvement with these Appellants, particularly through his family's trading history with Stonegalleon Plc.

172. All of the deals for which input tax is in dispute were carried out within short time frames and with very similar patterns of dealing, involving a small number of counterparties as both buyers and sellers.

173. The Appellants provided no evidence of deal failures or over or under supply of goods; all of the transactions in question neatly matched buyers and sellers.

174. The Appellants provided no evidence of the commercial negotiations which formed the basis of a single one of these 52 transactions.

175. The profit margins obtained by the Appellants on each of the transactions were consistently in the region of 10%, significantly higher than the margins made by other participants in the chain. The profit margins were consistent even when the purchase price of a particular phone model changed.

176. The documentation which supported each of these transactions was brief and formulaic despite the high value of the transactions undertaken. The goods were sold on ship on hold terms but the basis on which title to goods passed was not clear.

177. The technical specification of the phones bought and sold meant that they could not realistically be sold to users in the UK or even in some cases in the European market without alteration.

178. The Appellants' pattern of dealing did not match the patterns of dealing described by Mr Corkery as common in the "grey market".

179. Redhill checks were carried out on sellers and purchasers on the date when invoices were issued for each of the 52 deals.

180. The goods were insured but the insurance terms were not market standard and the insurer was not a well recognised insurance company.

181. IMEI numbers were not recorded for the phones bought and sold by the Appellants.

182. The level of due diligence done on customers to whom valuable goods were sent was minimal and sometimes after transactions had taken place.

183. Mr Kohli's dealings with HMRC in his capacity as a director of each of the Appellants were non-co-operative.

Decision

184. The Appellants' main defence is (i) they only knew about the deals that they were involved in and (ii) they should not be judged with hindsight, they could only be expected to know what was apparent at the time. As a secondary argument they suggest that HMRC have not acted properly, both in disproportionately penalising these Appellants and in intentionally delaying the investigation process. In addition they raise some detailed points about some aspects of the documents which support the fraudulent chains which make up HMRC's case. They stress, correctly, that it is for HMRC to prove its case here and suggest that it has not done so.

185. In order to succeed, HMRC need to demonstrate to the ordinary standard of civil proof, that in relation to each of the transactions for which the Appellants make a claim for input tax (i) there was a tax loss (ii) the tax loss resulted from fraudulent evasion (iii) each of the Appellants' transactions was connected to that fraudulent evasion and (iv) the Appellants, acting through Mr Kohli, knew or should have known of that connection.

Tax losses connected with fraud

186. The Appellants' main arguments were based upon their lack of knowledge of either the contra-traders or the fraudulent tax chains produced by HMRC. As a matter of logic it therefore seems difficult for the Appellants to contest any elements of this evidence from HMRC and the Appellants did not put forward a positive case to dispute any of issues (i), (ii) or (iii) before the Tribunal or in any written submissions. However, the Appellants did contest HMRC's conclusions on some specific points in relation to issues (i), (ii) and (iii) and we have considered those objections leaving aside that larger conclusion.

187. The rather unusual circumstances of the case and in particular the lack of any representation for the Appellants for most of the hearing before the Tribunal led HMRC to resist a direction reflecting the *Fairford* decision [*HMRC v Fairford Group plc (in liquidation)* [2014] UKUT 329] that HMRC's evidence should be taken as not contested unless the Appellants produced substantive arguments to oppose that evidence.

188. Having examined the evidence provided by HMRC's witnesses relating to the tax losses and the very detailed tracing exercising undertaken by HMRC, the Tribunal had no real doubt that each of the 52 disputed transactions can be traced back to one of Only Quality, Woodworks and Steven Ellison and that each of those entities had defaulted on significant amounts of VAT giving rise to a VAT loss.

