This is the successful MTIC appeal of Express Computers Limited where CTM instructed tax counsel to defend an allegation that its director knew or should have known of a connection to fraud when purchasing computer parts. CTM offered a contingency fee arrangement where 50% was paid upfront and the remainder only if successful.

The Judge found that Offices had not been honest in their evidence and the MTIC appeal was allowed in full. This shows the importance of not just defending allegations but showing the HMRC Officers to be untrustworthy.

FIRST-TIER TRIBUNAL
TAX

EXPRESS COMPUTERS UK LIMITED
HILLCRAFT TRADING LIMITED
Appellants

- and -

THE COMMISSIONERS FOR HER MAJESTY'S REVENUE AND CUSTOMS
Respondents

DECISION NOTICE

TRIBUNAL: Judge Peter Kempster
Mr Alban Holden

Mr Hywel Jenkins of counsel, instructed by CTM Tax Litigation Limited, for the Appellant

Mr Mark Bryant-Heron and Miss Laura Mackinnon of counsel, instructed by the General Counsel and Solicitor to HM Revenue and Customs, for the Respondents

DECISION

1. By decisions dated 23 April 2008 the Respondents ("HMRC") refused repayments of input tax claimed by the Appellants. Express Computers UK Limited ("Express") was refused £419,043.19 in respect of the VAT quarter ended July 2006, and £54,501.65 in respect of the VAT quarter ended October 2006. Hillcraft Trading Limited ("Hillcraft") was refused £189,046.82 in respect of the VAT quarter ended August 2006. The reason given for the refusals was that HMRC believed the relevant transactions were connected with Missing Trader Intra-Community fraud ("MTIC fraud"). Both companies appealed against the

respective decisions on 14 May 2008. Both companies are under common control and pursuant to earlier case management directions the appeals were heard together.

2. The Tribunal took evidence from the following witnesses. For the Appellants, Mr Stephen Bradshaw (director of the Appellants) confirmed and adopted five witness statements dated 1 May 2009, 4 September 2009, 22 March 2010, 15 April 2010 and 21 April 2010, and gave oral evidence. For HMRC, (1) Mr Walter Watt (HMRC officer who took over responsibility for the disputed input tax refunds from his colleague Ms Jennifer Cottrell in November 2008) confirmed and adopted three witness statements dated 13 March 2009 (re-signed on 19 April 2010), 22 October 2009 and 22 March 2010, and gave oral evidence; (2) Mr Vincent D'Rozario (HMRC officer responsible for the VAT affairs of Hillcraft between August 2003 and February 2005, when responsibility passed to his colleague Ms Gellvear) confirmed and adopted a witness statement dated 19 October 2009, and gave oral evidence; (3) Ms Susan Allen (HMRC officer responsible for the VAT affairs of Express in 2004) confirmed and adopted a witness statement dated 12 April 2010, and gave oral evidence; (4) Mr William Hodgson (HMRC officer monitoring traders in 2005 and 2006) confirmed and adopted a witness statement dated 29 March 2010, and gave oral evidence; (5) Ms Kathryn Smith (HMRC officer responsible for FCIB investigation work) confirmed and adopted an amended witness statement dated 25 May 2010, and gave oral evidence; and (6) Mr Roderick Stone (HMRC officer with technical oversight of MTIC fraud on behalf of HMRC) confirmed and adopted a witness statement dated 12 February 2009, and gave oral evidence.

MTIC fraud and the loss of the right to repayment of input tax

3. By way of background description of MTIC fraud, we adopt the explanation given by Lewison J in *RCC v Livewire Telecom Ltd* [2009] STC 643 (at ¶ 1):

> "Value added tax ('VAT') fraud is a serious problem for national taxing authorities throughout the European Union. VAT fraud can take a number of forms. The particular form of fraud with which these appeals are concerned is known generically as missing trader intra-community fraud or MTIC fraud. This is a description coined by Her Majesty's Revenue and Customs ('HMRC'), but is generally used by those who specialise in this area. Even this generic type of fraud can itself take different forms:
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> (i) In its simplest form it is known as an acquisition fraud. A trader imports goods from another member state. No VAT is payable on the import. He then sells on those goods to a domestic buyer and charges VAT. He dishonestly fails to account for the VAT to HMRC and disappears. The importer is labelled a 'missing trader' or 'defaulter'.
>
> (ii) The next level of sophistication involves both an import and an export. A trader once again imports goods from another member state. No VAT is payable on the import. Typically the goods are high value low volume goods, such as computer chips or mobile phones. He then sells on those goods to a domestic buyer and charges VAT. He dishonestly fails to account for the VAT to HMRC and disappears. The domestic buyer sells on to an exporter at a price which includes VAT. The exporter exports the goods to another member state. The export is zero-rated. So the exporter is, in theory, entitled to deduct the VAT that he paid from what would otherwise be his liability to account to HMRC for VAT on his turnover. If he has no output tax to offset against his entitlement to deduct, he is, in theory, entitled to a payment from HMRC. Thus HMRC directly parts with money. Sometimes the exported goods are re-

> imported and the process begins again. In this variant the fraud is known as a carousel fraud. There may be many intermediaries between the original importer and the ultimate exporter. These intermediaries are known as 'buffers'. The ultimate exporter is labelled a 'broker'. A chain of transactions in which one or more of the transactions is dishonest has conveniently been labelled a 'dirty chain'. Where HMRC investigate and find a dirty chain they refuse to repay the amount reclaimed by the ultimate exporter."

4. A VAT registered trader enjoys the right to repayment of input tax where the credit due to him exceeds his output liability: Art 17 EC Sixth VAT Directive, incorporated into UK domestic legislation in ss 24 to 26 VAT Act 1994. However, that right can be lost if the facts fall within the legal principle stated by the Court of Justice of the European Communities ("the ECJ") in a number of cases, and in particular *Kittel v Belgium; Belgium v Recolta Recycling SPRL* (Joined cases C-439/04 and C-440/04) [2008] STC 1537. *Kittel* at ¶ 62:

> "… 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 fraudulent evasion of value added tax, it is for the national court to refuse that taxable person entitlement to the right to deduct."

5. The exact nature of this test was recently explained by the Court of Appeal in *Mobilx Ltd & others v RCC* [2010] STC 1436. That decision was issued during the course of the hearing of the current appeals, and both parties made submissions on it. From that decision we draw the following points (paragraph references are to the judgment of Moses LJ):

> (1) The Tribunal should refuse to allow the right to deduct where it is established, on the basis of objective evidence, that the right is being relied on for fraudulent or abusive ends. (¶ 39)
>
> (2) This includes a trader who himself had no intention of committing fraud but who is to be treated as a participant by virtue of the fact that he knew or should have known that by his purchase he was taking part in a transaction connected with fraudulent evasion of VAT. (¶¶ 41 & 43)
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> (3) A trader who has the means at his disposal of knowing that by his purchase he is participating in a transaction connected with fraudulent evasion of VAT but who fails to deploy means of knowledge available to him, loses his right to deduct. The loss of right of deduction by such a trader is not a penalty for negligence but instead because the objective criteria for the scope of that right are not met. (¶ 52)
>
> (4) The test in *Kittel* is simple and should not be over-refined. It embraces not only those who know of the connection with fraudulent evasion of VAT but those who should have known from the circumstances which surround their transactions that those transactions 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. (¶ 59)
>
> (5) For the right to deduct to be lost it is not sufficient that a trader should have known that by his purchase it was more likely than not that his transaction was connected with fraudulent evasion of VAT. 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. (¶ 60)

(6) A trader who decides to participate in a transaction connected to fraudulent evasion, despite knowledge of that connection, is making an informed choice; he knows where he stands and knows before he enters into the transaction that if found out, he will not be entitled to deduct input tax. A trader who has the means of knowledge but chooses not to deploy it knows that, if found out, he will not be entitled to deduct. If he chooses to ignore obvious inferences from the facts and circumstances in which he has been trading, he will not be entitled to deduct. (¶ 61)

(7) The ultimate question is not whether the trader exercised due diligence but rather whether he should have known that the only reasonable explanation for the circumstances in which his transaction took place was that it was connected to fraudulent evasion of VAT. (¶ 75)

(8) If HMRC assert that a trader's state of knowledge was such that his purchase is outwith the scope of the right to deduct then HMRC must prove that assertion. (¶ 81)

(9) The surrounding circumstances can establish sufficient knowledge to treat the trader as a participant. The Tribunal should not unduly focus on the question whether a trader has acted with due diligence. Even if a trader has asked appropriate questions, he is not entitled to ignore the circumstances in which his transactions take place if the only reasonable explanation for them is that his transactions have been or will be connected to fraud. The danger in focussing on the question of due diligence is that it may deflect the Tribunal from asking the essential question, namely, whether the trader should have known that by his purchase he was taking part in a transaction connected with fraudulent evasion of VAT. The circumstances may well establish that he was. (¶ 82)

(10) Circumstantial evidence may indicate that a trader has chosen to ignore the obvious explanation as to why he was presented with the opportunity to reap a large and predictable reward over a short space of time. A trader who chooses to ignore circumstances which can only reasonably be explained by virtue of the connection between his transactions and fraudulent evasion of VAT, participates in that fraud and, by his own choice, deprives himself of the right to deduct input tax. (¶¶ 84 & 85)

Background

6. Express was incorporated in October 1997 and Hillcraft in June 2003. Mr Bradshaw is sole director of both companies. Mr Geoffrey Bradshaw, Stephen Bradshaw's brother, is company secretary of both companies.

7. Express registered for VAT in October 1997 with its business described as retail of computers and equipment, and projected annual taxable turnover £500,000. Hillcraft registered for VAT in July 2003 with its business described as wholesale general consumer goods. Both companies made various requests to move to monthly VAT returns but these were refused by HMRC, originally because there was insufficient evidence of continued repayment trader status and later because of concerns that given the companies' trade sectors they may expose HMRC to a loss of revenue.

8. On 2 August 2006 Express filed its VAT return for the quarter ended July 2006, showing a net reclaim of £419,043.19. On 29 August HMRC notified the company that its claim was subject to extended verification – an audit procedure whereby HMRC examines the relevant transactions and verifies their authenticity. On 4 September 2006 Hillcraft filed its VAT return for the quarter ended August 2006, showing a net reclaim of £189,046.82. On 20 September HMRC notified the company that its claim was subject to extended verification. On 11 December 2006 Express filed its VAT return for the quarter ended October 2006, showing a net reclaim of £54,501.65. HMRC notified the company that its claim was subject to extended verification.

9. In April 2008 HMRC formally decided not to make the repayments, as detailed in ¶ 1 above.

10. HMRC contend that both Express and Hillcraft were brokers; that the transactions giving rise to the denied repayments were connected with fraudulent evasion of VAT; and that both companies knew or should have known that they were participating in transactions connected with fraudulent evasion of VAT. The Appellants do not contest that the transactions giving rise to the denied repayments were contained in dirty chains; but they deny that they knew or should have known that they were participating in transactions contained in dirty chains.

11. We deal with the evidence and our conclusions by reference to the following three issues:

(1) Was there a fraudulent evasion of tax?

(2) If so, were the disputed transactions connected with that fraudulent evasion?

(3) If so, did the Appellants know of that connection, or should they have known of that connection?

Was there a fraudulent evasion of tax?

12. Appendix One to this decision notice is a table of the transactions in each of the three VAT returns under appeal which gave rise to disputed input tax reclaims. The numbering is that used during the hearing, and is not sequential because of other non-reclaim deals.

