[2011] UKUT 496 (TCC)
Appeal number
FTC/10/2011

Value Added Tax – input tax – disallowance of input tax – MTIC fraud – transactions connected with fraudulent evasion of VAT – whether Appellant knew or should have known that its purchases were connected with VAT fraud

UPPER TRIBUNAL
TAX AND CHANCERY CHAMBER

A ONE DISTRIBUTION (UK) LIMITED **Appellant**

- and –

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

Tribunal: The Hon Mr Justice Arnold

Sitting in public in London on 2 December 2011

Simon Taylor, instructed by Smith & Williamson, for the Appellant

Jonathan Hall, instructed by Howes Percival LLP, for the Respondents

MR JUSTICE ARNOLD:

Introduction

1. This is an appeal from a decision of the First-Tier Tribunal (Tax) (Tribunal Judge Howard M. Nowlan and Nicholas Dee) ("the Tribunal") dated 16 September 2010 [2010] UKFTT 439 (TC) dismissing the appeal of A One Distribution (UK) Ltd ("A One") against a decision of the Commissioners for Her Majesty's Revenue and Customs ("HMRC") to deny entitlement to the right to deduct input tax in the total sum of £300,237 in respect of four purchases of electronic goods in the period 08/06. The ground for that decision was that the input tax incurred by A One arose from transactions connected with the fraudulent evasion of VAT and that A One knew or should have known of that fact. In short, this is another case about MTIC (Missing Trader Intra Community) fraud.

2. The background may be summarised as follows. It is common ground that A One had traded honestly for many years and that its basic business was one of importing computer casings and other computer components, holding them in its substantial warehouse, and then supplying them to numerous customers in the UK. At the time in question it had 20 employees, and its total turnover was about £13 million. After a salesman called Michael Imms joined the company in 2004, A One considered whether to commence undertaking "back-to-back" trades in electronic components. Back-to-back deals all involved matched purchases and export sales on, or virtually on, the same day with the goods never coming into A One's custody but being held throughout by a freight forwarder. Tom Naughton, one of A One's directors, was initially opposed to the idea because he considered that the claimed returns were "too good to be true".

3. In about mid-2005, however, A One decided to embark on such trades in a small way. A One resolved that it would only trade with a supplier or customer that had been in business for at least two years and whose trade was in the electronics area. It would also send questionnaires or due diligence packs to potential suppliers and customers, requiring certain information about their trading, and representations that they had had no contact with MTIC trading, and no VAT problems. Initially, the level of exports was restricted by a monthly limit. This was likely to result in small transactions not occasioning requests for VAT repayments, since in A One's main trade, virtually all of its products were imported and sold in the domestic market, such that most of its gross sales attracted a liability to pay VAT.

4. A One did a number of back-to-back deals in the period between July 2005 and the end of May 2006. An MTIC Officer of HMRC, Margaret Pearson, visited the company to raise a number of questions in relation to the company's back-to-back trades and its due diligence procedures for the VAT period 02/06, and she cleared the claim for repayment of the VAT in relation to the export deals done in that period. She said that the company's due diligence procedures were reasonably satisfactory, albeit that she recommended that VAT numbers of trading partners should be verified through HMRC's Redhill VAT office ("Redhill"), rather than with the

national contact centre. Following this visit, A One made a few improvements to the due diligence forms, and it started making Redhill checks of the continuing validity of both suppliers' and customers' VAT numbers prior to undertaking transactions.

5. Subsequently, A One abandoned the policy of not exceeding the monthly limit. A One did four back-to-back deals in its VAT period 08/06. The first was a purchase of 2520 AMD64 CPUs from Plazadome Ltd ("Plazadome") and the sale of those CPUs to a Dutch company, Zaanstrait BV ("Zaanstrait") effected between 19 and 25 July 2006. The second, third and fourth deals were all purchases from Culmain Ltd ("Culmain"), and sales to an Austrian company, ASAP Trading GmbH ("ASAP"). Deal 2, effected on 1 August 2006, involved 4000 4bit iPods, Deal 3 on 3 August 4000 semi-conductor digital-to-analogue converters ("DACs") and Deal 4 on 8 August 3760 DACs.

6. These transactions resulted in actual requests for repayment of VAT. Eventually, HMRC disallowed all the relevant input tax in a letter sent to A One on 25 February 2008. A One appealed to the Tribunal against this decision. A One conceded during the proceedings that each of the four transactions in question was connected with fraudulent evasion of VAT. Thus the sole issues for the Tribunal were whether HMRC had proved that A One had actually known, or ought to have known, that that was the case at the time of entering into those transactions.

