TC04625

Appeal number: TC/2011/01928

VAT – Input Tax –transactions in televisions - whether appellant knew or should have known its transactions were connected to fraudulent evasion of tax – yes - appellant should have known – appeal dismissed

Default surcharge – whether appellant's disputed earlier VAT repayment claims which were later allowed by HMRC meant that there was no "outstanding VAT" for purposes of default surcharge provisions or that the appellant had a reasonable excuse for not paying VAT due in respect of later periods – no – appeal dismissed

FIRST-TIER TRIBUNAL
TAX CHAMBER

AC (WHOLESALE) LIMITED **Appellant**

- and -

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

TRIBUNAL: JUDGE SWAMI RAGHAVAN
TYM MARSH MA MBA

Sitting in public at the Royal Court's of Justice on 24, 25, 26 November and 1 December 2014

Timothy Brown, counsel for the Appellant

Stuart Biggs and Natasha Barnes, counsel, instructed by the General Counsel and Solicitor to HM Revenue and Customs, for the Respondents

DECISION

Introduction

1. AC (Wholesale) Ltd ("the appellant"), a wholesaler of electrical goods appeals HMRC's decisions denying it entitlement to the right to deduct input tax in the total sum of £107,838 for monthly accounting periods: 10/09 (£33,375.00), 08/10 (£18,355.00), 09/10 (£25,490.00) and 10/10 (£30,618.00).

2. The denial of input tax related to purchases of TVs and is based on HMRC's view, applying the legal principle in *Kittel*[1] that the appellant knew or ought to have known that its purchases were connected to fraud.

3. The appellant also appeals HMRC's decision to impose default surcharges totalling £1,537.49 on the appellant for five later VAT periods; 11/10 (£463.83), 01/11 (£249.63), 02/11 (£34.25), 03/11 (£283.14) and 12/11 (£506.64).

Evidence

4. We were provided with witness statements from the following:

(1) Mr Neil Brownsword, and Mr Lee Nevin, on behalf of HMRC.

(2) Mr Dan Lawson on behalf of the appellant.

5. We heard oral evidence which was cross-examined from Mr Nevin, and from Mr Lawson, the director of the appellant. Mr Brownsword's evidence covers facts relevant to Winnington Networks Limited, a company which appeared in one of the transaction chains relating to a deal where the appellant's input tax is under appeal (deal 17). The appellant accepted that this deal was connected through Winnington Networks Limited who was acting as a "contra-trader" to defaulting traders and we therefore do not set out any detail in relation to Mr Brownsword's statement. We nevertheless considered it and in particular the references made to it in the witness statement of Mr Nevin.

6. Mr Nevin has been employed by HMRC and before that HMCE since 1985 in a number of administrative, VAT assurance and fraud investigation roles. He has worked in MTIC fraud investigation since 2006.

7. The appellant says we should give little weight to Mr Nevin's evidence as it contains opinion, irrelevant matters and further errors despite correcting witness statements. We have disregarded matters of opinion in his evidence. In the context of the volume and range of matters dealt with in Mr Nevin's evidence the nature of the errors made were minor and did not betray concerns about its reliability. We found Mr Nevin to be a credible witness of fact.

8. For the reasons set out below at [120] we did not find Mr Lawson's evidence to be wholly reliable and approached it with caution.

[1] *Kittel v Belgium; Belgium v Recolta Recycling SPRL* (Joined cases C-439/04 and C-440/04)

9. From the evidence we heard we were able to make the following findings of fact.

Background facts

10. The appellant, AC (Wholesale) Limited, was incorporated on 15 April 2002. Its trade category was stated in HMRC's database (FAME) as being "wholesale of consumer electronic products." It was set up by Mr Lawson, who is its sole shareholder and who dealt with the import / export and wholesale of consumer electronics. The main product lines bought and sold were TVs and audio-visual equipment. It did not have a retail outlet.

11. Mr Lawson had worked for the Dixons Store Group from 1989 to 1991 as a sales assistant and as a computer centre manager. From 1991 to 1996 he worked for Richer Sounds PLC starting out as a sales assistant and rose through the ranks to become a Managing Director of Richer Sounds International where his role included finding and developing new overseas suppliers for Richer Sounds. On leaving Richer Sounds in 1996 he started Carotino EU Ltd. a company in relation to which he is still a director. It deals with the import of food products (mainly cooking oils) which it sells to UK supermarkets. From 1997 he was involved with an import/export wholesaler of consumer electronics through a company (Audio Channels Ltd.) which he had set up. The company ceased trading in 2002.

12. The appellant's turnover in the years ending 31 March 2003 to 31 March 2011 was as follows:

2003 - £6,621,587

2004- £6,897,020

2005 - £4,937,153

2006- £9,749,126

2007 - £9,548,049

2008 - £4,924,450

2009 - £8,000,077

2010 - £10,189,470

2011 - £3,933,574

Staff

13. The appellant employed a sales manager, Tony Jones from approximately 2000 to 2012. Mr Jones was the main person in charge of developing existing sales, obtaining new sales contacts and managing the sale process in conjunction with Cornelia Hummer and also with the assistance of Mr Lawson and the financial controller. Mr Jones and Ms Hummer were married to each other and had met while working at the appellant.

14. Mr Jones earned commission on the transactions. His initials appeared on the invoices in order to identify his transactions. In 2003 his commission was around 5% of the net profit.

15. The office where Mr Lawson and the above staff worked was a small one and staff typically did not communicate which each other by e-mail. In summer Mr Lawson worked from his home office at his holiday home in Cyprus.

16. There is a disputed issue of fact as to the extent of Mr Lawson's involvement in the day to day running of the company which we discuss at [116]. He was working on other projects. In addition his young son who was disabled and who had undergone a number of operations from 2008 was sick at the time. Dealing with this took up a lot of Mr Lawson's time.

VAT registration and returns

17. The appellant submitted an application to register for VAT on 14 May 2002 which stated the main business activity to be the sale of electrical items and estimated the annual turnover to be £4,000,000. It was registered for VAT with effect from 20 May 2002.

18. The table below sets out the VAT returns HMRC received during the relevant periods, the amounts due according to those returns, details of interim payments that were released to the appellant, the date of the final decision and the amount by which the return was altered by.

VAT Return	Date received	Net Tax	Interim payments made	Final decision
01/09	18/12/09	£88,191.95 Repayment	£6033.45 on 27/3/09 £37,020.00 on 15/04/09	15/10/10 Return altered by £44,446.50
02/09	26/03/09	£66,534.60 Repayment	£27,291.40 on 19/05/09 £6232.50 on 19/05/09	15/10/10 Return altered by £25,447.50
03/09	27/04/09	£86,689.89 Repayment	£12,429.10 on 05/06/09	15/10/10 Return altered by £78,112.50
04/09	05/06/09	£2,021.59 Payment to HMRC	Nil	15/10/10 Return altered by £7164.00
05/09	02/07/09	£50,097.17 Payment to HMRC	Nil	15/10/10 Return altered by £17,122.50

06/09	21/07/09	£39,593.93 Payment to HMRC	Nil	15/10/10 Return altered by £21,540.30
07/09	21/07/09	£6,419.59 Repayment	Nil	02/02/12 Return altered by £43,627.00
10/09	19/11/09	£62,138.73 Repayment	Nil	02/02/12 Return altered by £33,375.00
08/10	30/09/10	£9,605.79 Repayment	Nil	07/11/11 Return altered by £18,375.00
09/10	04/11/10	£41,475.35 Repayment	Nil	07/11/11 Return altered by £25,490.85
10/10	03/12/10	£56,969.47 Repayment	Nil	07/11/11 Return altered by £30,618.00

The deals

19. It should be noted that the subject matter of this appeal originally concerned a number of deals (1-16) where HMRC have subsequently conceded that input tax is due either for reasons relating to lack of connection to fraudulent evasion of VAT or because they accept that they cannot meet the burden of showing in relation to the particular deals that the appellant knew or ought to have known that its transactions were connected to fraudulent evasion of VAT. The relevance of these previous deals is a matter of dispute and we discuss this further at [105] below.

20. The remainder of this section focuses on the deals under appeal and in relation to which the appellant accepts are deals where its purchases were connected to fraudulent tax loss. However to the extent it is relevant to consider in building up a picture of what the appellant would have been aware of and its approach to due diligence we have set out details of the warning letters and due diligence performed in relation the prior deals as well as the deals under appeal.

Deal 17 (VAT period 10/09)

21. On 23 October 2009 the appellant bought 899 LG32LH2000 TVs from Overture Trading Ltd for £255,877.88 (£222,502.50 + £33,375.38 VAT). It sold them under

two invoices in respect of 600 and 299 TVs both dated 23 October to HB Austria for a total amount of £233,740. The invoice under which Overture sold the goods to the appellant was dated 27 October 2009 and stated "For immediate settlement All goods remain the property of Overture Trading Ltd until paid in full".

22. Overture Trading Limited had bought the goods from Winnington Networks Ltd who had bought them from Opifex (Lithuania). It is not disputed Winnington Networks Ltd was in the jargon of MTIC fraud a contra-trader; in other words a trader who off-set input tax claims in a chain in which they acted as a broker (a trader selling to another EU country) and which contained defaulters (a so called "dirty chain") against output tax due on goods acquired from another EU country (the "clean chain"). The aim of this was to make it more difficult for HMRC to notice that there was MTIC fraud (indicated by a missing or defaulting acquirer in a chain where input tax reclaim was sought by a broker). If HMRC looked down the clean chain they would not see that the acquirer had gone missing leaving a substantial amount of VAT unpaid. Their attention would not be drawn to the dirty chain as no input tax reclaim had been made. The Appellant's purchase traced through Winnington Networks Ltd to defaulting traders who deliberately failed to meet their VAT liabilities.