13. HMRC compiled "deal sheets" for each transaction giving rise to an input claim, and these formed part of Mr Watts' evidence. These look beyond the immediate counterparties to the deal and trace back up the chain of transactions; HMRC are able to do this because there should be corresponding transactions at each stage of the chain which they can access from the VAT records (the "electronic folder" maintained on each VAT registered trader). From the deal sheets and other information HMRC concluded that every one of the broker transactions on all three VAT returns could eventually be traced back to a defaulter or a highjacked VAT registration.

14. The deal sheets show that:

(1) Of the 16 disputed transactions in Express's July 2006 VAT return,

(a) Five (deals 1, 2, 3, 4 & 7) traced eventually to a defaulter and missing trader Technologz.Net Limited.

(b) Four (deals 8, 16, 17 & 18) traced eventually to a defaulter and missing trader UR Traders Limited.

(c) Four (deals 10, 12, 14 & 15) traced eventually to a hijacked trader Okeda Limited.

(d) One (deal 11) traced eventually to a defaulter West 1 Facilities Management Limited.

(e) One (deal 13) traced eventually to a defaulter and missing trader XS Enterprises Limited.

(f) One (deal 5) traced eventually to a defaulter SNC Info Solutions UK Limited.

(2) Of the seven disputed transactions in Hillcraft's August 2006 VAT return,

(a) Two (deals 1 & 2) traced eventually to a defaulter and missing trader Crossview Consortium Limited.

(b) Three (deals 3, 4 & 5) traced eventually to Okeda Limited (above).

(c) One (deal 6) traced eventually to UR Traders Limited (above).

(d) One (deal 7) traced eventually to a defaulter and missing trader Kaymore Exports Limited.

(3) Of the two disputed transactions in Express's October 2006 VAT return,

(a) One (deal 2) traced eventually to a defaulter Ultimate Wholesale Limited.

(b) One (deal 4) traced eventually to Kaymore Exports Limited (above).

15. The deal sheets showed that the person at the top of each chain was a defaulter or a highjacked VAT registration and the losses of VAT to HM Treasury were clearly attributable to fraud, rather than, say, normal commercial insolvency.

16. The deal sheets also show the description of the goods in each deal, the transaction values at each stage of the chain, and the freight forwarder where the goods were located. In most cases the goods were computer chips. In most cases the goods remained at a single freight forwarder's premises through several successive transactions, usually only leaving for their export abroad by the Appellants.

17. Two of the disputed transactions (deal 11 in Express's July 2006 VAT return and deal 6 in Hillcraft's August 2006 VAT return) related to purchases of Nokia mobile phones from Phoenix Tech Limited. In relation to the Hillcraft deal HMRC had compared the International Mobile Equipment Identifier numbers (which are unique to each handset) for those goods with the data on HMRC's "Nemesis" database, and had ascertained that all the IMEI numbers were already registered – indicating that those handsets had previously been scanned on import to the UK, which is suggestive of the goods being "carouselled" around the EU.

18. HMRC submitted it was notable that the identity of the buffers used was largely steered by the identity of the defaulter. Also, the profit margins enjoyed by the buffers (but not the broker) were very small and remarkably consistent. HMRC contended that such factors

could not be genuine coincidences but instead were clear evidence of contrived fraud. Thus every chain was a dirty chain.

19. First Curacao International Bank ("FCIB") was a bank based in the Netherlands Antilles which in October 2006 was closed by the Dutch authorities because of suspected involvement in fraud and money laundering; HMRC believed FCIB was used extensively by parties to MTIC transactions. Ms Smith's evidence concerned an extensive exercise she had performed comparing Mr Watts' deal sheets with the FCIB records that were available to HMRC. The object was to follow the money both upstream and downstream from the disputed transactions. Ms Smith fairly accepted that the exercise had limitations:

> (1) The bank records available were only those of FCIB. Although she had non-FCIB bank statements for the Appellants there were generally no non-FCIB bank statements for other parties in the chains.
>
> (2) The Appellants had non-FCIB bank accounts as did other parties at the "bottom end" (ie the broker end) of the chains. Some parties did not have an FCIB account.
>
> (3) Although some transactions were obviously reflected in the FCIB records – exact amounts on the invoice dates – many were in amounts similar but not exact to the invoice sums. Also, many traders indulged in bulk payments, whereby money was dispersed by a number of transfers on the same day. Thus Ms Smith had had to make certain assumptions (which she considered reasonable) as to the source and destination of funds where the amounts did not tally exactly.
>
> (4) Some money flows reached a "dead end" where Ms Smith could not follow the money further as it moved entirely away from FCIB, or the fragmentation of the funds proved too difficult to analyse.

20. Within those limitations Ms Smith had established:

> (1) There were a number of third party payments evident in the flow of funds. HMRC regarded such diversion of funds as suspicious and a hallmark of MTIC transactions.
>
> (2) Most accounts enjoyed a large throughput of funds on a back-to-back basis but a small or negligible balance after such transactions. HMRC considered these FCIB accounts were merely conduits for buffer transactions. A common feature was there were insufficient funds in an account to meet a purchase payment obligation until sales consideration for the back-to-back deal had already been received.
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> (3) Many sums varied up or down slightly from the expected transaction value, possibly indicative of the payment or receipt of commissions or third parties taking a "cut" of the deal.
>
> (4) There were several instances where traders appeared more than once in a chain, and would use money received from one transaction in the chain to fund payment for another transaction in that chain. HMRC considered this "circularity" to be suspicious and indicated contrivance in the make-up of the chain.

21. The Appellants did not contest that there had been fraudulent evasion of VAT by third parties unconnected to the Appellants.

Conclusion:

22. Having considered all the evidence produced to the Tribunal we are satisfied that there was fraudulent evasion of VAT by the person at the head of each dirty chain described in the deal sheets.

Were the disputed transactions connected with that fraudulent evasion?

23. HMRC contended that the deal sheets and the FCIB money flows taken together proved that the disputed transactions were connected with fraudulent evasion of VAT.

24. Arising from his cross-examination of Ms Smith, Mr Jenkins for the Appellants contended:

> (1) The exercise was of necessity, and as fairly accepted by Ms Smith, limited in scope. FCIB was not the dominant mode of transfer of funds at the broker end of the deals, with parties such as the Appellants, Pars Technology and Double V. Looking only at the FCIB accounts ignored the rest of the picture; once divorced from the deal chains the exercise of following the money became highly judgmental; without exact transaction details it became necessary to make assumptions which might not prove justified; there were anomalies in the dates shown on the FCIB statements on at least one transaction.
>
> (2) The allegations of circularity were flawed. HMRC had merely identified a number of parties all trading with one another on a number of transactions; it was possible to draw a circle around certain money flows but that did not mean anything; HMRC had themselves amended their conclusions on at least one transaction so as to retract the allegation of circularity, and had also accepted that money moving around between parties did not necessarily equate to a funding of the deal.

Conclusion:

25. Having considered all the evidence produced to the Tribunal we are satisfied that each of the disputed transactions was the broker transaction in a dirty chain, and thus they were all connected with fraudulent evasion of VAT.

Did the Appellants know of that connection, or should they have known of that connection?

26. We detail below a number of contentions put forward by HMRC. It was common ground that:

> (1) The burden of proof was borne by HMRC – see Moses LJ in *Mobilx* at ¶ 81.
>
> (2) The appropriate standard of proof was the balance of probabilities – see Lord Hoffman in *Re B* [2009] 1 AC 11 at ¶ 13.
>
> (3) The relevant knowledge or means of knowledge was that of Mr Bradshaw.

Contention: Mr Bradshaw engaged in an area of business susceptible to MTIC fraud and he was aware of that.

27. HMRC's arguments:

(1) The disputed transactions took place in mid-2006 – when MTIC fraud in computer components and electronic goods was at its height. Everyone in that line of business would have been acutely aware of the risks they were running of getting caught up in an MTIC fraud dirty chain. If they chose to continue to participate then they needed to exercise a very high level of care.

(2) Mr Bradshaw had been warned on several occasions of the risks of MTIC fraud and its prevalence in the area of computer component trading. As early as August 2003 Mr Bradshaw received HMRC's Notice 726, explaining the problem of MTIC fraud and warning of the potential for joint and several liability where a tax loss is discovered. In March 2004 HMRC sent to Express a letter highlighting the risks of involvement in MTIC fraud transactions; stating that computer equipment, mobile phones and ancillary equipment were susceptible commodities; stating that there were ongoing problems in the trade sector; and informing that verification of VAT status of counterparties should be undertaken with the specialist HMRC unit at Redhill (see ¶ 31 below). A similar letter was sent to Hillcraft.

(3) Mr D'Rozario made visits to Hillcraft in March 2004 with his supervisor Ms Allen, and in November 2004 with Ms Gellvear. Mr Bradshaw explained that he was considering expanding into exporting computer equipment; that he intended to perform Redhill checks and obtain credit reports by way of due diligence on counterparties; that he would use freight forwarders for inspections; he was already advertising on the International Computer Brokers website; he had identified some potential suppliers; funding would be from his own savings and loans from his father and brother, and perhaps a bank loan; banking would be through Barclays' St Helens branch; he requested monthly returns but was told there was insufficient record of repayment trading at that time.

(4) In July 2006 – which is in the period covered by these appeals – another letter was sent reiterating the problems in the trade sector and giving further guidance. This included advice on due diligence checks; request for verification of VAT numbers on a transaction-by-transaction basis; warning about third party payments; warning about the risk of joint and several liability; and giving guidance on record keeping.

(5) Mr Bradshaw 's introduction to the business of computer component trading appears to have been through a Mr Thomas Hugh Lacey, who at one point had been a director of Hillcraft and invested £37,000 in the business. Mr Lacey owned a company called Sceneklik Limited which from 2002 traded in mobile phones and was deregistered by HMRC in 2004 following involvement in deal chains that traced to defaulters.

(6) Three VAT returns (VAT quarters ended January 2005 and April 2005 for Express, and VAT quarter ended January 2005 for Hillcraft) had been selected by HMRC for extended verification procedures, and Mr Bradshaw was fully aware of HMRC's concerns. Mr Stone's evidence was that in conducting an extended verification on a broker HMRC would expect to see purchase and sale invoices; shipping documents; stock documents; inspection reports; due diligence reports; evidence of payment. These may be inspected on visits and/or using records provided by or taken from the broker. The exercise would be enlarged to examine each link in the transaction chain, so far as possible. If the chain led back to a defaulter then an assessment would be raised on the defaulter. The broker would

be informed that a dirty chain had been identified; it was not automatic that the broker's input reclaim would be denied but that would be considered.

(7) The repayments for the three VAT quarters selected for extended verification were paid on a "without prejudice" by HMRC; this was a practice followed by HMRC where they were undertaking verification of transactions but were unlikely to be able to complete their enquiry in a reasonable timescale. Again, this should have alerted Mr Bradshaw to HMRC's concerns.

28. Appellants' arguments:

(1) Mr Bradshaw was interested in computers from an early age and began to be involved in IT from about 1980. He gained an O-level in computer science. He joined the Royal Navy in 1984 and became a communications and radars specialist, involved with surveillance, radar and computerised weapons systems. After service at home and abroad he left the Royal Navy in 1990 and initially helped with the family business of a small chain of video rental shops. In 1991 he became involved in the new phenomenon of mobile phones, which initially he saw as merely an additional business stream but which became very successful. However, his main interest was in preparing computers and he concentrated on his business as an IT support technician, offering IT support to home and business users; configuring all aspects of computer hardware, networks, and internet connectivity; and repairing software and hardware problems. In 1994 he began buying and selling secondhand computers, which was a profitable business. Express was established in 1996. Mr Bradshaw was satisfied he had a good business - there was a real lack of independent computer dealers in and around the St Helens area. Within 18 months he had cornered the local market. He was able to buy goods by the pallet load. He advertised in local magazines and, when the local market was saturated, moved to national magazines. Around 2000 the market changed with the concentration on the internet; a new breed of web seller evolved and there was a squeezing of margins throughout the computer industry. As well as a very busy retail side, including mail order, Express had many trade customers across the UK. These included schools, universities, hospitals, and trade dealers.