The Tribunal's decision

7. The Tribunal's decision is a lengthy and detailed one running to 211 numbered paragraphs and 59 single-spaced pages. It is structured as follows: paragraphs 1-17 are an introduction which includes a summary of the decision; paragraphs 18-25 mention a number of points which had fallen away in the light of the decision of the Court of Appeal in *Mobilx Ltd v Commissioners for Her Majesty's Revenue and Customs* [2010] EWCA Civ 517, [2010] STC 1436; paragraphs 26-30 describe the evidence before the Tribunal; paragraphs 31 set out the factual background under various headings; paragraph 134 summarises the law applied by the Tribunal; paragraph 135 summarises A One's contentions; paragraphs 136-138 summarise HMRC's contentions; paragraphs 139-198 set out the Tribunal's primary findings of fact under various headings; paragraphs 199-201 set out reasons for the Tribunal's conclusion that A One had actual knowledge that its transactions were connected to VAT fraud; paragraphs 202-209 set out the reasons for the Tribunal's conclusion that, even if A One did not have actual knowledge, it ought to have known that its transactions were connected to VAT fraud; and paragraphs 210-211 deal with costs and the right to appeal.

8. It is convenient to quote the Tribunal's own summary of what it perceived to be the main issues and its reasons for its decision:

> "11. We consider that there are three broad areas for us to consider in this case.

12. The first is whether we consider the due diligence to have been satisfactory, whether we consider that the Appellant should have followed up failures on the part of trading counter-parties to answer some questions or forward some documents, and whether the Appellant should have sought to verify some of the answers given. In short the dilemma here, and the dispute between the parties, was whether the Appellant was swapping 'due diligence' questionnaires just as a smoke-screen to seek to block a possible HMRC challenge of its transactions, and to claim that it had done all that it could reasonably do (as the Respondents contended); or whether its exercise was a genuine one, really to scrutinise matters and seek to uncover dubious trading partners (as the Appellant contended). In this context we accept that it may not be enough for us to conclude that the due diligence was inadequate, in that we should also consider what else, or whether anything else, could and would have been discovered if the Appellant had pursued due diligence more vigorously.

13. The second area for consideration relates to the way in which trading was done, with a view to ascertaining whether the terms of trade sustained the Appellant's contention that the trading was all done commercially, and with a view to minimising commercial risks, or whether some of the aspects of the trading were so extraordinary that they could only be explained by the feature that some at least of the trading counter-parties had to be dubious, at best, or knowingly connected with fraud, at worst.

14. The third area for consideration revolves around the fact that much of the contact between Michael Imms, the individual trader employed by the Appellant, and both counter-parties in the second, third and fourth deals was undertaken by way of MSN messages. This has enabled us to read 120 pages of text-type messages, giving the precise wording of these computer messages that the parties to the conversations wrote. Whilst in some respects these messages are supportive of the Appellant's case in that they show that some deals fell through, and that there was some real negotiation, they also reveal some materially less supportive exchanges. Naturally there was other contact between the parties by phone, mobile phone and conventional e-mail, so that we do not have the totality of the contemporary evidence of the exchanges. What we do have, however, is very significant.

…

16. Our decisions on the points canvassed in paragraphs 12 to 14 above are that:

- There is considerable evidence that the Appellant treated the due diligence exercise in the manner suggested by the Respondents.

- The failure of the Appellant to chase up occasions where counter-parties failed to respond, and the failure to seek to verify any information was not only unacceptable but was consistent with the attitude being that the exchange of due diligence information was done as the smoke-screen to fool and to block HMRC, rather than as a genuine exercise.

- It was unacceptable for the Appellant to indicate in its questionnaires that it would take up trade references and then not to do so as a matter of policy, and it was unacceptable to say that the Appellant had a policy of never visiting trade partners, as Notice 726 recommended, because "they might be good actors, and they might lie". If this were so, it seemed all the more obvious that when due diligence forms were completed, or rather part-completed, in a very sloppy manner, then if no effort was made to check a single piece of information, and it leapt off the page that some of the answers called for further enquiry, all the answers might indeed be a pack of lies.

- In the event many of the answers have been shown to be lies.

- Had the Appellant pursued some of its enquiries more diligently, it would have ascertained facts sufficient to put it on notice that it had been given dishonest answers to some of its questions, and it would have ended up with the gravest suspicion that if it entered into the transactions, those transactions would be connected to fraud.

- There are, as the Respondents suggested, many fairly extraordinary features to the terms of the four deals.

- In particular, we are unclear whether the Appellant had acquired title to goods when it purportedly sold them to its customer, at a time when the suppliers themselves had not been paid. At least in one case, the suppliers' Terms and Conditions (the only ones that we, or the parties, could read) made it clear that title did not pass to the Appellant until the supplier had been paid in full.

