[2018] UKFTT 532 (TC)

TC06702

Appeal number: TC/2015/02873

VALUE ADDED TAX – Wholesale scrap metal transactions undertaken by Appellant building company - Denial of input tax - Was there a tax loss? - Yes - Did that loss result from fraudulent evasion? - Yes - Were the transactions subject to the appeal connected with that evasion? - Yes - Did the Appellant know or should it have known that the transactions were connected with fraud? - Yes - Appeal dismissed

FIRST-TIER TRIBUNAL
TAX CHAMBER

MD CONSTRUCTION (BRADFORD) LIMITED

Appellant

- and -

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

TRIBUNAL: JUDGE CHRISTOPHER MCNALL
MISS SUSAN STOTT

Sitting in public at Phoenix House, Rushton Avenue, Bradford BD3 7BH on 5-7 March 2018

Mr J Christopher Yewdall FCA, an Accountant, of Spenser Wilson Ltd, Accountants and Business Advisers, for the Appellant

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

DECISION

1. This appeal was brought by MD Construction (Bradford) Limited ('**the Company'**) on 20 April 2015. It challenges HMRC's decision dated 9 December 2014 (upheld at departmental review on 23 March 2015), following extended verification, to deny the Company's claim for input tax amounting to £70,993.33 in relation to the period 1 June 2013 to 31 August 2013 (i.e., VAT quarter 08/13) and to amend the Company's VAT return accordingly.

2. The VAT owed was adjusted to £45,240 owing to an inaccuracy in the return for the 08/13 period. In a summary decision released on 19 February 2016, the Tribunal (Judge Richard Thomas) decided that the requirement to pay £45,240 would cause the Company to suffer hardship, and so decided that the appeal could be entertained by the Tribunal without the payment of that sum.

3. The Appellant is a legal person. It operates through natural persons, namely its directors, Mr Michael Dunbar and Mrs Keeley Dunbar, who are a married couple. There are no other directors. The Appellant has about 23 employees. At the time of the wholesale scrap metal deals in question, the Company had been trading in the construction industry – as a house-builder and commercial contractor - for over 20 years, and had been registered for VAT since 1997.

4. The denied claim for input tax relates to a series of individually identified transactions (**'the Deals'**), each involving the wholesale purchase and sale of non-ferrous (copper) scrap metal.

5. The details of the Deals are as follows:

Deal	**Purchase Invoice Date**	**Quantity (Kg)**	**Supplier to the Appellant**	**Customer from the Appellant**	**Net Invoice £**	**VAT £**
1	14.6.13	23,469	Parr Metals UK Ltd	Inter Trade Global	89,299	17,859
2	26.6.13	47,000	Parr Metals UK Ltd	Douglas Waste Management	175,780	35,156
3	16.7.13	23,545	Parr Metals UK Ltd	Douglas Waste Management	89,980	17,978

6. The Company had only ever undertaken three scrap metal transactions before Deal 1. They are referred to in this Decision as Deals A, B, and C. The earliest, Deal A, took place on 28 March 2013 and was a purchase by the Company from Douglas Waste Management Ltd with a sale to Manholme Associates trading as Yorkshire Metal Recycling Ltd. Deals B and C both took place on 17 May 2013. Both were purchases by the Company from GTC Young Ltd and were sales by the Company to Morley Waste Traders.

7. Deals A, B and C (i) all fell into the VAT period (05/13) immediately preceding the VAT period which is under scrutiny in this appeal, (ii) were not subject to extended verification, and (iii) were not subject to any denial of input tax. Indeed, in its Skeleton Argument, HMRC accepts that it has been unable to trace Deal A definitively to a tax loss.

8. Nonetheless, it seems to us that the circumstances of Deals A, B, and C do have some relevance for the purposes of this decision. They provide an important part of the Company's overall trading picture, and it would be artificial to ignore them, especially given two particularly prominent features: (i) they were all 'back-to-back' purchases and sales; and (ii) they involved Mr Chris Howard, who played an important role in introducing the Appellant to the scrap metal business, and in bringing about those deals. We shall return to both these features below.

The Law

9. The right to deduct input tax is derived from Articles 167 and 168 of Council Directive 2006/112/EC of 28 November 2006 which has been implemented into UK domestic law by sections 24-26 *Value Added Tax Act 1994* and Regulation 29 of *The VAT Regulations 1995* (SI 1995/2518).

10. In brief terms, if a trader has incurred input tax which is properly allowable, he is entitled to set it against his output tax liability (or to receive a repayment if the input tax credit due to him exceeds that liability). Evidence is required in support of a claim: see Article 18 of the Sixth Directive and Regulation 29(2) of the 1995 Regulations. Traders are required, amongst other things, to hold or provide any document required by Regulation 13 of the 1995 Regulations or such other evidence to support the claim as HMRC may direct.

11. An exception to the above entitlement was identified by the European Court of Justice in the joined cases *Axel Kittel v Belgium; Belgium v Recolta Recycling SPRL* (C-439/04 and C-440/04) [2006] ECR I-6161. In a judgment on references for a preliminary ruling, the ECJ articulated the legal basis and circumstances in which the right to deduct may be lawfully denied by the taxation authorities:

> "51 […] it is apparent that traders who take every precaution which could reasonably be required of them to ensure that their transactions are not connected with fraud, be it the fraudulent evasion of VAT or other fraud, must be able to rely on the legality of those transactions without the risk of losing the right to deduct the input VAT [...]
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> 52. It follows that, where a recipient of a supply of goods is a taxable person who did not and could not know that the transaction concerned was connected with a fraud committed by the seller, Article 17 of the Sixth Directive must be interpreted as meaning that it precludes a rule of national law under which the fact that the contract of sale is void, by reason of a civil law provision which renders that contract incurably void as contrary to public policy for unlawful basis of the contract attributable to the seller,

causes that taxable person to lose the right to deduct the VAT he has paid. It is irrelevant in this respect whether the fact that the contract is void is due to fraudulent evasion of VAT or to other fraud.

53. By contrast, the objective criteria which form the basis of the concepts of 'supply of goods effected by a taxable person acting as such' and 'economic activity' are not met where tax is evaded by the taxable person himself [...]

54. As the Court has already observed, preventing tax evasion, avoidance and abuse is an objective recognised and encouraged by the Sixth Directive...Community law cannot be relied on for abusive or fraudulent ends [...]

55. Where the tax authorities find that the right to deduct has been exercised fraudulently, they are permitted to claim repayment of the deducted sums retroactively … It is a matter for the national court to refuse to allow the right to deduct where it is established, on the basis of objective evidence, that that right is being relied on for fraudulent ends [...]

56. In the same way, a taxable person who knew or should have known that, by his purchase, he was taking part in a transaction connected with fraudulent evasion of VAT must, for the purposes of the Sixth Directive, be regarded as a participant in that fraud, irrespective of whether or not he profited by the resale of the goods.

57. That is because in such a situation the taxable person aids the perpetrators of the fraud and becomes their accomplice.

58. In addition, such an interpretation, by making it more difficult to carry out fraudulent transactions, is apt to prevent them.

59. Therefore, it is for the referring court to refuse entitlement to the right to deduct where it is ascertained, having regard to objective factors, that the taxable person knew or should have known that, by his purchase, he was participating in a transaction connected with fraudulent evasion of VAT, and to do so even where the transaction in question meets the objective criteria which form the basis of the concepts of ‘supply of goods effected by a taxable person acting as such’ and ‘economic activity’.

[...]

61 …where it is ascertained, having regard to objective factors, that the supply is to a taxable person who knew or should have known that, by his purchase, he was participating in a transaction connected with fraudulent evasion of VAT, it is for the national court to refuse that taxable person entitlement to the right to deduct.”

12. These principles - often referred to, in shorthand, as the 'Kittel' principles - were amplified and clarified, in a domestic context, by the Court of Appeal in *Mobilx Ltd (in administration) v HMRC [2010] EWCA Civ 517*. Moses LJ (with whom Carnwath LJ, as he then was, and Sir John Chadwick agreed) remarked:

> "[30] ... the Court made clear that the reason why fraud vitiates a transaction is not because it makes the transaction unlawful but rather because where a person commits fraud he will not be able to establish that the objective criteria which determine the scope of VAT and the right to deduct have been met...
>
> [...]
>
> [41] ...*Kittel* did represent a development of the law because it enlarged the category of participants to those who themselves had no intention of committing fraud, but who, by virtue of the fact that they knew or should have known that the transaction was connected with fraud, were to be treated as participants. Once such traders were treated as participants their transactions did not meet the objective criteria determining the scope of the right to deduct."