189. HMRC's witness evidence including the evidence of officers Humphries and Mendes in particular was not challenged by the Appellants and in the Tribunal's view establishes, on the balance of probabilities, that each of the transactions in which the Appellants were involved as a broker could be linked to transactions which were connected with fraud through the contra-traders dealt with consistently by the three Appellants; Kensai, Globalex and Worldwide. The FCIB evidence demonstrates control of payment flows between a small number of connected parties while the inclusion of payments from the third party entity, Freeview Properties Limited is also telling.

190. The FCIB evidence of Mr Humphries and Mr Mendes also demonstrates that the deals in which the Appellants were involved were carried out in very narrow time windows, with large numbers of payments, including the Appellants' purchase and sale payments, being made in very quick succession, despite the fact that the documents relating to the Appellants' deals made no suggestion that payment had to be made on a particular day, let alone at a particular time. We agree with HMRC that this demonstrates that the Appellants' deals were linked with the other payments (and transactions) in the fraudulent chains of transactions as part of an orchestrated scheme to defraud HMRC.

191. The Tribunal agrees with HMRC that it is not relevant to this question whether the Appellants, through Mr Kohli or anyone else, were aware at the time of their transactions of the specific details of the fraudulent transactions at the level of the defaulters and contra-traders or of the details of the chains which linked the defaulters, the contra-traders and the Appellants. Nor is it necessary to show that the fraud in question occurred before the Appellants' deals were carried out; this is made clear by the *Fonecomp* decision. It is only necessary for HMRC to demonstrate by reference to what the Appellants did know at the time, that they knew or should have known that the disputed transactions were connected with fraud "*that had occurred or will occur, at some point in some transaction to which his transaction is connected*". Arden LJ para [51] *Fonecomp.*

Knew or should have known

192. The Appellants say that HMRC has no direct proof that the Appellants knew about the whole of the defaulting trader and contra-trading structure; evidence on this is circumstantial going to the part which the Appellants played in the "engineered" framework. They argue that the evidence is not sufficient to suggest that the Appellants did know about the wider context of trades. However, it is not necessary for HMRC's case to succeed that the Appellants can be demonstrated to have known about this wider context, it is only necessary to demonstrate that they knew or should have known that their own deals were connected with fraud. Nor is it necessary for

HMRC to demonstrate that the Appellants knew all the details which have only subsequently been established by HMRC. If this was not clear on the basis of the *Kittel* decision it was made clear in the *Fonecomp* decision.

193. While Mr Kohli on behalf of the Appellants made numerous detailed criticisms of HMRC's case he did not, in our view, at any stage properly meet the central challenge of explaining a commercial rational for these transactions or how he was able to satisfy himself that they were not connected with fraud.

194. In considering whether the Appellants knew or should have known that their deals were connected with fraud we have taken account only of what was known at the time by the Appellants, or Mr Kohli on their behalf, about the Appellants' own deals and what the Appellants knew about the market; (i) they knew that this market was liable to fraud (ii) and these deals had some features which were distinctive and would have been clearly apparent to the Appellants; these deals were generating very large profits; they were being done in a very short time frame; the goods which were the subject of these deals were not for consumption in the UK (or in some cases, the EU). What reasonable explanation could the Appellants have considered there was for the way these deals were being structured?

195. The Appellants refer to aspects of the deals from which they say they derived comfort: (i) that Redhill clearances had been given, (ii) that the suppliers had not been investigated by HMRC to date, (iii) that HMRC had not suggested that further due diligence was required and in fact had been complimentary about the due diligence which was being done.

196. Even in the light of those factors, our view is that there were a number of salient features of these deals which pointed in quite another direction and which no reasonable person would have accepted without question and without undertaking significantly more due diligence that the Appellants did, unless they knew that these deals were connected with fraud. Mr Kohli's willingness to turn a blind eye to these features can only, in our view, be because he knew that each of these transactions undertaken by the Appellants was connected with fraud.