- The suppliers were paid as soon as the customer indicated to the Appellant that it had seen and accepted

the freight forwarders' report in relation to the goods, regardless of the fact that the goods would not have been seen by the customer at that point. If this indicated that the Appellant considered that from that point onwards it had no risk of complaint or action by the customer, should the goods not have met the invoice description, the customer appeared to take an astonishing risk. This was all the more obvious when the customer in three of the deals indicated that it thought that the freight forwarders were all fools who could not even count. If the customer might still complain, and one of the Appellant' witnesses suggested that the customer might complain, and that in this event, the price received would be refunded, and the supplier be sued in turn, the Appellant appeared to have a very material unprotected risk. This and other features of the trading were extraordinary.

- Even allowing for banter, there are a number of most damaging excerpts in the MSN messages.

- The artificial terms of trade and the damaging references in the MSN messages led us to the conclusion that the Appellant had actual knowledge of the connection to fraud. Were that wrong, the totality of the evidence certainly led us to conclude that the Appellant ought to have known that there could be no other explanation for its transactions than that they were connected to VAT fraud."

The law

9. In Joined Cases C439/04 and C440/04 *Kittel v Etat Belge* [2006] ECR I-616 at [61] the Court of Justice of the European Communities (Third Chamber) held that:

> " … 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 VAT, it is for the national court to refuse that taxable person entitlement to the right to deduct."

10. In *Mobilx v HMRC*, the Court of Appeal had to consider the proper interpretation and application of the ECJ's decision in *Kittel*. The Tribunal summarised the guidance given by the Court of Appeal in its decision at [134] as follows:

- "The Respondents have the burden of proof, to the civil standard of the balance of probabilities,

- It is for the Respondents to show, in relation to the third of the Kittel tests, that the Appellant either knew or ought to have known that its four transactions were connected to VAT (or indeed other) fraud.

- We are required, before we can reach that conclusion, to decide that the Appellant knew or should have known, on making reasonable enquiries, that its transactions **were** connected to fraud, and not that it was merely **more likely than not** that they were so connected.

- We can consider that the relevant test has been satisfied by the Respondents if we consider that the Appellant knew or ought to have known that there could be no other reasonable explanation for its transactions than that they were connected to fraud.

- Finally in considering the case we should not dwell excessively on the due diligence, and whether or not that was necessarily satisfactory, and on the issue of what **would have been discovered** had further due diligence been undertaken, but we should consider all the circumstances, in the round."

11. No criticism of this direction has been made by A One on the present appeal.

The nature of an appeal from the First-Tier Tribunal to this Tribunal

12. Section 11(1) of the Tribunals, Courts and Enforcement Act 2007 provides for a right of appeal to the Upper Tribunal "on any point of law arising from a decision made by the first tier tribunal other than an excluded decision". It was common ground before me that the principles established under section 11(1) of the Tribunals and Inquiries Act 1992 and its predecessors were equally applicable under section 11(1) of the 2007 Act.

13. In *Edwards v Bairstow* [1956] AC 14 Viscount Simonds said at 29:

> "… though it is a pure finding of fact, it may be set aside on grounds which have been stated in various ways but are, I think, fairly summarised by saying that the court should take that course if it appears that the commissioners have acted without any evidence or upon a view of the facts which could not reasonably be entertained."

Lord Radcliffe said at 36:

> "If the case contains anything ex facie which is bad law and which bears upon the determination, it is obviously, erroneous in point of law. But, without any such misconception appearing ex facie, it may be that the facts found are such that no person acting judicially and properly instructed as to the

> relevant law could have come to the determination under appeal. In those circumstances, too, the court must intervene."

14. In *Georgiou v Customs and Excise Commissioners* [1996] STC 463 Evans LJ, with whom Saville and Morritt LJJ (as they then were) agreed, said at 476:

> "There is a well-recognised need for caution in permitting challenges to findings of fact on the ground that they raise this kind of question of law. … It is all too easy for a so-called question of law to become no more than a disguised attack on findings of fact which must be accepted by the courts. As this case demonstrates, it is all too easy for the appeals procedure to the High Court to be abused in this way. Secondly, the nature of the factual inquiry which an appellate court can and does undertake in a proper case is essentially different from the decision-making process which is undertaken by the tribunal of fact. The question is not, has the party upon whom rests the burden of proof established on the balance of probabilities the facts upon which he relies, but was there evidence before the tribunal which was sufficient to support the finding which it made? In other words, was the finding one which the tribunal was entitled to make? Clearly, if there was no evidence, or the evidence was to the contrary effect, the tribunal was not so entitled.
>
> It follows, in my judgment, that for a question of law to arise in the circumstances, the appellant must first identify the finding which is challenged; secondly, show that it is significant in relation to the conclusion; thirdly, identify the evidence, if any, which was relevant to that finding; and fourthly, show that that finding, on the basis of that evidence, was one which the tribunal was not entitled to make. What is not permitted, in my view, is a roving selection of the evidence coupled with a general assertion that the tribunal's conclusion was against the weight of the evidence and was therefore wrong."