(2) When Mr Bradshaw began to consider exporting he was visited by Mr D'Rozario and explained his intentions. In the expectation of extra wholesale and export trading, he established Hillcraft in June 2003. The initial funding came from an investment of personal savings by Mr Bradshaw and a loan of some £50,000 from his father. The customers Mr Bradshaw had initially identified, in Germany, turned out to be too aggressive on price and there was no successful trading relationship. However, Pars Technology Limited had been a supplier to Express since 1997; a section of that company concentrated on supplying trade customers with the full range of computer components and Mr Bradshaw dealt actively with them. With the commencement of the export trade in January 2005 Mr Bradshaw continued to purchase from Pars. The deals undertaken in the disputed periods were similar to those undertaken beforehand, although the volume may have been greater as the business was growing.

(3) When HMRC informed the Appellants that they were conducting extended verifications on both VAT periods (January and April 2005) Mr Bradshaw's understanding was that HMRC were looking into the supplier and the supply chain to check everything was satisfactory and that there was no problem. Those exercises encompassed purchases from both Pars and Silverstar. In due course HMRC completed their extended verifications and Express and Hillcraft were repaid the balance of repayments due. Mr Bradshaw deduced that everything was completed to their satisfaction and that there were no problems. At the time of the disputed transactions Mr Bradshaw was not aware that HMRC had started denying VAT repayments to Pars.

(4) In cross examination Mr Stone had accepted that where an extended verification exercise had been conducted and a VAT reclaim paid to a broker then the broker could legitimately believe that the chain had been established to be clean.

(5) Mr Lacey was a longstanding friend of Mr Bradshaw; they played football together. Mr Bradshaw had not known of Sceneklik until some time later; the decision to start exporting was his alone and nothing to do with Mr Lacey.

Contention: Scrutiny of the deal chains reveals several features that should have aroused the suspicions of the Appellants

29. HMRC's arguments:

(1) Mr Stone's evidence was that the legitimate "grey market" in computer components and mobile phones is driven by three factors:

(a) Pricing arbitrage between markets, including currency rate differences.

(b) Dumping surpluses of stock.

(c) Unmet consumer demand, including manufacturer underestimates.

(2) HMRC accept there is legitimate wholesale dealing in computer components, but the disputed transactions are attached to lengthy chains involving parties none of whom are a manufacturer or an end-user. That is a hallmark of MTIC fraud rather than *bona fide* grey market trading. Nether Appellant at any stage dealt with either a manufacturer or an end-user; instead, they exported goods without questioning the position. While Pars was an authorised retailer, the purchases by the Appellants were wholesale transactions. Mr Bradshaw should have enquired as to the status of other parties in the chains – perhaps not actual identities, which may have been considered commercially confidential, but whether they were authorised dealers or retailers. Not to do so was tantamount to turning a blind eye.

(3) Ms Smith's work was sufficient to establish circularity of funds in several of the disputed deal chains, and that demonstrated contrived transactions which should have alerted Mr Bradshaw to the non-commerciality of the transactions.

(4) The same handful of traders appears in the chains. The Appellants contend that the disputed transactions took place in a genuine open market with competitive trading. But the counterparties are confined to only a few companies, which suggests an artificial pattern. Why should someone undertaking genuine

trading confine themselves to a handful of suppliers and customers? There was no evidence that Mr Bradshaw actively researched other possible sellers and buyers.

(5) The mark-ups earned by the persons in the chains are suspicious. Given the Appellants' contention that the disputed transactions took place in a genuine open market with competitive trading, one might expect to see each trader maximising their profit. But in fact everyone except the broker earns only a modest profit margin – often a mark-up of less than 1%. That contrasts with the broker (the Appellants) who achieves a mark-up of 4 – 6%. The buffers are apparently unable or unwilling to access that profitable deal. That suggests an artificial pattern – one preordained to give a return to the broker for its participation in the dirty chain.

(6) Money is paid away to persons outside the invoice chain, by way of third party payments. HMRC regard such payments as a key badge of MTIC fraud. There are several instances in the chains.

(7) The scale of fraud perpetrated by the defaulters is significant. Of the Appellants' eight suppliers, three have been deregistered by HMRC and the other five have been denied input tax in similar VAT periods to those under consideration in these appeals. Taking all the traders in all the chains, 22 have been deregistered; ten have been dissolved; nine are in liquidation and five have proposals to strike off registered at Companies House. Technologz was deregistered in July 2006, owing £1.3 million to HMRC. UR Traders disappeared in July 2006 after service of VAT assessments totalling £66 million. West One Facilities Management disappeared in June 2006 owing £126 million. Excess Enterprise Systems owes £5.2 million, and Crossview Consortium a similar amount. Kaymore Export owes £2.7 million for one period alone.

(8) Even the Appellants' non-export deals in the relevant periods track back to defaulters. These transactions are not the subject of the current appeals but are informative.

(a) In the Express July 2006 return as well as the 16 broker deals there were also four sales to UK companies. Two (deals 9 and 19) were sales to GB Distribution UK Limited, a company owned by Mr Geoffrey Bradshaw, Stephen Bradshaw's brother, and operating from the same address as Express. Another (deal 6) was to Pars Technology, which was also the main supplier of Express. The last (deal 20) was a sale to a company called XEL Multicomponent Limited.

(b) All the deals on the Hillcraft August 2006 return were broker deals.

(c) In the Express October 2006 return as well as the two broker deals there were also eight sales to UK persons. One of these (deal 7B) was a sale to GB Distribution UK Limited (Mr Geoffrey Bradshaw's company) and another (deal 7C) was a sale to a Mr Roger Hanson, an HMRC officer, which is described later (see ¶ 47 below).

30. Appellants' arguments:

(1) The Appellants dealt only with their immediate suppliers and customers, and were completely oblivious to the activities of other persons in the deal chains. The direct suppliers and customers were reliable and had an established record.

(2) It is normal commercial practice to keep the identities of one's suppliers and customers confidential. It was not commercially viable to interrogate customers and suppliers about their own counterparties. That was commercially confidential information that would not be shared. Disclosing that information to one's competitors would give them the opportunity to bypass your business and trade direct with those persons. So it is no surprise that where there is a chain of transactions, any particular "link" in that chain would be ignorant of the other links in the chain with the exception of the one before and after it – that person's immediate supplier and immediate customer. Any attempt to establish the identities of the other links would be refused, for the reasons of commercial confidentiality given above. For example, where one supplier had inadvertently let slip the identity of a counterparty (Tradex) Mr Bradshaw had been able to capitalise on that by going direct to that person, cutting out the previous supplier (see ¶ 46(10) below).

(3) The Appellants had no knowledge or means of knowledge of the profit margins of other persons. Neither Appellant had made any third party payments in connection with any of the disputed transactions, and had no knowledge or means of knowledge of third party payments by other persons in the deal chains.

Contention: Redhill verifications were late or non-existent.

31. HMRC's arguments:

(1) A prevalent feature of VAT fraud is the falsification of VAT registration numbers, and the highjacking of legitimate numbers, by fraudsters. HMRC advise traders to check the identity of counterparties by contacting the HMRC dedicated office in Redhill, Surrey and verifying the VAT details for the counterparty. This will also alert the trader to a counterparty having had its (otherwise genuine) VAT registration suspended or cancelled by HMRC. The literature provided to traders by HMRC is clear that a verification is not some form of authorisation to conduct a particular trade – only the trader can make that decision for itself – but it does confirm the VAT registration is valid. For traders in a high risk business area such as computer components, HMRC insist that Redhill checks are performed for every transaction and on the day of trade (to ensure the information is as up-to-date as possible). Notwithstanding that, it was a regular occurrence that Mr Bradshaw performed Redhill verifications only after a deal was concluded.

(2) Mr Stone's evidence was that HMRC had warned traders of the high risks in this market sector and advised careful due diligence, including checking the VAT registration numbers of counterparties. HMRC was not in a position to insist but they did strongly encourage a "Redhill check". The Europa website was an EU facility enabling traders to check the validity of a VAT registration number. The Redhill check went beyond this by being able to check address details etc which offered some protection against a fraudster using a highjacked VAT number. The information normally provided by a trader was a letter of introduction from the counterparty, a copy certificate of incorporation (or overseas equivalent), and a copy VAT registration certificate (or overseas equivalent). The Redhill check was not tied to a particular transaction but as an important due diligence step it would be expected to be performed before a transaction actually took place. Traders were encouraged to make checks even where they had a continuing course of business with a particular party. A Redhill check response was not any form of

authorisation by HMRC in relation to a transaction. Whether to conduct a particular transaction was entirely a commercial decision for the trader. HMRC also operate a procedure called a "veto letter" whereby if HMRC deregister a trader or otherwise have cause for concern, other traders who obtained a Redhill check on the suspected trader in the previous 12 months are alerted of the change of circumstances.

32. Appellants' arguments:

(1) The picture painted by HMRC was misleading. Redhill checks had been made frequently and repeatedly. Every requested check had received a positive reply. The numbers of checks made from the start of the export trading were:

Pars – 21

Silverstar – 14

Supreme – 10

Megantic – 6

Nu-Life – 1

Tradex – 4

Bytel – 3

Double V – 33

All Trading – 22

Tele Trading – 3

Tradius - 1

(2) The Redhill check requests detail the vendor, the goods and price paid; the export customer and the price received; and the location of the goods. Where a trader deals repeatedly with a supplier or customer one might expect that only occasional checks would need to be made, but HMRC insisted on a new verification being made for every transaction, on the day of the trade. There were delays in obtaining Redhill verifications – occasionally as long as four days – and it was not commercially viable to wait for verification from Redhill before concluding a transaction. Given the extensive checks successfully made, the criticism as to timing was weak. It was reasonable for a trader who was repeatedly receiving confirmations form HMRC to assume that the counterparty could be trusted as bona fide.

(3) To examine a specific example, on Express deal 12 - Redhill validations for both supplier Megantic and customer All Trading were requested on the 15th but did not come through until the 17th. Mr Bradshaw stated that he could not afford to wait two days for the validation, as the customer was anxious to get the stock and the supplier was anxious to sell it - so waiting two days could jeopardise the entire deal. As a precaution for the delay from Redhill he used the EU VAT checker and checked the VAT details there. So far as he was aware at that time that VAT site was completely up to date. A further precaution was that sometimes when stock was shipped it was shipped on hold so that it would be held in an overseas freight centre and not released until the Redhill validation had been received. However, at the time of this particular transaction Express has been

dealing with All Trading for quite some time and received satisfactory Redhill validations on All Trading at least 20 times previously with no problems.

(4) No veto letters were issued by HMRC to the Appellants. Thus, again, the Appellants had no reason to think they were dealing in anything other than bona fide transactions.

Contention: High value goods were not adequately insured, or insufficient care was taken to ensure proper insurance.

33. HMRC's arguments:

(1) The deals concern high value items in international transit; a prudent businessman engaged in legitimate trading would be concerned to establish proper arrangements for insurance in transit, as well as while the goods were in storage (for example at the premises of a freight forwarder).

