



**TC01302**

**Appeal numbers: MAN/2008/0393  
MAN/2008/0593  
MAN/2008/0772**

*VAT – MTIC fraud – whether fraudulent evasion of VAT established – yes, except in relation to two deals – whether Appellant knew or should have known that its purchases were connected with fraud – on the facts, no – appeal allowed*

**FIRST-TIER TRIBUNAL**

**TAX**

**THE HIRA COMPANY LIMITED**

**Appellant**

**-and-**

**THE COMMISSIONERS FOR HER MAJESTY'S  
REVENUE AND CUSTOMS (VAT)**

**Respondents**

**TRIBUNAL: KEVIN POOLE (TRIBUNAL JUDGE)  
CHRISTINE OWEN FCA**

**Sitting in public in Manchester on 19 to 22 October 2010 with subsequent written final submissions**

**Nigel Gibbon, instructed by Ruffles & Co Limited, for the Appellant**

**Jonathan Cannan, instructed by Howes Percival, for the Respondents**

## DECISION

### Introduction

1. These three appeals are related to allegations commonly referred to as “MTIC” (or “missing trader intra-community”) fraud.

- 5 2. The appellant company, The Hira Company Limited (“Hira”), a dealer in various goods including mobile phones, appeals against decisions of the Respondents (“HMRC”) contained in three decision letters from HMRC to Hira. These letters denied Hira the right of input tax deduction in respect of the following amounts of VAT:

<b>Date of letter</b>	<b>VAT period affected</b>	<b>Input VAT denied</b>
6 March 2008	Month ended 30 June 2006	£177,918.48
18 April 2008	Month ended 31 July 2006	£160,835.33
3 June 2008	Month ended 30 September 2006	£4,577.83
	<b>Total input VAT denied:</b>	<b><u>£343,331.64</u></b>

3. HMRC claim to be entitled to take this action because the relevant sales by Hira (19  
10 in the VAT period 06/06, 16 in the VAT period 07/06 and one in the VAT period 09/06) are, in their view, part of an orchestrated VAT fraud. They say that in relation to each of these sales an earlier supplier of the phones in question in the chain of transactions leading to Hira always fraudulently intended that the VAT due on its supply of those phones within the UK would not be paid, and that VAT has indeed gone unpaid. They say that by tracing the chains  
15 of transactions (and the associated flows of money) involving these phones within and out of the UK, the overall fraud becomes clear; that there is a connection between the fraudulently unpaid VAT and Hira’s transactions; and that Hira (through its director Nari Hira and/or its senior employee Sanjay Hira) knew or should have known of the fraud.

4. Hira claims that the transactions were perfectly normal commercial trading  
20 transactions, bearing few or none of the usual hallmarks of MTIC fraudulent trading. It claims to have had no knowledge of the fraud, and that it did everything appropriate to ensure the transactions were not connected with any fraud. It therefore claims HMRC have no right to refuse its VAT repayment claim. In addition, it does not accept that some of the transactions in question can be shown to have been connected with fraudulent evasion of  
25 VAT.

5. There are no allegations of what is often called “contra-trading”: all the transactions of Hira the subject of the appeal are alleged to trace directly back (through chains of UK sales and purchases) to UK defaulters.

### Legal background

- 30 6. The leading authority in this area of law is the decision of the ECJ in the joined cases of *Axel Kittel v Belgium* and *Belgium v Recolta Recycling* C-439/04 and C-440/04 [2006] ECR I – 6161. The ECJ ruled (at [59] and [61]) that the right to deduct input tax may be refused if:

“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”

7. In the Court of Appeal judgment in the joined cases of *Mobilx v HMRC*; *HMRC v Blue Sphere Global Limited*; and *Calltell Telecom Limited v HMRC* [2010] EWCA 517 at [49] it was made clear that this refusal of the right to deduct does not depend on any specific UK legislation:

“It is the obligation of domestic courts to interpret the VATA 1994 in the light of the wording and purpose of the Sixth Directive as understood by the ECJ (*Marleasing SA* 1990 ECR I-4135 [1992] 1 CMLR 305) (see, for a full discussion of this obligation, the judgment of Arden LJ in *Revenue and Customs Commissioners v IDT Card Services Ireland Limited* [2006] EWCA Civ 29 [2006] STC 1252, §§ 69-83). Arden LJ acknowledges, as the ECJ has itself recognised, that the application of the *Marleasing* principle may result in the imposition of a civil liability where such a liability would not otherwise have been imposed under domestic law (see *IDT* § 111). The denial of the right to deduct in this case stems from principles which apply throughout the Community in respect of what is said to be reliance on Community law for fraudulent ends. It can be no objection to that approach to Community law that in purely domestic circumstances a trader might not be regarded as an accessory to fraud. In a sense, the dichotomy between domestic and Community law, in the circumstances of these appeals, is false. In relation to the right to deduct input tax, Community and domestic law are one and the same.”

8. The substance of the *Axel Kittel* test is generally broken down into its constituent elements in order to apply it. The parties agree with this approach, and indeed have agreed on the wording of the four required elements of the test, which they have specified in question form. They are agreed that if the Tribunal answers four questions in the affirmative in relation to any purchase of mobile phones by Hira, then the right of deduction of input VAT in relation to that purchase is lost. The questions must be considered (as *Axel Kittel* itself makes clear) having regard to “objective factors”, and the four questions agreed on by the parties are as follows:

(1) Is there a tax loss? (“The tax loss question”.)

(2) If so, does that tax loss result from fraudulent evasion? (“The fraud question”.)

(3) If there is fraudulent evasion, were Hira’s transactions connected with the fraud? (“The connection question”.)

(4) If they were connected, did Hira know or should Hira have known that its transactions were connected with the fraud? (“The knowledge question”.)

9. In relation to the first three questions, clearly all the evidence has been assembled by HMRC from its extensive casework on MTIC fraud generally. Hira broadly takes no stance on that evidence. It has no direct knowledge of the matters concerned and does not cast general doubt on the accuracy of the picture which is painted by HMRC. It merely observes that there are some gaps and anomalies (which are considered below) and believes that HMRC should be “put to proof” on the questions. This necessarily involves the Tribunal in a

detailed examination of those gaps and anomalies and in reaching a decision whether or not to accept the explanations given for them by HMRC.

10. Hira accepts that if the Tribunal answers the tax loss question and the fraud question in the affirmative, then if the existence of a chain of UK sale and purchase transactions between the fraudulent tax loss and its own purchases is established, as a matter of law the connection question must also be answered in the affirmative.

11. For the knowledge question to be answered in the affirmative without HMRC proving actual knowledge of the fraud on Hira's part, it is not sufficient for them to show that Hira should have appreciated there was a risk, or even a likelihood, that its purchases were connected with VAT fraud; they must establish that it should have known that the only reasonable explanation for those purchases was that they were connected with VAT fraud:

“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.”  
[per Moses LJ in *Mobilx* at [60]]

12. HMRC accepted that the burden of proof in relation to all four questions falls on them, and it is clear that the relevant standard of proof is the normal civil standard – the balance of probabilities.

13. This decision sets out first a background summary of Hira's history and trading, before turning to the particular transactions the subject of this appeal and the four questions set out above.

14. The “tax loss”, “fraud” and “connection” questions fall naturally to be considered together. The “knowledge” question (which lies at the heart of this appeal) will then be considered in detail.

## **Background summary**

### *History of Hira*

15. Some history of the business was set out in the witness statement of Mr Nari Hira, who also gave oral evidence. He is a director of Hira. He came across as a reliable witness, who has clearly committed most of his adult life to the development of the company and identifies with it strongly.

16. Hira was incorporated on 16 April 1959. It was set up by Mr Shyam K Hira (Nari Hira's father). Initially the business of the company was trading in suiting and cotton sales for export. Nari Hira joined the company in 1964, making lengthy annual international trips over the next five years or so with a view to developing Hira's business overseas. His three brothers also joined the company in 1969.

17. Hira developed an import business as well, dealing mainly with consumer products such as radios, televisions, lighters, umbrellas, tools, gifts and stationery from the Far East. Through its extensive network of contacts it was able to source most products if a customer

asked it to. It developed its own brand of calculators, electronic gadgets and office equipment in the UK, called “Texet”, which it sold extensively through major high street retailers. Hira deals with a significant number of national retailers, including the main supermarket chains.

5 18. Hira also exported branded products such as Sharp televisions. Over time, it established strong trading links with UK distributors for various Japanese companies, developing a particular line in cameras, watches and calculators, which it exported mainly to the EU. Nari Hira described this as a “vibrant market”. He explained there were many unexpected trading opportunities due to quirks in the market and the classic example he cited  
10 was the ability to make a profit through re-exporting Japanese-made watches back to Japan. Hira had been strong in the Italian market since the 1970’s, supplying watches, electronic and other consumer products.

15 19. Through his travels, Nari Hira gained business contacts all over the world, particularly in the middle and far east, certain parts of Europe, South America and the Caribbean. Many business opportunities came to the company through referrals from existing customers. Mr Hira explained that if he liked people and got on with them, he would give them credit quite early in their trading relationship – this flexibility is one of the reasons why people deal with Hira. He said that until the 2008 collapse of Woolworths, the company’s biggest bad debt for  
20 many years was £5,000 so his judgment must be sound. He did use credit reference agencies sometimes, but considered personal references from existing contacts more useful.