15. In *Procter & Gamble UK v Revenue and Customs Commissioners* [2009] EWCA Civ 407, [2009] STC 1990 Jacob LJ, with whom Mummery and Toulson LJJ agreed, said at [11]:

> "It is also important to bear in mind that this case is concerned with an appeal from a specialist Tribunal. Particular deference is to be given to such Tribunals for Parliament has entrusted them, with all their specialist experience, to be the primary decision maker, see per Baroness Hale in *AH (Sudan) v Secretary of State for the Home Department* [2007] UKHL 49, [2008] 1 AC 678 at [30] …."

16. What Baroness Hale said in *AH (Sudan)*, which has since been approved by Sir John Dyson SCJ giving the judgment of the Supreme Court in *MA*

(Somalia) v Secretary of State for the Home Department [2007] UKSC 49, [2011] 2 All ER 65 at [43], was this:

> " … This is an expert tribunal charged with administering a complex area of law in challenging circumstances. To paraphrase a view I have expressed about such expert tribunals in another context, the ordinary courts should approach appeals from them with an appropriate degree of caution; it is probable that in understanding and applying the law in their specialised field the tribunal will have got it right: see *Cooke v Secretary of State for Social Security* [2002] 3 All ER 279, para 16. They and they alone are the judges of the facts. It is not enough that their decision on those facts may seem harsh to people who have not heard and read the evidence and arguments which they have heard and read. Their decisions should be respected unless it is quite clear that they have misdirected themselves in law. Appellate courts should not rush to find such misdirections simply because they might have reached a different conclusion on the facts or expressed themselves differently. … "

The appeal

17. A One challenges the decision of the Tribunal on six grounds. Before considering those, it is convenient first to deal with two general points.

18. First, counsel for A One sought to place reliance upon comments made by Judge Nowlan after the Tribunal issued its decision in an email dated 11 November 2010. The circumstances in which the email was sent are as follows. On 18 October 2010 Andy Bugden of Zaanstrait, who was not called as a witness at the hearing before the Tribunal, sent an email to the Tribunal Services complaining that the Tribunal's decision contained a racist comment. The complaint was primarily based on the fact that the Tribunal described Mr Bugden in its decision at [79] and [95] as "an Irishman", but in addition Mr Bugden was critical of a number of other passages in the decision concerning himself and Zaanstrait. Mr Bugden's email was forwarded to Judge Nowlan, who saw it on 10 November 2010. On 11 November 2010 Judge Nowlan emailed a detailed response to the complaint to Mr Bugden, Mr Dee, the Equality and Human Rights Commission, the Tribunals Service, HMRC and HMRC's solicitors and counsel (but not A One or its solicitors and counsel). I note that Judge Nowlan stated in his response that he was "extremely annoyed" by the complaint, which he described as "ludicrous". On 23 November 2011 A One's representatives were provided with copies of Mr Bugden's complaint and Judge Nowlan's response.

19. It is important to note that A One does not suggest that Judge Nowlan's email provides grounds for any complaint of apparent, still less actual, bias on the part of Judge Nowlan. Rather, counsel for A One sought to rely upon certain passages in Judge Nowlan's email as supporting some of A One's grounds of appeal against the Tribunal's decision. In my judgment, however, the email is not admissible for this purpose. In the absence of any complaint of apparent

bias, the Tribunal's reasoning falls to be assessed on the basis of what the Tribunal said in its decision, not on the basis of what one member of the Tribunal said extra-judicially, possibly in some heat as a result of what he regarded as an unjustified complaint of racial prejudice, nearly two months later.