(2) However, HMRC contended there was little evidence that Mr Bradshaw concerned himself with this important issue. There were emails to the freight forwarders stating that each customer was providing its own transit insurance but the substantiating documentation was unclear. The insurance documents provided by Double V to Mr Bradshaw are dated May 2008 (and were apparently not translated from Dutch until 2009) which is after the deals. Similarly, the insurance documents from All Trading Worldwide and TeleTrading indicate they were signed in October 2007, and appear not have been sent until May 2008. It was accepted that there were some mentions of insurance in the MSN messaging texts.

(3) Further, in early 2006 two of the freight forwarders used by Mr Bradshaw (Paul's Freight and Humber Freight) alerted him that, due to statutory changes, they were not able to provide full value insurance and informed him in writing, "It is therefore essential as a client you arrange your own all-risk insurance for the full value of your cargo." When HMRC asked Mr Bradshaw, at a visit in September 2006, about his insurance arrangements, he admitted he was unsure. Mr Bradshaw had described the normal terms of trade as "CIF" but there appeared to be an absence of proper insurance arrangements.

34. Appellants' arguments:

(1) Mr Bradshaw did make appropriate arrangements as to insurance cover. Initially Mr Bradshaw had made freight insurance arrangements himself but he realised that his export customers carried their own freight insurance policy and thus he was duplicating insurance. Although he did not acquire or retain copy documentation, he ascertained at the time of the trades that his customers had carriage insurance.

(2) Mr Bradshaw arranged with Double V that they would use Double V's freight insurance policy. That was illustrated by the contemporaneous evidence of the MSN messaging with Double V. He subsequently obtained confirmation from Double V and copy policy documentation, to satisfy HMRC requests raised at visits. The policy showed cover from July 2005 to July 2007 (by extension) up to €750,000 for unlimited transport within Europe.

(3) Similarly, All Trading subsequently provided a copy of a policy covering the period May 2005 to May 2006 and then with 12 month extensions.

(4) There was also documentation obtained from Tradius that, although obtained after the event, did cover the period of the disputed transactions and supported the assertion on Tradius' purchase order that it carried freight insurance of €50,000 per package. Tradius's purchase order mentioned insurance and the instructions given to Forward Logistics included, "please note Tradius are providing the transit insurance".

(5) It was true there might be a very short period of time when the goods belonged to Express or Hillcraft and were physically present at the freight forwarder's premises. Freight forwarders had in the past handled insurance arrangements but, because of legislative changes, had become unable to do that. Mr Bradshaw had no concern about this he knew that the security facilities at the freight forwarders were very sound and he thought there was no major risk for a relatively short period of time.

Contention: Banking through FCIB avoided UK anti-money laundering procedures.

35. HMRC's arguments:

(1) From 2005 traders in the mobile phone sector found it difficult to open or maintain bank accounts at UK banks; the banks refused new business from such businesses and also closed many existing accounts. The mobile phone trade press carried reports that HMRC had put pressure on the banks to do this. Mr Stone's evidence was that HMRC had had no policy to that effect, but the money laundering compliance requirements applicable to the UK banks would have highlighted the sorts of transactions and accounts that carried the characteristics of MTIC fraud and led the banks to what they considered to be the appropriate course of action.

(2) Many traders in this sector had UK bank accounts as well as FCIB accounts. In particular, HMRC would not pay a VAT refund to a non-UK account so brokers needed a UK account to receive their input tax repayments.

(3) Mr Bradshaw's suspicions should have been raised when his customer Double V told him that as a Belgian company they were not allowed by Belgian Customs to hold an FCIB account.

36. Appellants' arguments:

(1) In 2004 Mr Bradshaw became aware of "World Pay System" through advertisements on the International Computer Brokers website. It offered commercial advantages in not having banking cutoff times and the information on ICB indicated it might be useful to have an FCIB account. Having opened an account in 2004 it was not used for over a year.

(2) UK bank accounts were mostly used by the Appellants. All transactions with Pars Technology were conducted through UK bank accounts. Similarly, all transactions with the customer Double V were conducted through UK bank accounts.

(3) Some export sales were in euros and the currency exposure would be covered by fixing a rate with HSBC. For example, Express deal 14 was a purchase by Express from Bytel and sale to Double V. The purchase was in sterling but the sale was in euros. Double V paid into Express's HSBC euro account. To cover the

currency fluctuation risk Mr Bradshaw telephoned HSBC Treasury to book a rate for the foreign currency being received. Mr Bradshaw then transferred sterling from Express's HSBC sterling account into Express's FCIB sterling account and then made a payment to Bytel's FCIB account.

(4) Mr Bradshaw had not attached any significance to the casual comment in messaging chat concerning Belgian companies not being able to open FCIB accounts.

Contention: Trading terms on significant contracts were vague or unspecified.

37. HMRC's arguments:

(1) Despite the significant size of the trades, it is difficult to establish what were the trading terms. Who had responsibility for the goods? What was the recourse in the event of faulty goods? There appear to be no written terms and conditions of business.

38. Appellants' arguments:

(1) Standard form terms of business were printed on the back of hard copy invoices and other trade documentation. It was accepted that this would not have been apparent in transactions where documents were transmitted electronically.

Contention: Express enjoyed a rapid, large increase in turnover with no extra capital or employees.

39. HMRC's arguments:

(1) Express doubled its turnover from £3.3 million in the year ended October 2005 to £6.8 million in the year ended October 2006, without any additional commitment of capital or staff. That alone should have prompted Mr Bradshaw to query the *bona fides* of the trading he was involved in.

(2) The aggregate profits on the disputed transactions were around £193,000 in a four month period. Mr Bradshaw was an experienced businessman and must have realised that this was too good to be true for the small amount of work involved.

(3) The Appellants achieved significant turnover levels with relatively low capital commitment. Mr Bradshaw's own explanation for this was that he was always paid by his customer before his supplier required payment.

40. Appellants' arguments:

(1) Mr Bradshaw had extensive experience in the computer business and as a retailer he built from a standing start within one year turnover of over £600,000. Hillcraft had working capital in the region of £200,000; Express had working capital in the region of £500,000 and also a credit facility with HSBC of £500,000.

(2) The impression that the trading produced "easy money" was false; finding, negotiating and satisfying the trades was difficult and demanding hard work; he would often be using simultaneously several telephones, emails and MSN messaging screens; it was also necessary to arrange the foreign currency fixes and the other banking transactions.

Contention: The trades happen in a very short space of time.

41. HMRC's arguments:

(1) The deals in the chain follow each other quickly – often on the same day. To happen on a consistent basis this must be preordained in some way.

(2) Concentrating on just the Appellants' involvement, one would expect sourcing of opportunities on both the buy and sell sides; negotiation with both parties; establishment of insurance, payment and other terms and conditions; VAT verification; transport arrangements; inspection arrangements with the freight forwarder; and banking (for both purchase and sale). Yet the Appellants seemingly achieve these transactions at a profit consistently in the space of hours – is that a credible illustration of *bona fide* commercial trading?

(3) On one occasion in June 2006 the main supplier Pars Technology actually put Mr Bradshaw in contact with a possible customer (Incoparts) rather than execute a trade themselves. Why should Pars pass over a potential profitable deal, unless this was contrived trading?

42. Appellants' arguments:

(1) Transactions were not as straightforward as HMRC suggest, as can be seen from two examples illustrated by the contemporaneous MSN messaging. First, in May 2006 Express purchased some Intel chips from Bytel; on offer, through an advertisement on the International Computer Brokers website, was a batch of 1300 chips in retail boxes but Express negotiated for purchase of just 1000 of those; they were used to satisfy an order the same day from All Trading; so there was negotiation of not just price but also quantity. Second, in June 2006 Express was negotiating with Double V and it was clear there was active negotiation of prices, quantities and chip type; in particular, in this instance Express could not quote a sufficiently attractive price and did not secure any trade that day with Double V.

(2) It was accepted that the Appellants dealt on a back-to-back basis – buying to satisfy particular orders rather than carrying stock. That was a legitimate way of conducting business and had the commercial advantage that it was not necessary to physically transport goods if they happened to be located at a freight forwarder used by both the Appellants and the vendor. There were at least two instances where Double V gave instructions for purchased consignments to be delivered to their own premises rather than another forwarder.

(3) There was evidence that the chains were not contrived. For example, on one occasion (Express deal 5) having purchased 1700 Intel chips from Pars, Express was able to sell only 1500 of those to Double V. Mr Bradshaw was left with 200 unsold chips which, 10 days later, he resold to Pars at a lower price than he had paid to buy them. That was perfectly normal commercial behaviour. If matters had been contrived then Double V would have had no difficulty buying the full consignment of 1700, and Pars would have had no reason to cut the price on repurchasing any surplus. On another occasion Pars had refused to extend to the Appellants £30,000 credit, and a potential deal foundered because of that refusal.

(4) It was denied there was any contrivance apparent to the Appellants in the relevant transactions. Mr Bradshaw negotiated all the stock prices himself and there was much haggling. Some deals did not go through because price could not

be agreed. All the relevant transactions were genuine deals. He had no idea that they could have been involved in chains giving rise to a VAT loss, because HMRC had repeatedly undertaken extended verifications and inspected all paperwork and confirmed that everything was fine. Mr Bradshaw had never had any reason to suspect that there were any problems whatsoever.

Contention: Inspection of valuable goods is delegated to freight forwarders but no attention is paid to warnings of damage etc.

43. HMRC's arguments:

(1) There is no suggestion that Mr Bradshaw ever took the trouble to examine the high value goods being traded; he delegated that entirely to freight forwarders. Mr Bradshaw obtained inspection sheets from the freight forwarders, and some of those should have prompted further enquiry by him. Some reports noted damage to boxes, including references to knife and pen marks. Others noted the removal of labels or the presence of stamps attached by other freight forwarders; this was an indication that the same cartons had already been exported once before and should have raised suspicion that the goods were being "carouselled" around the EU.

(2) Mr Bradshaw should have been particularly alert to this matter because of his previous experience with the non-existent LCD projectors (see ¶ 50 below). He should have been diligent to ensure he was getting what he was paying for, and the lack of any such concern was cause for suspicion.

44. Appellants' arguments:

(1) There was nothing sinister about some boxes being marked with a stamp for a different freight forwarder – indeed, as the goods would have been earlier imported one might expect there to be the mark of the forwarder handling the import. HMRC had the benefit of the deal sheets and could see (after the event) how the goods had moved but it was incorrect to impute any such knowledge to a trader, such as the Appellants, who was dealing with just its immediate counterparties. There was nothing in HMRC's literature provided to traders to highlight this issue of previous freight forwarders.

(2) Mr Bradshaw had many years experience of involvement in shipping of stock using couriers and pallet shipping. It was common experience that the external boxes would always pick up some degree of minor damage, scuffing, label removal, penmarks etc. Boxes being opened for inspection and then resealed with tape was standard practice. This was generally confined to the outer packaging - within each item would be retail boxed, shrink-wrapped and protected and in a perfectly saleable condition. None of the inspection reports cited by HMRC state that the stock itself is damaged, not even that the boxes have been split open. He had never received back any rejected stock. Overall, only some consignments had comments on the inspection reports and those concerned only a small number of boxes in each consignment.

(3) Mr Bradshaw was based in St Helens and it was unrealistic to expect him to travel to, say, Heathrow to open boxes and physically examine a consignment. The trades were conducted rapidly and any delay would lose the deal.