25 20. In April 2001, Nari Hira’s son Sanjay Hira joined the company. He had previously worked for an investment bank in the City. He was given a wide-ranging role in the company with no particular agenda. He was effectively asked to create his own job. He was given a title of “Vice President” but was not made a director of Hira. He made a witness statement and also gave oral evidence at the hearing.

30 21. We found him to be a reliable, intelligent and thoughtful witness, though on occasion we felt his answers to questions were more careful than forthcoming. Mr Cannan sought to persuade us in his closing submissions that Sanjay Hira’s evidence was unsatisfactory and unreliable. There certainly were matters of detail on which his memory was, after four years or more, somewhat hazy and he had a tendency to qualify his answers accordingly. He was also reluctant to give direct answers to questions which he felt were loaded or irrelevant. There were certainly one or two areas in which he attempted to evade questions, and others in which he became confused. We were satisfied on the whole however that he was a truthful witness.

35 *Commencement of Hira’s trading in mobile phones*

40 22. As part of Sanjay Hira’s work, he looked at enquiries for sourcing of goods received by Hira from companies all around the world. He saw that there had been many enquiries from customers about sourcing mobile phones from 1997 onwards. In August 2001 there was an approach from an Italian contact with a request to Hira to source some mobile phones and Sanjay Hira took it up. He found the Nokia distributor for North Wales and agreed to buy the phones from them. The business developed from there. The customer was happy and more requests for stock started to come in.

23. Sanjay Hira took on responsibility for the development of the mobile phone trading activities of Hira. He also dealt personally with the negotiation of the deals and all associated activities other than some administrative tasks relating to invoicing, payment and shipping instructions. In considering the state of Hira's knowledge about the deals it was entering  
5 into, we are satisfied that Sanjay Hira's knowledge should be attributed to Hira due to his pivotal role in this part of the company's business. The knowledge of Nari Hira in relation to the individuals and businesses with whom Hira dealt must also be attributed to the company.

*Historical evidence of Hira's trading in mobile phones*

24. In order to form a picture of Hira's state of knowledge at the time of the deals under  
10 appeal, it is important to understand the history of its dealings in the mobile phone market.

25. The details of Hira's historical trading in mobile phones contained in the evidence before us were patchy.

26. There was nothing beyond Sanjay Hira's brief oral evidence covering the period from commencement of trading (in August 2001) up to November 2002. For the period thereafter,  
15 a great deal of documentary evidence was provided (mostly in the evidence of Mr Silvester and Mr Moody of HMRC) but this evidence was not well organised and on occasion it was self-contradictory.

27. We were provided with a spreadsheet headed "all deals – 1 January 2003 onwards" which, according to its heading, purported to show all the mobile phone deals carried out by  
20 Hira from that date up to the end of May 2006. From the written evidence of Mr Silvester (HMRC assurance officer dealing with Hira's affairs), it appears that this is a combination of two spreadsheets, the first covering the period from January to September 2003 and the second covering the period from December 2003 to May 2006. This combined spreadsheet was missing various months' information (much of which was supplied separately at the  
25 hearing) and it contained a number of unexplained items. It also contained some information about purported deals in January 2006 which appeared to conflict directly with the information extracted from Hira's records and supplied by HMRC in relation to that month. We therefore take this combined spreadsheet as being incomplete and somewhat unreliable. When taken together with the further information supplied, it does however give a general  
30 background picture of Hira's trading over the relevant period.

28. Copies of Hira's audited group accounts were also included in the evidence, which in general backed up the picture painted by the spreadsheet, though of course we have treated those accounts with caution as they cover all the activities of Hira and its subsidiaries (which include a Spanish company which was involved in property development and then running a  
35 hotel complex over the relevant period).

29. We were also provided with a short analysis of Hira's total sales in 2006, showing the percentage of total sales represented by sales of mobile phones in each month of that year. This analysis does not appear to reconcile with the other information referred to above, but this only became apparent on close examination of the documents after the hearing and  
40 therefore no explanation of the inconsistency is available to us. Some of the monthly figures are significantly different, though the year's total of £17.1 million shown in the analysis is overall not greatly different from the figure of a little over £17.5 million disclosed in the deal listings, once we had assembled a full picture from the various documents scattered around

the bundles. This once again emphasises that the information provided to us about this period of Hira's history must be treated with caution.

30. Finally, some background to the bare figures was provided in oral evidence from Sanjay Hira at the hearing.

5 *Summary of Hira's trading in mobile phones*

31. Although Sanjay Hira gave evidence (which we accept) that the trading started in August 2001, HMCE did not become aware of it until May 2002, when they approached Hira for information as a result of "reference received" (which we take to mean that Hira's name had come up as a result of another trader attempting to verify its VAT status with HMCE for the purposes of trading with it).

32. Sanjay Hira gave evidence that he did approximately three or four deals per month in mobile phones from his commencement of trading in August 2001 for the rest of that year. Unfortunately we had no other information about those early deals before us, and almost no information about the level of trading in mobile phones during 2002, although from the written evidence of Hira's former HMRC assurance officer Michael Everett it is clear that Hira was trading in significant volumes – a VAT repayment of over £700,000 was attributable to UK purchases of phones sold abroad by Hira in the last two months of 2002, and a deal listing for December 2002 showed total sales for the month (exclusive of VAT) to a value of approximately £1.87 million.

33. In the period from January to March 2003, Hira traded very actively, buying from a wide range of UK suppliers (with just one purchase from a non-UK supplier) and selling to a fairly wide range of EU customers in Italy, Germany and Denmark. On sales of nearly £10.75 million during that three month period, it generated gross profits of nearly £475,000.

34. In its accounts for the year ended 16 April 2003, Hira reported an increase in group turnover from £17 million to £43 million (substantially accounted for by an increase in its sales to EU countries from £9.4 million to £37.2 million), on the basis of a substantially unchanged principal activity (as reported by its directors in the accounts).

35. In April 2003, its activities suddenly reduced sharply. In the whole month, it sold only approximately £278,000 of phones to just one of its established Italian customers, generating a gross loss of over £47,000. These deals took place before the new anti-MTIC "joint and several liability" provisions came into force in that month.

36. In May 2003 Hira recommenced significant levels of trading, but with a new structure to take account of the new joint and several liability provisions (and the strength of Sterling against the US dollar at that time): it bought the vast majority of its phones in US dollars overseas (mostly in Dubai). In the same month, it carried out its first sale to Sea Srl of Italy ("Sea"), which immediately became its main customer, buying around two thirds of the phones sold by Hira up to April 2004 and around 75% in the following year.

37. Its volumes dropped sharply from previous levels, totalling about £13.3 million for the whole of the year to April 2004, generating gross profits of around £450,000. Its customers were still largely overseas – it made a few sales to UK customers from September 2003 until January 2004, but then reverted wholly to overseas sales.

38. Hira's accounts for the year ended 15 April 2004 showed a corresponding reduction in turnover, from £43 million to £21.9 million (largely accounted for by a drop in its European sales from £37.2 million to £14.9 million).

39. There was another change of pattern in mid 2004. After a quiet February and March, Hira carried out no trades in April 2004 and then in May 2004 its buying policy changed completely. This coincided with the time when HMRC were carrying out a detailed verification of its VAT repayment claim for the month of November 2003, which was completed in late April 2004. Hira reverted to a policy of buying the vast majority of its phones in the UK, and almost all from one supplier New Way Associates Limited ("New Way") (a company from which it had only bought on three previous occasions, in June and July 2003). Sanjay Hira's explanation of the reason for this change was that the joint and several liability provisions were no longer quite such a worrying and unknown quantity and delays on imports had caused Hira a few problems – it had got "stuck" with a large consignment of phones which it had bought in December 2003, taking several months to sell them all.

40. In August 2004, Hira sold its first phones to Online Cellular Multimedia SL ("Online Cellular"), a Spanish company. It dealt reasonably heavily with Online Cellular over the following three months, then ceased to deal with it until it restarted in June 2005. From that time on, it dealt heavily with Online Cellular right up to the summer of 2006.

41. During the period May 2004 to April 2005, Hira sold mobile phones to a value of approximately £16.8 million, making a gross profit of around £900,000. Its accounts for the year to 15 April 2005 record turnover slightly up at £25.4 million, reflecting a sharp increase in its European sales (from £14.9 million to £21.4 million) and a reduction in its UK sales (from £6.5 million to £3.5 million).

42. From the summer of 2005, Hira's activities again increased sharply. The total mobile phone sales disclosed on its deal schedules for the year from May 2005 to April 2006 show total sales of around £42 million, generating a gross profit of around £1.8 million. Its accounts for the year to 15 April 2006 record turnover roughly doubled, from £25.4 million to £52.5 million. The increase is largely attributable to the growth of its European turnover from £21.4 million to £42.2 million.