20. Second, counsel for HMRC submitted that in substance A One's appeal was an attempt to overturn the Tribunal's findings of fact, but that there was ample evidence before the Tribunal to entitle it to make those findings of fact, and in particular its finding that A One should have known that the transactions were connected with VAT fraud. In this regard, he pointed out that the Tribunal's decision was given after an eight day hearing at which seven witnesses gave oral evidence, including Mr Imms and two other witnesses on behalf of A One. The Tribunal concluded that Mr Imms' evidence was "less than candid" (decision at [30]). It also commented adversely upon the absence of any evidence from Vijay Kerai, A One's purchasing manager, who was the only one from A One who had actually met Mr Bugden and Wolfgang Seher of ASAP (decision at [177], [200]). Nor did A One adduce any evidence from Mr Bugden or Mr Seher, let alone representatives of Plazadome or Culmain. Importantly, the Tribunal placed considerable weight upon a large quality of MSN messages disclosed by A One relatively late in the proceedings, numerous extracts from which it quoted in the decision at [119] and [123]-[133] and which it regarded as strongly supportive of HMRC's case. I agree that in these circumstances A One faces a high hurdle to overcome. Nevertheless, I shall consider each of the grounds of appeal relied upon.

Ground 1

21. A One's first ground of appeal is that the Tribunal reached conclusions that were influenced by the Tribunal's own theories or preconceptions rather than being based on the evidence before it. In this regard, A One complains about three passages in the decision.

22. The first passage is at [150]-[154], headed "The simple maths in relation to honest and dishonest import and export transactions". In this passage, the Tribunal considered the implications of the fact that, as was common ground, the goods the subject of the four transactions in question had been imported into the United Kingdom before A One exported them. Having considered some hypothetical figures, the Tribunal stated at [150]:

> "What is staggeringly obvious from these two simple examples is that the feature of bringing goods into the UK and of then exporting them entirely honestly is something that generates no potential profits. … It is only if there is VAT fraud, and the exporter recovers the VAT, that there is any inherent profit in exporting goods that have been imported."

23. Counsel for A One submitted that this was a theory of the Tribunal's which was not based on the evidence before it and that it was wrong, because there were a number of reasons why goods could be legitimately and profitably exported from the UK despite having previously been imported into the UK. I

do not accept this submission. As counsel for HMRC submitted, the Tribunal was entitled to consider whether A One could have thought that the transactions in question were legitimate, and to that end to consider what legitimate commercial explanation for the transactions there could be. This is a matter which HMRC's Notice 726 advises traders to consider, and one that was explored in the evidence before the Tribunal. I accept that, considered in isolation, the two sentences I have quoted appear rather sweeping, but they have to be read in context. In context, it is clear that the Tribunal was not intending to say that there was no possibility at all of a legitimate commercial explanation for the transactions, as can be seen from the next passage complained about.

24. The second passage is at [155]-[158], headed "Some observations about supposed grey trading". In the course of this passage the Tribunal stated at [156]:

> "… there was no clear evidence about the existence of any honest grey market in iPods, CPUs or [DACs]."

25. Counsel for A One submitted that this again demonstrated a preconception on the Tribunal that there could not be a honest grey market for the goods in question, and that the Tribunal had wrongly placed the burden on A One to prove the existence of an honest grey market whereas it was HMRC's burden to prove the absence of one. I do not accept this submission, which is again based on taking the quoted passage out of context. The Tribunal's conclusion in this passage of the decision at [158] was as follows (emphasis added):

> "We appreciate that our decision should be based on evidence and findings of fact but we do also note that much of the assumption behind the Appellant's trading model, and the case that the Appellant has advanced, is that there was a virtual daily supply of product to be acquired in the honest grey market, all of which might be exported at a significant profit, and without risk, effort or any remote contribution of value into the trading cycle. The proposition is that by simply accessing a web-site, and despatching e-mails to unknown entities, it was quite easy to generate risk-free, matched, and profitable domestic purchases and export sales. Whilst there was no evidence to dispute this expectation, in reality it appears to be sufficiently improbable for it to be incumbent on the Appellant to have conducted its due diligence very genuinely in order to avoid being tainted with MTIC fraud that was known and appreciated to be a major risk in these product areas. *We are not saying that the Appellant has the burden of proof in illustrating the extent of the grey market, and it would have been for the Respondents to demonstrate the low level of grey market trading, had they wished to do so. We are simply saying that the obvious risks of MTIC fraud, and the equally obvious absence of any clear rationale for large volumes of honest grey market trading should, quite apart from recommendations from HMRC, have led the Appellant to pursue its due diligence very*

> *genuinely*. We will now address the issue of whether the Appellant did indeed approach the due diligence exercise genuinely."

Thus the Tribunal was explicit that it recognised that A One did not bear the burden of proving the existence of a legitimate grey market. All it was saying was that the obvious risk of fraud, and the equally obvious absence of any clear commercial rationale for profitable back-to-back trades of the kind in question, were relevant considerations when assessing A One's state of mind.