Deal 18 (VAT period 08/10)

23. On 9 August 2010 the appellant bought 300 Samsung LE40b530 TVs from TMP Distribution for £105,750.00 (£90,000 + £15,750 VAT). It sold them to NetOnNet (based in Sweden) the same day for £92,100. The invoice for the appellant's sale was dated 9 August 2010.

24. TMP's sale traced back through E-Tel (UK) Ltd and Life Services Ltd who had bought them from Carmor Ltd. It is not disputed that Carmor Ltd was a defaulting trader who had failed to account for and pay to HMRC the output tax it had charged on its sale. Carmor Ltd had bought from HBM Logistics (based in Portgual) who had bought from Profitrade Baltic (based in Estonia) who in turn had bought from SCM Impex (based in Hungary) who in turn had bought from Radio Marrelli (based in Germany).

Deal 19(VAT period 08/10)

25. On 13 August 2010 the appellant bought 50 Samsung LE40B530 TVs. For £17,625.00 (£15,000 + £2,625 VAT). It sold them to Fortuna (based in Jersey) for £15,750. The invoice for the appellant's sale was dated 13 August 2010. The chain of supply preceding the appellant's purchase and which again included Carmor Ltd was identical to Deal 18 above.

Deal 20 (VAT period 09/10)

26. On 13 September 2010 the appellant bought 220 Samsung LE40B6000 TVs from TMP for £117,617.50 (£100,100 + £17,517.50 VAT). It sold them to EW Digital (Austria) for £104,500. The invoice for the sale was dated 14 September 2010. The preceding chain of supply again included Carmor Ltd but instead of Life Services Ltd the goods passed through a company called Zero Balance Ltd.

Deal 21 and 22 (VAT period 09/10) and (VAT period 10/10)

27. On 21 September 2010 the appellant bought 209 Samsung LE32C450 TVs from TMP for £53,535.35 (£45,562 + £7,973 VAT). It sold them to EW Digital (Austria) for £49,716.07. The invoice for the appellant's sale was dated 30 September 2010.

28. On 19 October 2010 the appellant bought 324 Samsung UE40C6500 TVs from TMP for £205,578 (£174,960 + £30,618). It sold them to EW Digital (Austria) for £205,578 (£174,960 + £30,618). The invoice for the sale was dated 19 October 2010.

29. In both the above transactions HMRC were unable to trace the goods further. TMP failed to declare the sales and failed to pay HMRC the output tax charged on the sales.

Facts relating to deals under appeal – the suppliers

Overture

30. Overture's director was Mr Deniz Ali (from 27 October 2004 to 1 July 2010), its company secretary was Ms Claire Leak (from 27 October 2010 onwards). It had one full time employee, Mr Sol Solomonides, who was also briefly a director between 1 July 2010 to 30 July 2010. The company had been incorporated as Live Telecoms (International) Limited on 27 October 2004. The company changed its name to Overture Trading Limited on 6 December 2007. The company was registered for VAT with effect from 1 August 2005. Its business activity was stated as "the purchase of mobile telephones in the UK and sell to customers abroad". The VAT returns submitted for the periods 09/05 to 03/08 showed no trade. Overture's outputs on its VAT returns were as follows:

VAT period	Outputs
06/08	£4,899
09/08	£18,011
12/08	£38
03/09	£667,500
06/09	£4,311,030
09/09	£5,490,587
12/09	£7,441,840
03/10	£6,867,468
06/10	£5,573,504

31. Mr Deniz Ali and Mr Jones (the appellant's sales manager) were on very familiar terms with each other. This was evident from the tone of the e-mails they exchanged.

32. Overture knew the identity of one of the appellant's customers, TJ Hughes. Mr Lawson's explanation in cross-examination for this disclosure was that this was due to threatened legal action by TJ Hughes and that Mr Jones had disclosed TJ Hughes' identity having been asked to do so by either Mr Ali or Ms Leak.

33. When Mr Nevin visited Overture on 8 July 2009 he met with Mr Ali and Ms Leak. His note of the visit records that Overture's due diligence was carried out in the form of credit safe check, trade application form, companies house details and taking up references.

34. Overture ceased trading on 27 September 2010 and became insolvent with effect from 23 November 2010.

TMP Distribution Limited

35. TMP Distribution Limited registered for VAT with effect from 1 March 2001 stating its business activity as the printing of instruction manuals for electrical equipment. This trade activity was reflected in their VAT declarations for the periods 05/07 to 02/10. On 3 March 2010 the trader wrote to HMRC to say they would be wholesaling electrical equipment. TMP's returned VAT output figures were as follows:

VAT period	Outputs
05/07	£24,158
08/07	£50,223
11/07	£10,517
02/08	£27,893
05/08	£20,977
08/08	£18,098
11/08	£10,813
02/09	£13,707
05/09	£11,152
02/08	£27,893
05/08	£20,977
08/09	£14,477
11/09	£35,806
02/10	£12,282
05/10	£2,668,894

08/10	£1,821,048

36. Mr Ali wrote his letter of introduction from TMP to the appellant on 17 March. The appellant first traded with TMP on 25 March 2010. Mr Ali resigned as a director of Overture on 1 July 2010.

Other types of business

37. The appellant bought audio equipment from an authorised distributor of Samsung and Panasonic audio equipment and sold these on to UK and EC customers including retail outlets. HMRC did not find tax losses in these transaction chains. The appellant also bought headphones and cordless headphones from Sennheiser UK Ltd a manufacturer and sold retail via E-Bay. HMRC did not find any tax losses in these chains

Goods

38. Goods received into company's warehouse (a sub-contracted third party warehouse) and were independently checked both in and out before being sold to customers.

39. HMRC were not able to trace the goods back to either a manufacturer or an authorised distributor.

Other features of the deals

40. In relation to deals 1-22 the appellant made a profit on 20 out of the 22 deals. The profits per unit the appellant achieved on games consoles ranged between 89 pence per unit to £11.82 per unit. The profits achieved on the televisions ranged between £4.55 per unit and £20 per unit.

41. For Deals 6-9, 12,13, 15 and 17-20 the goods entered the UK from a non UK EU country and were traded a number of times in the UK and then sold back to a trader in a non-UK EU country. We did not see evidence of any written contracts between the parties.

Other transactions with Overture and TMP

42. At the hearing the appellant put before us a SAGE print out of purchases it had made from Overture and TMP. The print out was a schedule which set out the transaction number, date, account reference (Overture or TMP), reference, details of the product (the goods were either TVs or computer consoles/games), the net amount, the tax amount and the gross amount.

43. In relation to Overture there were 53 transactions between 8 May 2009 and 8 April 2010. One of these included deal 17 where the appellant concedes there was tax loss. But they also included deals 10-16 which HMRC say linked to tax loss. In addition there were eight transactions within the 53 where the goods were sold to a non UK EU trader. Of the transactions 21 were ones where goods were sold on to Richer Sounds. There were five where the goods were sold on to TJ Hughes. There

were 39 transactions before deal 17 on 27 October 2010 (including seven where HMRC say there was tax loss and seven with exports to non UK EU traders.) HMRC's letter of 15 September 2009 (see [64] below) had at this point notified that two of these purchases traced to a tax loss.

44. After 15 September 2009 (the date of HMRC's warning letter regarding two tax loss links with goods which were bought from Overture) the appellant carried out transactions on 21, 22 and 24 September 2009. In the first two the goods (Samsung TVs) were sold to Richer Sounds. After Deal 17 there were a further 13 transactions with Overture (five of which where the subsequent customer was Richer Sounds) up until 8 April 2010.

45. In relation to TMP for the period 31 March 2010 to 19 October 2010 there were 21 transactions. Five of these are accepted to relate to tax losses (deals 18-22). In relation to deals 18 and 19 the consignment was split with some goods being exported and some staying in the UK. Nine were ones where goods were sold on to Richer Sounds and one where goods were sold on to TJ Hughes.

46. HMRC say the transactions on 21 and 28 September 2010 relating to sales to Richer Sounds trace to tax loss as TMP did not declare any sales during this period.

Warnings from HMRC

Mr Nevin's visit on 17 February 2009

47. Mr Nevin visited the appellant in order to collect information and the relevant paperwork concerning a transaction whereby the appellant bought 650 Sony Play station Games Consoles from Electro Centre on 29 October 2008 (which transaction traced to a tax loss). During the visit Mr Nevin discussed the appellant's business activities and also explained MTIC fraud to Mr Lawson and the in-house accountant Mr Raj Kothari. He issued Notice 726 (excerpts of which are set out below).

48. On 5 March 2009 HMRC wrote to the appellant to inform them that their VAT return for the Period 01/09 was to be verified. On 6 March 2009 HMRC wrote a letter explaining MTIC fraud and giving details of how to verify the VAT registration numbers of potential suppliers and customers with HMRC-Wigan.

Notice 726

49. Notice 726 explains to traders how they could be made jointly and severally liable for the unpaid VAT of another VAT registered business when it buys and/or sell specified goods. It describes MTIC as follows:

> "In its simplest form, the fraud involves a fraudster obtaining a VAT registration number in the UK for the purposes of purchasing goods free from VAT in another EU member State, selling them at a VAT inclusive purchase price in the UK and then not paying the output tax due to HMRC. The goods are then sold through a number of UK businesses and finally sold outside the UK free from VAT. The final UK business claims a VAT repayment from HMRC that, if paid, crystallises the loss at the start of the UK supply chain."