43. The following table shows the levels of Hira's dealings with New Way, Sea and Online Cellular over the periods from May 2003:

	May 2003 to April 2004	May 2004 to April 2005	May 2005 to April 2006	Tot May 2004 to end 2006
Total sales	£13.3 million	£16.9 million	£42 million	£62.9 million
% of total purchases made from New Way	1.7%	92.7%	94.8%	94.4%
% of total sales made to Sea	67.5%	75.0%	47.2%	56.6%



% of total sales made to Online Cellular	0	7.7%	38.4%	29.0%
% of total sales made to Sea and Online Cellular	67.5%	82.7%	85.6%	85.6%

44. Up to the end of Hira’s mobile phone trading in December 2006, the deal schedules before us showed a total of approximately £4.2 million in mobile phone sales from May 2006. The accounts for the year ended 15 April 2007 are roughly in line, showing a reduction in turnover from £52.5 million to £18.5 million (mostly resulting from a reduction in European sales from £42.2 million to £8.8 million).

45. As will be seen below, the deals the subject of the appeals all involved purchases from New Way and sales to either Sea or Online Cellular. The evidence as to how those three relationships came into existence and developed is therefore important.

*The relationship with New Way*

46. Sanjay Hira said that this relationship started in 2003 through a referral from an employee, one Stuart Hobbs, who had previously worked for Unique Distribution Limited (one of Hira’s longstanding suppliers and also a trading partner of New Way). He said he had heard New Way’s name “in the market” but when Hobbs recommended them as suppliers, he had gone to meet them and over time the relationship had developed into a good one.

47. Sanjay Hira said he had carried out a Companies House search, a credit reference agency check and had spoken to others in the market place to check up on New Way. He also carried out checks on its VAT number initially (and from time to time thereafter). Although the only copies of accounts and credit references contained in the evidence dated from 2005 and 2006, we accept that other such checks were also done earlier.

48. There had been a number of occasions over the period after 2003 when Hira’s repayment claims had been subject to verification and no problems had ever arisen with phones bought from New Way, so far as Sanjay Hira could recall. They seemed reliable, the goods bought from them were always in good condition and their prices were competitive. He said he visited them in London monthly and that they became “as close to friends as possible”. He said they also gave Hira credit – up to 7 days - and sorted out any problems effectively. For this reason, he was content to regard them as his near sole supplier from May 2004 when he made the decision to “repatriate” his sourcing of phones to the UK.

*The relationship with Sea*

49. The initial introduction to Sea came to Nari Hira through a Mr Piconti at a company called Electrofusion in Rome, who had been known to Nari Hira for many years. Hira sold them batteries and related products. Mr Piconti told Nari Hira that a contact of his, a Mr Franco Terenzi, was interested in buying mobile phones. It was quite common for Nari Hira to receive introductions of this type from his existing contacts around the world. Mr Piconti

gave an informal reference for Mr Terenzi and Nari Hira said he would try him as a trading partner.

50. He carried out very basic checks to establish the legal existence and VAT registration of Mr Terenzi's company, and visited him at his office in Italy. This was in 2003. As well as  
5 phones, Hira sold some televisions to Sea on three occasions.

51. Sea placed their first order for mobile phones in May 2003. In line with their normal practice, Hira required cash on delivery in relation to the first orders but the relationship progressed smoothly and soon they were granting credit. Nari Hira said he had a personal approach to credit which he believed was part of the success of Hira: if he liked a customer  
10 and got on with him then he would be much more flexible on credit than many others in the market. He believed this to be part of the reason for Hira's success and he claimed to have a very good record on bad debts, specifically because he relied on his personal judgment rather than on credit reference agencies.

52. Nari Hira met Mr Terenzi in Italy again in March 2004 and in May, June and October  
15 2006. Sanjay Hira said he had met Mr Terenzi in Italy at least two or three times in 2004, and twice in 2005. There were also other more recent meetings, postdating the periods under appeal.

53. The day to day relationship with Sea was largely handled through Sanjay Hira, who negotiated the deals (generally with an assistant to Mr Terenzi, whose English was poor).

#### 20 *The relationship with Online Cellular*

54. Sanjay Hira's evidence was that the owner of Online Cellular (one Ramesh Karnani) was the son in law of a longstanding trusted personal friend of his father. Both families came from the Sindhi community. He believed their family business was an authorised distributor for Toshiba in Spain. They had met at a family wedding in Madrid and then subsequently at  
25 a trade show in Germany called "Ceebit" in February 2003 (at which Karnani was exhibiting mobile phones) and they had exchanged business cards. There followed numerous telephone enquiries before the relationship bore fruit in August 2004 with the first deal. Sanjay and Nari Hira gave evidence that they had both visited Online Cellular in Spain on separate dates in 2005.

30 55. Sanjay Hira said that Hira had carried out basic checks on Online Cellular (of the same type as had been done in relation to Sea) before dealing with it.

#### **Trades the subject of the current appeal**

56. The appeal is concerned with a total of 36 deals: 19 during June 2006, 16 during July  
35 2006 and one during September 2006. During June 2006, Hira carried out another two deals which were not traced back to defaulting traders, in July 2006 it carried out another two deals which were not traced back to defaulting traders and in September 2006 it carried out another six deals which were not traced back to defaulting traders.

57. A summary of all the deals the subject of these appeals is set out in Appendix 1.

58. In every deal under appeal, Hira bought the relevant phones from New Way.

59. In June 2006, Hira sold to Sea in 17 of the 19 deals under appeal. In the other two, it sold to Online Cellular. In the two deals which were not found to trace back to defaulters, Hira sold to Sea.

60. In July 2006, Hira sold to Sea in 15 of the 16 deals under appeal. In the other deal, it sold to Online Cellular. In the two deals which were not found to trace back to defaulters, Hira sold to Sea.

61. In September 2006, Hira sold to Sea in the one deal under appeal. In the other six deals which were not found to trace back to defaulters, it also sold to Sea.

10 **Questions 1, 2 & 3 - was there a tax loss resulting from fraudulent evasion connected to the purchases by Hira?**

*Preliminary matters*

62. It is necessary to address this question individually in relation to each of the relevant purchases by Hira.

63. The fraudulent evasion with which we are here concerned is the fraudulent evasion of VAT.

64. In this case, the “connection” alleged by HMRC in each case is through a simple and direct chain of sales and purchases of the mobile phones in question from a fraudulent VAT defaulter to Hira. There is no allegation of what is commonly called “contra trading”. Hira accept (rightly) that if that chain is established, then a “connection” exists as a matter of law between their purchase and the fraudulent evasion of the defaulter.

65. It is logical therefore to consider the issue of “connection” first – unless a chain is established, there is no point in examining an allegedly fraudulent evasion of VAT at its beginning.

*The chains of sales and purchases – connection*

25 Introduction and general finding

66. HMRC’s identification of the chains changed over time. Partly this was due to further information becoming available and partly it was due to mistakes being made in tracing the chains through the existing information. A final version of the alleged chains was only set out in the exhibits to Mr Silvester’s statement dated 1 October 2010.

67. Hira did not positively dispute any of the chains. It had pointed out some date anomalies in some of the chains as originally alleged by HMRC, as a result of which HMRC had rechecked them and changed some of them.

68. Subsequent to these changes, Hira’s stance remained essentially the same: it did not admit the chains, but neither did it positively dispute them.

69. We accept the explanations given by Mr Silvester in relation to the apparent breaks in the relevant chains and (subject to one qualification, as set out below) we find as a fact that the chains are established as set out in exhibits 6(8) and 6(9) to his witness statement dated 1

October 2010 (in relation to the June 2006 and July 2006 deals respectively) and in exhibit 1 to his statement dated 1 April 2009 (in relation to the September 2006 deals). Some doubt was raised by Mr Gibbon on behalf of Hira as to some persistent unexplained anomalies in timings in deals 1 and 15 of June 2006, but we accept the explanation of the evidence in relation to those apparent anomalies put forward by Mr Cannan on behalf of HMRC in his closing submissions.

70. Before identifying our one qualification to the above general finding, we must make two comments about individual items within it.

71. First, in deal 5 in June 2006 we note that there is uncertainty as to the identity of the entity which sold the relevant phones to Princeways Limited but we are satisfied that the chain leads back to Performance Specifications Limited (“PSL”), whichever version of the chain is correct.

72. Second, we were initially unsure about the identification of the chain in relation to deal 2 of June 2006. No issue arose about tracing it back to High Speed Business Limited, but there was some doubt as to where it led before that company. There was some ambiguity in Mr Silvester’s witness statements as to whether one part of the chain then ended at PSL or whether it could be traced further back to Udeil Solutions Limited (“Udeil”).

73. After a careful review of the evidence of Mr Edwards (in relation to the alleged defaulter Udeil), we are satisfied that the relevant 1500 Samsung D600 phones can be traced back through PSL and Atlantic Catering Limited to Udeil. It was only on discovering sales invoices from Udeil exhibited to the witness statement of Mr Edwards which had not been referred to by Mr Silvester and further evidence both in Mr Edwards’ statement and that of Mr Shorrocks (showing a history of third party payments from PSL to Macdelta of Cyprus and evidence of release of the goods by that company) that we felt able to reach this view.

74. On balance, therefore, we take the view (and find as a fact) that the source of the 1500 Samsung D600 phones sold by Hira in deal 2 of June 2006 was the 1500 phones supplied by Udeil to Atlantic Catering Limited, and therefore the chain is established back as far as Udeil.