197. In order of significance, our view is that no businessman would have accepted that deals could be done in such a short time frame and with consistently similar counterparties and sustaining consistent margins without wondering if there was something unusual going on; the Appellants seemed to be able to locate buyers and sellers who were prepared to do deals with them in a very straightforward way, for exactly the right amount of stock, in timeframes which were more akin to dealing times in a regulated global financial market with significant volume of supply and demand, than to an intermediary dealing in an off-market, retail product such as mobile phones.

198. The profit margins which were generated by the Appellants' sales were remarkably consistent, and did not exhibit the sort of volatility which might be associated with the need to efficiently match buyers and sellers which Mr Kohli suggested was how his deals were driven. For example WTL deals 1, 7 and 9 were all

for the same make of phone; the Nokia 8800. These were all done within 6 days of each other. The price paid for the phones by WTL however increased significantly from 20 June to 26 June, from £369 per phone to £585 per phone. Despite this price change, WTL was still able to sell its Nokia 8800s at a 10% profit on the same day. There is no evidence that Mr Kohli considered that this was odd, though most people would have found it so. On the contrary, Mr Kohli defended this pattern of dealing to us, saying that his only concern was to match buyers and sellers to make a profit and that he did not consider the pattern of dealing to be odd at all, without giving a convincing explanation of why he did not consider the transactions unusual.

199. Second, Mr Kohli on behalf of the Appellants, aware of this unusual dealing framework, nevertheless had a remarkably cavalier attitude to the custodianship of the goods which he was selling. The speed and manner in which the goods were bought and sold suggested, at best, a sophisticated dealing system with significant sums of money changing hands. In those circumstances most businessmen might have thought that they needed to take extra care to ensure that their transactions were watertight. That was not Mr Kohli's attitude; we heard from HMRC's witnesses that his standard of documentation and level of due diligence on the parties with whom he was prepared to do business worth very significant sums of money, was basic, often after the fact and sometimes non-existent. To exhibit this degree of carelessness in transactions of this value demands some explanation. Mr Kohli's only explanation was that many aspects of these deals were dealt with by telephone and that a lack of documentation and back to back dealing does not necessarily suggest that these deals are fraudulent.

200. We agree that poor documentation and back to back deal structures could have an explanation other than fraud, but that is much less plausible, if plausible at all, when account is taken of the fact that Mr Kohli was dealing in a market which was known by him, and had been notified to the Appellants by HMRC, to be a source of fraudulent transactions. What businessman in their senses could possibly have decided in that market that he would take such a laissez-faire and sporadic attitude to due diligence and risk management? Goods, whose whereabouts and existence was often not known, were insured on unusual terms with a small insurer based outside the UK, with payment not backed up by clear terms and conditions and no certainty of when title passed.

201. The only explanation why a businessman in Mr Kohli's position with the knowledge that Mr Kohli had could possibly have been persuaded to approach his counterparties in this way is if he knew that there was no real commercial risk in the trades at all because they were part of a fraudulent chain of transactions.

202. Mr Kohli's suggestion that he knew nothing about the deals to which the Appellants were not themselves parties, nothing about the tax losses and nothing about the contra-trading chains which are post hoc constructs by HMRC does not help him; HMRC do not need to demonstrate that Mr Kohli knew anything about the details of those chains or the precise nature of the tax losses, but only that the nature of the transactions which the Appellants were actually involved in must have

indicated, at the time when they were entered into, that they could only be driven by fraud.

203. All businessmen are susceptible to making a quick profit, but most would accept that the opportunity of making a sudden and unexpected profit from a particular type of transaction does not come up very often; in most markets the opportunity will disappear as soon as other people start to participate in the same opportunity. Mr Kohli however was repeatedly offered the opportunity of making a large mark-up on phones acquired in the UK which he knew were not intended for the UK market and which resulted in a turnover for each of these companies of nearly £130 million for these periods. Despite this, there is no suggestion that he ever questioned why this should be so or how it could be that he had managed to place so many successful deals, with not one of them giving rise to any issues over delivery, returns or damaged stock. Even the most credulous of traders might have started raising questions after more than one or two similar deals had been done. Mr Kohli never raised those questions even after 52 similar deals had been done.