26. The third passage complained of is at [184]-[185], in which the Tribunal stated:

> "184. The extracts quoted at paragraph 123 above make it perfectly clear that the Appellant is being inserted into transactions between Culmain and ASAP because Culmain has run out of VAT (possibly this meant that it had hit the limit of its taxable supplies such that further exports would require repayment claims to be made, or possibly it was just worried about not receiving VAT repayments following problems with its 03/06 return), and because the Appellant did have 'VAT to play with'. There is considerable evidence that certainly in the early transactions the Appellant was seeking to limit back-to-back transactions so that it would merely reduce its output liability, rather than have to make repayment claims. By the period that falls after the four deals in this case, Michael Imms was talking quite openly, in the passages quoted in paragraphs 129 and 130 above, about not worrying the nervous FD, and about keeping below the HMRC 'radar screen' by limiting its export deals to the level of its substantial standard rated supplies.
>
> 185. We find both of these features highly suspicious. If Culmain's transactions were honest, it seems difficult to suppose that it would encounter serious delays or difficulties in making VAT repayment claims. The Appellant knew that Culmain passed over £42,260 of profit to the Appellant in Deals 2, 3 and 4, because that was the profit that the Appellant stood to make if it recovered the VAT. To forego that level of profit merely because of a reluctance to make repayment claims should have seemed very odd to the Appellant, and to indicate that Culmain's concerns were geared not to a short-term cash flow deficit but to a rather more serious concern. Since in any event, it was perfectly obvious that the Appellant itself attached very considerable significance to the ability to export product without having to make repayment claims, these two factors are strongly suggestive that the Appellant actually knew that the relevant transactions would be likely to be challenged if undertaken by Culmain, but might avoid challenge if they could be hidden."

27. Counsel for A One submitted that this reasoning was founded upon an unsupported theory of the Tribunal to the effect that Culmain would not have experienced delays in receiving VAT reclaims if its claims were honest. I do not accept this submission. The question why A One should have been inserted between Culmain and ASAP was explored in the evidence before the Tribunal. In my judgment the Tribunal was entitled on the evidence before it to take the view that it did.

Ground 2

28. A One's second ground of appeal is that the Tribunal took the wrong approach to assessing its due diligence, attached too much weight to the issue and fell into the error of speculating about what might have been discovered, rather than finding what would have been discovered, had better due diligence been undertaken. In essence, counsel for A One submitted that, notwithstanding The Tribunal's correct direction to itself on the law at [134], examination of the decision showed that the Tribunal had fallen into the same trap as the tribunal in the *Blue Sphere* case: see *Mobilx v HMRC* at [70], [75] and [82].

29. I do not accept this submission. As the Tribunal made clear at [12] and elsewhere in the decision, it considered A One's due diligence to see whether it was a genuine attempt to avoid becoming involved in transactions which were connected with VAT fraud or whether it was a "smoke-screen". The Tribunal concluded that it was the latter (decision at [16], [173], [199] and [203]-[204]). In my judgment this was a conclusion it was entitled to reach on the evidence before it. At [159]-[160] the Tribunal considered the MSN messages, which showed "the formalistic and often amused and contemptuous attitude taken by the parties to due diligence". At [161]-[167] the Tribunal considered the standard of the responses received by A One to its due diligence questionnaires, concluding for the reasons it explained that they could "only … be described as appalling". At [168]-[173] the Tribunal considered the evidence of A One's witness Craig Bentham that it was A One's policy never to follow the strong suggestions in the HMRC leaflets of going to meet potential trading partners at their offices, never to take up trade references and never to make further requests for information or documents that had been ignored in the initial responses. The Tribunal was understandably critical of this policy. It also accepted counsel for HMRC's submission that "that the information that the Appellant in fact obtained was either absolutely useless or it was disturbing, and it called for further enquiries to be made". Accordingly, the Tribunal concluded that A One was not genuinely trying to avoid being involved in transactions which were connected with VAT fraud. In my judgment that was a conclusion the Tribunal was entitled to reach on the evidence before it.

30. Furthermore, I do not accept that the Tribunal's consideration of due diligence deflected it from asking and answering the essential questions of whether A One knew, or should have known, that the particular transactions in issue were connected with VAT fraud. The Tribunal squarely addressed and answered those questions in its decision. As can be seen from summary at [16] quoted above, and in more detail at [199]-[208], the Tribunal's assessment of A One's

due diligence was just one of the factors it relied on in reaching its conclusion on those questions.

31. Finally, I do not accept that the Tribunal fell into the trap of speculating about what might have been found if A One had carried out due diligence properly, rather than finding what would have been ascertained by A One. In the first place, the Tribunal's reasoning was that the fact that A One's due diligence was a smoke screen was one of the matters it relied upon as justifying the inference that A One was turning a blind eye to the nature of the transactions. Secondly, when it addressed the consequence of the inadequate due diligence, the Tribunal expressed itself in terms of what A One "would have ascertained": see the decision at [16] (quoted above), the heading to [174]-177] and [205].