50. The appellant highlights the following:

> "Notice 726 states:
>
> Section 4.1 – HMRC **will** [emphasis added] send you a notification letter if:
>
> • You have bought/sold a quantity of the specified goods; and
>
> • The transaction took place within a supply chain where VAT was unpaid by another supplier in the chain; and
>
> • HMRC believe it can show that you knew or had reasonable grounds to suspect that VAT would go unpaid."

51. Section 4.2 describes a notification letter which will be headed "Notification of joint and several liability".

52. Section 6.3 states:

> "If you have genuinely done everything you can to check the integrity of the chain, can demonstrate you have done so, have taken heed of any indications that VAT may go unpaid and have no other reason to suspect VAT would go unpaid, the joint and several liability rules will not be applied."

53. No such joint and several liability letters were sent from HMRC to the appellant.

Warning letters

54. On 5 March 2009 HMRC wrote to the appellant advising that its 01/09 VAT return had been selected for extended verification.

55. On 6 March 2009 HMRC wrote to the appellant. The letter explained MTIC fraud.

56. On behalf of HMRC, Mr Nevin wrote a number of letters to the appellant (addressed for the attention of Mr Lawson) which were written in the following basic format. After an introductory paragraph which referred to the investigation of MTIC fraud being "top VAT fraud priority" for HMRC and that Customs had in place provisions enabling it to impose joint and several liability on VAT unpaid the letters go on to say:

> " I am writing to you because as a result of enquiries in respect of your transaction chains we now know of [ ] transactions that commenced with defaulting traders, resulting in the loss of revenue exceeding [ ].
>
> Your sale invoices which have been traced to transaction chains that commenced with a VAT loss are as follows:"

57. There then followed a table setting out the Invoice number, the invoice dates, the Customer, the Goods and the Net value. After referring to the point made in Notice 726 (above at [52]) the letter stated:

> "From your records you will be able to ascertain who supplied you with the goods detailed above, and you may wish to consider what appropriate action is needed to ensure that the VAT does not go unpaid in respect of any future transactions."

58. We set out below further detail in relation to the dates the particular letters from HMRC were sent together with details of the supplier of the goods. (While the supplier was not identified in the text of the letter it could be identified by the trader by tracking through the invoice details which had been provided to see who the trader had bought the goods from.)

59. On 15 April 2009 HMRC wrote to the appellant. The letter notified that five of the appellant's sales in October and November 2008 where its supplier was Electro Centre connected to tax loss.

60. On 28 April 2009 HMRC sent a tax loss letter to the appellant advising that Deal 1 (which took place on 9 January 2009) where its supplier was Electro centre traced to tax loss.

61. On 2 July 2009 HMRC advised that the appellant's sales in Deals 2 (19 January 2009), 3 (19 February 2009) and 4 (5 February 2009) where its supplier was Electro Centre traced to tax loss.

62. On 8 July 2009 HMRC advised that the appellant's sales in Deal 5 (2 March 2009) where its supplier was Electro Centre traced to tax loss.

63. On 22 July 2009 HMRC notified the appellant that deal 2 where the appellant's supplier was Electro Centre traced to tax loss.

64. On 15 September 2009 (a letter HMRC placed significant emphasis on in their submissions given the letter was sent before the first Overture deal under appeal) HMRC notified that deals 10 (8 May 2009) -11 (18 May 2009) where its supplier was Overture traced to tax loss.

65. On 9 February 2010 HMRC notified that deals 8 (14 April 2009) and 9 (24 April 2009) where the appellant's supplier was Winnington connected to tax loss.

66. On 19 June 2010 HMRC notified that deals 12 (4 June 2009) and 13 (9 June 2009) where its supplier was Overture traced to tax loss.

Due diligence by trader

67. Mr Lawson's witness statement exhibited a file containing the due diligence carried out by the appellant.

68. His evidence in cross-examination was that he had oversight of the due diligence. His evidence was that in the majority of cases the trading partners had been known to the appellant and had traded with it for prolonged periods of time and that they were substantial trading entities in their own right. For instance the appellant had worked with Electro Centre for the best part of 10 years. Mr Lawson said he had met with the owner personally on 2-3 occasions and had visited their trading premises. He said Tony Jones had visited them on numerous further occasions over the years.

69. The due diligence Mr Lawson provided took the form of variously : VAT Registration Validation Responses from the Europa website, companies house reports, credit reports from Euler Hermes, Graydon UK and Eolis, website print outs and in some cases letters of introduction, VAT and incorporation / change of name certificates. Mr Lawson was not personally involved in carrying out any of the due

diligence. From the documents we can make the following findings as to what the appellant knew and when in relation to the various suppliers Electro Centre, Winnington, Overture and TMP (covering deals 1-22).

Electro Centre:

70. A Euler Hermes credit limit enquiry dated 18 January 2010 stated: "Latest decision: Limit not found." A Graydon Level 3 Credit Rating Report supplied on 29 January 2010 stated GBP 14,000 as the "monthly credit guide" and stated the "Risk Category" to be "above normal risk".

71. The Europa validation response and the Companies House report both dated 10 November 2010 revealed that the supplier had respectively a valid VAT number and that it had been incorporated in March 2001.

Winnington:

72. In a letter dated 6 March 2009 addressed to "Dear Tony", and headed "Introduction letter", Winnington enclosed details of its website, company details, certificate of incorporation, HMRC's VAT registration certification and its terms and conditions of purchase and sale.

73. The Europa validation response confirming a valid VAT number was dated 14 April 2009. The Euler Hermes credit limit enquiry reported "Limit not found". The Graydon credit report dated 29 January 2010 stated next to "Graydon rating" "OD" and then "Less than GBP1 – This does not necessarily mean the company is not creditworthy." Next to "monthly credit guide" was "GBP 0". The risk category was "above normal risk". Company details from Companies house were printed out on 10 November 2010.

Overture:

74. On 8 May 2009, Deniz Ali, as company director of Overture Trading Ltd faxed a letter to the appellant:

> "Dear Sirs
>
> I would like to take this opportunity to thank you for choosing Overture Trading Ltd as your trusted trade partner.
>
> Overture Trading Ltd. was formed in 2007 and has a strong team of individuals with years of experience and a broad knowledge in a number of industries, trading in a variety of commodities.
>
> We have a number of customers / supplies from within the UK and worldwide, from distributors, resellers and manufacturers.."

75. The fax attached copies of the company certificate on change of name (from Live Telecoms (International) Limited on 6 December 2007 and VAT registration.

76. On 18 November 2009 and again on 13 May 2009 the Europa validation response confirmed the VAT number was valid.

77. The Euler Hermes credit limit enquiry dated 18 January 2010 stated "Limit not found".

78. The Graydon credit report supplied on 29 January 2010 had an "X" next to Graydon Rating and the statement "Credit is not recommended". The monthly credit guide was GBP 0 and the risk category "high risk". In the official company data section the company's status was described as "dormant". In a companies house search on 10 November 2010 the company was described as "active", shown to be incorporated in 2004. The last filed accounts at Companies House were stated to be those to 31 July 2009.

79. Mr Lawson's evidence was that Tony Jones visited Overture to meet with the directors.

TMP:

80. The Graydon credit report dated 22 February 2010 stated next to "Graydon rating" "OD" and then "Less than GBP1 – This does not necessarily mean the company is not creditworthy." Next to "monthly credit guide" was "GBP 0". The risk category was "above normal risk".

81. On 17 March 2010 Mr Deniz Ali wrote to the appellant as follows:

> "Ref: Continuous Co operation
>
> Dear Tony,
>
> As you are aware we have been doing business over a period of time. I have left overture and decided to join Hands with TMP Distribution."

82. After explaining that TMP worked with a range of businesses and that it was a "Pan-European Distributor for Electronics, Games Consoles, IT hardware and accessories" Mr Ali went on to say:

> " I would like to continue our previous business relationship forward through TMP and hope we can have the same sort of understanding and co operation as before. We can offer you better prices and product availability."

83. The letter included an undated generic letter of introduction from the director Simon Warren.

84. On 25 March 2010 the Europa validation confirmed the VAT number was valid. On 9 April 2010 a companies house printout showed the company was active. On 16 April 2010 HMRC (Wigan) wrote to the appellant to confirm the VAT registration appeared to be valid.

Appellant's response to warnings:

85. On 16 April 2009 Mr Lawson wrote an e-mail to Mr Nevin (copying in Mr Lothari the accountant and Mr Gilbey the manager, Mr Jones and Ms Hummer). After thanking Mr Nevin for his recent correspondence and advice it went on to say:

> "We have now taken additional measures to verify validity of VAT number (both suppliers and customers) for **each and every transaction** we do. The printout of check carried out via recommended web site by yourself will be attached to every invoice/ purchase order and filed together. This measure is already in place.

> We have also discussed our situation with supplies from Electrocentre. It's apparent that supplies from Electrocentre are causing concerns to HMRC. We have therefore discontinued any further purchases from Electrocentre until we are satisfied that everything is correct. To this extent we would be grateful for your advice if it is OK to purchase from them again in future…
>
> I do hope that above bring are closer to finalising your verifications and that we will receive outstanding VAT soon."

Law

86. HMRC's skeleton argument set out the background European law, UK and case law excerpts which we gratefully adopt and set out below with some minor adaptations.