13. On the issue of knowledge, the Court of Appeal gave the following guidance:

> "MEANING OF *'SHOULD HAVE KNOWN'*
>
> [52] If a taxpayer has the means at his disposal of knowing that by his purchase he is participating in a transaction connected with fraudulent evasion of VAT he loses his right to deduct, not as a penalty for negligence, but because the objective criteria for the scope of that right are not met. It profits nothing to contend that, in domestic law, complicity in fraud denotes a more culpable state of mind than carelessness, in the light of the principle in Kittel. A trader who fails to deploy means of knowledge available to him does not satisfy the objective criteria which must be met before his right to deduct arises.
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> [...]
>
> EXTENT OF KNOWLEDGE
>
> [56] It must be remembered that the approach of the court in *Kittel* was to enlarge the category of participants. A trader who should have known that he was running the risk that by his purchase he might be taking part in a transaction connected with fraudulent evasion of VAT, cannot be regarded as a participant in that fraud. The highest it could be put is that he was running the risk that he might be a participant. That is not the approach of the Court in *Kittel*, nor is it the language it used. In those circumstances, I am of the view that it must be established that the trader knew or should have known that by his purchase he was taking part in such a transaction, as the Chancellor concluded in his judgment in *Blue Sphere Global*:-

"The relevant knowledge is that Blue Sphere Global ought to have known by its purchases it was participating in transactions which were connected with a fraudulent evasion of VAT; that such transactions might be so connected is not enough." (Para 5).

[57] HMRC object that the principle should not be restricted to those cases were a trader has deliberately refrained from asking questions lest his suspicions should be confirmed. This has been described as a category of case which is so close to actual knowledge that the person is treated as having received the information which he deliberately sought to avoid...

[58] As I have endeavoured to emphasise, the essence of the approach of the court in *Kittel* was to provide a means of depriving those who participate in a transaction connected with fraudulent evasion of VAT by extending the category of participants and, thus, of those whose transactions do not meet the objective criteria which determine the scope of the right to deduct. The court preserved the principle of legal certainty; it did not trump it.

[59] The test in *Kittel* is simple and should not be over-refined. It embraces not only those who know of the connection but those who "should have known". Thus it includes those who should have known from the circumstances which surround their transactions that they were connected to fraudulent evasion. If a trader should have known that the only reasonable explanation for the transaction in which he was involved was that it was connected with fraud and if it turns out that the transaction was connected with fraudulent evasion of VAT then he should have known of that fact. He may properly be regarded as a participant for the reasons explained in *Kittel.*

[60] The true principle to be derived from *Kittel* does not extend to circumstances in which a taxable person should have known that by his purchase it was more likely than not that his transaction was connected with fraudulent evasion. But a trader may be regarded as a participant where he should have known that the only reasonable explanation for the circumstances in which his purchase took place was that it was a transaction connected with such fraudulent evasion."

14. The Court of Appeal referred with approval to the judgment of the then Chancellor, Sir Andrew Morritt, in *Blue Sphere Global Ltd v HMRC* [2009] EWHC 1150 (Ch) where, in relation to the issue of 'connection' with fraud, the judge remarked (see Paras. [42]-[45]):

"…The nature of any particular necessary connection depends on its context, for example electrical, familial, physical or logical. The relevant context in this case is the scheme for charging and recovering VAT in the member states of the EU. The process of off-setting inputs against outputs in a particular period and accounting for the difference to the relevant revenue authority can connect two or more transactions or chains of transaction in which there is one common party whether or not the commodity sold is the same. If there is a connection in that

sense it matters not which transaction or chain came first. Such a connection is entirely consistent with the dicta in *Optigen* and *Kittel* because such connection does not alter the nature of the individual transactions. Nor does it offend against any principle of legal certainty, fiscal neutrality, proportionality or freedom of movement because, by itself, it has no effect.

Given that the clean and dirty chains can be regarded as connected with one another, by the same token the clean chain is connected with any fraudulent evasion of VAT in the dirty chain because, in a case of contra-trading, the right to reclaim enjoyed by C ... in the dirty chain, which is the counterpart of the obligation of A to account for input tax paid by B, is transferred to E .. in the clean chain. Such a transfer is apt…to conceal the fraud committed by A in the dirty chain in its failure to account for the input tax received from B."

15. We also have regard to the remarks of Christopher Clarke J (as he then was) in *Red12 v HMRC* [2009] EWHC 2563 at [109]-[111] which were also approved by the Court of Appeal in *Mobilx:*

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

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

[111] Further in determining what it was that the taxpayer knew or ought to have known the tribunal is entitled to look at the totality of the deals effected by

the taxpayer (and their characteristics), and at what the taxpayer did or omitted to do, and what it could have done, together with the surrounding circumstances in respect of all of them."

16. In *Megtian Limited (in administration) v HMRC* [2010] EWHC 18 (Ch) Briggs J (as he then was) stated at [34], and [37]-[38]:

> "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.
>
> 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."

17. The burden of proof in this type of case rests with HMRC. Moses LJ made this clear in *Mobilx*:

> "[81] ...it is plain that if HMRC wishes to assert that a trader's state of knowledge was such that his purchase is outwith the scope of the right to deduct it must prove that assertion.
>
> [82] But that is far from saying that the surrounding circumstances cannot establish sufficient knowledge to treat the trader as a participant....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 by his purchase that he was taking part in a transaction connected with fraudulent evasion of VAT. The circumstances may well establish that he was.
>
> [85] ....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."

18. The test in *Kittel* is simple and should not be over-refined.

19. It is also clear that we must look at the totality of the evidence, and not adopt an approach which is 'over-compartmentalised'.

20. The standard of proof in this case is the ordinary civil standard, namely, the balance of probabilities. In *Re B (Children) (Care Proceedings: Standard of Proof) [2008] UKHL 35*, the Supreme Court made it very clear that there is no enhanced burden even if the allegations - as in this case - are ones where the gravity of misconduct alleged is serious, with serious consequences.

21. Lord Hoffmann made the following remarks concerning the operation of the standard when it comes to fact finding:

> "[2] If a legal rule requires a fact to be proved (a 'fact in issue') a judge or jury must decide whether or not it happened. There is no room for a finding that it might not have happened. The law operates a binary system in which the only values are zero and one. The fact either happened or it did not. If the tribunal is left in doubt, the doubt is resolved by a rule that one party or the other carries the burden of proof. If the party who bears the burden of proof fails to discharge it, a value of zero is returned and the fact is treated as not having happened. If he does discharge it, a value of one is returned and the fact is treated as having happened.
>
> [13] ... I think that the time has come to say, once and for all, that there is only one civil standard of proof and that if proof that the fact in issue more probably occurred than not."

The Issues

22. In a case of this nature, four issues conventionally arise:

(1) Was there a tax loss? (**Issue 1**)

(2) If so, did this loss result from a fraudulent evasion? (**Issue 2**)

(3) If so, were the transactions which are the subject of this appeal connected with that evasion? (**Issue 3**)

(4) If so, did or should the Appellants have known that the transactions were so connected? (**Issue 4)**

23. The Tribunal had not made (nor been asked to make) any *Fairford*-type directions (see *Fairford Group plc (in liquidation)* [2015] STC 156).

24. But, at the very outset of the hearing, Mr Yewdall confirmed that there was no dispute that there was a tax loss, and that the Appellant was involved in 'dirty chains'. It is disappointing that the issues could not have been clarified in that way sooner than

they were, since this led to the production and reproduction of thousands of pages of evidence, none of which actually ended up being in dispute, and which was not referred to at all during the course of the hearing.

25. Mr Yewdall also clarified, at the outset of the hearing, that the issue in dispute is whether the Appellant 'was aware of the fraud'. We took that to refer to the last limb of the *Kittel* test. Our understanding was consistent with, and borne out by, the way in which the hearing of the appeal and the evidence evolved.

Issue 1 - Was there a tax loss?

26. This issue was not ultimately in dispute.

27. HMRC bears the burden on this issue. The standard of proof is the balance of probabilities. We are satisfied that it has discharged that burden to that standard. Accordingly, the answer to Issue 1 is 'yes'.