#### Qualification to the general finding – deal 18 of July 2006

75. The qualification to our general finding relates to deal 18 of July 2006.

76. In his witness statement dated 1 April 2009, Mr Silvester indicated that the chain of transactions could only be traced back to Cirex Corporation Limited (“Cirex”). He said that Cirex had produced only a partial record of the deals it had carried out in June, July and August 2006, and no details of its sale of the relevant phones (which Hira eventually acquired in deal 18 of July 2006) were included in that record. He observed however that in each of the 108 deals for which records had been provided, Cirex had been supplied by one of five named traders. He went on to say that as each of those traders had been identified as a defaulting trader, it was more likely than not that Cirex had been supplied by a defaulting trader.

77. Upon reviewing the witness statement of Andrew Shorrocks (in relation to FCIB payments) it became apparent (as was briefly mentioned at the hearing) that in fact a payment of an amount clearly referable to this deal had been made on 28 July 2006 by Cirex to Phone

City Limited (“Phone City”), one of the five possible defaulting traders named by Mr Silvester in his witness statement.

78. On balance, therefore, we take the view (and find as a fact) that the source of the 1000 Black Motorola V3 phones sold by Hira in deal 18 of July 2006 was Phone City.

5 *Fraudulent VAT evasion*

Summary

79. In most of the chains, HMRC were able to trace back to a trader which they alleged was a fraudulent VAT defaulter.

10 80. Witness statements were included in the bundles in respect of each of the alleged fraudulent VAT defaulters at the start of the various transaction chains.

81. Mr Silvester included some material in his own witness statement in relation to Kaymore Export Limited, however a subsequent witness statement from Sarah Barker of HMRC about this trader was included in our bundles and we take this as superseding the earlier material in Mr Silvester’s witness statement.

15 82. Hira did not actively dispute the evidence of the various HMRC officers in relation to the defaulting traders. However, they did not actually admit the existence of the fraudulent tax losses either. They simply left in the hands of the Tribunal the question of whether that evidence was sufficient to establish the existence of tax losses resulting from fraudulent evasion.

20 83. There were initially three (and subsequently four) chains where no fraudulent VAT defaulter could be identified at the beginning due to what HMRC called “blocking buffers” (so called because HMRC assert they acted deliberately in a way intended to prevent HMRC from tracing the chain back to actual fraudulent defaulters hiding behind them). These were deals 2, 5 and 6 of June 2006 and deal 18 of July 2006. HMRC argued that the evidence  
25 available allowed the Tribunal to reach the conclusion that fraudulently defaulting traders would have been found if it had been possible to trace the chains past the blocking buffers.

84. As mentioned above, we find that in fact deal 2 of June 2006 traces back to Udeil and deal 18 of July 2006 traces back to Phone City. These companies are both alleged fraudulent defaulters, about which there was a great deal of evidence before us.

30 85. This meant that, on our findings of fact, there are only two alleged blocking buffers to be considered, namely PSL (in deal 5 of June 2006) and Sundial International Stocktraders Limited (“Sundial”) (in deal 6 of June 2006).

86. We deal first with the question of fraudulent VAT evasion in relation to the identified defaulters, then consider the position in relation to the alleged blocking buffers.

35 Identified fraudulent defaulters

87. There were witness statements from a number of HMRC officers relating to the identified fraudulent VAT defaulters. Details are set out in Appendix 2.

88. Subject to the following qualification, we accept the evidence of the various officers and find as a fact that each of the identified entities was guilty of fraudulent evasion of VAT in relation to its output VAT liability arising from its sale of mobile phones at the start of the chain of transactions which culminated in Hira's purchase.

5 Qualification relating to Phone City

89. Mr Silvester in his witness statement dated 1 April 2009 referred to a witness statement of Malgorzata Wanat in relation to Phone City. There was in fact no witness statement from Ms Wanat contained in our bundles, but a witness statement was given by Officer George Edwards instead (dated 20 September 2010).

10 90. That witness statement was expressed to be made not for these appeals but for the purposes of an appeal by a company called Vortech Limited in relation to a deal in period 06/06.

15 91. In it, Mr Edwards states that Phone City was deregistered for VAT on 25 July 2006 – though the letter notifying Phone City of its deregistration was only sent on that date, and was incorrectly addressed. There is evidence that other letters similarly addressed had reached Phone City without problem, and a further copy of the letter was sent again on 18 August 2006, correctly addressed.

20 92. Mr Edwards also exhibited a copy of the listing of deals for which an eventual VAT assessment was raised against Phone City for the period up to its deregistration. The relevant sale by Phone City to Cirex is not included in that listing, no doubt because it did not take place until a few days after the deregistration date of 25 July 2006.

25 93. Notwithstanding these undoubted shortcomings in the evidence in relation to Phone City we have come to the view that the evidence, viewed as a whole, shows that Phone City was involved in a sustained and fraudulent attack on the VAT system as a whole and we find that its sale of 1000 Black Motorola V3 phones to Cirex on or about 28 July 2006 was a part of that fraud.

Blocking buffers

30 94. The alleged blocking buffer in deal 5 of June 2006 was PSL, whichever of the two possible versions of the chain was correct. In deal 6 of June 2006 the alleged blocking buffer was Sundial.

95. Whilst the point had not arisen during the hearing, in his closing submissions, Mr Gibbon "upon reflection" suggested that HMRC had not made a case for the existence of fraudulent tax losses in relation to those the deals involving supposed blocking buffers. We take it that Mr Gibbon's submission should apply therefore to deals 5 and 6 of June 2006.

35 PSL

96. In his witness statement dated 1 April 2009 Mr Silvester gave details of the known trading of PSL arguing that it showed, on a balance of probabilities, that if the deals had been traced back they would have been found to begin with fraudulent defaulters.

97. The basis of this argument was that PSL had only provided information about 147 deals which it had carried out in April and May 2006 and those deals “have all been traced back to a defaulting trader and a tax loss”. However, neither in Mr Silvester’s statement nor in the exhibits supporting it was there any allegation that these identified tax losses were fraudulent. The closest that Mr Silvester came to an allegation of fraud was when he said that PSL’s failure to provide promised deal information appeared to be “a deliberate attempt to frustrate the efforts of HMRC in tracing supply chains for these transactions.” This however relates to the behaviour of PSL, and not the fraudulence or otherwise of its suppliers.

98. The unpaid VAT of PSL amounts to £66,972.64 according to Mr Silvester. Its taxable supplies of mobile phones for the very short period of its mobile phone trading (probably a little over a month) amounted to more than £171 million, but these facts on their own cannot in our view justify a finding of fraudulent evasion on the part of PSL, even when considered in conjunction with its unhelpfulness to HMRC in providing details of its suppliers.

99. Therefore whilst we accept that PSL’s purchases may well have traced back to defaulting traders, we do not consider there is sufficient evidence to support a finding that there would have been fraudulent evasion of VAT by those traders. We bear in mind that the burden of proof on this issue of course lies on HMRC.

100. We therefore find that in relation to deal 5 of June 2006, HMRC have failed to discharge the burden of showing, on a balance of probabilities, that Hira’s purchases of phones are connected to fraudulent evasion of VAT.

#### Sundial

101. We were provided with a witness statement of HMRC officer Karen Bradley in relation to this company. Ms Bradley had not dealt with Sundial herself, she was compiling information contained in HMRC’s records from the work of other officers, all of whom have left HMRC.

102. Ms Bradley’s statement gives some history of Sundial’s trading. The information is sketchy, particularly in relation to June 2006. The sole director of Sundial claimed that all the relevant business records of Sundial were stolen from his car, so he was unable to give details of Sundial’s trading. It is therefore not possible to trace the supplier from which Sundial purchased the 595 Nokia 6280 mobile phones comprised in deal 6 of June 2006.

103. It is quite clear from Ms Bradley’s statement that Sundial has traded extremely irresponsibly over a period of many months in goods which are typically the subject of MTIC fraud. It has gone into liquidation without being in a position to settle its VAT and other tax liabilities. Outstanding VAT assessments against it of a little over £8,000 remain unpaid.

104. However the case put forward by HMRC is not that Sundial itself has fraudulently evaded VAT; it is that a predecessor in title to the relevant phones has done so. Without any direct evidence as to the identity of that predecessor in title, Ms Bradley has sought to demonstrate that the known trades in which Sundial was involved can be traced back to defaulters and therefore it can safely be assumed that this deal would do so, if it were possible to trace it.

105. Unfortunately, however, we do not consider the evidence to be sufficiently clear or compelling to discharge the burden of proof lying on HMRC. The origin and significance of the spreadsheets exhibited to Ms Bradley's witness statement are unclear. For example, she says that HMRC "holds information on 75 of the 76 deals listed in the spreadsheets which  
5 involve Sundial" and there is exhibited to her statement a spreadsheet which appears to list a number of deals involving mobile phones and other items purchased during May 2006 from "Let's Talk Ltd", "Fone Fingz" and "Easyway Limited" and sold on to various other traders. The inference is that this list shows items bought and sold by Sundial. Yet in her witness statement she says that none of its business records for the relevant period were produced by  
10 Sundial, so the origin of this list is unclear. She also refers to numbers of deals being "listed" for Let's Talk and Fonefingz, but without providing copies of the lists in question or explaining how or by whom they have been compiled. She also refers to those listed deals being traced back to defaulting traders but the lists exhibited to her witness statement do not support these assertions in any way which we could follow. Then the evidence of Mr  
15 Shorrocks is that Sundial made payment for the phones in question to a company in France called Intertech SARL and there is no attempt to explain the apparent discrepancy.