87. Articles 167 and 168 of Council Directive 2006/112/EC of 28 November 2006 which are implemented into UK law by ss24-26 Valued Added Tax Act 1994 provide the right for taxable person to deduct input tax. HMRC relies on the exception to this right identified by the European Court of Justice ("the ECJ") in its judgment dated 6 July 2006 in the joint cases of *Axel Kittel v Belgium & Belgium v Recolta Recycling* SPRL (C-439/04 and C-440/04) where the Court stated:

> "51. … traders who take every precaution which could reasonably be required of them to ensure that their transactions are not connected with fraud, be it the fraudulent evasion of VAT or other fraud, must be able to rely on the legality of those transactions without the risk of losing the right to deduct the input VAT.
>
> 52. It follows that, where a recipient of a supply of goods is a taxable person who did not and could not know that the transaction concerned was connected with a fraud committed by the seller, Article 17 of the Sixth Directive must be interpreted as meaning that it precludes a rule of national law under which the fact that the contract of sale is void, by reason of a civil law provision which renders that contract incurably void as contrary to public policy for unlawful basis of the contract attributable to the seller, causes that taxable person to lose the right to deduct the VAT he has paid. It is irrelevant in this respect whether the fact that the contract is void is due to fraudulent evasion of VAT or to other fraud.
>
> 56. … a taxable person who knew or should have known that, by his purchase, he was taking part in a transaction connected with fraudulent evasion of VAT must, for the purposes of the Sixth Directive, be regarded as a participant in that fraud, irrespective of whether or not he profited by the resale of the goods.
>
> 57. That is because in such a situation the taxable person aids the perpetrators of the fraud and becomes their accomplice.
>
> 58. In addition such an interpretation, by making it more difficult to carry out fraudulent transactions, is apt to prevent them.
>
> 59. Therefore, it is for the referring court to refuse entitlement to the right to deduct where it is ascertained, having regard to objective factors, that the taxable person knew or should have known that, by his purchase, he was participating in a transaction connected with fraudulent evasion of VAT, and do so even where the transaction in question meets the objective criteria which form the basis of the

> concept of "supply of goods effected by a taxable person acting as such" and "economic activity".
>
> 61. … where it is ascertained, having regard to objective factors, that the supply is to a taxable person who knew or should have known that, by his purchase, he was participating in a transaction connected with the fraudulent evasion of VAT, it is for the national court to refuse that taxable person entitlement to the right to deduct."

The should have known test

88. The law in this field received clarification from the Court of Appeal in the conjoined appeal cases heard before it under the reference: *Mobilx Limited & Others v The Commissioners for Her Majesty's Revenue & Customs* [2010] EWCA Civ 517.

89. It is accepted by both parties that for the purposes of the "should have known" test it is not enough to show the trader should have known that by its transaction there was a possibility or even a probability of tax loss.

90. In *Mobilx* the Court of Appeal confirmed at [59]-[60]:

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

91. The Court of Appeal confirmed that the burden of proof in these proceedings lies with HMRC (at [81] of its decision). The standard of proof is the ordinary civil standard, proof on the balance of probabilities.

92. In *Megtian Limited* [2010] EWHC 18 (Ch), Mr Justice Briggs emphasised the distinction between the 'knew' and 'should have known' test, stating at [41] that:

> 'It is important to bear in mind, although the phrase "knew or ought to have known" slips easily off the tongue, that when applied for the purpose of identifying the state of mind of a person who has participated in a transaction which is in fact connected with a fraud, it encompasses two very different states of mind. A person who knows that a transaction in which he participates is connected with fraudulent tax evasion is a participant in that fraud. That person has a dishonest state of mind. By contrast, a person who merely ought to have known of the relevant connection is not dishonest, but has a state of mind broadly equivalent to negligence.'

93. In *Davis & Dann Limited v HMRC* [2013] UKUT 0374 (TCC), the Upper Tribunal said in respect of the 'should have known test':

> [38] 'This test presents a high hurdle for HMRC which we think is most easily appreciated by noting that it is not enough that the circumstances of the taxpayer's transactions might reasonably lead him to suspect a connection with fraud; nor is it enough that the taxpayer should have known that it was more likely than not that his purchase was connected to fraud. In other words, he can appreciate that everything may not be right about the transaction but that is not enough. He should have known that the transactions in which he was involved were connected to fraud: he should have known that they were so connected because that is the only reasonable explanation that can be given in the circumstances of the transactions.'

Legal issues to resolve

HMRC must show only reasonable explanation?

94. The appellant argues by reference to *Mobilx* ([59] of the decision set out above but also [74] and [75]) and the passage in *David and Dann* that it is only when the circumstances surrounding the transaction are such that there is only one reasonable explanation that it can properly be said that the trader should have known its purchase connected with fraud. Further the appellant maintains that it is for HMRC to prove that there was only one reasonable explanation for the transaction being connected with fraud and that they must eliminate all other reasonable explanations for the appellant entering into the transaction. The appellant referred us to the FTT's decision in *GSM Export Ltd. v HMRC* [2012] UKFTT 744(TC) and submitted that the approach taken there had wrongly widened the means of knowledge test in suggesting that it could be satisfied by something other than a demonstration that the only one reasonable explanation was fraud. HMRC disagree that they must show there is only one reasonable explanation and argue the reference to reasonable explanation is illlustrative. In relation to this point on the afternoon after the hearing finished HMRC drew the Tribunal's and the appellant's attention to the Upper Tribunal's decision in *GSM Export Ltd. v HMRC* [2014] UKUT 0457.

95. The grounds put forward by the appellant trader who had lost before the FTT included an argument that *Mobilx* had held that either actual knowledge of fraud had to be shown or if not that there was no other reasonable explanation for the transaction apart from such a connection to fraud and that in that case the appellant's legitimate grey market trading provided a reasonable explanation.

96. Proudman J dealt with the argument as follows:

> "However *Mobilx* does not purport to change the test in Kittel's case. The requirement as to the taxpayer's state of mind squarely remains "knew or should have known". The reference to "the only reasonable explanation" is merely a way in which HMRC can demonstrate the extent of the taxpayers' knowledge, that is to say, that he knew, or should have known, that the transaction was connected with fraud, as opposed to merely knowingly running some sort of risk that there might be such a connection. The FTT rightly recognised this in its decision (at [121]–[122]). The FTT therefore did not incorrectly construe and apply the test in Kittel's case."

97. In holding that the "only reasonable explanation" reference was illustrative the UT also must be taken to have rejected the view that it fell to HMRC to eliminate all other reasonable explanations and show that the only reasonable explanation for the transaction was fraud.

98. The appellant referred us to excerpts from the FTT decision of *Hira* at [115] and [116] inviting the Tribunal to take care imputing the trader with knowledge of matters that are only appreciable with the benefit of hindsight. HMRC say we should read those in context. In our view the appellant's arguments on *Hira* do not assist – it is already clear that what we need to focus on is the *Mobilx/ Kittel* test. The observations in *Hira* are simply that it is more difficult to reach the conclusion there was actual knowledge by inference than it is in the case of showing means of knowledge.

99. HMRC also submitted that (1) the law should be read purposively (to reduce and deter MTIC crime) and (2) negligence is central to the should have known test in that a trader who fails to spot warning signs that a reasonably diligent trader would have recognised will fail the should have known test.

100. Paying heed to the call by Moses LJ in *Mobilx* not to over-refine the test in *Kittel* in relation to (1) there appears to us to be no support or need to take a purposive interpretation of the law beyond that which is stated by *Kittel*. In relation to (2) this formulation is simply another way in our view of expressing how the test in *Kittel* might be approached. We note it still requires it to be considered in doing so what for instance would constitute "warning signs" and whether a reasonably diligent trader would have recognised them.

101. We ought to mention, because it is relevant to the issue of what it is that the trader ought to have knowledge of, that since the hearing of the appeal the Court of Appeal issued its decision in *Fonecomp Ltd v HMRC* [2015] EWCA Civ 39 (leave to appeal to the Supreme Court was refused).

What is it that the trader has or ought to have knowledge of?

102. In *Fonecomp* the FTT made findings that Fonecomp did not know exactly how the fraud was perpetrated:

> "We do not find that Fonecomp knew or should have known that Softlink would default or that there was a defaulter whose fraud Klick would arrange to cover up."

103. At [48] of Court of Appeal's decision in *Fonecomp* Arden LJ (with whom the other LJs agreed) had this to say about the issue of what knowledge was required:

> "Lack of knowledge of the specific mechanics of a VAT fraud affords no basis for any argument that the decision [of either the FTT or the UT] was wrong in law: what is required is simply participation with knowledge in a transaction "connected with fraudulent evasion of VAT" (*Kittel* [61] [set out at [87] above])

104. Also at [51] the decision noted:

> "...the holding of Moses LJ does not mean that the trader has to have the means of knowing how the fraud that actually took place occurred. He 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. This is apparent from [56] and [61] of Kittel cited above. Paragraph 61 of Kittel formulates the requirement of knowledge as knowledge on the part of the trader that "by his purchase he was participating in a transaction connected with fraudulent evasion of VAT". It follows that the trader does not need to know the specific details of the fraud."

Relevance of other deals and transactions and connection to tax loss?

105. The appellant disputes HMRC's suggestion that Deals 1-16 trace back to tax loss. It says the evidence on these transactions was not tested before the tribunal. For instance in Deal 6 it is accepted from the chart there is insufficient evidence. Without testing the evidence the appellant queries how the tribunal could be sure any of these deals took place? The units purchased and sold were different and HMRC had withdrawn their decisions in relation to Deals 1-16.