204. In a standard market where all other dealings were above board, we think that even one of these issues would have given a normal businessman pause for thought and might at least have made him ask further questions either of HMRC or of his counterparties. In a market which is known to be susceptible to fraud and which Mr Kohli knew to be susceptible to fraud, it is inconceivable that a businessman would have continued to do business as Mr Kohli did unless he knew, but did not care, that his deals were connected with fraud.

205. There were other aspects of the evidence which did not support Mr Kohli's suggestion that he intended to deal straightforwardly with HMRC; all of HMRC's witnesses who dealt directly with each of the Appellant companies and Mr Kohli suggested that he was unco-operative to say the least, and resisted providing the information which HMRC required. This attitude was reflected by Mr Kohli's dealings with the Tribunal in the lead up to the hearing and for the days when he was present at the hearing. If Mr Kohli, as he would have us believe, had no reason to be concerned that any of his deals were other than normal commercial deals, he should have had no reason not to provide the information which HMRC required in at least a reasonably timely fashion. Rather than that Mr Kohli prevaricated, made difficulties in having meetings with HMRC and produced documents only many years, in some instances, after they were first requested.

206. To attempt to suggest that somehow HMRC's silence in the face of the due diligence which had been done by the Appellants, their previous repayments of input tax and the Redhill checks which were done, were enough to allay Mr Kohli's suspicions and should absolve him of any further responsibility for considering the real implications of these transactions stretches the bounds of credibility. No reasonable business person undertaking significant transactions in a high risk arena would rely on any assurances but his own that his deals were safe. Redhill checks provide confirmation from HMRC that a trader remains registered for VAT in the UK, but that is far from a complete assurance that they are not involved in fraudulent activities. Reliance on Redhill checks on the day when the deals were entered into

should not have been enough by themselves to put Mr Kohli's mind at rest. Repayment of input VAT on earlier deals was no guarantee that later deals were safe from fraud. The only way in which these checks were effective was as an attempt to demonstrate to HMRC that some due diligence had been done.

207. Mr Kohli made much of the fact that the deals in which the Appellants were involved were not, unlike all other participants in the chain, carried out from a common IP address, suggesting that this in itself supported the Appellants' innocence. The use of a particular IP address is evidence only of the particular location from which an electronic banking transaction is carried out. On its own, it indicates nothing about involvement or otherwise in these transactions. A common IP address is often adduced as evidence of orchestration through chains of dealing in cases like this; suggesting that all transactions in a chain are initiated from the same computer if not by the same person. But the converse is not necessarily true; that merely dealing from a different location suggests that an appellant is not part of the chain of dealing. There might be many reasons why one party to an otherwise connected series of transactions does not, or is not able, to utilise the same IP address and in the wider context of the circumstances of this case it is certainly not enough of itself to remove any suggestion that Mr Kohli knew that these deals were connected with fraud.

208. Our view is that even one of the indicators of fraud set out above would be sufficient to demonstrate that each of the Appellants, through Mr Kohli, should have known that their deals were linked to fraudulent transactions in a market in which they knew fraud was prevalent. In combination they provide a telling picture of Appellants who were taking a positive decision not to consider the real implications of the way these deals were done, the only reasonable explanation for which can be that they knew that these deals were connected to fraud.

209. We have also taken account of the fact that for WTL and WIE significant changes in their business and the move to dealing in mobile phones coincided with Mr Kohli's appointment as a director. Mr Maini's explanation of how this change occurred at WIE is suggestive of an intention to use the company to claim large VAT repayments, rather than for any other commercial purpose: *"In early May 2006 Mr Kohli, who knew of the company, asked if he could use it for mobile phone trading. As WTL was doing well and had recently received a payment of VAT, it was agreed that the business activity of the company would be changed"*.