28. But, for the sake of completeness, we squarely address one of the Appellant's arguments. As a matter of law, it is not necessary for HMRC to identify and 'allocate' tax losses so as to 'marry' or match the tax loss relied upon with the individual deal in dispute. In *Mobilx* the Court was clear that the *Kittel* principles may engage even when there is no correlation between the amount of output tax of which a fraudulent trader has defrauded HMRC and the amount of input tax which another trader - in this case, the Appellant - has been denied: see Para [65].

29. The Tribunal (Judge Brannan and Mr Perrin) took a similar approach in *Digi-Trade Limited v HMRC [2011] UKFTT 566 (TC).* They did not believe that any such apportionment was necessary under the *Mobilx* test, and neither do we. The decision in *Calltech Telecon Ltd [2009] EWHC 1081 (Ch)* emphasises that the objective of not recognising the right to repayment is not simply to ensure that the Exchequer is not harmed by fraud, but also extends to combating fraud and discouraging taxpayers from entering into transactions which they knew or ought to have known were connected with fraud.

30. All of the Deals which are the subject matter of this appeal involved purchase from Parr Metals UK Ltd ('**Parr Metals'**).

31. Parr Metals was incorporated on 20 February 2013. At the time of its incorporation, a Mr Trevor Parr was sole director, but he and Mr Michael Dunbar were named as equal shareholders (albeit Mr Dunbar was very quickly removed from the Register of Shareholders).

32. On 3 April 2013, Parr Metals made an online application to register for VAT with effect from 1 March 2013. On 11 September 2013, HMRC made an unannounced visit to Parr Metal's principal place of business, which was a residential address, and where there was no answer.

33. On 20 September 2013, Parr Metals was de-registered for VAT purposes.

34. On 2 October 2013, HMRC made an announced visit to Parr Metals at a commercial address in Leeds, where HMRC met with Mr Parr and Mr Yewdall. This meeting was for HMRC to consider whether Parr Metals' registration should be reinstated.

35. On 24 January 2014, Parr Metals was notified that all its transactions in the VAT period 08/13 (that is to say, including the Deals) all traced to tax loss, resulting in a loss to the public purse of about £80,000.

36. On 27 February 2014, HMRC denied Parr Metals a claim for input tax of £83,213.56 (arising from 9 transactions, including three to the Company) for the quarter 08/13. On 8 April 2014, a notice of assessment in the sum of £70,166.49 was issued to Parr Metals for the period 08/13. On 27 February 2014, HMRC issued Parr Metals with a further notice of assessment in the sum of £41,754 for the period 1 September 2013 to 30 September 2013. On 29 September 2014, Parr Metals was wound up with a claim from HMRC for about £135,022.

37. All of the Deals trace through Parr Metals to React (UK) Ltd ('**React**'). React was assessed for a total of £1.141m before being declared insolvent.

38. React was incorporated on 31 August 2011. It was registered for VAT on 14 September 2011 when its main business activity was described on the Form VAT1 as 'sewing garments. Labour and sewing suppliers'. Its estimated turnover in the next 12 months was £80,000, but in fact its turnover for the year 31 August 2011 to 31 August 2012 was £500. In its returns for VAT periods 11/11 to 02/13 React never declared sales of more than £500. Its VAT return for 02/13 was its last submitted return.

39. A visit to React's principal place of business on 20 November 2013 was found to be a residential address. Despite repeated attempts, HMRC were unable to meet any of React's directors or officers. E-mail contact was made with a Mr Kian Thal Singh, and a Ms Nancy Black.

40. On 29 November 2013, HMRC wrote to React advising that it had received evidence that React had been trading regularly since 05/13, including making sales to Parr Metals in VAT period 08/13, including the Deals. The total identified output tax on these sales was £428,766.

41. On 13 December 2013, HMRC received an email from Ms Nancy Black saying that she had sold the company and had no knowledge of its trading. She went on to say that she had never heard of React (UK) Ltd.

42. On 8 January 2014, HMRC raised an assessment on React of undeclared and unpaid output tax of £694,603. On 4 March 2014, HMRC issued React with a penalty of £486,222.

43. Neither the assessment nor the penalty has been paid.

Issue 2 - Did this loss result from a fraudulent evasion?

44. This issue was not ultimately in dispute.

45. HMRC bears the burden on this issue. The standard of proof is the balance of probabilities. We are satisfied that it has discharged that burden to that standard. Accordingly, the answer to Issue 2 is 'yes'.

Issue 3 - Were the transactions which are the subject of this appeal connected with that evasion?

46. This issue was not ultimately in dispute.

47. HMRC bears the burden on this issue. The standard of proof is the balance of probabilities. We are satisfied that HMRC has discharged that burden to that standard.

48. All the Deals lead back to React, which is a defaulting trader.

49. HMRC's position, set out in the witness statement of Officer Warren, is that the Company was the second line buffer in the deal chains, with the broker traders in Deals 1 and 2 being Metal Interests Ltd and in Deal 3 being Simms Group UK Ltd.

50. Accordingly, the answer to Issue 3 is 'yes'.

Issue 4 –Did or should the Appellant have known that the transactions were so connected?

51. This is the key issue in this Appeal.

52. It is necessary for us to determine whether the Appellant limited company, acting through its directors, Mr and Mrs Dunbar, either (i) did know or (ii) even if it did not know, nonetheless should have known that the transactions which are the subject matter of this appeal were so connected. HMRC advanced its case under both (i) and (ii) although Ms Barnes acknowledged in closing – it seemed to us appropriately – that many of her points and the thrust of the cross-examination was more targeted at (ii) ('should have known') than at (i) ('did know').

53. This issue has to be proved by HMRC, but only to the civil standard - namely, whether HMRC is able to show that it is likelier than not that the Company (through its directors) either did know or should have known that the transactions were connected to fraud. As already explained, there is no enhanced civil burden of proof simply because the allegations involve actual or constructive knowledge of fraud.

54. In arriving at our findings, it is clear (for instance, from *Mobile Export 365 v HMRC*) that we are entitled to rely on inferences drawn from the primary facts. It is also clear, from the approach taken by Christopher Clarke J in *Red12 v HMRC*, and approved by the Court of Appeal in *Mobilx*, that we should not unduly focus on whether a trader has acted with 'due diligence' but should consider the totality of the evidence.

55. We are not required to consider whether 'the only reasonable explanation' for the transactions is connection to fraud. This was made clear by the Upper Tribunal in *AC*

Wholesale Ltd v HMRC [2017] UKUT 191 (TCC) (Proudman J and Judge Sinfield), especially at Paragraphs [29] and [30]. But, of course, we are bound to consider and weigh up, as part of our consideration of all the evidence, taken together, any explanation or explanations put forward by the Appellant.

HMRC's case

56. Since HMRC bears the burden on this issue, we outline HMRC's case first. It says that the Appellant (through Mr and Mrs Dunbar) either knew or should have known that the Deals were so connected.

57. In broad summary, HMRC relies on the following features:

(1) The deals were 'too good to be true':

(a) The Company had no previous experience in the wholesale scrap metal sector;

(b) The Deals were being set up or orchestrated by a third party, Chris Howard, who was apparently working for free;

(c) Deals A, B and C were back to back deals;

(d) Deal A was acknowledged by the Company to be a 'paper exercise'

(e) Deal 1 and Deal 2 were 'back to back' deals, with the Company's purchase and onward sale being on the same day;

(f) Deal 3 had the onward sale being on the day after the Company's purchase;

(g) The Company was not adding any value to the scrap metal;

(h) The Company was never required to pay its supplier until it had been paid by its customer;

(i) The Company made a profit of £1,382 on the Deals (and a profit of about £4,500 on Deals A-C), although it had effectively done nothing to set up the Deals (or Deals A-C), progress them, or add value.

(2) The Company had a general awareness of MTIC fraud, arising from a visit by HMRC on 11 April 2013, when HMRC discussed the Appellant's diversification into the scrap metal wholesale trade and MTIC fraud. Similar advice was provided in the annexe to a letter on 15 April 2013;

(3) The Company's relationship with Parr Metals was not at arms' length and itself generated suspicion:

(a) Parr Metals had been incorporated on 20 February 2013 – i.e., less than four months before Deal 1;

(b) Mr Dunbar told HMRC in August 2013 that he had been introduced to Parr Metals by Mr Howard, whereas in fact Mr Dunbar had been a 50% shareholder in Parr Metals at its incorporation.