106. HMRC take objection to this argument being raised in closing submissions as it was. HMRC had made it clear in its opening that it was relying on the earlier deals to show the wider circumstances of the deals under appeal. It called Mr Nevin and Mr Nevin's statement goes through each deal and refers to evidence of other witnesses e.g. Mr Brownsword. It submits that if the appellant took issue it should have cross examined him on it. HMRC maintain contrary to what the appellant says that Deals 3,4,5,7 and 10-16 do trace to tax loss (the reason why input tax was not eventually denied on these deals because HMRC acknowledge they had insufficient evidence on knowledge / means of knowledge). For deals 1, 2, 6, 8 and 9 HMRC say it cannot show the deals involved the same goods but it says there is sufficient evidence to show the parties were trading together in same type of goods round about the same time.

107. The appellant conceded after hearing the evidence that was given that Deals 17-19 were connected to tax losses (having accepted previously the tax losses were fraudulent).

108. Further, HMRC say it is misleading to say, as the appellant does, that only small numbers of deals trace to tax loss. HMRC only analysed the broker deals. Mr Nevin's job was only to look at VAT reclaims so e.g. the UK deals to Richer Sounds and AV premier went "under the radar". All the deals involving TVs connected to tax loss but only some relate to input tax denial. HMRC also say it is significant that it is not just export deals which are connected to tax loss but also sales to retailers – this puts into context the frequency of tax loss.

109. In our view it is not however necessary to the issue before us to make a finding on whether HMRC have shown that as a matter of fact deals 1-16 connect to fraudulent evasion of tax loss. Even if one or more of those deals were connected to tax loss that would not help us on the issue of whether the appellant ought to have known that Deals 17-22 were connected to fraudulent tax loss. The fact of tax loss does not make it more likely to be the case that the appellant ought to have known subsequent deals were connected with tax loss. (This is distinct from the facts surrounding the circumstances of such transactions e.g. details as to the warning letters or due diligence in relation to those other transactions which could be relevant

to as such evidence assists in building up a picture of the appellant's general level of awareness by the time they entered into the particular deals under appeal).

110. As regards the relevance of the fact of connection to tax loss in previous deals to actual knowledge, again we think this does not assist in the circumstances of this case.

111. In their closing submissions HMRC maintained that the means by which the fraud operated was by the importation of zero-rated goods by a defaulting trader, who failed to account for the VAT charged on its onward supply in the UK. The goods were then sold down a chain to the appellant and either exported or sold on to an end user within the UK. It is apparent from this that the means by which fraud operated indicate an acquisition fraud (the object being non-payment of acquisition VAT by the defaulting trader) rather than MTIC fraud (the object of the fraud being the reclaim of input tax by a broker exporting to the EU). At the hearing HMRC submitted that the number of links in the supply chain were there to distance the final sale from the defaulting trader.

112. It might be argued that findings of connection to tax loss in previous deals would be relevant in the context of organised MTIC fraud (in that the more deals the trader had entered into with different suppliers which were connected to tax loss the more likely it was that the trader was in on the scheme because of the difficulty of making the fraud work without the traders in the chain acting in an orchestrated way). However the issue of connection to tax loss in deals where the trader had not dealt directly with the defaulting trader would not be relevant in the same way to the question of actual knowledge of fraud in the deals under appeal which HMRC say concerns acquisition fraud. The mere fact a trader played a role in previous deals which connected to tax loss would not make it any more likely that they had actual knowledge of fraud in the transactions they undertook. Even if it were accepted that there was connection to tax loss in deals 1-16 this would not therefore make it more likely than not to be the case that the appellant had actual knowledge their transactions in deals 17-22 were connected to fraud. A finding that HMRC had not shown connection to fraud in Deals 1-16 would similarly not assist the appellant – it would not make it any less likely to be the case that the appellant lacked actual knowledge in relation to Deals 17-22.

113. A further reason why the mere fact of connection would not assist HMRC's case arises from the absence of evidence as to the circumstances in which the appellant came to trade with the sellers in deals 1-16. So, if it was the case that the sellers had approached the appellant rather than the other way round the fact of tax loss in deals 1-16 would be just as consistent with an explanation whereby the appellant had been duped into entering into those transactions. Repeated transactions with the same seller in such circumstances would also be just as consistent with the behaviour of an innocent trader as one who had actual knowledge.

114. We should also note that to the extent the appellant invites us to find that Deals 1-16 together with a number of the other transactions were *not* connected to tax loss and were examples of the appellant trading legitimately, in order to further a submission that the features of such deals were identical to the supplies where fraud was shown to exist, there is insufficient evidence before us to make such a finding. Even if it were correct that Deals 1-16 did not take place along the transaction chains that HMRC suggest, the appellant has not advanced a case which sets out what the transaction chains were for the deals which did in fact take place and satisfied us that

there was no fraudulent loss of tax in such deals. Similarly in relation to the other transactions on the SAGE print outs the appellant has referred us to it has not been demonstrated what the transaction chains were and that there was no fraudulent evasion of tax in such chains.

115. Mr Nevin's evidence was that there were certain deals which did not have tax losses namely those in relation to audio equipment (from an authorised distributor or Samsung and Panasonic audio equipment) and headphones and cordless headphones from a manufacturer and where the goods were sold retail. While these deals did not contain tax losses this does not assist the appellant as there was no evidence before us on the circumstances of these transactions and how if at all they were similar to the transactions which form the subject of this appeal. What evidence there is on these transactions suggest the purchases were from authorised distributors of the manufacturer or the manufacturer themselves. Those transactions do not appear comparable to the deals under appeal.

Factual issues to resolve

Who was the appellant's controlling mind? Mr Lawson, Mr Jones or both of them?

116. HMRC argue that in reality Mr Lawson had little to do with the day-to-day operation of the appellant by the time of the transactions under appeal. He did not set up the trades or deal with the paperwork. He was not responsible for conducting due diligence. His account of his oversight varied and HMRC suggest his later evidence that every transaction would have been brought to his attention was an exaggeration as Mr Lawson recognised the difficulties his limited involvement presented.

117. When asked about the level of his oversight his initial answer was:

> "I don't know each individual nuance of each transaction I admit. But I did get actually sales reports and weekly updates on what's going on so I was aware of the transactions in the chain… Its not my job, actually, to know exactly what [Tony Jones] does in every single – he's been with me for ten years by then".

118. Later on in his cross-examination he then said:

> "And actually I was considering what you were suggesting earlier. I would just like to point out that every single transaction we have done would have been brought to my attention as it was happening. We are buying from here, selling to there, this is the margin, including transport, excluding transport, this is our cash-flow position. Do we proceed? Do we not? That was standard trading facts. I have not mentioned this to you earlier."

119. Mr Lawson's name was not apparent on the documents in the six deals in issue, he had not provided evidence of the weekly reports he mentioned, he was focussed on other projects and on looking after his sick son. HMRC provide a whole raft of examples of documents which point to Mr Jones in particular being involved in the conduct of the transactions. HMRC also place significance on Mr Jones being on the front line as regards dealings with HMRC.

120. Mr Lawson's evidence was not wholly reliable. It revealed inconsistencies because as described above he changed stance on the level of his involvement and

oversight of the transactions. In his witness statement he stated that the HMRC letter referring to Overture tax losses (this must have been the letter dated 15 September 2009 as the second one was dated 19 June 2010) was first received on 18 May 2010 but when asked about when the 15 September 2009 letter was received in cross-examination his answer was confused. His evidence in certain areas was also vague and unclear given his role as the director and sole owner of the appellant for example he was not also able to answer directly as to whether the appellant sold games consoles or televisions to a major customer TJ Hughes.

121. We agree with HMRC's submission that Mr Lawson was seeking to exaggerate his involvement to serve his case according to his understanding. We find that he had minimal involvement in the day to day running and oversight of the appellant at the time of the deals in question.

122. The relevance of this finding is considered below at [141].

123. In relation to HMRC's invitation to us to draw adverse inferences from the non-attendance of Mr Jones and Ms Hummer despite witness summons being issued to secure their attendance we decline to do so. The summons had been issued at the request of the appellant and it was we think open to the appellant to retract its request for a summons as it did on the basis that it no longer sought to rely on the evidence of those witnesses.

Actual knowledge?

124. The appellant argues there is no evidence to suggest the appellant knew of any fraud in its purchases. They highlight that HMRC make no allegation that goods were "carouselled", that the appellant's customers were not bona fides, that TVs were sold at unrealistic prices or that the appellant's mark-up was unusual or unrealistic. The commerciality of the deals was not called into question.

125. HMRC say there was an orchestrated scheme to defraud. Mr Lawson conceded this in his evidence and it is also apparent from the number of the traders in the chain and the short time the goods spent in the UK with no apparent value added and cost and risk increased. They also point to the feature of the suppliers "stepping up a level" and say this was consistent with the appellant helping them to contrive this. By this they mean that Winnington which was Electro Centre's supplier in Deals 8-9 replaced Electro Centre as the appellant's immediate supplier after the appellant was notified in April 2009 that purchases from Electro Centre traced to tax loss and that in Deals 10-17 Winnington was replaced as the appellant's immediate supplier by Overture which had been Winnington's previous supplier.