210. For all of the reasons we find that the Appellants, acting through Mr Kohli knew that each of the 52 disputed transactions was connected with the fraudulent evasion of VAT.

Disproportionality

211. The Appellants' secondary arguments relate not to what they could or should have known, but how HMRC should have dealt with them as taxpayers. They suggest that it was disproportionate for HMRC to refuse to repay them input tax in circumstances where other taxpayers had their own input tax repaid and that HMRC intentionally delayed dealing with the Appellants' VAT reclaims.

212. The concept of disproportionality and the extent to which it can be relied on by taxpayers in the context of EU legislation such as VAT has been considered on a number of occasions by this tribunal. The Appellants did not make clear whether they were relying on EU legislation or the UK's Human Rights Act 1998 in making this argument. In the context of the EU legislation the most definitive view of the ability of a taxpayer to argue that HMRC has acted in a disproportionate manner is the *Total Technology* decision (*HMRC v Total Technology (Engineering) Limited* [2013] STC 681). Disproportionality in that case and in the context of EU law was as between the offence (late payment of VAT) and the penalty (the VAT surcharge). That is not the sense in which the Appellants complain of disproportionality, which is as between their treatment and the treatment of other taxpayers who were involved in other parts of these transaction chains. It is clear for both EU and UK law purposes that the remit of this Tribunal does not extend to HMRC's differential treatment of allegedly similar taxpayers; that is a question of the exercise of HMRC's discretion and is properly dealt with by way of judicial review.

213. The Appellants also state that HMRC intentionally delayed issuing decision letters to the Appellants for two years in order to put them out of business and asked for documents in a piecemeal fashion to camouflage their lack of decision making. The Appellants were made to look unco-operative by HMRC, but HMRC was applying a blanket delaying strategy. The Appellants state that they did not have the opportunity to demonstrate these claims before the Tribunal as a result of Mr Kohli's absence on health grounds from the main part of the hearing. However, even had Mr Kohli been present to make these claims, they also relate to issues of HMRC's administrative functions which are outside the remit of the Tribunal on the basis of the decision in *HMRC v Abdul Noor* ([2012] UKFTT 157(TC)). Like the Appellants' disproportionality claims, such issues fall within the remit of administrative law which can only be dealt with by a claim for judicial review before the High Court**.**

Discrimination

214. The Appellants also suggest that the denial of input tax in this case amounts to illegal discrimination and an irrational breach of neutrality by HMRC which is counter to EU law and Article 22(8) of the Sixth Directive in particular. It has been made clear in numerous cases up to and including the *Kittel* decision and most recently in *Fonecomp*, that while VAT is intended to operate neutrally between traders, that neutrality, represented by the right to deduct input tax, is overridden in circumstances where the VAT rules have been abused, including in particular where a trader who knew or should have known that he was participating in a transaction connected with fraud, that participation being viewed as part of the abusive fraudulent transactions. The UK courts have an obligation to ensure that the VAT rules are not used for abusive or fraudulent purposes; the Tribunal cannot see how any arguments based on discrimination or neutrality can aid a taxpayer whose transactions are connected with fraudulent evasion.

215. Finally we have considered the Appellants very specific issues and objections made to aspects of HMRC's case:

(i) *WTL deal 12 - The fraudulent Eurotunnel tickets*; despite the Appellants' contentions we do not agree that their alternative explanations for the timing discrepancies in these documents is any more credible than HMRC's explanation. Even if we did agree with the Appellants, we do not think, as the Appellants suggest, that this is indicative of a wider issue with the credibility of HMRC's evidence. In many instances the shortcomings in HMRC's evidence arose from a failure by the Appellants to provide documentation and information to substantiate the deals to which they were a party.