(4) The timing of knowledge in connections with the projector transaction was important (see ¶ 51 below) – this was another example of HMRC imputing knowledge after-the-event.

(5) On Express deal 14 - There was an inspection report from Forward Logistics saying that 25 outer boxes had been damaged. Also, that two boxes had been opened by Customs. Mr Bradshaw's evidence was that when he noticed this he contacted Forward Logistics who advised him that periodically Customs would just open boxes to have a look inside and then close them up. There was no suggestion that Customs had expressed any concern about the boxes.

(6) On Hillcraft deal 3 - The inspection report showed that two boxes had been opened by Customs. The only significance Mr Bradshaw drew from this was that the boxes had been examined by Customs, opened and checked.

(7) On Express deal 5 - The inspection report pointed out that a few of the boxes had Geologistics stamps and some labels had been removed. This did not raise any concerns with Mr Bradshaw as he assumed that destination labels would be removed and new labels fixed during transhipment.

Contention: Due diligence was inconsistent and not all the documents said to have been received were provided to HMRC.

45. HMRC's arguments:

(1) Notice 742 emphasised the importance for traders in high risk business sectors to check the status of their suppliers and customers.

(2) The Appellants did conduct some credit checks with agencies such as Dunn & Bradstreet and CreditSafe on their suppliers and customers. However, many of these checks were outdated. Some adverse information had not been heeded.

46. Appellants' arguments:

(1) Mr Bradshaw's due diligence was necessarily confined to the immediate counterparties. The Appellants traded with their immediate counterparties – suppliers and customers – and had a duty to check the *bona fides* of those persons by appropriate due diligence. Mr Bradshaw is a businessman; he is not, unlike HMRC's witnesses, a trained Customs investigator. He did everything that could be reasonably expected of him in his due diligence on his suppliers and customers. He satisfied himself that his suppliers were credible business organisations and would be able to supply the contracted goods; that they were run by real individuals with community ties.

(2) The export trade commenced in January 2005 and that explains why the Dunn & Bradstreet enquiries and other due diligence date from that month. These reports were not directly linked to particular transactions, but rather a general exercise undertaken to keep an ongoing check on suppliers. With a Dunn & Bradstreet full monitoring service there would be updates included for 12 months. If full monitoring had not been requested then within the next six months an e-alert would be sent to inform him of any changes within the following six months. Details would not be provided under this service and it would be up to Mr Bradshaw to follow-up. There was a similar system with CreditSafe. A service called risk trackers was activated by Mr Bradshaw on all his main suppliers and

customers to give information. The alert facilities were rather like the HMRC veto letter procedure, to give a subsequent alert of change of circumstances.

(3) The due diligence conducted by Mr Bradshaw on the Appellants' suppliers and customers was as set out below. Copies of these documents had been provided to HMRC either at the relevant times, or as part of one of their verification exercises, or as part of the disclosure for this hearing.

(4) Pars Technology ("Pars") – this supplier was the largest supplier of the Appellants in the relevant periods. From 1996 when Mr Bradshaw opened his retail shop he subscribed to Computer Trade Only magazine, which was considered to be the bible of the computer industry. Pars advertised heavily in the magazine, having all the prime advertising slots. They assembled their own brand of PCs and laptops. They were a large scale system builder and Mr Bradshaw dealt with them extensively over the years. Mr Bradshaw visited the computer trade shopper show at Birmingham NEC every year and Pars had a stand there. He met Pars on several occasions at the shows. Pars were a large company with huge warehousing space at Milton Keynes. From the late 1990s Mr Bradshaw had bought a lot of equipment from Pars, having an account manager there. When the export trade started he expected that Pars would be his main supplier, and that had proved the case. He was very satisfied with the relationship with Pars and had never had any cause for complaint.

(a) Copy of incorporation certificate obtained and retained.

(b) Copy of VAT registration certificate obtained and retained.

(c) Dunn & Bradstreet credit report obtained in January 2005, describing Pars as having financial strength of at least £1.5 million, with a recommended credit limit of £680,000. Further reports obtained including in April and November 2005. CreditSafe credit report obtained in June 2006.

(d) Copy of utility bill dated 22 November 2005 obtained and retained.

(e) Copy of passport of a director of Pars obtained and retained.

(f) 21 Redhill check VAT verifications.

(5) Bytel – Since 1996 Mr Bradshaw had dealt with a company called Logitech whose offices were close to his shop in St Helens. Two senior sales staff from Logitech moved to Bytel and in May 2006 Mr Bradshaw dealt with Bytel.

(a) Copy of incorporation certificate obtained and retained.

(b) Copy of VAT registration certificate obtained and retained.

(c) CreditSafe credit reports obtained in June and July 2006.

(d) Copy of utility bill obtained and retained.

(e) Copy of passport of a director obtained and retained.

(f) Three Redhill check VAT verifications.

(6) Phoenix – Phoenix was a relatively new supplier. Mr Bradshaw contacted Phoenix from seeing advertisements on websites. He visited their premises. He met the director Nisakat Khan, who he understood was a long-time established

businessman in Birmingham. At the premises there appeared to be some 20 employees. Redhill validations were carried out. Phoenix also completed a due diligence questionnaire; this was a document Mr Bradshaw had seen used elsewhere and thought that it would be a useful part of his own due diligence programme, so he adapted the form for use by the Appellants; it was used for new suppliers. As Mr Bradshaw had a previous trading history with Phoenix in relation to CPUs, he felt comfortable buying mobile phones from them. He had physically visited Phoenix before that particular transaction.

(a) Copy of incorporation certificate obtained and retained.

(b) Copy of VAT registration certificate obtained and retained.

(c) A CreditSafe credit report.

(d) Copy of council tax bill for a director obtained and retained.

(e) Copy of passport of a director obtained and retained.

(f) Completed due diligence questionnaire.

(g) Photographs of Phoenix's business premises.

(h) Details of bank accounts with Lloyds and FCIB.

(7) Megantic – Megantic advertised on the ICB website. Mr Bradshaw was contacted by Mr Alsop, who had worked for a long time for VIP Computer Centre - a large computer distributor based in the North West. Mr Alsop was Mr Bradshaw's account manager and they had a long history of dealing. Mr Bradshaw visited the premises. He did not do a large amount of business with Megantic as he had regular suppliers in Pars and Silverstar.

(a) Copy of incorporation certificate obtained and retained.

(b) Copy of VAT registration certificate obtained and retained.

(c) Copy of telephone bill for a director obtained and retained.

(d) Copy of utility bill obtained and retained.

(e) Copy of driving licence of a director obtained and retained.

(f) Six Redhill check VAT verifications.

(g) Dunn & Bradstreet credit report obtained in January 2006.

(8) Nu Life – This was a company set up by a former senior sales manager at Pars, who Mr Bradshaw had known well at that time. Mr Bradshaw visited Mr Palmer as his new premises. He took photographs as part of his due diligence programme. There was only one purchase from Nu Life in 2006.

(a) Photographs of company's business premises.

(b) Completed due diligence questionnaire.

(c) Copy of passport and driving licence of a director obtained and retained.

(d) CreditSafe credit reports obtained in June 2006.

(e) Redhill check VAT verification on 18 May 2006.

(9) Supreme Distribution – Mr Bradshaw had been dealing with Supreme since he started Express in 1996. They advertised in the CTO magazine and were a general trade distributor with a large warehouse and a wide range of stock. They offered competitive pricing and were a long-standing supplier.

(a) Copy of incorporation certificate obtained and retained.

(b) Copy of VAT registration certificate obtained and retained.

(c) Copy of passport of a director obtained and retained.

(d) Details of bank account at NatWest.

(e) Ten Redhill check VAT verifications.

(f) Dunn & Bradstreet credit reports obtained in July, November and December 2005.

(10) Tradex – Mr Bradshaw had noticed that on a piece of deal documentation from Silverstar the supplier had failed to redact the name of its own supplier - this was usually deleted so as to keep the identity of the supplier from the customer. Mr Bradshaw made enquiries, tracked down Tradex and contacted them. Thus he was able to cut out Silverstar and get some better pricing. He performed due diligence on them. Towards the end of the relevant period he did quite a bit of business with them.

(a) Copy of VAT registration certificate obtained and retained.

(b) Details of bank account at RBS.

(c) Copy of utility bill obtained and retained.

(d) Trade references.

(e) Copy of incorporation certificate obtained and retained.

(f) Copy of utility bill of a director obtained and retained.

(g) Completed due diligence questionnaire.

(h) Two CreditSafe credit reports obtained in July 2006.

(i) Four Redhill check VAT verifications.

(11) Silverstar – The sales staff at Silverstar had previously worked for a large trade distributor called Red Star Marketing, which Mr Bradshaw had dealt with. When the staff moved to Silverstar they contacted Mr Bradshaw. He obtained Dunn & Bradstreet and CreditSafe reports.

(a) Copy of incorporation certificate obtained and retained.

(b) Copy of VAT registration certificate obtained and retained.

(c) Dunn & Bradstreet credit reports obtained in April and November 2005.

(d) Premises visit.

(e) 14 Redhill check VAT verifications.

(12) Double V – This was the major customer of Express. As a foreign company due diligence would be expected to be more difficult. Although Mr Bradshaw did not visit Double V he had much contact with the main executive,

Jan. There was never any problem dealing with Double V who were very professional.

(a) 33 Redhill check VAT verifications.

(b) Dunn & Bradstreet credit reports obtained in July and November 2005.

(13) Tradius – Also a foreign company. Mr Bradshaw was contacted by Tradius and took up informal references with Forward Logistics who confirmed that Tradius was a reliable company. Mr Bradshaw undertook an initial small deal and shipped goods on hold, to ensure they were not released until he had received payment. The transaction was successful.

(a) Redhill check VAT verification.

(14) All Trading – Also a foreign company. Dunn & Bradstreet reports were obtained, as these can be obtained on overseas companies as well as UK companies, but at more expense. Redhill validations were obtained. Mr Bradshaw visited All Trading twice - in 2005 and early 2006 - when he met the director Carlos Lynch. There were warehousing facilities and a number of staff.

(a) Dunn & Bradstreet credit report obtained in November 2005.

(b) 22 Redhill check VAT verifications.

(15) Tele Trading – Also a foreign company. Mr Bradshaw was aware that Tele Trading was the sister company of All Trading. Both companies had the same director Mr Carlos Lynch who Mr Bradshaw had met on more than one occasion. All Trading was primarily concerned with computer components, while Tele Trading was more concerned with mobile phone trading. This was the first wholesale mobile phones transaction Mr Bradshaw had undertaken. At the time he was finding certain computer equipment difficult to get hold of and so looked to other commodities to trade. Having a trading history with All Trading, he felt comfortable dealing with Tele Trading.

(a) Three Redhill check VAT verifications.

Contention: HMRC officers did not suggest the Appellants' trading was acceptable nor support Mr Bradshaw's due diligence on counterparties.

47. On this point we put first the Appellants' arguments:

(1) In 2004 Mr Bradshaw took the decision to go into the export trade. He was entirely transparent about what he was doing. On 30 November he had a meeting with Mr D'Rozario and confirmed that he was considering exporting computer components, and that he intended to finance these deals by personal savings and loans from his father and perhaps his brother. From the outset he indicated that his likely supplier would be Pars Technology. He explained the due diligence he was going to undertake. Also the prices and his intention to use Forward Logistics for stock inspections.