126. They also ask us to note the evidence that Overture knew the identity of the appellant's customer (TJ Hughes) and that this is indicative of collusion. This is on the basis that a trader would not want their supplier to know who the trader's customer was for fear that the supplier would trade directly with the trader's customer. They say that the explanation given by the appellant that the name was disclosed because there was a threatened legal action from the customer if their order was not fulfilled or late is illogical.

127. HMRC also say that the due diligence performed by the appellant was window dressing. The appellant only did it because they knew that it was necessary in order to get a reclaim.

128. Our conclusion is that the points HMRC have raised do not persuade us the appellant had actual knowledge that their transactions were connected with fraud and that there is insufficient evidence before us to make such a finding.

129. The "stepping up" of the transactions highlighted by HMRC is also we think consistent with normal commercial behaviour where traders in a supply chain would so far as possible seek to cut out "the middle man". Furthermore we did not receive any evidence which would allow us to make a finding on whether it was the appellant who made the approach to the new supplier or whether the new supplier approached the appellant. If the latter the appellant would not necessarily be likely to know that the new supplier had been in the previous chain (unless they had been the immediate supplier). While with the benefit of the deal charts that have subsequently been prepared it appears that the chain was contrived, in the absence of evidence as to who approached who we decline to conclude, as HMRC suggest, that the appellant's knowledge of fraud explains the ease of "stepping up". The stepping up could be explained by Electro Centre asking Winnington to contact the appellant.

130. Reflecting the discussion above at [105] on the relevance of the appellant's other transactions, we would also observe that the fact the transactions chains look to be contrived as to who sold to who is less indicative of a finding of actual knowledge where the fraud at issue is alleged to be acquisition fraud. If, as HMRC say, the contrivance was targeted simply at ensuring distance between the defaulter from the end of the chain the contrivance would only need to go as far as ensuring that a *sufficient number* of links went into in the chain. By contrast the higher degree of contrivance if demonstrated in an MTIC fraud case requiring orchestrating the particular *identity* of those in the chain, ensuring there was a broker sale and the particular prices of transactions would be more indicative of a broker trader's actual knowledge that it was participating in a fraud.

131. It follows from the observation above about commercial behaviour that a supplier in a chain would be careful not to reveal the identity of its customers to the trader it was buying from. In relation to the point made about Overture being told that TJ Hughes was a customer of the appellant we agree with HMRC that any argument that this information had to be revealed to fend off a legal dispute threatened by the customer is illogical; the appellant could have expressed the view that the supply was urgently needed due to threatened legal action without disclosing who the customer was. However we do not accept that the disclosure by the appellant of its customer necessarily amounts to evidence of collusion between the appellant and Overture such that the appellant had actual knowledge of fraud by its purchase. As we have noted above at [31], Mr Jones and Mr Ali were on familiar terms. It is not implausible that a relationship of personal trust existed between them to an extent that Mr Jones was comfortable mentioning the name of the customer to Mr Ali without being concerned that Mr Ali would use the information to bypass the appellant.

132. While we accept the due diligence that was carried out was done because this was what the appellant thought it needed to do to get its input tax reclaim that fact does not of itself point towards the appellant knowing its transaction was connected

with fraud. It is just as consistent with the appellant not knowing of the connection but being concerned to have its input tax claim accepted by HMRC.

Means of knowledge?

133. The appellant highlights that the Tribunal should ignore various factors (length of deal chains, other parties, mark-ups, financial arrangements) outside of the appellant's knowledge – it should look at the relationships with suppliers and customers and the transactions themselves. It should take into the account the whole of the circumstances of the transaction and not just whether the appellant carried out due diligence.

134. There are a variety of reasons as to why the appellant says it has not been shown that it ought to have known the deals to which their appeal relates were connected to fraudulent tax evasion.

135. Essentially these are to the effect that the appellant reasonably assumed deals were not connected to fraudulent tax loss because:

(1) No joint and several liability letters had been issued as had been indicated by Notice 726;

(2) the appellant had assumed all deals would be checked by HMRC not just the ones which involved an export; it had assumed that all the non-export deals where no tax loss letters had been sent were legitimate; and

(3) the tax loss deals were different as far as the appellant was concerned because they involved games consoles rather than TVs.

Notice 726 and lack of Joint and several liability letters

136. The appellant points to the fact that HMRC had through its notice indicated that it would take certain actions (imposing joint and several liability) if certain criteria were not met. The appellant did not receive any joint and several liability letters. The appellant argues that the test is almost identical to that for denying input tax and that this was accepted by Mr Nevin. It says this was acknowledged in terms by Moses LJ in *Mobilx* at [85]. HMRC point out that Mr Nevin's evidence was that he was working in a role to do with making decisions on allowing input tax.

137. We are not persuaded the appellant's argument is correct. There is insufficient evidence and we do not find it likely as a matter of fact that the appellant had actually carefully scrutinised the terms of Notice 726 in the way the appellant now invites us to do. We do not accept that the appellant thought that everything was fine (despite warning letters being repeatedly sent) just because joint and several liability had not been imposed by HMRC. Even if one were to read Notice 726 so literally so as to be saying a trader was safe to deal with other particular traders until HMRC told them otherwise the criteria were based on the trader having done everything they could to check the integrity of the supply chain. Given there was no continuous and timely reporting system of the due diligence that had taken place by traders to HMRC it is difficult to see how a trader could in any case have reasonably thought that HMRC would know what due diligence had taken place in order to be able to make up to date decisions on joint and several liability in a systematic fashion.

Just export deals checked?

138. Even if the appellant's argument was correct at best all the appellant could have thought was that HMRC had not at a given point in time identified a link to tax loss. It could not reasonably have been concluded by the appellant from the absence of warnings or other action from HMRC that as a matter of fact there was no tax loss in the chain.

139. In particular we are not persuaded by the appellant's argument that the fact that Winnington was still "allowed" to trade acted as some kind of endorsement of Winnington. It would be apparent to a trader in the appellant's circumstances who had received the letters at the time the appellant did that there was a time lag between the deals taking place and the point in time notification of the deals linked to tax loss was given. The appellant cannot have reasonably expected that if companies had not been shut down by HMRC this was a sign that it was fine to trade with them.

Tax loss deals were games consoles rather than TVs

140. We agree with HMRC that the difference in type of electrical goods traded is not a reasonable distinction to draw. Even if this was something that Mr Lawson thought at the time – (and we think it is doubtful as there is no evidence he played a role in the TV deals) it is not a reasonable explanation. Having been warned that the Electro Centre deals traced back to tax loss a reasonably diligent trader would, we think, take all the more care before reaching the conclusion they could continue to trade with that supplier in electrical goods of any kind even if they were not the same electrical goods as those in which tax losses had been identified.

Significance of the level of Mr Lawson's involvement in the business

141. Although we have indicated above that Mr Lawson was not as heavily involved in the day to day business of the appellant as he was inclined to make out we do not think that this fact in and of itself means the appellant company ought to have known the transactions it undertook were actually connected with fraud. It is necessary to first consider amongst other matters the adequacy of the due diligence procedures that might reasonably have been put in place, the enquiries that might reasonably have been made and further what information these procedures and enquiries would have revealed.

Due diligence

142. We agree with HMRC's observations that the appellant's due diligence was inadequate. Mr Lawson did not carry it out – he was unclear in relation to who had done it and in relation to which companies it had been done. Crucially what due diligence there was, was often done after the deals commenced and in some cases after the deals were concluded. The information received was limited or negative (high credit risk). The due diligence which was carried out was for the purposes of successfully reclaiming input tax from HMRC. A further deficiency was the fact that due diligence was entrusted to sales personnel including Mr Jones, someone who was incentivised to maximise profit from the making of deals as his remuneration included commission based payments.

143. Mr Lawson said Mr Jones had spoken with Electro Centre following the appellant being notified that Electro Centre was a participant in carouselling. HMRC

draw attention to the fact that no evidence was provided of such a conversation and also make the point it would be difficult to see what reassurance a telephone conversation would provide that it was safe to trade. We agree. A reasonably diligent trader would have done far more before deciding to continue to trade.

144. We think it is clear from appellant's answers in cross-examination that getting credit reports from Grayden whom he held in low regard was something which was simply done to placate HMRC.

145. We find the appellant's argument that it did not bother with carrying out too much due diligence because these were trusted long-time suppliers unpersuasive in that while we accept this may be the basis on which it approached its due diligence as a matter of fact, we do not accept that this was a reasonable way to proceed. A reasonable trader would not, having received the warnings HMRC gave, have relied on previous dealings where previous dealings had not been an effective means of identifying connection to fraud. If anything, the fact that fraud had been linked to trusted long time suppliers ought to have been even more of a wake up call that wholesale improvements in whatever due diligence procedures there had previously been needed to be implemented.

146. In relation to whether the appellant had been remiss, as HMRC were suggesting, in failing to seek trade references, Mr Lawson's answer, HMRC say, does not make sense. There would be no issue with say a supplier saying its buyer was e.g. an identified reputable department store. Mr Brown's reply for the appellant on this was that there would be an issue as wholesalers would be clamouring to do business with the department store if they knew it dealt with persons other than manufacturers / OEMS. The issue of trade references would be sensitive in relation to current business customers but not previous business. HMRC argue that in any case the appellant could have satisfied itself as to what due diligence systems its supplier had in place and asked them to do the same with their supplier.

147. The appellant did not to our mind seek to mount any serious challenge to HMRC's criticisms of the due diligence that took place. The appellants' riposte was that due diligence was not the be all and end all of the analysis on means of knowledge. The main criticism of the due diligence was that it was done in the main after the deals were done. We should however be careful not to read too much into the appellant's treatment of the due diligence it carried out. The due diligence that was done was not done for commercial reasons but to satisfy the requirement they perceived on HMRC's part for repayment of input tax.