106. We therefore find that in relation to deal 6 of June 2006, HMRC have failed to discharge the burden of showing, on a balance of probabilities, that the purchase of phones by Hira is connected to fraudulent evasion of VAT.

#### 20 **Questions 1, 2 & 3 – conclusion**

107. It follows that we answer questions 1, 2 and 3 in the affirmative in relation to all the deals the subject of the present appeals apart from deals 5 and 6 of June 2006, where we find no tax loss to have resulted from any fraudulent evasion connected to the purchases by Hira.

#### 25 **Question 4 - did Hira know or should Hira have known that its transactions were connected with the fraud?**

##### *Preliminary points*

108. This question is at the heart of the present appeals. HMRC put their primary case quite clearly. They alleged that Hira, through Sanjay Hira, had actual knowledge of the connection to fraud. As a fallback argument, they submitted that even if Hira did not have  
30 actual knowledge of the fraud, it should have known of the connection to fraud.

109. HMRC have adduced a great deal of evidence concerning the overall fraud which they say appears when one stands back and considers the picture as a whole. They refer specifically to long deal chains; no added value; generally escalating margins; circularity of goods; circularity of cash flows; acquisition from the EU; third party payments; dispatch to  
35 the EU; and much larger margins on dispatch to the EU.

110. We agree that all these characteristics are present and we agree (as indeed did Sanjay Hira, albeit reluctantly, during cross examination) this clearly indicates overall fraud connected with Hira's deals that is, to a greater or lesser extent, orchestrated. More importantly, however, we have already made findings (see above) as to the existence of  
40 specific fraudulent VAT evasion which is connected to Hira's specific purchases.



111. The crucial question therefore at this point is not whether fraudulent VAT evasion was taking place which was connected to Hira's purchases; it is whether Hira knew or should have known at the time of its purchases both (a) that such evasion was (or would be) taking place and (b) that its purchases were (*not* "possibly were" or even "probably were") connected with it.

112. We accept Mr Gibbon's submission, following the extract from the Court of Appeal's judgment in *Mobilx* at [11] above, that:

"The burden of proof rests with the Respondents throughout to prove that the Appellant knew, or should have known, that the only reasonable explanation for the circumstances in which each transaction took place was that it was connected with fraudulent evasion."

113. We agree with Mr Cannan's submission that no single factor is determinative of the issue of knowledge. As Christopher Clarke J in *Red 12 Trading Limited v HMRC* [2009] EWHC 2563 said (at [109] to [111]):

"Examining individual transactions on their merits does not, however, require them to be regarded in isolation without regard to their attendant circumstances and context. Nor does it require the tribunal to ignore compelling similarities between one transaction and another or preclude the drawing of inferences, where appropriate, from a pattern of transactions of which the individual transaction in question forms part, as to its true nature e.g. that it is part of a fraudulent scheme. The character of an individual transaction may be discerned from material other than the bare facts of the transaction itself, including circumstantial and "similar fact" evidence. That is not to alter its character by reference to earlier or later transactions but to discern it.

To look only at the purchase in respect of which input tax was sought to be deducted would be wholly artificial. A sale of 1,000 mobile telephones may be entirely regular, or entirely regular so far as the taxpayer is (or ought to be) aware. If so, the fact that there is fraud somewhere else in the chain cannot disentitle the taxpayer to a return of input tax. The same transaction may be viewed differently if it is the fourth in line of a chain of transactions all of which have identical percentage mark ups, made by a trader who has practically no capital as part of a huge and unexplained turnover with no left over stock, and mirrored by over 40 other similar chains in all of which the taxpayer has participated and in each of which there has been a defaulting trader. A tribunal could legitimately think it unlikely that the fact that all 46 of the transactions in issue can be traced to tax losses to HMRC is a result of innocent coincidence. Similarly, three suspicious involvements may pale into insignificance if the trader has been obviously honest in thousands.

Further in determining what it was that the taxpayer knew or ought to have known the tribunal is entitled to look at the totality of the deals effected by the taxpayer (and their characteristics), and at what the taxpayer did or omitted to do, and what it could have done, together with the surrounding circumstances in respect of all of them".

114. There is no direct evidence put forward by HMRC of Hira's actual knowledge of a connection with fraudulent evasion. We are effectively invited to draw an inference, from "a wide range of factors", that it must have known of the connection. If we do not feel such an

inference is warranted, then we are invited to make what is effectively a lesser finding that it should have known.

115. There are difficulties with this process. Of course, if there is direct evidence of actual knowledge of the fraud, of if there is sufficient evidence to give rise to an inference that the trader was knowingly involved right from the beginning, then matters are more straightforward. But if this is not the case, then when considering “a wide range of factors” it is difficult to be forensically analytical about when a trader’s “suspicion” of a connection with fraud actually hardened into “knowledge” of that connection; and only marginally less difficult to say when that hardening should have taken place.

116. A very convincing picture will need to be painted before a tribunal can make an inferential finding of actual knowledge of a connection to fraud. Whilst a tribunal should not shy away from such a finding where it feels the evidence supports it, a finding that a trader should have known of a connection to fraud will by definition be much less hard to make – it requires the tribunal only to exercise its own judgment based on the established facts, rather than to look inside the head of the trader (or that of each relevant individual within a corporate trader). But in either case, the approach should be to consider all the evidence in the round and then reach an overall judgment, rather than to consider particular pieces of evidence in isolation then attempt to synthesise the results of that consideration into a single overall finding. That is the approach we have followed, though in deference to the submissions of the parties, we have felt it appropriate to make comments about some of the specific points which they have put to us.

117. It is clear that Sanjay Hira was experienced in the field of business generally, having worked as a derivatives trader in an investment bank. He also had a very good general awareness of MTIC fraud from the early days of Hira’s trading. Indeed, he was involved in a trade body’s consultation with HMRC on the implementation of the “joint and several” liability provisions in 2003. He knew that the fraud, in its most potent form, involved goods being repeatedly dispatched to and acquired from the EU, and that the bona fides of Hira’s customers was therefore just as important as that of its suppliers, though it is fair to say that HMRC’s focus until 2006 was almost exclusively on the “supplier” side of a trader’s dealings. This experience and knowledge must be borne in mind when considering what conclusions Sanjay Hira should have reached from facts which came to his attention.

118. It is against the background of these preliminary points that we must reach a decision as to whether Hira knew or should have known that its purchases were connected to fraudulent evasion of VAT. We comment below on some of the more significant elements of the overall picture, as put forward by HMRC.

*Factors tending to suggest actual or imputed knowledge*

The fraud was so large that Hira must have known of it – or should have done so.

119. Andrew Shorrocks of HMRC gave evidence in relation to the movement of large volumes of funds, often in circles, through First Curacao International Bank (“FCIB”) accounts. Although Hira did not have an FCIB account, it was clearly shown that some of the money it paid for its purchases ended up as part of this massive circular money flow. We take the view that Mr Shorrocks’s evidence supports the proposition (which is not seriously contested by Hira) that fraud was indeed taking place on a massive scale at the time of Hira’s

dealings and involving some of the traders it dealt with; however it does nothing to support the proposition that Hira knew or should have known of the fraud.

120. Mr Cannan invited us to find that the scale of the fraud was so large that it simply could not have been carried on without Hira having actual or “blind eye” knowledge of it.  
5 We cannot accept his invitation as we find no evidence of Hira having any specific knowledge which would (or should) have brought the fraud to its attention.

#### Hira’s withdrawal from the market at the end of 2006

121. Hira decided to withdraw from the mobile phone trading market in the UK in December 2006. Mr Cannan sought to persuade us that there was no apparent change in  
10 circumstances between June/September 2006 and December 2006, therefore Hira’s level of knowledge of the risks which actually led it to cease the trade in December should have caused it to withdraw much earlier. We do not agree. Many things would have changed over this period, not least the cumulative effect of the increasingly aggressive stance being taken by HMRC to repayment claims. This proposition was not put to Sanjay Hira during cross  
15 examination, so we discount it.

#### Sanjay Hira’s close control of the mobile phone trading

122. Mr Cannan pointed out that the mobile phone trading business was run very much as a segregated business under the close personal control of Sanjay Hira. This was, he said, in stark contrast to how the rest of Hira’s business was run. He invites us to infer that this close  
20 control and segregation was required because Sanjay Hira was aware of the involvement with fraud. We reject this inference. The picture we took away was of a young man who was trying to make a mark in the family business after working in the City and who had chosen this trade (however ill-advisedly) as his means of doing so. In the circumstances, we find it unsurprising that he wanted to keep close control of it and therefore that it should be, to an  
25 extent, segregated from the rest of Hira’s business.

#### Inconsistent evidence about Stuart Hobbs

123. There was one employee in the mobile phone side of the business apart from Sanjay Hira. This was one Stuart Hobbs, who had been recruited in 2003 from one of Hira’s mobile phone suppliers to help Sanjay Hira in the development of the business. He actually  
30 introduced Hira to New Way. He left the company in 2005, supposedly due to boredom as there was now only one main supplier and one main customer. This begged the question as to why Stuart Hobbs had not been tasked with going out to find more customers and deals.