(2) So as early as the autumn of 2004 HMRC were aware of the export intentions and the identity of the main supplier. The export trade began in January 2005 with a supply from Pars Technology. Mr Bradshaw also dealt with Silverstar, another of the major suppliers. As soon as the export trade had commenced HMRC instituted an extended verification investigation. Express's VAT period for the

quarter ended January 2005 was selected for extended verification. This period included the first month or two of the export trade and included the purchases from Pars Technology. Mr Bradshaw was informed that an extended verification was being undertaken, that HMRC were continuing their enquiries in relation to the transactions undertaken in that period, and that in the meantime a without prejudice repayment was being made for some of the total claim. Ms Gellvear told him this was routine. This was the first VAT return showing a net repayment and so Mr Bradshaw was not concerned. His accountant confirmed this was normal. The full amount of the repayment was made shortly afterwards.

(3) The very next period for the quarter ended April 2005 was also subject to an extended verification exercise. Mr Bradshaw was informed that HMRC had decided that based on the evidence currently available, the balance of the claim had to be repaid, but the repayment was being made without prejudice to any other action that may result from HMRC's continuing enquiries into the relevant supply chains. HMRC stated that their enquiries were still continuing and that Mr Bradshaw would be notified in due course of the outcome. A full refund was eventually paid.

(4) Similarly, the VAT return of Hillcraft for the period ended January 2005 was also selected for extended verification. A without prejudice interim payment was made and, in due course, the full reclaim was paid.

(5) To someone outside HMRC it appeared as though HMRC were paying up as they cleared or confirmed various transactions on the VAT return under verification. So there were three investigations that would have led Mr Bradshaw to the conclusion that HMRC were happy that the people with whom he was dealing were not involved in deal chains that had resulted in tax losses. Mr Stone had confirmed in his evidence that that was a legitimate interpretation by a trader.

(6) Mr Bradshaw recalled his VAT officers as being Mr D'Rozario from early 2005; then Ms Gellvear; then from about summer 2005 Roger Hanson. Between January 2005 and March 2006 he was visited regularly by HMRC officers. They inspected in detail the documentation he had prepared and was made available to them. He was never given the impression that there was anything insufficient about the record keeping; they always said all the record keeping and procedures was fine and did not give any cause for concern. Mr Hanson stopped visiting from March 2006; instead Mr Bradshaw provided information on a spreadsheet given to him by Mr Hanson - this required details of suppliers, customers, freight forwarders, buying and selling prices etc. Mr Bradshaw e-mailed the spreadsheets to Mr Hanson. Mr Bradshaw was never told that Mr Hanson had been replaced as his VAT officer and had been contacting Mr Hanson regularly to chase up VAT repayments and similar matters.

(7) In Summer 2005 Mr Bradshaw called at HMRC's offices by appointment to deliver a selection of documents illustrating his due diligence procedures. Ms Gellvear, who had taken over as responsible officer, was not present or in a meeting so Mr D'Rozario met Mr Bradshaw. Mr Bradshaw's evidence was that Mr D'Rozario examined the documents and told him his paperwork was superb.

(8) Mr William Hodgson accompanied Mr Hanson on visits and, because he was older than Mr Hanson, Mr Bradshaw assumed that Mr Hodgson was the senior officer. Like Mr Hanson, Mr Hodgson appeared happy with the paperwork

presented by Mr Bradshaw. In November 2005 Mr Hodgson told Mr Bradshaw that he needed a new computer mouse and Mr Bradshaw recommended an optical mouse. He sold him one for one pound and issued an invoice. He was not sure of Mr Hodgson's surname and made the invoice out for "Bill". He felt this was suggestive that HMRC were happy with his supply chain, because Mr Hodgson was unconcerned at purchasing an item from Express.

(9) In August 2006 Mr Hanson telephoned Mr Bradshaw to ask about iPods. He wanted advice on the best make and model for a gift for his daughter. He also asked for a price for the model that Mr Bradshaw recommended. He arranged to come to Mr Bradshaw's home address to collect the iPod and pay for it - due to ill health Mr Bradshaw had closed the shop by this time and his home address was the registered office address of Express. The price was £109 plus VAT which Mr Bradshaw believed was close to the cost price to him - this was one of the items from Express October deal 4 which had included a part batch where he had five or six items left and was looking to clear them. Mr Bradshaw saw nothing suspicious in making this sale. It reassured him that everything must be fine with his suppliers as his VAT officer would not be buying stock off him if he had any concerns about the suppliers. He was contacted by Mr Hanson after the sale in connection with a software fault on the machine which Mr Bradshaw advised him how to rectify. They parted on very friendly terms.

(10) Mr Hanson was subsequently disciplined for a number of matters including the purchase of the iPod, and dismissed from HMRC. His union representative at the disciplinary hearing had been Mr Hodgson. It was clear from the transcript of Mr Hanson's evidence at his disciplinary hearing that, regardless of the appropriateness of his purchasing the iPod from Mr Bradshaw, he saw nothing of concern in acquiring those goods: "I didn't find anything of concern. I didn't find where he may have defaulted in any way, shape or form. ... I didn't believe the goods to be anything other than legitimate." On its own that may be interpreted as a self-serving statement by Mr Hanson but it was in the context of both Mr Hanson and Mr Hodgson being the only HMRC officers on the front line with Express and Hillcraft in the period following 12 months after VAT returns had been subject to extended verification on three occasions, all resulting in full repayments to Express and Hillcraft. Taken together, the picture presented to Mr Bradshaw was that there was no concern on the part of HMRC that any of his supply chains were questionable.

(11) Mr Hodgson’s own evidence was that Mr Bradshaw could well have been left with the impression that all his paperwork and his checks were in order.

(12) In early 2006 Mr Hanson and Mr Hodgson visited and Mr Bradshaw's accountant, Mr Gray, was present. Again the officers said that everything was fine with all the paperwork and had no problems with anything. Mr Hodgson then made a racist comment that the trade sector problems lay with Asians. Mr Bradshaw was taken aback, not expecting such a comment from an HMRC officer, but thought nothing further of it. They parted on friendly terms. However, Mr Gray was very annoyed at this comment.

(13) All the way through the disputed transactions there were validation applications to Redhill, all of which received positive replies. HMRC were fully apprised of the identities and VAT registrations of every single counterparty. There had been no change in the major suppliers since the extended verification

exercises 12 months earlier. It was reasonable for Mr Bradshaw to conclude that he was in a superior position to many other traders, who might not have had their chains subject to extended verification on even one, let alone three, occasions.

48. HMRC's arguments:

(1) The selection of the returns for extended verification and the caution that the interim payments were made on a without prejudice basis, should have warned Mr Bradshaw that HMRC had concerns.

(2) Mr Hanson had been disciplined and dismissed for a number of incidents including an inappropriate relationship with a trader in a high risk MTIC sector, being the purchase of the iPod from Express in August 2006. Little weight should be attached to statements he made at his disciplinary hearing, where he faced serious consequences. Another unsatisfactory aspect of Mr Hansom's behaviour was that he had apparently failed to file any reports of his visits to his allocated traders.

(3) Concerning the Summer 2005 meeting between Mr Bradshaw and Mr D'Rozario, Mr D'Rozario's evidence was that he met Mr Bradshaw because Ms Gellvear was unavailable; they spent 10 to 15 minutes together; there were no interview rooms so they met in the cafeteria area. Mr D'Rozario did not make a note of the meeting, because he was merely collecting some records on behalf of his colleague. Mr D'Rozario flicked through the information to ensure Mr Bradshaw had brought the sort of documents that his colleague would be expecting but expressed no view on the adequacy of the information; he had not been through the documents to evaluate them and he would not have expressed any view on the quality of the information being provided because he was unaware of the underlying transactions.

(4) Mr Hodgson's evidence was that he denied purchasing the optical mouse; he did not have a computer at home until some time later, as evidenced by the purchase invoice for his home computer, and his work computer was maintained by HMRC so he had no need to buy peripherals. He denied making the racist comment; he was a trade union representative and a school governor and had no racist sympathies.

Contention: Mr Bradshaw's behaviour in other respects is also relevant.

49. HMRC submitted that Mr Bradshaw's behaviour in three other matters was pertinent: (a) the 2003 projector transaction; (b) the 2004 software bulk trades; and (c) Mr Bradshaw's criminal conviction in 2009.

(a) The 2003 projector transaction

50. The evidence of Mr D'Rozario was as follows.

(1) Mr D'Rozario was the HMRC officer responsible for the VAT affairs of Hillcraft between August 2003 and February 2005. In November 2003 Mr D'Rozario visited Mr Bradshaw concerning the first transactions undertaken by

Hillcraft. These were a purchase and sale of 1750 Sony Discmen and 96 LCD projectors; there was a single vendor and a single purchaser. Mr Bradshaw had failed to make Redhill checks on either party and had made a third party payment; Mr D'Rozario told Mr Bradshaw he should make Redhill checks, and not make third party payments.

(2) In December 2003 Hillcraft undertook another transaction with those same parties involving some 2000 minidiscs; Mr Bradshaw again made a third party payment. Mr Bradshaw said he was having difficulty getting through to Redhill by phone or fax and had spoken to a staff member called Julie. Mr D'Rozario made enquiries of Redhill and was told there was no one called Julie working there, and they were not aware of any problems with phone or fax contact.

(3) In July 2006 Mr D'Rozario informed Mr Bradshaw that his investigations into the earlier LCD projectors deal had revealed that the goods could not have existed in that quantity; that there was a fraudulent trade; that Hillcraft had been a buffer in the chain and a VAT Tribunal had upheld HMRC's decision to deny a refund of VAT input tax to the exporter broker (a trader called Micropoint). The value to Hillcraft of that deal had been around £500,000. In Mr D'Rozario's opinion if Mr Bradshaw had undertaken rudimentary due diligence, such as the enquiries made by Mr D'Rozario, he would have been alerted to the impossibility of the goods being genuine and thus alerted to the fraudulent nature of the transaction chain. Mr D'Rozario had not thought it appropriate to discuss the case with Mr Bradshaw while it was ongoing, but brought it to his attention in July 2006 the month after the decision was released.

51. For the Appellants Mr Jenkins submitted:

(1) Mr Bradshaw's evidence was that the position on third party payments had not been explained to him properly at the first meeting; he thought Mr D'Rozario's warning only applied to new parties. After he had understood the explanation he never again had made a third party payment.

(2) Mr Bradshaw's evidence was that he originally thought Redhill checks were necessary only when trading in computer components. Mr D'Rozario had no personal experience of getting a verification out of Redhill and was repeating the comments of his colleagues.

(3) Mr Bradshaw was told about the problems with the projector transaction only in July 2006 – almost three years after it took place. The Tribunal case concerned only the export broker (Micropoint) and neither Hillcraft nor Mr Bradshaw was challenged.

(b) The 2004 software bulk trades

52. The evidence of Ms Susan Allen was as follows.

(1) In March 2004 Ms Allen and Mr D'Rozario visited Mr Bradshaw and received the following information.

(a) Express's role was retail and Hillcraft had been established to deal with "bulk trades". Hillcraft had undertaken bulk trades but some had

also been conducted through Express, because Mr Bradshaw's father had been very ill and his partner was pregnant. Also, the bulk deals were software and Express dealt in software.

(b) He had received emails from various sources in response to information placed on trade websites enquiring what types of goods he sold. Although the margins were modest he was paid for the goods before he had to pay his supplier. His then suppliers were STS Corporate and EMR Trading. He had met EMR Trading at a trade show in Birmingham and after running some checks on them had placed orders in excess of £1 million.