(c) There were documents, ostensibly emanating from the Company, which apparently showed that the Company and Parr Metals were trading 'in partnership' with each other: see the letters dated 27 March 2013 (EX1-512) and 16 May 2013 (EX1-518).

(4) The evidence, taken in the round, '*reveals a pattern of trade so far removed from ordinary commercial practice that either the Appellant knew that the Deals were connected with fraud but was prepared to proceed regardless or should have known that the Deals were connected with fraud'.*

The Appellant's case

58. In summary, the Appellant's case, is as follows:

(1) The Company, which was engaged in business originally as a house builder, but then in commercial contract work for local authorities, schools and larger commercial customers, entered into these scrap metal transactions in order to increase its overall turnover so that it could qualify for the tendering process leading to the award of larger commercial building and maintenance contracts. The company's turnover had previously been a problem in this regard;

(2) Heed was taken of due diligence guidance provided by HMRC, and reasonable, appropriate checks and proper due diligence was carried out by the company on its intended counterparties;

(3) The transactions were entered into on 'a strict commercial basis';

(4) There was no awareness of fraud prior to the company undertaking these transactions, and no awareness that the trading of the vendors was in any way connected to fraud;

(5) The company ceased trading in metals after only six deals, and as soon as it became aware of possible perceived fraud in the industry;

(6) The appellant had met the seller's director and had been to the seller's yard and offices to check the viability of the company;

(7) The chain of each transaction was wholly transparent;

(8) There is photographic evidence of the metals delivered to the Company's extensive yard and being sorted and processed ready for dispatch;

(9) There was no loss of Revenue to the Crown in relation to these particular transactions;

(10) HMRC 'should not be able to claim any missing VAT back from a successful, profitable, trading business which is purely an innocent party in the offending transactions'.

The evidence of Officer Warren and Officer Tosta

59. The witness statements of Officer Marchant-Williams (the allocated officer for Douglas Waste Management), Officer Marsh (the allocated officer for React UK Ltd),

and Officer Lill (the allocated officer for Intertrade Global Ltd) were taken as read. Those officers were not required for cross-examination. We accept their evidence.

60. We heard evidence from Officer Diane Warren. Her evidence-in-chief was contained in a detailed witness statement dated 17 August 2016. She is a highly experienced officer, with particular experience of VAT fraud. At the time of the events in question in this appeal, she been an officer of HMRC for over 30 years, and had been a member of the Missing Trader Intra-Community fraud team for about 7 years.

61. She has detailed personal knowledge of this case, having attended the important meeting with the Company on 11 April 2013. Thereafter, she became the responsible case officer for the Company and took the decision, in October 2013, to place the Company's VAT return for 08/13 into extended verification. Latterly, she was the officer who took the decision to deny the claim to input tax which is now appealed against.

62. Her oral evidence was consistent with her written evidence. We were impressed by her evidence, which was given carefully and in detail, and we accept it.

63. We do not consider that HMRC, through Officer Warren, was pursuing this Company tactically, as 'the last man standing', in circumstances where its counterparties had disappeared or entered insolvency. As VAT Notice 726 makes clear, liability for VAT in these circumstances can be joint and several, so that it simply makes no difference whether the counterparties still exist or not.

64. Officer Warren was clear as to the process which had been gone through in order to arrive at a decision to deny this claim for input tax. That process obviously took time. In our view, it is just a coincidence that, in the meanwhile, Parr Metals happened to have entered insolvency. But it was perhaps regrettable, in the overall context of this case, that HMRC did not give the Company monthly updates on the progress of the extended verification process. There was a long gap in the correspondence from 30 January 2014 (when HMRC sent the Company a tax loss letter advising it that the deals in question had commenced with a defaulting trader, resulting in a fraudulent tax loss) until the decision was eventually issued on 9 December 2014. This led to the situation where the Company suddenly received – as it saw, out of the blue – the decision. But, and although we can understand the Company's frustration at this, it is not a factor which undermines the integrity or validity of the reasoning behind the decision.

65. Officer Stefan Tosta is a case worker in the Leeds organised civil crime team. His witness statement was dated 16 August 2016. He is also an experienced officer, having, at the relevant time, worked for HMRC since 2001. He has particular knowledge of VAT fraud having in March 2012 joined the operational team collecting, collating, monitoring and verifying repayment claims for traders identified as either unwittingly or wittingly participating in transactions linked to sustained and persistent VAT fraud against HMRC.

66. His evidence was given in detail, and was not substantially challenged. He had also attended the important meeting on 11 April 2013. He had also made an announced

visit to Parr Metals principal place of business on 2 October 2013, where he had met Mr Parr and Mr Yewdall. Officer Tosta's evidence was that Mr Parr on that occasion had described Mr Dunbar as 'a very good friend' who had helped set up Parr Metals, and who had been influential in recommending that Mr Parr go into the metals trade. This evidence was not challenged.

67. Officer Tosta's oral evidence was consistent with his written evidence, and we accept it.

The evidence of Mr and Mrs Dunbar

68. Mr Dunbar gave evidence for a whole day. He describes himself as a 'hands-on' individual, with practical experience of construction. He gave us the impression of being nobody's fool. He and his wife have built up a substantial trading enterprise, being conducted not only through the present Appellant, but through another company as well.

69. Mr Dunbar, rather than Mrs Dunbar, was the director who took the lead when it came to the scrap metal trades.

70. Mrs Dunbar gave evidence for two hours. She was said to have been the director responsible for the paperwork and back office, but she did not seem to know much detail about any of the Deals.

71. In the circumstances, it is appropriate to focus on Mr Dunbar's evidence. Having had a good opportunity to hear and assess Mr Dunbar, the overall and consistent impression which he gave us was of a man who was profoundly incurious about the deals which the Company was entering into, in circumstances which would reasonably and objectively have prompted curiosity.

72. In the course of his evidence, Mr Dunbar posed the following question: "*What could be simpler than buying something and basically selling it"* (Day 2 Page 36). As far as it goes, the question is accurate. But it reveals a lack of any real awareness – even now - of the relevant context and the issues which he and the Company should have considered during the period the Company was engaged in dealing in scrap metal.

73. Mr Dunbar was candid with us that his interest was simply in buying and selling, and making a profit. But, beyond that, he seemed blasé and indifferent both to the identity and bona fides of those who he was buying from, or those who he was selling to, or to fraud or the possibility of fraud.

74. As to the latter, Mr Dunbar appeared indifferent to the possibility (for example) of being sold stolen goods. To avoid any doubt, there is no suggestion in this case – whether by HMRC, or by the Tribunal - that any of the scrap metal traded by the Company was stolen, or that the Company, Mr Dunbar or Mrs Dunbar ever stole anything, or handled any stolen goods. Mr Dunbar was asked questions which sought to explore what safeguards the Company had against buying or selling stolen metal. Whilst Mr Dunbar objected to this line of questioning, we considered that his objections missed the point. The questions were fair ones. They were seeking to explore what

safeguards the Company had to make sure that it was not buying or selling stolen scrap metal, which in reality amounted to safeguards that the Company was not getting sucked into fraud in general, and VAT fraud in particular. It is obvious that such caution or safeguards would be especially important to a new entrant to the trade which was doing deals for tens of thousands of pounds, in a commodity with which it was not familiar. The answer was that the Company did not have any safeguards, and indeed Mr Dunbar did not seem to think that any such safeguards were ever needed. That feeds as a factor into the overall picture which we form of the Company and Mr Dunbar's direction of it.

75. In our view, Mr Dunbar's attitude to risk and compliance is rightly characterised as 'cavalier', and the Company's approach to its scrap metal deals (both the deals which are subject to this appeal, and, to the extent that those are relevant, to the earlier deals) was cavalier.

76. In his evidence, Mr Dunbar said that '*I trusted a lot of people; that's my problem'*. For reasons which remain far from clear, even if Mr Dunbar did trust people, and in particular Mr Chris Howard (who Mr Dunbar described as 'a trusted person': Day 2 Page 81) and Mr Trevor Parr, it was neither sensible nor reasonable for Mr Dunbar (and, through him, the Company) to have trusted either of them. The nature and extent of their involvement with the Company, and the Deals, was something which should not have been taken at face value, or trusted. Mr Dunbar was (at best, and giving him the benefit of the doubt) closing his eyes to obvious risks.