124. This question was not put to Sanjay Hira in cross examination, and we can only guess at the answer. We certainly do not consider that it points towards any kind of knowledge or  
35 suspicion on Hira’s part as to the bona fides of its mobile phone trading.

#### Terms of trading

125. We accept that Sanjay Hira was less than clear in his evidence about the terms of trade that applied to the mobile phone deals. There were standard terms and conditions printed on the reverse of Hira’s invoices but we do not find it unusual for even senior  
40 employees of a company to have a less than perfect grip on the legal terms and conditions

applying to the company's business. We also note that, crucially, there did not appear to be any difference in this regard between Hira's mobile phone trading and its other dealings.

Incredible that New Way always provided the best price and Sea were always the best customer

5 126. The evidence Sanjay Hira gave in relation to his dealings with New Way was that they were his preferred supplier but he always checked prices elsewhere. He did occasionally do deals with New Way at a price a little above what he felt was the market price because of the comfort factor of dealing with a known and trusted supplier. On one occasion, New Way even gave him a retrospective discount on a deal where he found out he had paid more than  
10 what he regarded as the market rate and complained to them. Given that the purpose of reducing his previous multiple lines of supply down to one preferred supplier was to secure a line of supply from a company which he felt was reliable and trustworthy (as well as being good to do business with), this does not appear inherently implausible.

15 127. So far as Sea is concerned, the question was not put to Sanjay Hira in cross examination, so we can only guess at the answer. However, his evidence was that by this time, Hira's deals were partly generated by customer enquiry and partly by stock offers from New Way. If the customer enquiries came largely from Sea, then we can see why he might wish to approach them when he had available stock to offer. He should have been suspicious if they invariably "snapped up" whatever stock he offered them, but we had no evidence as to  
20 what contact had taken place with Sea about stock offers to them which might have helped us form a clearer view on this point.

128. As a general point, we do not consider that having a small number of preferred trading partners is inherently suspicious, especially when there is a plausible history of how that position has been arrived at.

25 Phenomenal overnight success of the business and history of easy, consistent and risk free profits by June/July/September 2006

30 129. Mr Cannan pointed out that the trade in mobile phones became a phenomenal success, "almost overnight" and without any prior experience or expertise in the market, which should give rise to suspicion. This ignores the fact that by 2006, Hira had been dealing in that market for well over four years. We had no evidence before us as to the sales or profit achieved in the business up to December 2002 (by which time it had been trading in the sector for well over a year). By 2003 it was extremely active and profitable, and things improved again in 2005 after a flat 2004. But this does not allow us to reach a view that the business had attained implausibly rapid initial growth.

35 130. So far as profitability is concerned, an analysis of the totality of deals for which we have the evidence up to December 2006 shows that the profits were certainly not consistent, indeed there were some losses suffered. Profits were generally in the range of 3% to 8%, but fluctuated fairly widely in that range (and quite often fell outside it). In the last year or so of trading, margins were falling more consistently towards the lower end of that range. Given  
40 that most if not all of Hira's deals were supposed to have been carried out "back to back" in the later stages of its trading, we find its losses a little surprising but no questions were put to Sanjay Hira in cross examination about it and the amounts involved were usually comparatively small so we do not feel able to draw any inferences from these losses. One

most interesting pair of transactions took place in May 2006 however, when Hira took its largest losses of all in two sales to Online Cellular, losing over £70,000 on two sales totalling a little over £168,000. It would have been particularly interesting to hear the explanation of these two transactions, but this was also not explored in cross examination and therefore we can draw no inferences from them.

131. Overall, therefore, we do not consider that the pattern of profitability can give rise to any adverse inferences.

#### New Way's failure to seek out export opportunities was suspicious

132. Mr Cannan points out that New Way's role, given its large size, did not make sense. Why did it not seek out itself the more lucrative export opportunities which it was passing up in favour of Hira? Sanjay Hira's answer was that New Way appeared happy to limit itself to UK activities, and may not have had the finance necessary to fund export deals. This is not an incredible scenario, and no other evidence was available to contradict it. In fact, the deal sheets show that New Way was making a healthy profit on its sales to Hira and that may have been another reason why it was content not to get involved in exporting. But whatever the true position, we do not consider that Sanjay Hira should have had his suspicions aroused by New Way's apparent lack of interest in getting involved in the export market itself.

#### Why have Hira not called Mr Terenzi of Sea to give evidence?

133. Mr Cannan observes that much suspicion hangs over Sea in this case, and that it would have been a simple step to ask Mr Terenzi to give evidence before the tribunal to dispel that suspicion. He invites us to draw negative inferences from Hira's failure to do so.

134. The relevant issue in these appeals is what knowledge Hira had (or should have had) about the involvement or otherwise of Sea in VAT fraud in 2006. It is difficult to see how Mr Terenzi's evidence could have helped the tribunal in relation to this issue. We decline to draw any negative inferences from Hira's failure to call him as a witness.

#### Due diligence

135. HMRC point out that any trader (we take this to mean any honest and diligent trader) dealing in this market, which was known to be rife with fraud, would want good evidence as to the integrity of customers and suppliers. They say that Hira has failed to obtain that evidence and therefore cannot be considered an honest and diligent trader.

136. They point also to VAT Notice 726, which includes examples of reasonable steps which a trader can take to establish the integrity of its customers, suppliers and supplies. They say that Hira did not carry out most of the possible checks listed in VAT Notice 726. They checked that the companies existed and had a VAT registration (or its overseas equivalent), but nothing more. They did not repeat these checks prior to every deal, or even particularly regularly.

137. They invite the tribunal to infer that the reason why Hira did not carry out full checks was because it knew full well that the deals would go through with no commercial risk to Hira because they were fraudulently pre-planned. In other words, they argue that failure to carry out the full checks is in fact evidence that Hira were knowingly involved in the fraud.

They do not argue – indeed the argument would be illogical and unsustainable – that failure to carry out full checks is evidence that Hira should have known of the connection to fraud. Neither is there any evidence to suggest that if Hira had carried out more extensive checks in 2006, they would have discovered the problems with Sea or Online or that New Way was in any way dubious.

138. Before considering what checks Hira carried out, it is important to note that even if all the suggested checks in Notice 726 are carried out by an honest and diligent trader, it will in most cases not “flush out” a possible MTIC fraud. It is in the nature of the fraud that the fraudster is generally concealed from the exporter/dispatcher of the goods by one or more intermediate traders – “buffers” in HMRC parlance – and the exporter/dispatcher is only able to carry out checks on its immediate counterparties.

139. Nevertheless, a trader will generally wish to ensure that it carries out all the due diligence listed in VAT Notice 726, simply to avoid HMRC accusations that it has fallen short of the required standard. If Hira had been knowingly involved in the fraud, we have little doubt that they would have meticulously ticked all the boxes on the “Notice 726” checklist.

140. Hira’s response is that they did obtain copies of the crucial documents from New Way, Online and Sea and they did meet them all (New Way on a regular basis of little more than monthly); they did verify their continuing VAT registrations from time to time (though admittedly not on every deal); they did limit their trading relationships to just a few trusted counterparties who they got to know well; but most crucially, there had been introductions to all three traders through supposedly reliable sources. In addition, they obtained and kept all the transaction documents mentioned in Notice 726 in relation to their deals.

141. We read and heard much evidence of the due diligence which Hira did and did not carry out on its counterparties. The alleged shortcomings in that due diligence do not persuade us that Hira knew of the connection to VAT fraud in its purchases, nor (as mentioned above) do they assist us at all in reaching a view on what knowledge of that fraud Hira should have had.

#### Discrepancies and shortcomings in the deal documents

142. We approach all the evidence on this issue in the light of the fact that, by the time of the deals the subject of the current appeal, Hira had a long-established relationship and pattern of trading with New Way, Sea and Online Cellular.

143. Mr Cannan pointed out that there seemed to be a number of significant documents missing from all the deal packs produced by Hira, in particular purchase orders from Hira, delivery confirmations from New Way, confirmations from Hira’s freight forwarder, instructions to its inspection company and notes of negotiations. Supplier declarations from New Way were often received after Hira had ordered the dispatch of the phones, as were inspection reports and sometimes even purchase orders.

144. The picture which we built up overall, however, was that the trade was carried on by Hira in much the same way as it carried on the rest of its trade, subject to the changes that were required because of the nature of the mobile phone trade. It was not careful to obtain and retain all these extra documents in the course of its longstanding trade, it obtained what it

needed to from a commercial viewpoint, and it took calculated risks in dealing with its customers and suppliers. We did not consider that any of the specific discrepancies in deal documents pointed out by Mr Cannan provided convincing support to his submissions.