(c) The product was called SmartSoft; he did not know the name of the manufacturer; he did not have any supply licence; he did not know the names of any end-users; it was not suitable for retail as it was sold in bundles of 1,000 units. The goods were delivered to him by courier in a sealed box containing sealed packages; the disks were in one envelope and the licences in another, but both envelopes were packaged together; he had opened and examined some of the first packages he received. He took out no insurance above the normal courier insurance.

(d) His sale price was £22 per unit and his profit margin on sales was £200 per 1,000 units. He showed the officers a PowerPoint presentation about the software, but the website for the software was not operational. Ten out of his eleven sales at that time were to Prime Export; he had spoken to, but not met, the managing director; delivery was by AmTrak; the delivery notes gave the address as just "SW6, London". He had not kept records of the licence numbers but, on HMRC's warning of the dangers of carouselling, he would do so in the future. He did not know if the product carried a warranty; he had never had any goods returned but if he did then he would revert to his supplier.

(2) In June 2004 a colleague asked Ms Allen to investigate an apparent mismatch between input tax reclaimed by Prime Export and the output tax reported by Express. Ms Allen spoke with Mr Bradshaw who explained his accountant had failed to record the bulk sales because they had gone through a different bank account; he had given the relevant sales and purchase invoices to his accountant; he confirmed he had not been doing bulk sales recently. Mr Bradshaw was unable to attend a meeting but Ms Allen met with his accountant, Mr Gray, on 6 July. Mr Gray explained that bulk sales by Express had been put through a different bank account from the retail sales, and had been omitted from the VAT return because Mr Gray was not aware of that account. Ms Allen ascertained that the missing item represented around £1.4 million sales. Ms Allen discussed with Mr Gray the then new joint and several liability measures; the high risks in the relevant business sector; the desirability of making Redhill checks; and the fact that STS Corporate – one of Express's software suppliers – had been deregistered in June 2004. They tried the website for the software but it was still not up and running. Mr Gray said he would try to dissuade Mr Bradshaw from any further bulk deals. Ms Allen prepared a formal note of the meeting on her return to her office the same day.

53. For the Appellants Mr Jenkins submitted:

> (1) Without the authorisation code the software was valueless, so the absence of additional insurance was understandable.
>
> (2) Ms Allen may have recalled incorrectly Mr Gray's statement about future bulk deals; he denies it; two months later Mr Gray wrote to HMRC requesting monthly returns for Express because it was about to start exporting computer items and would have net refunds, so clearly the Appellants were proposing to continue bulk deals.

(c) Mr Bradshaw's criminal conviction in 2009.

54. HMRC sought to introduce evidence of two criminal convictions sustained by Mr Bradshaw. One of those dated from 1996 and the Tribunal declined to hear evidence on that matter as it appeared to be a spent conviction, or at least so remote in time as to attract little weight. The other related to a conviction for dishonesty in September 2009. Having heard submissions from both parties the Tribunal ruled on the admissibility of that evidence (that ruling is reproduced as Appendix Two to this decision notice).

55. On 16 September 2009 at Preston Crown Court Mr Bradshaw, on his own confession, was convicted on indictment on 12 counts of possessing or controlling in the course of a business counterfeit goods for sale. The allegations were dated 17 July 2008. The vehicle for those offences was Express and the goods were computer memory sticks and cards. On 20 October 2009 he was sentenced to carry out 100 hours unpaid work and given a 52 weeks imprisonment order, suspended for two years. In her sentencing remarks HHJ Badley said, "In your case as a man of 44 with extensive business experience particularly in the field of computers it is a very poor excuse to say you thought you were dealing with a reputable company in China; that you were importing genuine items."

56. HMRC contended this demonstrated Mr Bradshaw is a man who is prepared to take commercial risks that may not be legal.

57. For the Appellants Mr Jenkins submitted that the conviction postdates by some time the events relevant to the current appeal and little weight should be attached to it.

Consideration and Conclusions re whether the Appellants knew or should have known of the connection with fraudulent evasion of VAT

General awareness of MTIC fraud and suspicious circumstances

58. We find that Mr Bradshaw was well aware of the dangers lurking in the business of trading in the grey market in computer components and electronic goods. It was, as Mr Bryant-Heron put it, a hornets' nest. Mr Bradshaw had many years experience in the computer supply business, both in retail and with trade customers such as schools, colleges and other institutions. He must have gone into this line of business with his eyes wide open. He was given all the usual information by HMRC including meetings with specialist officers and Notice 726. He was cautious in that he used mainly suppliers he had dealt with before going into exporting. Pars Technology was his main supplier and he had dealt with that large company for many years; he had good reason to believe Pars was a legitimate

components trader. In relation to his other suppliers he usually knew particular individuals from previous trading relationships when he ran the retail shop and business. He also took the trouble to visit some of them, and obtain and retain documentary evidence that these had real presence – with staff, premises, a trading history established by credit ratings, etc – and so far as he could establish were genuine businesses.

59. We note that Mr Bradshaw's circumstances are different from a number of other cases that have come before this Tribunal, where the traders previous to commencing large-scale export of high risk goods had no, or only peripheral, involvement in the relevant business sector. In contrast Mr Bradshaw had been in the computer business (albeit not significantly exporting) for many years.

60. HMRC gave to Mr Bradshaw all the generalised warnings they gave to all traders in this high risk sector. But at no point, for example arising from one of the extended verification procedures, did they raise a flag and caution him that any further trades with one or more counterparties could result in a refusal of repayment of input tax. This contrasts with other cases that have come before this Tribunal; for example in *Mobilx* the Tribunal stated (Decision Number 20687 at ¶ 105) (emphasis added):

> "... a trader in Mobilx's position is almost certain to know less, and possibly nothing at all, of suppliers at one or more removes; but that is not to his prejudice, as he is to be fixed only with knowledge which he has, or could obtain "by taking every precaution which could reasonably be required". We do not think it could be argued that, for example, a trader in Mobilx's position should be required to demand of his supplier that the supplier disclose the identity of his own supplier, in order that the first trader can carry out his own due diligence into that supplier, still less is it realistic to expect him to go all the way up the chain. But there must come a time when a trader, *told repeatedly that every one of his purchases followed a tainted chain*, is compelled to recognise that without a significant change in his trading methods every one of his future purchases is more likely than not also to follow a tainted chain—in other words, he cannot possibly be satisfied, on the balance of probabilities, that each transaction he enters into will not be connected with fraud. [The Appellant was], at best, reluctant to accept that this was so, but in our view it is inescapable."

The contrast is that it appears Mobilx were, as Mr Jenkins put it, being given a running commentary by HMRC on their trades being part of dirty chains, while the Appellants were never given any such alert.

61. So Mr Bradshaw was well aware of the dangers inherent in his export trading; he dealt mainly with vendors he had dealt with previously (eg Pars); he undertook due diligence on all counterparties; and, importantly, he was given no indication by HMRC anything was wrong with any of his counterparties.

Redhill validations

62. HMRC emphasised that some Redhill checks were not made on particular transactions, or only received back after the transaction had concluded. The Appellants accept this criticism as a fact but contend that the delays in obtaining Redhill checks made it uncommercial to wait for a response on every occasion. We believe the question to ask is, did Mr Bradshaw behave appropriately in concluding trades while awaiting Redhill check responses? That needs to be examined in the factual context of the large number of Redhill checks made by

Mr Bradshaw on his suppliers and customers. The statistics are at ¶ 32 above but for example in a period of around two years Mr Bradshaw requested over 20 Redhill checks on Pars alone. Every single one of his Redhill checks on every supplier and customer was satisfactory. The overall picture we have is that Mr Bradshaw made a large number of checks on his various counterparties, repeatedly, and saw nothing arising from that work to alert him that any of his customers or suppliers was regarded by HMRC as not being an appropriate counterparty.

Extended verifications and without prejudice repayments

63. On three separate occasions input tax repayment claims by the Appellants were subject to extended verification procedures by HMRC, and repayments were expressly made on a without prejudice basis. That should have highlighted to Mr Bradshaw that HMRC had concerns about his suppliers. However, every one of those extended verifications resulted in full repayments to the Appellants. It was reasonable for Mr Bradshaw to draw the inference that HMRC were checking his supply chains "behind the scenes" and the results were that those chains were, so far as HMRC could establish, clean. Mr Stone fairly accepted that this was a reasonable inference for a taxpayer to draw from several successive extended verification exercises all of which resulted in full repayments.

Insurance

64. Although the full picture concerning the insurance of the goods was made clear rather late in the day – and the Appellants could have made this aspect of their case clearer prior to the hearing rather than during it – the final picture is that the goods were shipped on the purchaser's insurance cover, and we accept that Mr Bradshaw was aware that was being done at the time of the transactions.

65. Until early 2006 freight forwarders arranged insurance cover for goods located at their premises but, due to legislative changes, that ceased then. It would have been prudent for Mr Bradshaw to have arranged insurance cover – even given his explanation that the time-at-risk was short and the premises were extremely secure – but we do not interpret his failure to pursue this as suspicious.

FCIB banking

66. It appears that most of the banking transactions by the Appellants on the disputed deals were conducted through UK bank accounts. Neither the main supplier (Pars) nor the main customer (Double V) operated FCIB accounts.

Ease of trading and profitability

67. Mr Bradshaw's evidence was that trading was not straightforward. There were negotiations on price that might lead to no deal being concluded. On one occasion he had to buy more goods than he could sell and ended up offloading the excess back to the vendor at a loss. Those explanations were supported by the MSN messaging evidence.

68. Mr Bradshaw had a long track record in the computer business. He had built from scratch a successful retail and trade business. As we state at ¶ 59 above, the current case differs from others that come before this Tribunal in that there are good reasons why Mr

Bradshaw should have commenced export trading in computer components and electronic goods, and also why he should be able to achieve a good level of profit for the work he put in.

Damage reported on inspection reports

69. Mr Bradshaw's evidence was that he was unconcerned by superficial damage to the outer shipping cartons as knew the goods inside were further packaged in retail sale packaging. Only if that inner packing had been damaged would he be concerned, and that did not occur. We conclude that none of the freight forwarders' inspection reports gave a message that the goods themselves seem to have suffered damage.

70. The references to the other freight forwarder stamps are fairly cryptic – eg "24 Geologistics stamps". We understand the freight forwarders' inspection reports formed part of the documentation examined by HMRC officers on their visits. If the comments highlighted by HMRC raised any concerns for the officers, there is no evidence that those concerns were conveyed to Mr Bradshaw at the time.

Due diligence

71. HMRC made many criticisms of Mr Bradshaw's due diligence on the suppliers and customers of the Appellants. But having considered the evidence in the round in relation to the disputed deals we conclude that most of those criticisms are not fully borne out.

72. We are mindful of the words of Moses LJ in *Mobilx* concerning the weight to be given to evidence of due diligence checks, and also the comments of Christopher Clarke J in *Red 12 Trading Limited v HMRC* [2010] STC 589 (cited with approval by the Court of Appeal in *Mobilx*). Moses LJ stated (at ¶ 82):

> "... tribunals should not unduly focus on the question whether a trader has acted with due diligence. Even if a trader has asked appropriate questions, he is not entitled to ignore the circumstances in which his transactions take place if the only reasonable explanation for them is that his transactions have been or will be connected to fraud. The danger in focussing on the question of due diligence is that it may deflect a tribunal from asking the essential question posed in *Kittel*, namely, whether the trader should have known that by his purchase he was taking part in a transaction connected with fraudulent evasion of VAT. The circumstances may well establish that he was."