77. Mr Dunbar's evidence was that he did not see himself '*as doing any fraud.'* But this serves simply to highlight his narrow and erroneous view of the matter. It seemed to us that he had not really grasped that liability of the kind which is in issue in this appeal does not need to depend on actual knowledge of fraud, nor upon being a fraudster oneself. As repeatedly explained by the Courts and Tribunals (for example in the cases discussed above) liability can go much further and can catch 'buffer' traders.

78. Having read the documents, and heard the oral evidence, we have no hesitation in deciding that the Company, through its directors, should have known that the Deals under appeal were connected with fraud and that therefore the appeal should be dismissed.

79. We set out the detailed reasons for this below.

The Company's entry into the scrap metal business

80. The Company's turnover in the year ending 30 November 2009 was £3.465m, but that was a peak. The turnover in 2010, 2011, and 2012 was between £2.67m and £2.93m, or a range of about 10%, and hence was relatively consistent. However, in the year ending 30 November 2013 its turnover dropped to £2.308m, which was its lowest turnover for any of the five years 2009-2013. There was a year on year fall from 2011 to 2013, being about £620,000, or about 20%. We consider that this would have placed financial pressure on the Company.

81. Alongside this, the Company's profit fell from a high of £351,719 in 2009 to £13,364 in 2012, and in 2013 the Company made a substantial loss, £320,366.

82. We consider Mr Dunbar's evidence to be truthful when he accepted that he was *'extremely keen'* to reverse the decline in turnover and to 'keep turnover up' (Day 2 Page 34).

83. However, we reject the reason given by the Company, which was that its wish to keep its turnover up was attributable to tendering rules or requirements (for instance, the need to have a minimum turnover). No documentary evidence of any tendering rules or requirements was put before us. No documents relating to tenders, or their refusal, were placed before us.

84. Rather, the oral evidence was more focused on increased competition in that part of the construction sector occupied by the Company. Larger companies (which previously had tendered only for bigger jobs) were beginning to tender for smaller jobs. This is suggestive of more widespread commercial pressure in the construction industry. There is no reason to think that the Company was immune from this commercial pressure. Its turnover and profit figures, taken together, seem to point clearly to a non-trivial degree of commercial pressure. Even including the turnover attributable to its scrap metal deals, the Company's turnover was shrinking significantly.

85. We conclude that this general commercial pressure is relevant, since it fed into the Company's lack of concern and diligence as to the bona fides of the scrap metal transactions it was entering into.

86. It does not make much commercial sense for the Company, in this difficult financial position, to have diversified into scrap metal, as opposed to diversifying into some enterprise where it could use its existing knowledge and experience. This was an entirely new sphere of business, both for the Company, and for Mr Dunbar. Mr Dunbar knew about house-building and contracting. But he did not know anything of any real substance about scrap metal. All he had was some experience salvaging, giving away, and sometimes selling small amounts of 'rebar' from sites. The sorts of quantities involved were small - he told us that the proceeds were used to *'buy the sandwiches in the cabin'*. On one site, the Company had also encountered a length of copper cable. This was far from sufficient to give it any experience to enter the scrap metal industry, dealing in tens of thousands of kilograms (i.e., tens of metric tons) at a time.

87. Mr Dunbar said that he did not do any research into the scrap metal industry. That is surprising since, if the object (which was in fact accomplished) was to increase the Company's turnover, the Company was going to need to be buying and selling tens (in fact, as it turned out, hundreds) of thousands of pounds worth of scrap metal. With reduced turnover and profit from construction, the Company was – on the face of it – taking tremendous risk. It was staking its commercial future on the scrap deals. Those features alone are a further illustration of Mr Dunbar closing his eyes to obvious risks.

88. Had he done some research, even perfunctorily, he would quickly have realised that there were widely reported concerns with the integrity of the scrap metal industry, and especially the issue of theft of copper cable. That is to say, he would have realised that there were widespread concerns with exactly the sort of commodity which the Appellant came to deal in.

89. The Company was involved in the scrap metal business from 27 March 2013 to 16 July 2013. Even though this was a fairly short-lived venture, Mr Dunbar still did not personally acquire any real knowledge about what the Company was buying and selling. For example, he was not able to explain how goods being brought in as '96% copper birch cliff' were being sold as 'bright wire' (Day 2 Page 96). He himself asked whether these were different products. He did not know.

90. It also became obvious that Mr Dunbar did not have any real understanding of the structure or mechanism of the scrap metal deals which the Company did. This became clear in a passage of cross-examination which sought to explore his understanding of the moment at which risk and title to the goods would pass, especially in the context of back-to-back sales. His answer was that in a back-to-back deal '*you don't really own the goods, do you?*' (Day 2 Page 106). That is wrong, both as a matter of law and as a matter of fact. His answer betrays the sense of 'detachment' between the Company and the deals, and adds to the impression that the Company was being used simply as a convenient VAT-registered vehicle for these goods to pass through.

91. This absence of prior experience and knowledge is relevant and striking when set against the deals which were actually done, and especially their mechanism, and the speed and apparently complete ease with which they were done.

The involvement and role of Mr Howard

92. Mr Chris Howard was instrumental in bringing about the Company's involvement in the scrap metal business, and in conducting the Deals thereafter. His involvement and role remain very mysterious.

93. We did not hear any evidence from Mr Howard. We do not consider that the Appellant had taken reasonable steps to get in touch with him. We were told of one call to a disconnected mobile phone. Inferences can properly be drawn from Mr Howard's absence: *Wisniewski v Central Manchester Health Authority* [1998] PIQR P324. We do consider that Mr Howard would have had useful evidence to give, not least because his role was seen as sufficiently important for him to have attended the meeting with HMRC on 11 April 2013. Having said that, his absence is simply part of the overall picture, and the inferences to be drawn from it are not decisive.

94. We were left with no clear idea who Mr Howard really was, or how he came to be involved with this Company. Mr Dunbar's evidence in these regards was unsatisfactory. We do not consider that Mr Dunbar was really telling us the full truth about his involvement with Mr Howard. Even taken at face value, the explanations given by Mr Dunbar did not make much sense.

95. On Mr Dunbar's account, Mr Howard was not well-known to him. He said that he was not a friend, but was simply someone who Mr Dunbar had met – it seemed by chance, rather than on purpose - at a hotel a year or so before Deal A. Mr Dunbar said in his evidence that he did not have 'a relationship as such' with Mr Howard. He said he 'just knew the guy'. Mr Dunbar said that he knew very little about Mr Howard's personal or business background, except than Mr Howard had once worked on the 'cooling towers at power stations round Doncaster', and had some background in the scrap metal industry, although this was through Mr Howard's father who managed a scrapyard in Doncaster, but with whom Mr Howard had fallen out. Mr Howard did not himself have a scrap yard.

96. After that meeting in the hotel, Mr Dunbar did not see Mr Howard again for at least a year until, just before Deal A in March 2013, Mr Howard phoned Mr Dunbar and called to see him on a building site in Huddersfield to discuss scrap metal and to ask whether Mr Dunbar would like to buy some scrap. According to Mr Dunbar, the model which was proposed was for the Company to buy 20-25 tons of scrap, sort it, and thereby add value and make a substantial profit.

97. That was the discussion which led to Deal A. We shall return to the circumstances of Deal A.

98. Mr Howard was never an employee or a director of the Company. As Mr Dunbar accepted, Mr Howard was doing what he did for no financial reward. We do not accept the evidence, either of Mr Dunbar or Mrs Dunbar, that there was some agreement that Mr Howard could become an employee of the Appellant, and was (in effect, although it was not put in quite this way) on some sort of 'probation'.

99. The Appellant's evidence was that Mr Howard had spent 20 hours 'over the whole period' (that is to say, over about 3 months) working on setting up the deals. Those deals had made the Appellant a profit, albeit a modest one.

100. If Mr Howard really did expect to be getting a job in due course, it makes no sense that Mr Howard, when told (some months later, and having been involved in all the scrap metal transactions in the meanwhile) that the Company had stopped trading in scrap metals 'just accepted it' and walked away without asking for anything (for instance, a share of the profit, commission, or some sort of 'finder's fee'). After all, the Company's ostensible aim was to increase its turnover, and, by virtue of these scrap metal deals, it had increased its turnover by around £1/2m.