5 145. To a degree, we gained the impression that Hira did regard some of the documents which it had to obtain as fairly useless but necessary “box-ticking” to satisfy HMRC when it came to claiming its VAT repayment, documents which from a commercial point of view were as valueless to it in its mobile phone trading as they would have been in any other part of its trade. In some ways, it is difficult not to sympathise – is it really plausible that a supplier declaration was a truly worthwhile document? A fraudulent supplier would have no  
10 compunction about signing it, knowing it to be false. Thus its real value depended entirely on the honesty of the trader signing it. From Hira’s point of view, its main risk management exercise was in narrowing its sources of supply down to New Way, with which it had dealt for a number of years without significant problems coming to light. Sanjay Hira felt that through the original introduction and his subsequent regular visits he was comfortable with  
15 New Way’s reliability and this was far more important than creating a perfect paper file for each deal. It was however a known feature of dealing in this market that certain documents were important to satisfy HMRC and by and large Hira obtained and kept those documents.

### Inspections

20 146. We accept that Sanjay Hira’s evidence in relation to inspections was patchy. He seemed unclear as to the details of precisely what inspections entailed. This tends to suggest that to him the inspection reports were somewhat peripheral. There could be a number of reasons for this. One reason could certainly be that he did not concern himself with the reports because he knew they were a pointless paper exercise; however we tend to the view that he had a broad grasp of what was entailed and as long as the inspection reports threw up  
25 no obvious issues, he simply did not feel the need at a commercial level to spend too much time on them; thus his recollection became less reliable with the passage of time.

### Negotiation

30 147. Mr Cannan asserted that there was no evidence of any negotiations preceding the deals under appeal. Sanjay Hira said that all the negotiations had been oral and he had not kept any notes, just a spreadsheet of prices, currency rates, stock offers and the like which he used as a negotiating tool. Mr Cannan pointed to his failure to mention this document earlier or produce a copy of it as being suspicious.

35 148. We do not consider the lack of any available written evidence of negotiations before the deals to be particularly significant on its own. We accept Sanjay Hira’s evidence that there was verbal negotiation and we do not consider the evidence supports Mr Cannan’s suggestion that Hira’s customers simply took whatever they were offered.

### Terms of payment

40 149. Mr Cannan appeared to submit that the release of the goods both to and by Hira before any payment had been made for them was suspicious, as was the fact that there was no evidence as to the terms of payment.

150. We consider that the granting and obtaining of credit (in similar fashion to the rest of Hira's trade) is, if anything, indicative of the normality of the mobile phone trading rather than a cause of suspicion. In highly artificial trades one often sees rapid money flows through many accounts held with the same bank (generally FCIB), all around the time of  
5 release or delivery of the goods and with the same money clearly moving down the chain. In the present case, Hira had no FCIB account and therefore it experienced delays in both sending and receiving payment. Also, it did make payments to New Way before receiving payment from its customer – so clearly it was not simply “recycling” the same money as it received, it was providing its own finance for the deals.

10 Hira should have reviewed its relationship with Sea following the 11/03 verification results

151. HMRC carried out an extended verification exercise on Hira's mobile phone deals for November 2003, looking at its UK purchases. They eventually traced back all of these purchases to defaulting UK traders and notified Hira of that fact by letter dated 21 April 2004.

152. We note that Hira ceased to trade with its supplier in five of the six deals in question – the other supplier had supplied just 47 phones.

153. Mr Cannan criticised Hira's failure to take any action in relation to Sea (its purchaser in all but one of the six deals). Mr Gibbon replied that HMRC themselves took no further action on that repayment claim, as (according to Mr Mody's evidence) it was decided that it  
20 was not necessary to pass it up to the central MTIC team; also, there was nothing in HMRC's approach to suggest they were warning Hira about its customers in addition to its suppliers. In short, everyone was concentrating on the problem lying at the start of Hira's supply chain and neither Hira nor HMRC at that time gave any thought to there being a problem with its customers.

25 *Actions suggesting bona fide trade*

154. There were also a number of further facts which came out in evidence and which Mr Gibbon argued were pointers suggesting Hira was carrying out a bona fide trade. These included:

30 (1) The fact that Hira used its own freight forwarders and took physical delivery of the goods at their premises – it did not simply use the services of its supplier's freight forwarders.

(2) Hira arranged for all its shipments to be boxed up in wooden crates, rather than just passing them on in the condition it received them.

35 (3) Hira arranged for IMEI numbers to be scanned from an early stage on a voluntary basis and maintained a spreadsheet which enabled it to spot any duplications (which would have provided evidence that its customers were carouselling the phones back into the UK).

*Summary of our views on the “knowledge” issue*

40 155. We have seen and heard no direct evidence that Hira actually knew its purchase were connected with VAT fraud.



156. We also do not feel able to infer, from the evidence we have seen and heard, that it actually had such knowledge. In reaching this conclusion, a significant factor in our thinking is that if Hira had been knowingly involved in a large scale fraud, its involvement was very far from efficient. It sold mainly to Sea, which (on the evidence we saw from the Italian tax authorities) did not “carousel” the goods back to the UK or another EU country but sold them in Italy without accounting for VAT. This may have been a significant local fraud in Italy, but it did not exploit the far larger opportunities of recycling the goods for repeated VAT fraud. Also, Hira did not purchase large batches of phones that had been traded as a single “job lot” down a chain of buffers to it; nearly all its purchases were of only a fraction (often a very small fraction) of the phones which had originally been imported/acquired by the defaulter. The history of its relationship and dealings with Online Cellular certainly gave rise to some concerns in our mind as to the bona fides of those dealings, but those concerns are not sufficient to persuade us on a balance of probabilities that Hira was actually a knowing conspirator with Online Cellular.

157. Mr Cannan submits that even if it did not actually know, Hira should have realised that the deals it was undertaking were too good to be true, and the only explanation for them was that they were connected with fraudulent evasion of VAT.

158. We consider that this issue can only be considered sensibly against the background of all the other circumstances and the full history of Hira’s trading which were set out in the evidence (and some of which have been set out above). We should emphasise that we have viewed that evidence in the round. The fact that we have specifically mentioned only certain parts of that evidence in this decision (especially those parts which, it appeared to us, were most heavily relied on by HMRC) should not be taken to imply that we have only considered those parts of the evidence.

159. It is a finely balanced judgment, but in the circumstances of this case we do not consider that Hira (through Sanjay Hira and/or Nari Hira) either did know or should have known that the only reasonable explanation for the transactions the subject of these appeals was that they were connected with fraudulent evasion of VAT.

### **Conclusion**

160. The appeal must therefore succeed. We would note that, in relation to deals 5 and 6 of June 2006, we would have allowed the appeal in any event as HMRC have failed to establish the necessary connection to fraudulent evasion of VAT.

161. 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.



**KEVIN POOLE**  
**TRIBUNAL JUDGE**  
**RELEASE DATE: 6 July 2011**

## Appendix 1 - Summary of deals in June, July and September 2006 (including those subject to these appeals)

June 06:			Purchases:				Sales:							
Deal	Phone	Units	Date	Price/unit	Price (ex VAT)	VAT	Date	Unit price £	Unit price £	£ value	Exch rate	Total sale value £	Profit	Buyer
1	Samsung D600	250	05-Jun	£145.00	£36,250.00	£6,343.75	05-Jun	€ 225.00		£151.96	0.6754	£37,990.00	£1,740.00	Sea
2	Samsung D600	1500	05-Jun	£145.00	£217,500.00	£38,062.50	06-Jun		£152.50	£152.50	N/A	£228,750.00	£11,250.00	Online Cellular
3	Motorola V3 Black	500	06-Jun	£80.00	£40,000.00	£7,000.00	06-Jun	€ 124.00		£83.74	0.6753	£41,870.00	£1,870.00	Sea
4	Nokia 3250	200	05-Jun	£159.00	£31,800.00	£5,565.00	07-Jun	€ 244.00		£164.79	0.6754	£32,958.00	£1,158.00	Sea
5	Samsung D600	500	07-Jun	£140.00	£70,000.00	£12,250.00	07-Jun	€ 217.00		£146.55	0.6753	£73,275.00	£3,275.00	Sea
6	Nokia 6280	595	08-Jun	£155.00	£92,225.00	£16,139.38	08-Jun	€ 236.00		£159.39	0.6754	£94,837.05	£2,612.05	Sea
7	Nokia 3250	249	08-Jun	£158.00	£39,342.00	£6,884.85	08-Jun	€ 242.00		£163.44	0.6754	£40,696.56	£1,354.56	Sea
8	Motorola V3 Black	500	09-Jun	£80.00	£40,000.00	£7,000.00	09-Jun	€ 124.00		£83.74	0.6753	£41,870.00	£1,870.00	Sea
9	Nokia N80	400	12-Jun	£290.00	£116,000.00	£20,300.00	12-Jun		£301.00	£301.00	N/A	£120,400.00	£4,400.00	Online Cellular
10	Samsung P300	100	12-Jun	£184.00	£18,400.00	£3,220.00	12-Jun	€ 280.00		£189.10	0.6754	£18,910.00	£510.00	Sea
11	Motorola V3 Black	500	14-Jun	£80.00	£40,000.00	£7,000.00	14-Jun	€ 124.00		£83.74	0.6753	£41,870.00	£1,870.00	Sea
12	Samsung D600	500	19-Jun	£139.00	£69,500.00	£12,162.50	20-Jun	€ 215.00		£145.20	0.6753	£72,600.00	£3,100.00	Sea
13	Samsung P300	140	19-Jun	£184.00	£25,760.00	£4,508.00	20-Jun	€ 280.00		£189.10	0.6754	£26,474.00	£714.00	Sea
14	Samsung E900	200	20-Jun	£175.00	£35,000.00	£6,125.00	21-Jun	€ 268.00		£180.00	0.6716	£36,000.00	£1,000.00	Sea
15	Samsung D600	250	21-Jun	£135.00	£33,750.00	£5,906.25	22-Jun	€ 211.00		£142.50	0.6754	£35,625.00	£1,875.00	Sea
16	Nokia N80	100	21-Jun	£282.00	£28,200.00	£4,935.00	22-Jun	€ 422.00		£285.00	0.6754	£28,500.00	£300.00	Sea
17	Nokia N91	60	21-Jun	£280.00	£16,800.00	£2,940.00	22-Jun	€ 426.00		£287.70	0.6754	£17,262.00	£462.00	Sea
18	Sony E K750i	100	21-Jun	£111.00	£11,100.00	£1,942.50	22-Jun	€ 171.00		£115.49	0.6754	£11,549.00	£449.00	Sea
19	Samsung P300	300	27-Jun	£182.00	£54,600.00	£9,555.00	28-Jun	€ 278.00		£187.75	0.6754	£56,325.00	£1,725.00	Sea
20	Samsung D820	300	27-Jun	£139.00	£41,700.00	£7,297.50	28-Jun	€ 214.00		£144.53	0.6754	£43,359.00	£1,659.00	Sea
21	Nokia 6680	300	30-Jun	£138.50	£41,550.00	£7,271.25	30-Jun	€ 211.00		£142.50	0.6754	£42,750.00	£1,200.00	Sea