73. As Mr Bryant-Heron put it to us, it would be possible for a trader to go through the motions of due diligence merely to compile a file of documents to be available to show to HMRC on their next visit. Mere mechanical performance of due diligence, however efficiently performed, does not exonerate a trader in a high risk area from the requirement not to take for granted the *bona fides* of those seeking to do business with him but instead to make enquiries to the extent available to him, consider the context of his transactions, and heed any warnings flagged.

74. Looking at the due diligence performed by Mr Bradshaw we consider that he made exactly the type of checks advocated by HMRC in Notice 742 and, in the round, he received no information to cause him to conclude it would be unsafe to trade with those counterparties.

Assurances by HMRC officers

75. Mr Bradshaw was never told that any of his purchases followed a dirty chain. We find that it was reasonable for him to draw the inference from the three separate extended verification exercises all of which resulted in full repayments, that none of his purchases was contained in a dirty chain.

76. Mr Bradshaw goes further and has given evidence that HMRC officers actually reassured him that his trading chains gave no concern to HMRC. He contends that HMRC through its officers actively encouraged him to carry on his export business by complementing him on the quality of his due diligence and giving him the impression that they had no concerns on the deal chains incorporating his transactions.

77. We accept the evidence of Mr D'Rozario concerning the visit of Mr Bradshaw to HMRC's offices in Summer 2005. Comments made by Mr D'Rozario during that brief meeting were confined to confirming that Mr Bradshaw had brought with him the type of documentation requested by his colleague, not that such documentation was satisfactory (or otherwise) and Mr Bradshaw was not entitled to draw such a conclusion.

78. We heard no evidence from Mr Roger Hanson. He was dismissed from HMRC following disciplinary proceedings on a number of matters, including his purchase of an iPod from Mr Bradshaw. It appears that Mr Hanson was lax in filing his inspection reports – the word fairly used by Mr Bryant-Heron was "indolent". That resulted in there being no contemporaneous evidence of those visits, or at least none that was available to us. At his disciplinary hearing Mr Hanson stated "I didn't find anything of concern. I didn't find where he may have defaulted in any way, shape or form. ... I didn't believe the goods to be anything other than legitimate." Mr Bryant-Heron contended Mr Hanson had not told the whole story because entries he made on HMRC's electronic file in September 2005 indicate that Mr Hanson *did* have some concerns over some chains involving deals by the Appellants. However, any such concerns were never communicated to Mr Bradshaw. We consider the fact that Mr Hanson was willing to buy goods from Mr Bradshaw indicated to Mr Bradshaw that Mr Hanson, and thus HMRC, had no particular concerns over the sources of supply of the goods purchased by the Appellants.

79. There is also the disputed allegation that Mr William Hodgson (who retired from HMRC in 2009) purchased an optical mouse from the Appellants in November 2005. The Appellants produced a copy invoice showing a sale to "Bill from Customs". Mr Hodgson denied making the purchase. We found Mr Hodgson's evidence overall to be unreliable. He did not recall visiting Express's premises in 2006 but accepted that he had in that period visited GB Distribution UK Ltd – the company run by Mr Bradshaw's brother – which operated from the same address as Express. He denied making certain pejorative remarks about Mr Bradshaw (or, at least, the Appellants) but was contradicted by the transcript of Mr Hanson's disciplinary hearing. He was adamant that Mr Hanson was the lead officer in relation to the Appellants but again was contradicted by the transcript of Mr Hanson's disciplinary hearing – his explanation was that what he said at the disciplinary hearing was designed to assist his colleague. Because of those contradictions we place little weight on Mr Hodgson's evidence.

80. We do not consider it necessary to reach any conclusion on the alleged racist remark by Mr Hodgson. There was a difference of recollection and even if Mr Bradshaw's recollection was correct, he was not entitled to interpret the alleged remark as an indication to him that HMRC had no particular concerns about his export trades.

81. Taking together the absence of evidence from Mr Hanson, the unreliability of Mr Hodgson's evidence, and the unavailability of any contemporaneous visit reports, HMRC are (despite Mr Bryant-Heron's skilful cross-examination) simply not in a position to refute Mr Bradshaw's assertion that the officers directly responsible for the Appellants' VAT affairs stated to him that they were satisfied the Appellants' export businesses gave no cause for concern.

The projector deal

82. HMRC highlighted several suspicious characteristics of the projector deal: Mr Bradshaw made third party payments, and the goods were fictitious. However, there is no evidence that Mr Bradshaw made any third party payments after this transaction, when he was warned against third party payments by HMRC. The outcome of HMRC's investigation, the blocking of the input tax recovery of Micropoint (the broker), and the Tribunal appeal lost by Micropoint were all communicated to Mr Bradshaw only in July 2006, almost three years after the transaction. Mr D'Rozario's explanation, which we fully accept, was that he considered it inappropriate to mention this to Mr Bradshaw until Micropoint's appeal was determined. But the picture is that Mr Bradshaw was apparently unaware of the role he had played in this VAT fraud until July 2006 when Mr D'Rozario told him the details.

Criminal conviction

83. In relation to Mr Bradshaw's 2009 criminal conviction for dishonesty, we are careful as to the weight to be attached to an event that occurred after the events that are the subject of these appeals.

Other matters

84. We state clearly that we have concerns about several aspects of Mr Bradshaw's trading history: the software bulk sales; his association with Mr Lacey; his subsequent conviction for dishonesty. We have taken those concerns into account in reaching our conclusions.

Conclusions

Actual knowledge?

85. We do not consider that the evidence presented to us is sufficient to establish, on the balance of probabilities, that Mr Bradshaw had actual knowledge that any of the disputed transactions were part of a dirty chain connected with the fraudulent evasion of VAT.

Should have known?

86. The test, stated clearly in ¶¶ 59, 60, 75 & 85 of *Mobilx*, is whether the trader should have known that the only reasonable explanation for the circumstances in which his transaction took place was that it was connected to fraudulent evasion of VAT.

87. We consider that, on the balance of probabilities, that test is not satisfied. It was reasonable for Mr Bradshaw to hold the belief that the circumstances in which the disputed transactions took place were unconnected to fraudulent evasion of VAT. In particular, at the time of the transactions it was reasonable for him to believe that the HMRC officers responsible for the VAT affairs of the Appellants had satisfied themselves that there was nothing suspicious about the trading counterparties of the Appellants, and thus it was safe for export transactions to be undertaken with those counterparties.

Decision

88. For the reasons set out in ¶¶ 58 to 87 above, the appeals are ALLOWED.

Right of appeal to Upper Tribunal

89. Section 11 of the Tribunals, Courts and Enforcement Act 2007 provides that any party to a case has a right of appeal to the Upper Tribunal on any point of law arising from a decision of the First-tier Tribunal. The right may be exercised only with permission which may be given by the First-tier Tribunal or the Upper Tribunal. Rule 39(2) of The Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules 2009 (SI 2009/273) provides that a person seeking permission to appeal must make a written application to the Tribunal for permission to appeal which application must be received by the Tribunal no later then 56 days after the date that the Tribunal sends full written reasons for the Decision. Rule 39(5) provides that an application for permission to appeal must identity the decision of the Tribunal to which it relates, identify the alleged error or errors in the decision and state the result the party making the application is seeking.

90. This document contains the full written findings of fact and reasons for the Decision.

PETER KEMPSTER

TRIBUNAL JUDGE

RELEASE DATE: 25 August 2011

APPENDIX ONE

Table of immediate counterparties on disputed transactions

Deal	Seller	Appellant	Buyer
Express 07/06 Deal 1	Pars Technology Ltd	Express Computers UK Ltd	Double V Belgium BVBA
Express 07/06 Deal 2	Pars Technology Ltd	Express Computers UK Ltd	Double V Belgium BVBA
Express 07/06	Pars Technology	Express Computers	Double V Belgium

Deal 3	Ltd	UK Ltd	BVBA
Express 07/06 Deal 4	Pars Technology Ltd	Express Computers UK Ltd	Tradius BV
Express 07/06 Deal 5	Pars Technology Ltd	Express Computers UK Ltd	Double V Belgium BVBA
Express 07/06 Deal 7	Pars Technology Ltd	Express Computers UK Ltd	Double V Belgium BVBA
Express 07/06 Deal 8	Pars Technology Ltd	Express Computers UK Ltd	Double V Belgium BVBA
Express 07/06 Deal 10	Bytel Distribution Ltd	Express Computers UK Ltd	All Trading Worldwide BV
Express 07/06 Deal 11	Phoenix Tech Ltd	Express Computers UK Ltd	Tele Trading Worldwide BV
Express 07/06 Deal 12	Megantic Services Ltd	Express Computers UK Ltd	All Trading Worldwide BV
Express 07/06 Deal 13	Nu Life IT.com Ltd	Express Computers UK Ltd	All Trading Worldwide BV
Express 07/06 Deal 14	Bytel Distribution Ltd	Express Computers UK Ltd	Double V Belgium BVBA
Express 07/06 Deal 15	Bytel Distribution Ltd	Express Computers UK Ltd	All Trading Worldwide BV
Express 07/06 Deal 16	Phoenix Tech Ltd	Express Computers UK Ltd	All Trading Worldwide BV
Express 07/06 Deal 17	Phoenix Tech Ltd	Express Computers UK Ltd	All Trading Worldwide BV
Express 07/06 Deal 18	Phoenix Tech Ltd	Express Computers UK Ltd	All Trading Worldwide BV
Hillcraft 08/06 Deal 1	Pars Technology Ltd	Hillcraft Trading Ltd	Double V Belgium BVBA
Hillcraft 08/06 Deal 2	Pars Technology Ltd	Hillcraft Trading Ltd	Double V Belgium BVBA
Hillcraft 08/06 Deal 3	Silverstar Components	Hillcraft Trading Ltd	Double V Belgium BVBA
Hillcraft 08/06 Deal 4	Silverstar Components	Hillcraft Trading Ltd	Double V Belgium BVBA
Hillcraft 08/06 Deal 5	Bytel Distribution Ltd	Hillcraft Trading Ltd	All Trading Worldwide BV
Hillcraft 08/06 Deal 6	Phoenix Tech Ltd	Hillcraft Trading Ltd	Tele Trading Worldwide BV
Hillcraft 08/06 Deal 7	Express Computers UK Ltd	Hillcraft Trading Ltd	Double V Belgium BVBA
Express 10/06 Deal 2	Supreme Distribution	Express Computers UK Ltd	All Trading Worldwide BV

APPENDIX TWO

Ruling made during the hearing concerning admissibility of evidence of criminal conviction

Express Computers UK Limited and Hillcraft Trading Limited

Tribunal's reasons for decision to admit in evidence Mr Bradshaw's 2009 criminal conviction.

HMRC have advanced their case on the alternative bases of (i) actual knowledge of fraud, and (ii) should have known of fraud.

In assessing the knowledge and conduct of both Appellant companies, it is the knowledge and conduct of Mr Bradshaw (as the sole director and executive of both companies) which is crucial.

Although we have not yet heard the opening of the Appellants, from the Appellants' skeleton argument it is clear that there are likely to be contradictions of evidence between Mr Bradshaw and one or more witnesses for the Respondents. So the credibility of both sets of witnesses must be assessed by the Tribunal, and must be assessed as of now so a recent criminal conviction *could* be relevant in assessing the credit of a witness.

Also, in relation to the allegation of *actual* knowledge of fraud, Mr Bradshaw's honesty at the time of the disputed transactions is clearly relevant. The Tribunal shall, of course, bear in mind the question of the appropriate weight to give to the evidence.

We wish to consider only the certificate of conviction and any sentencing remarks; not any newspaper or other media comment on the case.