101. It is, objectively speaking, both odd and suspicious why someone should have given their time and effort to the Company to help it make money whilst not asking for anything, at the time, in return for themselves. It makes less sense why they would walk away. The reasonable person would inevitably ask 'What is in it for them?'. Some unarticulated, or poorly articulated, hope of one day being employed is not a satisfactory answer to that question.

102. There was also lack of proper oversight in the Appellant company as to Mr Howard's activity. We formed the impression that Mr Howard managed to insinuate

himself into the Company, but he was only able to do this by Mr and Mrs Dunbar's 'ask no questions' attitude.

103. One example of this phenomenon was the email sent by Catherine Richards, a secretarial employee of the Company, dated 1 March 2013 to Andy Douglas at Douglas Waste Management. That said that *'Chris Howard will act on behalf of MD Construction and Parr Metals'*. Mr Dunbar's explanation for how this email came to be written was that Chris Howard *'had probably gone into the office and asked Catherine to write the email'* (Day 2 Page 78). There was no evidence from Catherine Richards.

104. No good explanation emerged as to how Mr Howard came to be in a position where he could give instructions to Catherine Richards in relation to the writing and signing of letters, in the Company's open-plan office, and that these instructions would be followed, with no-one (including Mrs Dunbar, who was often in that office) stopping or questioning him.

105. We reject Mr Dunbar's evidence that the Company's offices and its secretarial/administrative facilities (which it was paying for) were (in effect) put at the disposal of other persons on what was put as a fairly free-and-easy basis.

106. Mrs Dunbar's evidence was that Mr Howard was brought into the office by Mr Dunbar *'just as if he was a new employee'*. But Mr Howard was not an employee. Mrs Dunbar said that '*it wouldn't be anything unusual for Chris Howard to be telling Catherine (the secretary) to write some letters'* (Day 3 page 5).

107. We reject this evidence. It is not at all credible. This was a long-standing family-run company with long-standing employees. We do not believe that the Company would routinely allow third parties free-rein and use of its facilities.

108. But, even taking what Mrs Dunbar said at face value, the administrative model described is extremely strange. It is – both figuratively and literally - an open door to fraud.

109. It was striking that Mr Dunbar did not accept, even in hindsight, that it had been an error to rely on Mr Howard. He went beyond this and was very careful to say that he was not placing any blame on Mr Howard. We cannot tell whether this flows from some misguided sense of loyalty, or from some other motive. However, it is a very strange attitude for Mr Dunbar, as a director of the Appellant limited company, to take. This is because, on any view, Mr Howard had definitely played a part in bringing about the position which the Appellant company found itself in, including being refused an input tax claim of several tens of thousands of pounds, having to pursue an appeal for over 3 years, instruct professional representatives, and attend the Tribunal to give evidence.

Mr Parr

110. The relationship with Trevor Parr is also very mysterious. There was no evidence from him, nor any satisfactory explanation as to why there was no evidence.

111. He had been in the carpet and flooring industry, and not in scrap metal, but it did not seem odd to Mr Dunbar that someone in the flooring industry should be contacting Mr Dunbar to 'diversify' into scrap metal. Nor did it seem odd to Mr Dunbar that someone he was seeing 'not even once a year' should phone him. Even though Mr Dunbar had not seen him for a long time, Mr Parr got Mr Dunbar's number, although Mr Dunbar did not know how, and, as Mr Dunbar accepted in his evidence, rang him up out of the blue and said 'Do you want to get into scrap metals together' (Day 2 Page 70).

112. Nor did it seem odd to Mr Dunbar that, at more or less the same time, two people – Mr Howard and Mr Parr (neither of whom Mr Dunbar really knew) - were independently contacting Mr Dunbar to ask about scrap metal. It should have rung alarm bells.

113. We accept Officer Warren's evidence that Mr Dunbar did not tell her, during the August 2013 visit, that he knew Mr Parr, or that he had been a shareholder in Parr Metals. We do not understand why Mr Dunbar did not mention those things. We accept that Mr Dunbar's inclusion as a subscribing shareholder to Parr Metals Ltd on 20 February 2013 was reversed very quickly. But none of this really explains why Mr Dunbar did not say anything about this at the August 2013 visit.

114. In his evidence, in response to a question from the Tribunal as to how he had found out that he had become a shareholder in Parr Metals Ltd, Mr Dunbar said that *'I think Chris told us'* (Day 2 Page 12). 'Chris' must mean Mr Howard. There was no explanation as to how Mr Howard came to know that Mr Dunbar had become a shareholder in Mr Parr's company. The answer suggests a link – known to Mr Dunbar – between Mr Howard and Mr Parr.

115. Several questions arise from this scenario, none of which is satisfactorily answered by the Appellant.

116. The first is that when Mr Parr registered Mr Dunbar as a shareholder in Parr Metals, he had done exactly what Mr Dunbar says he had told him not to do. However, Mr Dunbar nonetheless continued (on his own evidence) to trust Mr Parr, and indeed to do business with him. That suggests either that the true relationship between Mr Dunbar and Mr Parr was not in fact as described to us by Mr Dunbar, or that Mr Dunbar was an unusually and surprisingly relaxed individual when it came to his name being used in a business context against his wishes.

117. Neither of these scenarios really works to Mr Dunbar's advantage. Either he was not telling the truth about Mr Parr, or he is indifferent to the commercial bona fides or integrity of those he chooses to deal with.

118. It is also notable that the company formation documents for Parr Metals, including the registration of Mr Dunbar as a subscribing shareholder, were filed by Spenser Wilson Ltd, who were accountants for both the Company and Mr Parr (and who still are accountants for the Company). There was no evidence as to whether Spenser Wilson had consulted Mr Dunbar to ask his permission before putting his name

on that paperwork. In the absence of any evidence from anyone at Spenser Wilson (whose Mr Yewdall was representing the Company in this appeal) as to how this situation had come to pass, we cannot make any further findings in that regard, but it suggests (we cannot put it any higher than that) that there was an 'overlap' between the interests of Mr Parr and Mr Dunbar.

119. We also have regard to the 'introduction' letter, from Parr Metals Ltd, dated 28 May 2013 (EX1-492), to Yorkshire Metal Recyling Ltd. That letter was typed and signed by Catherine Richards (as 'C L Richards') *'per pro Mr T Parr Director'*. Catherine Richards was a secretarial employee of MD Construction. She did not work for Parr Metals or Mr Parr. We do not understand why she would have been doing anything on behalf of Parr Metals and/or Mr Parr.

120. A further feature is the email of 1 March 2013 (that is, about a fortnight after incorporation) sent by Ms Richards to Andy Douglas at Douglas Waste advising that Chris Howard was to act on behalf of the Company and Parr Metals (EX1-500).

121. This reinforces our impression that there was a three-cornered relationship between Mr Dunbar, Mr Parr and Mr Howard, of which the precise details remain a mystery.

122. The financial relationship between the Company and Parr Metals was peculiar. The Company advanced £14,500 to Parr on 1 August 2013. Mrs Dunbar's evidence was that this was done in anticipation of a trade which did not eventually come to pass, but there was no other evidence of this at all. Those moneys were returned on 21 August 2013, but described by the Company's bankers – on instructions from someone - as '*Returned Loan'*. A payment up front for a deal which does not happen is not a loan, and no-one would think that it was.

123. When it bought from Parr Metals, the Company did not pay Parr Metals, but instead paid a third party – Luciano's Business Services Ltd. An entity described as '*Luciano Business Solutions'* was described by Parr Metals, in an undated generic letter (EX1-495) as a 'payment processor', to whom all payments were to be made, unless otherwise instructed.

124. Payments to third parties are expressly identified as something to be aware of in VAT Notice 726. We accept Officer Warren's evidence that, in this case, given the sums of money which were involved, she would have expected further checks to be carried out by the Company both on Parr Metals and on Luciano's. But the Company does not seem to have regarded the use of a factoring agent as prompting any suspicion. It should have done. The use of a factor is normally to accelerate the payee's cash flow. But the Company was paying immediately, so there was no need for Parr to factor the invoices at all.

Deal A

125. On the basis of the authorities cited above, we consider that the correct approach to be adopted in this appeal is to recognise that, whilst we must consider the Deals

individually, the Deals need not be viewed in isolation from each other, nor in isolation from Deals A, B and C which preceded them.