32. Counsel for A One sought to support the submission by reference to some of the language used by the Tribunal at [174]-[177], but I do not agree that this shows that the Tribunal adopted the wrong approach. For example, the Tribunal said at [174]:

> "In the case of Culmain, one can only imagine that if the Appellant had visited Culmain's two rooms and asked to see its accounts, the Appellant would either have been met with a plainly unacceptable refusal, or would have seen that the turnover was 15 times higher than the declared £10 million."

Counsel for A One criticised the words "one can only imagine that", but the sentence would have the same meaning if those words were omitted.

33. Counsel for A One also made a series of detailed criticisms of the Tribunal's findings in relation to due diligence. I do not propose to go through these individually. I am satisfied that in each case the Tribunal's finding was one that was open to it on the evidence before it.

Ground 3

34. A One's third ground of appeal is that the Tribunal wrongly reached conclusions as to its knowledge based on evidence that post-dated the transactions in question. As counsel for A One accepted, however, the Court of Appeal in *Moblix* at [83] approved the statement of Christopher Clarke J in *Red12 Trading Ltd v Commissioners for Her Majesty's Revenue and Customs* [2009] EWHC 2563 (Ch), [2010] STC 589 at [109] to the effect that evidence that post-dated the transactions was admissible on this question. Only if the evidence in question was incapable of shedding light on A One's state of mind at the relevant dates would the Tribunal have made an error in taking it in account. That being so, I can deal with this point quite shortly.

35. A One's first complaint under this head relates to a passage in the Tribunal's decision at [178]-[181] in which the Tribunal considered A One's attempt to open an account with First Curacao International Bank (FCIB) and A One's evidence as to why this had not occurred. This was something that A One was trying to do, and telling Culmain and ASAP that it was doing, at the time of

Deals 2, 3 and 4: see the decision at [119]. It appears that one reason for this was that the counterparties, or some of them, banked with FCIB. Counsel for A One criticised the following statement by the Tribunal at [180]:

> "We find it difficult to see, however, why genuine traders in the grey market would consider clubbing together and agreeing all to place their banking with one bank, and indeed a slightly odd off-shore bank."

36. Counsel submitted that this showed that the Tribunal had proceeded on the basis that at the material time it was known that FCIB was not a reputable bank, whereas that only became public knowledge later. I do not accept that submission. FCIB was off-shore. While it is not clear what the Tribunal meant by "slightly odd", it did not say that FCIB was disreputable. Furthermore, the Tribunal went on at [181] to say that "the far more serious point" was that this was further evidence of A One's preparedness to breach its own rules for ensuring that it did not became involved in transactions which were connected to fraud.

37. A One's second complaint was that the Tribunal relied upon a number of MSN messages which post-dated the transactions. As can be seen from the decision at [159], however, the Tribunal recognised that it should only rely upon such evidence if satisfied that it cast light on A One's conduct and state of mind at the time. The Tribunal was evidently satisfied that all of the MSN messages in question did so, and in my judgment it was entitled to take that view.

Ground 4

38. A One's fourth ground of appeal is that the Tribunal made findings adverse to A One without giving its witnesses a proper opportunity to deal with the allegations in question. There is no doubt that, if well-founded, this would represent an error of law on the part of the Tribunal: see *Markem Corp v Zipher Ltd* [2005] EWCA Civ 267, [2005] RPC 31 at [57]-[60]. In his skeleton argument counsel for A One identified a number of matters which he suggested had been not put to A One's witnesses, but counsel for HMRC was able to show by reference to the transcript that each of the matters had been put. Counsel for A One also complained that the Tribunal had undertaken its own machine-assisted translation of a document in Dutch, but as can be seen from the decision at [166] the result was a finding in favour of A One. Thus there is nothing in this ground of appeal.