July 06:														
1	Nokia 6233	200	04-Jul	£159.00	£31,800.00	£5,565.00	05-Jul	€ 242.00		€163.44	0.6754	£32,688.00	£888.00	Sea
2	Motorola V3 Silver	500	06-Jul	£82.00	£41,000.00	£7,175.00	10-Jul	€ 126.00		€85.10	0.6754	£42,550.00	£1,550.00	Sea
3	Nokia 6280	494	06-Jul	£156.00	£77,064.00	£13,486.20	10-Jul	€ 237.00		€160.06	0.6754	£79,069.64	£2,005.64	Sea
4	Samsung D600	200	10-Jul	£129.00	£25,800.00	£4,515.00	10-Jul	€ 198.00		€133.72	0.6754	£26,744.00	£944.00	Sea
5	Nokia N80	100	10-Jul	£275.00	£27,500.00	£4,812.50	10-Jul	€ 417.00		€281.63	0.6754	£28,163.00	£663.00	Sea
6	Nokia N91	50	10-Jul	£275.00	£13,750.00	£2,406.25	10-Jul	€ 417.00		€281.63	0.6754	£14,081.50	£331.50	Sea
7	Samsung D820	360	12-Jul	£137.00	£49,320.00	£8,631.00	12-Jul	€ 211.00		€142.43	0.6750	£51,274.80	£1,954.80	Sea
8	Samsung D600	250	12-Jul	£128.00	£32,000.00	£5,600.00	13-Jul	€ 198.00		€133.61	0.6748	£33,402.50	£1,402.50	Sea
9	Motorola V3 Silver	400	17-Jul	£80.00	£32,000.00	£5,600.00	17-Jul	€ 125.00		€84.36	0.6749	£33,744.00	£1,744.00	Sea
10	Samsung D820	1400	20-Jul	£132.00	£184,800.00	£32,340.00	20-Jul		€139.00	€139.00	N/A	£194,600.00	£9,800.00	Online Cellular
11	Motorola V3 Pink	1500	20-Jul	£84.50	£126,750.00	£22,181.25	20-Jul	€ 131.00		€88.44	0.6751	£132,660.00	£5,910.00	Sea
12	Motorola V3i	300	20-Jul	£110.00	£33,000.00	£5,775.00	20-Jul	€ 169.50		€114.06	0.6729	£34,218.00	£1,218.00	Sea
13	Motorola V3 Pink	1000	21-Jul	£84.50	£84,500.00	£14,787.50	21-Jul	€ 131.00		€88.43	0.6750	£88,430.00	£3,930.00	Sea
14	Motorola V3 Pink	750	24-Jul	£84.50	£63,375.00	£11,090.63	24-Jul	€ 131.00		€88.43	0.6750	£66,322.50	£2,947.50	Sea
15	Samsung P300	100	24-Jul	£178.00	£17,800.00	£3,115.00	24-Jul	€ 272.00		€183.61	0.6750	£18,361.00	£561.00	Sea
16	Samsung P300	169	28-Jul	£178.00	£30,082.00	£5,264.35	31-Jul	€ 272.00		€183.61	0.6750	£31,030.09	£948.09	Sea
17	Samsung D820	100	28-Jul	£129.00	£12,900.00	£2,257.50	31-Jul	€ 196.00		€132.31	0.6751	£13,231.00	£331.00	Sea
18	Motorola V3 Black	1000	28-Jul	£83.50	£83,500.00	£14,612.50	31-Jul	€ 129.50		€87.41	0.6750	£87,410.00	£3,910.00	Sea

September 06:

Purchases:

Sales:

Deal	Phone	Units	Date	Price/unit	Price (Ex VAT)	VAT	Date	Unit price €	Unit price £	£ value	Exch rate	Total sales value £	Profit	Buyer
1	Nokia 6280	400	04-Sep	£153.00	£61,200.00	£10,710.00	04-Sep			£158.00		£63,200.00	£2,000.00	Sea
2	Samsung D830	200	04-Sep	£170.00	£34,000.00	£5,950.00	04-Sep			£176.00		£35,200.00	£1,200.00	Sea
3	Motorola V3i	259	05-Sep	£101.00	£26,159.00	£4,577.83	06-Sep	€ 158.00		£105.33	0.6666	£27,280.47	£1,121.47	Sea
4	Motorola V3 Black	500	11-Sep	£78.00	£39,000.00	£6,825.00	11-Sep			£82.00		£41,000.00	£2,000.00	Sea
5	Samsung D600	350	12-Sep	£121.00	£42,350.00	£7,411.25	12-Sep			£124.66		£43,631.00	£1,281.00	Sea
6	Samsung D830	300	25-Sep	£155.00	£46,500.00	£8,137.50	25-Sep			£161.33		£48,399.00	£1,899.00	Sea
7	Motorola K1	250	28-Sep	£176.00	£44,000.00	£7,700.00	29-Sep			£182.66		£45,665.00	£1,665.00	Sea

Total input VAT reclaimed:	£412,934.74
LESS input VAT on "non-defaulter" deals:	£69,603.10
Reclaimed input VAT disallowed:	<b>£343,331.64</b>

- Note 1: In June and July deals, "Total sale value £" column shows Sterling value of sales - actual value where sales were in Sterling, and notional value allocated by HMRC when sales were in Euros (applying exchange rates of between £0.6716 and £0.6754 per Euro)
- Note 2: In September deals, "Total sale value £" column shows notional Sterling values allocated by HMRC, based on supposed exchange rate of £0.6666 per Euro. No actual sales prices in Euros available for "no VAT evasion" deals.
- Note 3: Shaded lines are deals which do not trace back to VAT evasion, so VAT reclaim allowed and not subject to current appeals.

## Appendix 2

### VAT defaulters and related evidence

<u>Defaulter</u>	<u>Deal Month</u>	<u>No.</u>	<u>HMRC Officer</u>	<u>VAT loss £</u>
Taxable person purporting to be Subbuma Limited	June 2006	1	Barry Patterson	1,287,173.91
Infotel Communications Limited	June 2006	3, 8 & 11	Kathryn Ellis	3,845,272.26
Udeil Solutions Limited	June 2006	2, 4, 7	John McPartlin	7,672,682.25
Knightswood Limited	June 2006	9, 10, 13	James McGee	8,746,119.23
Phone City Limited	July 2006  September 2006	11, 12, 13, 14, 17 & 18  3	George Edwards	34,014,672.36
Muhammed Ali & Associates Limited	June 2006	12	Dean Foster & Anthony Gray	4,742,512.97
West 1 Facilities Management Limited	June 2006	14	Fu Lam	126,090,716.99
JD Telecom UK Limited	June 2006	15	David Maud	7,069,372.27
Universal Appliances Limited	June 2006	17	Paul Cole	1,910,281.82
R S Sales Agency Limited	June 2006 July 2006	18, 21 1	Vivien Parsons	29,964,535.90
Heathrow Business Solutions Limited	June 2006	20	Romaine Lewis	31,607,310.00
Taxable person purporting to be Parfums (UK) Limited	July 2006	2, 3, 4, 5, 6, 7, 8 & 9	Jonathan Read	5,100,533.2
Kaymore Export Limited	July 2006	10	Sarah Barker	3,937,019

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Note 1: No defaulter identified for June 2006 deals 16 & 19, July 2006 deals 15 & 16 or September 2006 deals 1, 2, 4, 5, 6 or 7 as no VAT loss is alleged in relation to these deals

Note 2: No defaulter identified for June 2006 deal 5 or 6 as these are alleged to be “blocking buffer” deals

Note 3: Figure of VAT loss for Subbuma is maximum possible figure, if all untraced purchases were imports or acquisitions

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