126. Deal A is not the subject matter of this appeal. But it is a very relevant part of the background, since many of its features appear and are visible in the deals which followed. Deal A set a pattern which was followed by subsequent deals, including those which are the subject matter of this appeal.

127. The way in which Deal A came about, and the ease with which it happened was obviously indicative of contrivance. This deal really appeared 'too good to be true'. It should have alerted Mr Dunbar, or any reasonable person in his position, that all was not as it seemed. But Mr Dunbar was just interested in the profit, and how much the Company would make. He was closing his eyes to everything else.

128. Deal A took place on 28 March 2013. It was a purchase from Douglas Waste Management and an immediate sale to Yorkshire Metal Recycling Ltd.

129. The Company had not had any dealings at all beforehand with Douglas Waste. It had only sent a letter of introduction to Yorkshire Metals on the day before (27 March 2013). But it did not seem 'too good to be true' to Mr Dunbar be writing a letter of introduction to a company one day, and to be doing about £140,000 (ex VAT) worth of trade with it on the very next day (Day 2 Page 93). We find this attitude startling.

130. On Mr Dunbar's evidence, Mr Howard had tempted the Company with the idea that it could buy 20 to 25 tonnes of scrap, sort it, and thereby – through sorting – make a profit. That is to say, the sorting was going to be the 'value added' by the Company.

131. But Deal A did not actually involve any sorting at all. As Mr Dunbar said (Day 2 Page 59), when he was told that there would not be any sorting, it was 'music to his ears'.

132. Deal A was a 'back to back' sale. Mr Howard had not only sourced the scrap, but had already managed to find a willing buyer for that supply. This was all for no charge to the Company. The scrap was going to move from seller to buyer without even passing through the Company's yard. The Company would not have even have to organise the transport.

133. Hence, and as Mr Dunbar accepted, Mr Howard was effectively doing everything and was doing it all for no fee (Day 2 Page 54). As is clear, and as Mr Dunbar accepted, Mr Howard was effectively offering the Company 'deals on a plate' (Day 2 Page 54), without any guarantee of any personal reward at all in it for himself.

134. It made absolutely no sense for Mr Howard to be gifting this deal to the Company. Indeed, it made little sense for the Company to be involved at all, except that the Company had a VAT number.

135. Therefore, on the face of it, the Company was effectively 'flying blind', entrusting its scrap metal dealings to Mr Howard. Mr Dunbar accepted that he 'just left a lot of things to Mr Howard' (Day 2 Page 14).

136. Deal A was described by the Company to HMRC on 11 April 2013 as a 'paper exercise', and this was true. The Company was not adding any value. It was being paid for nothing. The Company made a profit of £2,337 on Deal A (which was significantly greater than the profit made on any of the other deals). We agree with HMRC that the amount of profit needs to be placed in context. A profit of over £2,000 is a significant amount when the Company had done absolutely nothing for it.

137. Despite all of this, Mr Dunbar did not consider any of this to be strange. We find this hard to believe. But, even if he did not find it strange, it certainly should have done. This was not a deal like deals with plant and machinery, with identifiable machines, of which the provenance can be traced and checked. It was a deal with an unidentifiable load which no-one from the Company would ever even see. The deal and all its circumstances were inherently suspicious.

138. Deal A is marked by the inexplicable absence of commercial sense in the relationship between Mr Howard and the Company. Any further deal with the same sort of structure and mechanism would also be suspicious.

The meeting of 11 April 2013

139. Officers Warren and Tosta visited the Company on 11 April 2013. This was an announced visit. Mr Dunbar was there, as well as his accountant, Mr Yewdall, and Mr Howard, who was sitting on a couch and who came to join the meeting. In the context of this case, this was an important meeting. Mr Howard's role was ambiguous. He was described in HMRC's note as 'agent (?)'.

140. It is common ground that the Company previously had a good VAT compliance record. There was no suggestion that it had ever been visited by HMRC before 11 April 2013. But, even after one scrap metal deal (Deal A) it had been visited, at its business premises, by two HMRC officers. Their visit was prompted by Deal A. That very fact should have sharpened the Company's awareness of the business it was 'dipping its toe' into. As Mr Dunbar said himself in his evidence, '*When you get a letter saying that you're going to be visited by VAT, you – it puts you back a bit and you think 'Have I been up to summat'?'*)(Day 2 page 17).

141. It does not matter that the meeting was only 40 or so minutes long. We are satisfied that was sufficient time for HMRC to gather some information, and to offer some advice and guidance, especially when that guidance was laid down, at length, in paper form. We are satisfied that Officer Warren told the meeting that the purpose of the visit was '*regarding MTIC carousel fraud and the concerns HMRC had regarding metal commodities being used to perpetrate this fraud'*.

142. Nor does it matter that one purpose (or even, perhaps, the main original purpose) of the visit on 11 April 2013 was to sort out a mix-up with the Company's VAT number. As Officer Warren accepted in her written evidence, the need to verify the Company's VAT number brought to HMRC's attention that the Company had engaged in a single scrap metal deal.

143. We accept Officer Warren's evidence that the purpose, at least in part, of that visit was to educate – '*to find out what kind of trade the company does, and to educate the company or trader with respect to MTIC fraud'*.

144. We reject the argument that the Company had not been warned clearly, strongly, or strenuously enough at the meeting on 11 April 2013 as to the possibility of MTIC fraud. HMRC was not buying and selling scrap metal. It was not HMRC's task to run the Appellant's business. Nor was it HMRC's task to 'vet' the Appellant's clients and suppliers for it. That was and is the task of its directors who were and are under statutory duties to safeguard the Company's best interests.

145. HMRC's task was to advise the Company of the risks, and we are satisfied that was done, and done appropriately, bearing in mind that this was not a full assurance visit. HMRC were not visiting to discuss any part of the Appellant's construction business.

146. At that meeting, the Company was told about MTIC fraud, was given a copy of VAT Notice 726, and was given a copy of a leaflet on 'How to Spot MTIC fraud: A quick guide to helping you protect yourself or your business from organised criminals'.

147. Page 1 of 'How to Spot VAT missing trader fraud' says:

> "Be suspicious if your business or those you are dealing with show any of the following characteristics:…
>
> unsolicited approaches from organisations offering an easy profit on high-value/volume deals for no apparent risk…
>
> instructions to make payments to third parties…
>
> new companies managed by individuals with no prior knowledge of the product, who hire specialists from within the sector…
>
> *This list is not exhaustive – use your common sense and be suspicious'* (emphasis in the original).

148. That leaflet goes on to say

> "**Take care** that you know your business, suppliers and your customers; you satisfy yourself that a deal looks and feels genuine; and you know the provenance of the goods or services you are being offered…
>
> Even if an individual transaction looks fine, you need to consider the trading pattern for that particular commodity" (emphasis in the original).

149. It ends by saying:

'Did you know? .. Businesses can be targeted and drawn into fraud if they do not take appropriate care. If you're offered a trading opportunity that seems too good to be true, it probably is"

150. VAT Notice 726 is "Joint and several liability for unpaid VAT". Section 6 deals with "Dealing with other businesses – How to ensure the integrity of your supply chain". It sets out checks to undertake to help ensure the integrity of the supply chain, including "has a buyer and seller contacted you within a short space of time with offers to buy/sell goods of the same specifications and quantity?" It sets out checks as to the commercial viability of the transaction, including "have normal commercial practices been adopted in negotiating prices, and is there a commercial reason for any third party payments".

151. Mr Howard was at the meeting on 11 April 2013, although his role was not made entirely clear at the time. He took an active part in the meeting, and Officer Warren confirmed that HMRC did 'sort of' put their questions more to Mr Howard, who answered HMRC's questions to their satisfaction.

152. At that time, the Company had only done one deal, which was Deal A. After that visit, it went on to do Deals B, and C – which were not the subject of extended verification – and all the Deals which are the subject matter of this appeal. The fact that the Company had only done one deal, but was already being visited, and given oral and written advice, before it did any of the other deals, should have sounded a clear alarm that it needed to be careful.