Deal 17

148. The appellant argues it believed that all its deals not just broker ones would be scrutinised by HMRC. The appellant argues that by 23 October 2009 (the Deal 17 date) it had made over 38 separate purchases of goods of including game consoles and TVs from Overture and had been told that two were traced to tax loss. It believed all its transactions declared on returns 01/09 to 07/09 were subject to scrutiny.

149. The fraud was perpetrated by Winnington acting as a contra-trader. The appellant says there was no evidence to suggest it knew Winnington would appear in the chain or that it should have known the appellant was acting as a contra-trader.

150. HMRC highlight (and we find as fact) that rather than being advised of just two transactions (as the appellant says) connecting to fraud which had taken place while Mr Ali was at Overture, the appellant was advised of four transactions. (Not just Deals 12 and 13 on 19 June but also Deals 10 and 11 notified in letter of 15 September 2009.) The appellant first traded with TMP on 24 March 2010.

151. HMRC also ask us to note that the paperwork was in the incorrect order (see [21] above); the Overture sales invoice post-dated the appellant's invoice to its customer and the appellant's shipment of goods) and that the appellant's willingness to ship goods to which it did not have title and Mr Ali's willingness to let this happen demonstrated a lack of proper systems in the conduct of business between Mr Ali of Overture and the appellant.

Conclusion on means of knowledge for Deal 17

152. We find that the appellant ought to have known that deal 17 with Overture was connected to fraudulent evasion of tax for the following reasons.

153. The appellant received from HMRC a specific warning in relation to a transaction it had undertaken with Overture in HMRC's letter of 15 September 2009 (see [64]).

154. We consider that a reasonably diligent trader who had received such a warning would have stopped trading with Overture immediately. Having stopped trading, such a trader would only recommence trading having conducted rigorous due diligence to satisfy itself it was safe to deal with Overture without engaging in further transactions which were linked to fraudulent tax loss. The due diligence that would be reasonable in such circumstances would not be due diligence simply for commercial purposes but due diligence aimed at identifying so far as reasonably possible whether further transactions with Overture would not be connected to fraudulent tax loss.

155. As well as reminding the appellant of the prevalence of MTIC fraud and identifying that the appellant's transaction had been linked to tax loss we think the warning letter would also have signalled to the trader receiving it that whatever due diligence procedures the trader had had in place at the time of the identified transaction had been inadequate.

156. The appellant knew or can reasonably be taken have known from the many previous warning letters that had been received that there was a significant time lag between the warning letters and the purchases to which the warning letters related to. It could not, we think, reasonably have thought that the transactions it had undertaken in the meantime had been "blessed" by HMRC.

157. It cannot in any case have reasonably formed the view that the previous transactions which it had conducted but which had not been identified as being linked to fraudulent tax loss by HMRC were by dint of that not linked to fraudulent tax loss.

158. As noted above the fact there was a previous relationship of trust with Overture ought to have prompted the appellant to have carried out an objective, critical and comprehensive review of its dealings with Overture and Overture's background in order to be satisfied that it was safe to transact with Overture again if at all.

159. A reasonably diligent trader having received the warning relating to MTIC fraud which the appellant had would, we think, have asked Overture to provide details of its trading history including financial information e.g. accounts and/or turnover figures. If it had it would have discovered Overture had had a rapid increase in turnover.

160. While a relatively weak indicator by itself but of relevance when added to totality of the circumstances a reasonably diligent trader would have found out before carrying out any deal from a simple company search that Overture had changed its name from Live Telecoms.

161. The point HMRC make about trade references in relation to past business does no assist as it is not clear what if anything the appellant would have found out that would have indicated links to fraudulent loss of tax if references from Overture's customers had been sought. Similarly we put to one side HMRC's suggestion that the appellant ought if acting as a reasonable trader to have made enquiries as to what due diligence procedures Overture carried out because there was no evidence to suggest that these enquiries would have necessarily revealed anything untoward.

162. In summary it would have been apparent to a reasonably diligent trader that:

(1) goods which had been bought previously from Overture were linked to tax loss and that the fact that warning letters had not been received in relation to other transactions with Overture did not mean those transactions did not link to tax loss;

(2) previous due diligence had been deficient and that if changes were not made the due diligence would continue to be deficient;

(3) Overture had come from very humble beginnings but was able to achieve a rapid and spectacular increase in turnover; and

(4) Overture's previous name of Live Telecoms could suggest involvement in mobile phones a product known to be employed in MTIC fraud.

163. Our view is that a trader who in such circumstances then proceeded with Deal 17 ought to have known that its transaction with the same supplier it had been warned about would be a transaction which was connected with fraud.

Deals 18-22 with TMP

164. Having considered the particular circumstances of each of these deals our conclusion is that the appellant ought to have known that in each of these deals its purchase was connected to fraudulent evasion of tax for the following reasons.

165. While there was no specific warning from HMRC in relation to dealing with TMP, given the time lags in previous warnings the appellant cannot have reasonably thought the lack of a warning would give any comfort.

166. Again having received the warnings that it did in relation to previous suppliers a reasonably diligent trader would as discussed above have appreciated that whatever due diligence it had at the time was deficient and that the due diligence therefore needed to be made more rigorous.

167. A reasonable trader would not we think have proceeded to deal with TMP. Taking account of the findings in relation to what a reasonable trader would have

discovered in relation to Overture a reasonable trader would we think have been wary of carrying out transactions involving the same director particularly where that director was one of a small number of company officers at Overture.

168. The Graydon UK credit check of 29 January 2010 of Overture had stated the company to be dormant. The appellant's last transaction before this date was on 20 November 2009, and between that point and 8 April 2010 a seven further transactions were carried out with Overture. Mr Lawson's evidence was that Mr Jones visited Overture. It would we think have been apparent to a reasonably diligent trader in these circumstances that there was something untoward about its supplier being recorded as dormant but nevertheless continuing to trade

169. No due diligence or checks were made in relation to Mr Ali. It should not have mattered to the appellant that Mr Jones and Mr Ali were on familiar terms. Given the circumstances that ought to have signalled that more rigorous checks were in order. The fact the paperwork for Deal 17 indicated that goods had been sold on by the appellant before Overture had passed title for them would simply have added to the picture that these personnel were prepared to carry out transactions involving unusual levels of risk. If the thinking was that Mr Ali was fine to deal with it ought to have been expected that the appellant would have taken all the more care to make sure that Mr Ali understood that he should not use his contacts from Overture otherwise the further deals through those contacts would give rise to the same problems. It is difficult to see how by changing companies but using the same contact (and not making any effort to make sure Mr Ali did not exploit his old network of contacts) that things would change. Mr Lawson's evidence was that he thought Simon Warren (the other director at TMP) was apparently an old friend of Mr Ali. A reasonably diligent trader who had formed the impression that a director was moving to a new company where the existing director was an old friend could not have thought that whatever concerns there may have been about deals being run through Mr Ali would be assuaged by the move to the new company.

170. A director's search in relation to Mr Ali would have revealed that he remained a director of Overture despite having informed the appellant that he had joined TMP (the appellant said it was leaving Overture because of the warnings it had received) and despite, according to Mr Lawson's evidence, Mr Jones having been told that Mr Ali had had an argument with another person (Mr Lawson thought it was Ms Leak) and that Mr Ali did not want to work at Overture any more. In the circumstances the fact that Mr Ali remained as a director at Overture would we think have raised serious concerns.

171. The appellant says there are no documents to show it dealt with Mr Ali at TMP and that HMRC can only rely on inference. We think there is ample inference in the letter Mr Ali wrote about continuing relations (referred to at [81]). The fact the signature appearing on that letter does not appear to be the same as the signatures appearing on various TMP sales invoices, or that there were e-mails from other persons in TMP to the appellant does not mean Mr Ali was not the contact. In any case there is nothing to suggest that the concerns a reasonably diligent trader would have had about Mr Ali would be neutralised by other personnel signing invoices or corresponding with the appellant given the size of TMP.

172. A reasonably diligent trader would have made investigations into TMP's trading history. It would have appreciated that the appellant's name was "The Manual

People" and that it had previously been dealing in instruction manuals for electrical products. While as the appellant points out TMP was an existing company the appellant ought to have noticed that the company was embarking on a new direction and had had no history of dealing in TVs. The appellant ought, if had made the enquiries a reasonable trader would have made, have seen that TMP's turnover was very modest (tens of thousands per three month period). In the space of the period August to October 2010 it proceeded to trade close to half a million pounds of goods.

173. In relation to deals 21 and 22 the appellant drew our attention to the fact that TMP was not a classic MTIC fraud defaulter (although it accepts there was fraudulent evasion of VAT in failing to declare VAT for 11/10). The appellant says there is no evidence it knew or should or could have known this was going to happen. (It is clear however from *Fonecomp* that knowledge of the mechanics of the fraud is not required.)

174. It is enough that the appellant ought to have known that its purchases were connected with fraudulent evasion of tax.

175. Taking the above circumstances into account we come to the conclusion that the the appellant ought to have known that its purchases in relation to each of the Deals 18-22 were purchases connected to the fraudulent evasion of tax.