Ground 5

39. A One's fifth ground of appeal is that the Tribunal had erred in its approach to both the burden and standard of proof. So far as burden is proof is concerned, counsel for A One relied on the way the Tribunal dealt with the grey market and due diligence. I have already dealt with those issues above. As to standard of proof, counsel for A One submitted that the Tribunal ought to have had regard to the inherent improbability of A One knowingly engaging in transactions which were connected with VAT fraud having regard to its

previous track record. I do not accept this submission. First, the House of Lords and the Supreme Court have held that there is only one civil standard of proof, namely proof on the balance of probabilities, and that there is no necessary connection between the seriousness of an allegation and the improbability that it has taken place: see *In re B* [2008] UKHL 35, [2009] AC 11 at [15] and *Re S-B (Children) (Care Proceedings: Standard of Proof)* [2009] UKSC 17, [2010] 1 AC 678 at [34]. Secondly, the Tribunal expressly recognised A One's previous good trading history (see the decision at [1] and [31]-[32]). Thirdly, as the Tribunal also expressly recognised, A One's venture into back-to-back trading was a relatively new departure (decision at [3]-[5], [33]-[40]) which A One knew was quite different to its established business in terms of its exposure to the risk of VAT fraud (decision at [3], [50], [142]-[144]). Thirdly, even if I were to accept that A One's previous trading history meant that it was unlikely to have knowingly engaged in transactions which were connected with VAT fraud, that would not affect the Tribunal's conclusion that A One ought to have known that the transactions were connected with VAT fraud.

Ground 6

40. A One's sixth ground of appeal is that the Tribunal decided the appeal by reference to a case which HMRC had not pleaded. HMRC's statement of case alleged that

> "27.1 the transactions formed part of transaction chains in which one or more the transaction were 'connected with fraudulent evasion of VAT'; and
>
> 27.2 the Appellant 'knew or should have known' of that fact."

As noted above, there is no dispute as to the allegation in paragraph 27.1. In support of the allegation in paragraph 27.2, HMRC relied upon a series of facts and matters pleaded in paragraphs 22-26 of the statement of case.

41. Counsel for A One pointed out that Annex B to HMRC's statement of case identified the defaulters in relation to the four transactions as Capitazone Ltd in relation to deal 1 and E-Management Solutions Europe Ltd in relation to deals 2, 3 and 4. It is common ground that the reference to Capitazone was erroneous and that in fact the defaulter was ET Phones Ltd, but counsel for A One took no point on that. Instead, he argued that, whereas the pleaded fraud was that of the defaulters, the Tribunal had made findings of fraudulent activity on the part of Culmain, Plazadome, Zaanstrait and ASAP which was not pleaded.

42. I do not accept this argument. As Briggs J held in *Megtian Ltd v Commissioners for Her Majesty's Revenue and Customs* [2010] EWHC 18 (Ch), [2010] STC 840:

> "37. In my judgment, there are likely to be many cases in which a participant in a sophisticated fraud is shown to have actual or blind-eye knowledge that the transaction in which he is

> participating is connected with that fraud, without knowing, for example, whether his chain is a clean or dirty chain, whether contra-trading is necessarily involved at all, or whether the fraud has at its heart merely a dishonest intention to abscond without paying tax, or that intention plus one or more multifarious means of achieving a cover-up while the absconding takes place.
>
> 38. Similarly, I consider that there are likely to be many cases in which facts about the transaction known to the broker are sufficient to enable it to be said that the broker ought to have known that his transaction was connected with a tax fraud, without it having to be, or even being possible for it to be, demonstrated precisely which aspects of a sophisticated multifaceted fraud he would have discovered, had he made reasonable inquiries. In my judgment, sophisticated frauds in the real world are not invariably susceptible, as a matter of law, to being carved up into self-contained boxes even though, on the facts of particular cases, including *Livewire,* that may be an appropriate basis for analysis."

43. In the present case, as I have already observed, A One conceded that the transactions were in fact connected with fraudulent evasion of VAT. The only issues were whether A One knew, or should have known, that that was the case. HMRC's statement clearly alleged that A One knew, alternatively should have known, this. HMRC did not allege that A One knew the identities of the defaulters, still less that they had or would default. As counsel for HMRC made clear when he opened the case to the Tribunal, and cited the passage from *Megtian* quoted above, HMRC's case was that there were a series of facts and matters which justified the inference that A One knew that it was engaging in transactions which were connected with VAT fraud, albeit not necessarily the details of that fraud, alternatively that it should have known. As the statement of case made clear, some of these facts and matters concerned the parties whom A One was trading with, namely Plazadome, Culmain, Zaanstraint and ASAP.

44. I do not read the Tribunal's decision as making positive findings that any of Plazadome, Culmain, Zaanstraint and ASAP were themselves engaged in VAT fraud. Rather, I read the Tribunal's decision as finding that their behaviour was such as to arouse severe suspicion for reasons the Tribunal explained at some length, and that that was amongst the factors on which the Tribunal in making its findings of actual alternatively constructive knowledge on the part of the A One that the transactions in question were *connected* with VAT fraud. In my judgment that does not amount to a departure from HMRC's pleaded case, nor is it otherwise procedurally unfair to A One.

Conclusion

45. For these reasons the appeal is dismissed.

Mr Justice Arnold

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