(ii) *Deal chains and FCIB evidence***:** The Appellants suggest that had they had the opportunity to cross-examine Mr Mendes before the Tribunal or produce arguments before the Tribunal relating to the deal chains, they could have made a real challenge to these aspects of HMRC's evidence. We accept that Mr Kohli's illness meant that this was not possible before the Tribunal, but the Appellants had had many opportunities to put these points in writing prior to the hearing and also a final opportunity during closing submissions but at no point were substantive arguments made.

216. For all these reasons these appeals are dismissed and HMRC's decision to deny the Appellants' right to deduct input tax is upheld.

217. 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.

RACHEL SHORT
TRIBUNAL JUDGE

RELEASE DATE: 10 SEPTEMBER 2015

Schedule of Deals

Company/Deal number	Invoice Number	Date	Phone Type	Sale Price	Profit	Bought from	Sold to
1 WTL	4893	20 June 2006	Nokia 8800	£412	£43	Globalex Limited	Vanprugh Communications SL
2 WTL	4894	20 June 2006	Nokia N80	£378	£38	Worldwide UK Import Export Limited	Vanprugh Communications SL
3 WTL	4895	20 June 2006	Nokia 8801	£426	£43	Globalex Limited	Bleu Opale Technique EURL
4 WTL	4896	20 June 2006	Nokia 91	£382	£36	Worldwide UK Import Export Limited	Bleu Opale Technique EURL
5 WTL	4897	21 June 2006	Nokia 9500	£330	£32	Globalex Limited	Vanprugh Communications SL
6 WTL	4898	21 June 2006	Nokia 8801	£425	£43	Kensai Trading Limited	Vanprugh Communications SL
7 WTL	4899	21 June 2006	Nokia 8800	£413	£43	Worldwide UK Import Export Limited	Bleu Opale EURL
8 WTL	4900	21 June 2006	Nokia N80	£376	£37	Globalex Limited	Monza Trading SRL
9 WTL	4901	26 June 2006	Nokia 8800	£652	£67	Worldwide UK Import Export Limited	Vanprugh Communications SL
10 WTL	4902	26 June 2006	Nokia N80	£377	£38	Kensai Trading Limited	Bleu Opale Technique EURL
11 WTL	4903	26 June 2006	Nokia N91	£383	£36.50	Globalex Limited	Vanprugh Communications SRL
12 WTL	4904	26 June 2006	Nokia 8800	£415	£44	Kensai Trading Limited	Monza Trading SRL
13 WTL	4905	27	Nokia	£330	£33	Kensai	Bleu Opale

		June 2006	9500			Trading Limited	Technique EURL
14 WTL	4906	27 June 2006	Nokia 8800	£651	£67	Globalex Limited	Bleu Opale Technique EURL
15 WTL	4907	27 June 2006	Nokia N91	£383	£36.25	Kensai Trading Limited	Monza Trading SRL
16 WTL	4908	27 June 2006	Nokia 8801	£425	£42.50	Worldwide UK Import Export Limited	Monza Trading SRL
SGL Deals							
1 SGL	128	11 May 2006	Nokia 9500	£347	£37	Globalex Limited	Bleu Opale Technique EURL
2 SGL	129	11 May 2006	Nokia 8800	£426	£46	Globalex Limited	Bleu Opale Technique EURL
3 SGL	131	12 May 2006	Nokia 9500	£348	£37	Kensai Trading Limited	Pochard Sp Zoo
4 SGL	132	12 May 2006	Nokia 8800	£427	£46	Kensai Trading Limited	Pochard Sp Zoo
5 SGL	133	15 May 2006	Nokia 8800	£428	£45.50	Worldwide UK Import Export Limited	Pochard Sp Zoo
6 SGL	135	15 May 2006	Nokia 9300I	£337	£36	Kensai Trading Limited	Bleu Opale Technique EURL
7 SGL	136	15 May 2006	Nokia 9500	£349	£37.50	Kensai Trading Limited	Bleu Opale Technique EURL
8 SGL	137	16 May 2006	Nokia 9300I	£338	£36	Worldwide UK Import Export Limited	Bleu Opale Technique EURL
9 SGL	140	17 May 2006	Nokia 9500	£349	£37	Worldwide UK Import Export Limited	Pochard Sp Zoo
10 SGL	141	17 May 2006	Nokia 8801	£433	£46	Worldwide UK Import Export	Bleu Opale Technique EURL