Conclusion on repayment of input tax

176. The appellant's appeal is accordingly dismissed in relation to its input tax reclaims.

Default surcharges

177. The appellant appeals against VAT default surcharges for various periods totalling £1,537.49 which HMRC imposed as follows. (By way of reminder the periods which were the subject of the appellant's appeals in relation to input tax lay between 10/09 and 10/10):

VAT Period	Amount of VAT due	Calculation percentage	Amount
11/10	£23,191.72	2%	£463.83
12/10	£1,541.02	5%	£77.05
01/11	£2,496.31	10%	£249.63
02/11	£228.35	15%	£34.25
03/11	£1,887.62	15%	£283.14
12/11	£3,377.60	15%	£506.64

Total			£1,537.49

Law

178. Section 59(7) VATA 1994 provides:

> '(7) If a person who apart from this sub-section would be liable to a surcharge under sub-section (4) above satisfies the Commissioners or, on appeal, a Tribunal that in the case of a default which is material to the surcharge –
>
> (a) the return or as the case may be, the VAT shown on the return was despatched at such a time and in such a manner that it was reasonable to expect that it would be received by the commissioners within the appropriate time limit, or
>
> (b) there is a reasonable excuse for the return or VAT not having been so despatched then he shall not be liable to the surcharge and for the purposes of the preceding provisions of this section he shall be treated as not having been in default in respect of the prescribed accounting period in question (and, accordingly, any surcharge liability notice the service of which depended on that default shall be deemed not to have been served)'

179. Section 71 VATA 1994 provides:

> '(1) For the purposes of any provision of section 59 which refers to a reasonable excuse for any conduct -
>
> (a) any insufficiency of funds to pay any VAT due is not a reasonable excuse.'

Parties' submissions

180. The appellant argues that it had a reasonable excuse for the outstanding VAT not being paid. This was because:

> (1) it had an agreement with HMRC that it could offset its ongoing VAT liabilities against the amount in dispute in the appeals until those appeals were determined before the FTT.
>
> (2) In the alternative there were amounts of VAT under appeal that were greater than the liability on the unpaid returns.

181. As regards (1) the appellant referred to the FTT case of *Quartz Electrical and Mechanical Services Ltd v HMRC* [2013] UKFTT 451 (TC) by way of support for the proposition that an agreement with HMRC regarding payments is a reasonable excuse.

Did HMRC agree to offset VAT?

182. In support of its argument that there was an agreement to offset VAT with HMRC the appellant referred us to a letter dated 2 September 2009 from HMRC's "Large Debt Unit MTIC Co-ordination Team" to the appellant's accountant. This stated:

> "Further to your letter dated 10 July 2009 regarding [the appellant's] payment of VAT, we can confirm that as stated in your letter certain

> VAT periods are currently going through the verification process, once this process has been completed a decision will be made on whether the claims are paid back to the above company or not.
>
> During this time enforcement action will not take place for outstanding VAT returns.
>
> Please be aware that as normal procedure there may be financial penalties if VAT returns are not paid by the due."

183. The appellant's accountant's letter of 10 July 2009 advised that VAT due of £50,097.17 for the VAT return 31 May 2009 had not been paid for various reasons in essence relating to the failure to receive VAT repayments on time. The letter pointed out that £152,409.99 of repayments were still due and that the overall VAT account was therefore in credit. A request was made for the VAT due for 3 May 2009 to be formally offset against the balance due to the appellant. On 4 August 2009 the appellant's accountant wrote a further letter advising that:

> "…VAT due of £39593.93 for the VAT return for 30 June 2009 has not been paid and the overall VAT account is still in credit pending the release of repayments due for earlier months. Please offset the June 2009 payment due by our client against the net repayments to date due by HMRC."

184. It seems clear to us from this correspondence that HMRC were not agreeing to any offset. Given the reference in the last sentence to financial penalties if VAT returns were not paid when due the reference to suspension of enforcement action can only have made sense in relation to earlier VAT periods (where it appears from the table at [18] that payments were due to HMRC). The fact that the letter made it clear that there still might be financial penalties if VAT returns were not paid by the due date ought to have made it clear that the appellant's request for offset was not being acceded to. The appellant's request for offset was in any case a request in relation to specific periods (none of which are the periods before us on appeal.)

185. There being no agreement to offset it is not necessary to consider whether if there had been one this would have constituted a reasonable excuse.

Appellant's account in credit when amounts under appeal / HMRC's subsequent withdrawals taken into account

186. In relation to the appellant's alternative submission (2) above the appellant submits by reference to the VAT tribunal case of *Malcolm Bruce v CCE* VTD 16.660 that it is relevant for the Tribunal to take account of the withdrawal of HMRC's decisions which, if they had been made before the due date for the returns, would have put the appellant in credit with HMRC so that there would have been no VAT outstanding. The appellant also emphasises the fact that the drafting of s59 VATA essentially requires the tribunal to consider whether the taxpayer *has* a reasonable excuse not that he had one at the time of the default. (Section 59(7)(b) states "there *is* a reasonable excuse" rather than "there *was* a reasonable excuse"). The appellant also argues that if the Tribunal could not take account of later events (such as HMRC's withdrawal or the appellant having its appeal allowed) then taxpayers would have no remedy against having to pay a default surcharge which should never have been levied.

187. HMRC say each period has to be looked at by itself. If the appeal were successful then there are provisions for late award. The position cannot be that the appellant can choose whether or not to pay.

188. They also contend that the appellant's belief that VAT was not outstanding cannot constitute a reasonable excuse. The *Malcolm Bruce* case was unique in that HMRC were holding funds owed to the appellant. In the current case the appellant is not allowed to speculate on the outcome of VAT it is appealing.

189. We note that s59(1)(b) VATA 1994 refers to HMRC not receiving the amount of VAT "shown on the return as payable by him in respect of that period".

190. In *Malcolm Bruce* the VAT Tribunal ruled on the following preliminary issues (at [2] of its decision) on a case in which default surcharges had been imposed on the trader:

> "Does a subsequent outstanding credit balance held by the Commissioners in favour of the Appellant constitute payment of outstanding tax when the credit balance results from subsequent input of returns furnished late following the payment of centrally issued assessments, the centrally issued assessments having only been calculated after the effective due date for rendering returns and monies has passed? Does the discharge of outstanding VAT in this context fall within the definition of outstanding VAT within the Value Added Tax Act 1994 sections 59(4) and 59(6)?"

191. In that case it is recorded at [6] that "… the Appellant received and paid centrally issued assessments which were in excess of his liability subsequently shown on returns. The result was that by 31 August 1996 there was due to him from the Respondents the sum of £19,808". The appellant in that case submitted that there was no "outstanding VAT" during the period in which the appellant was in credit and therefore there was no liability to surcharge.

192. At [14] the Chairman explained his decision to answer both preliminary issues in the affirmative as follows:

> "I do not think that there can be any doubt but that a credit balance held by the Respondents in favour of the Appellant at any time in the circumstances of this case will have been held by the Respondents as VAT paid by the Appellant. As long as such a credit balance exceeded the amount of VAT due to the Respondents from the Appellant whether under returns or assessments, I do not think, in ordinary use of language, that there can have been "outstanding VAT" for the purposes of section 59(6) due from the Appellant…."

193. In relation to the argument following from what was said in *Malcolm Bruce* that there was no "outstanding VAT" during the period in which the appellant was in credit (despite there not having been any agreement to off-set as discussed above) we disagree that this argument assists the appellant in this case. The facts of *Malcolm Bruce* are not comparable in that the facts in that case as set out at [6] of its decision suggest that the assessments and the returns related to same period. This contrasts with the current situation where the subsequent credit arises in relation to an earlier period. On the facts of this case there was clearly VAT outstanding in respect of the periods which were the subject of the VAT default surcharge.

194. In relation to the appellant's argument that it had a reasonable excuse due to the fact that there were amounts of VAT under appeal that were greater than the liability on the unpaid returns, our conclusion is that this fact does not constitute a reasonable excuse.

195. We disagree with the appellant that the fact that s59(7)(b) states "there *is* a reasonable excuse" rather than "there *was* a reasonable excuse" means that the point in time at which to consider the reasonable excuse is something other than the time of the default. The reasonable excuse is "for the return or VAT not having been [despatched within the appropriate time limit]. Further the fact that Section 71 VATA which deals with the construction of sections 59 to 70 describes those sections as referring to "reasonable excuse for *any conduct*" (i.e. the conduct being the non-despatch of the return or VAT) is consistent with the reasonable excuse being understood as something which can only be relevant in relation to the circumstances that surrounded the default as at that time.

196. At the time of the due dates for payment of the returns in respect of which default surcharges have been imposed it would have been clear to the appellant that their earlier repayment claims were being disputed. Given the reply from HMRC referred to above (at [182]) and in the absence of any correspondence that HMRC's stance on offsetting had changed we do not think the appellant can reasonably have expected that the disputed earlier repayment claims would be put towards their future liabilities. We do not consider the relevance of what the appellant actually believed at the time and whether that could constitute a reasonable excuse as no evidence was put forward before us on that point.

197. In any case even if it were correct to take account of the fact that the dispute over repayments for earlier periods was resolved in the taxpayer's favour there was no evidence before us which would enable us to make relevant findings on whether the repaid sum would be applied by the appellant towards meeting its later liabilities.

198. There being no reasonable excuse the appellant's appeal against the VAT default surcharges is dismissed.

Conclusion

199. The appellant's appeals against HMRC's decisions to deny input tax and it appeals against the VAT default surcharge are dismissed.

200. 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.

SWAMI RAGHAVAN
TRIBUNAL JUDGE

RELEASE DATE: 17 SEPTEMBER 2015