						Limited	
11 SGL	142	17 May 2006	Sony Ericsson W900i	£335.50	£36	Globalex Limited	Pochard Sp Zoo
12 SGL	143	17 May 2006	Nokia 8800	£424	£45	Kensai Trading Limited	Bleu Opale Technique EURL
13 SGL	144	18 May 2006	Sony Ericsson W900i	£336	£36	Worldwide UK Import Export Limited	Bleu Opale Technique EURL
14 SGL	145	18 May 2006	Nokia 8800	£424	£45	Globalex Limited	Pochard Sp Zoo
15 SGL	146	18 May 2006	Nokia 8801	£432	£45	Kensai Trading Limited	Pochard Sp Zoo
16 SGL	147	25 May 2006	Nokia 8800	£428	£46	Worldwide UK Import Export Limited	Vanprugh Communications SL
17 SGL	148	25 May 2006	Nokia 8801	£432	£46	Globalex Limited	Vanprugh Communications SL
18 SGL	149	25 May 2006	Nokia 9300i	£336	£36	Globalex Limited	Vanprugh Communications SL
19 SGL	150	31 May 2006	Nokia 8801	£431	£46	Worldwide UK Import Export Limited	Vanprugh Communications SL
20 SGL	151	31 May 2006	Nokia 9500	£348	£37	Globalex Limited	Vanprugh Communications SL
WIE Deals							
1 - WIE	0008	25 May 2006	Nokia 8801	£428	£43	Kensai Trading Limited	Pochard Sp Zoo
2 WIE	0009	25 May 2006	Sony Ericsson W900i	£330	£34	Kensai Trading Limited	Pochard Sp Zoo
3 WIE	0010	25 May 2006	Nokia 9500	£340	£31	Globalex Limited	Bleu Opale Technique EURL
4 WIE	0011	25 May	Nokia 8800	£428	£49	Globalex Limited	Bleu Opale Technique

		2006					EURL
5 WIE	0012	26 May 2006	Nokia 8801	£428.50	£42.50	Globalex Limited	Vanprugh Communications SL
6 WIE	0013	26 May 2005	Nokia 8800	£427.50	£47.50	Globalex Limited	Pochard Sp Zoo
7 WIE	0014	26 May 2005	Nokia N80	£407	£42	Worldwide UK Import Export Limited	Bleu Opale Technique EURL
8 WIE	0015	26 May 2006	Sony Ericsson W900i	£331	£36	Worldwide UK Import Export Limited	Vanprugh Communications SL
9 WIE	0016	30 May 2006	Nokia 9300i	£333	£32.50	Kensai Trading Limited	Bleu Opale Technique EURL
10 WIE	0017	30 May 2006	Nokia 8800	£429	£48	Kensai Trading Limited	Bleu Opale Technique EURL
11 WIE	0018	30 May 2006	Nokia N91	£416	£40	Worldwide UK Import Export Limited	Bleu Opale Technique EURL
12 WIE	0019	30 May 2006	Nokia 8801	£428	£41.50	Worldwide UK Import Export Limited	Pochard Sp Zoo
13 WIE	0020	31 May 2006	Nokia 9500	£344	£34	Worldwide UK Import Export Limited	Pochard Sp Zoo
14 WIE	0021	31 May 2006	Nokia 9300i	£334	£33	Globalex Limited	Vanprugh Communications SL
15 WIE	0022	31 May 2006	Nokia N80	£408	£42	Kensai Trading Limited	Vanprugh Communications SL
16 WIE	0023	31 May 2006	Nokia 8800	£427	£46	Worldwide UK Import Export Limited	Vanprugh Communications SL