153. Whilst VAT Notice 726 does not contain specific guidance about VAT fraud in the scrap metal sector and what scrap metal dealers in particular should have done to verify suppliers and purchasers, it nonetheless in our view gives sufficiently clear warning of the general risks, especially when taken in combination with the other materials which the Company had been given. We accept Officer Warren's evidence that she specifically drew the attention of Mr Dunbar to Section 6 of that notice, which sets out how to ensure the integrity of a supply chain in the context of Value Added Tax.

154. We also accept Officer Warren's evidence that she and Officer Tosta explained that scrap metal was one of the commodities that had come into the MTIC area. We accept the evidence of Officer Warren, which is corroborated by Officer Tosta, that, when the officers left on 11 April 2013, Mr Dunbar was actually looking at VAT Notice 726 and section 6.2. Mr Dunbar himself accepted in his evidence (Day 2 Page 43) that the officers highlighted that scrap metal was an area with a high risk of fraud.

155. Whilst Officer Warren did not, at that meeting, definitely form the view that the Company was an MTIC trader, we accept that she did form the view (although she did not express it at the meeting) that there was a possibility that it was an MTIC trader. That was the reason which led her to issue the letter on 15 April 2013.

156. That letter ostensibly concerned "Alternative Banking Platforms", which is not a feature of this case. However, Page 1 of this letter said that:

"We strongly advise that … if you fail to carry out proper 'know your customer checks' (KYC) you may be putting your business at risk."

157. The letter said "As part of what you might want to do next the annexe to this letter provides a more detailed explanation of MTIC fraud together with some examples of factors HMRC has found to be indicative of MTIC fraud…You are responsible for carrying out all the due diligence necessary for your particular business".

158. The annex concerning 'Missing trader intra-community fraud' was not 'bumf'.

159. Mr Dunbar did not even ask Mr Yewdall about those materials. Mr Dunbar simply concluded – wrongly – that he did not need to take more care because he concluded – wrongly – that actual knowledge of fraud was what was needed.

160. Mr Dunbar's evidence (Day 2 Page 41) was that he had 'taken on board' the indicators of risk set out in VAT Notice 726, but we do not consider that he really had. The facts all point in the other direction.

161. HMRC's visit in April 2013, and the documents and information which were provided, drew attention to that risk. This Company did not alter its behaviour after the April 2013 visit. It did not seem to pay any attention at all to what it had been told.

Due Diligence

162. Although concerns about fraud in the scrap metal industry do seem to have played some part in the enactment of the *Scrap Metal Dealers Act 2013* (which introduced a registration scheme), that Act, although passed in February 2013 (i.e., before the Deals) did not come into force until October 2013 (i.e., after the Deals). Ms Barnes did not take the point that at the time of the deals in question any of the dealers should have been registered. Officer Warren confirmed in her supplementary evidence in chief that she did not rely on the point, so we give no weight to its existence or provisions.

163. As the evidence emerged, it became clear that the Company had an unduly narrow view of due diligence. They saw it as simply representing or addressing the commercial risk – i.e., the risk of not being paid. This was entirely consistent with the comment which we find Mr Dunbar made at the meeting in April 2013. In reference to VAT Notice 726, '*he noted the point that the supplier offered deals that carry no commercial risk and stated that this referred to their deal'* (which at that time can only have meant Deal A) *'but they did not want to pay upfront and be stuck with the stock'*.

164. So far as it went, the Company seems to have left due diligence to Mr Howard. It should not have done. Nothing stood in the way of the Company doing its own due diligence. We have already expressed our views as to the wisdom of allowing Mr Howard to undertake Company activities such as the dictation of correspondence.

165. We have no hesitation in rejecting Mr Dunbar's evidence that the Company did as much as it possibly could or known about to do at the time it was doing the deals. It did not.

166. In relation to Deal A, the furthest that due diligence went, according to Mr Dunbar, and bearing in mind that the goods had not actually passed through the Company's hands at all, was Mr Howard showing Officers Warren and Tosta 'pictures of the wagon tipping the metal up' (Day 2 Page 115). That was obviously, and self-evidently, inadequate.

167. No due diligence apparently had been done on Intertrade. Mr Dunbar's evidence was that Mr Howard had shown him *'bits and bats on his phone'* (Day 2 page 118). That is obviously inadequate. Mr Dunbar did not personally know anything about Intertrade (Day 2 page 125) although he said that Chris Howard 'would have known' about it.

168. In relation to Douglas Waste, Mr Dunbar said that he had been to its premises, and spoken to Mr Douglas *'about waste paper'* (Day 2 Page 132). We do not consider that the Company did conduct due diligence of an appropriate or conventional character on Douglas Waste. The Company did not conduct credit checks on Mr Douglas *'because he looked a very affluent person'* (Day 2 Page 133).

169. It was accepted by HMRC that the Company had obtained copies of certificates of incorporation and VAT registration; had verified VAT details; and had obtained signed letters of introduction. But the Company did not have written or trade references, nor had it performed any credit checks. VAT Notice 726 sets out a checklist of requirements which, so far as possible, enable a full picture to be obtained of a trading counter-party in the VAT context.

170. The inevitable risk, if things are not done, is that the picture will be incomplete. The underlying purpose is to minimise the risk of becoming unwittingly entangled in VAT fraud. Not obtaining the fullest picture means that the risk remains greater than it should otherwise be. We accept Officer Warren's evidence that VAT Notice 726 is only guidance, and is not exhaustive. It does not contain guidance which is specific to a new company. There we accept, as Officer Warren pointed out, that you could visit the new company, to meet the directors, and to look at the 'set-up' of the company, so that you could get an idea as to how it traded.

171. In our view, when it came to the Deals, the Company (through its directors) fell short of the degree of care and scrutiny which they should have exercised. The Company cannot reasonably seek to blame HMRC for the directors' own shortcomings in their attitude to risk and compliance.

172. The above features underlie and affect each of the three Deals in question.

Deal 1 – 14 June 2013

173. On 14 June 2013, Parr Metals sold 23.469 metric tons of '96% copper birchcliffe' to the Company. On the very same day, the Company made payment to Parr Metals via Luciano's. This was a back-to-back deal. On the very same day, the Company sold this, but described as 'bright wire' to Intertrade.

174. We are satisfied that the circumstances of this deal were such that the Company should have been aware that the transaction was connected to fraud. We incorporate the general discussion and features above.

175. This was a back-to-back transaction. Whilst these may or may not be commonplace for housebuilders in the construction industry – for instance, when buying land to build on, or buying plant and machinery - no documentary evidence was placed before us that this Company (or its affiliate MD Construction (Leeds) Ltd), in the course of its construction trade, had ever itself engaged in such back-to-back deals. We do not consider that reasoning automatically transfers across, without question, to the buying and selling of bulk commodities such as scrap metal. It is not self-evident that it should.

176. Mr Howard had not only managed to source this load, but had also found a ready and willing buyer for it, who could pay immediately. This is not only inherently suspicious, and making little commercial sense, for the reasons detailed above, but the fact this happened (in relation to the deals in this appeal) three times in about a month (and had previously happened for Deals A, B and C) was – put bluntly - just too good to be true.

177. There is a pervasive lack of credible, contemporary, corroborative evidence as to the fact of this deal and its circumstances.

178. There is no evidence as to how the deal was actually negotiated, in terms of the purchase price and the sale price.

179. There is no explanation as to how the description of the goods changed.

180. There is no explanation as to how the quantity bought and sold remained exactly the same, which indicates that no sorting took place.

181. There is no evidence that these goods ever actually came into the possession of the Company. We were shown photos of some scrap. Some of those photos were originally provided to HMRC on 12 February 2015 'showing the metal received in the yard and the subsequent processing of it'. In our view, the reliance placed on these by the Appellant is wholly misplaced. They are of no real evidential value. We do not know when these photos were taken. The photos are not date or time stamped. We do not know where they were taken, or why. They do not show anything conclusive.

182. The goods were apparently weighed at the public weighbridge at Gildersome Spur, but no weighbridge tickets or proof of payment for the weighbridge have been provided. We find this a very striking omission. As a matter of commercial common sense, the Company would have needed to know that the weight which it believed it was purchasing, and which it was paying for, was accurate and was not (for example) over-stated.

183. There was no evidence of any insurance of the goods. The Company latterly stated that it believed that the goods would have been insured by the haulier, but the Company has not put forward any evidence to back this up.

184. Intertrade (the purchaser) paid the Company £110,000 on 14 June 2013. That is to say, the Company was paid by its customer before it had to pay its supplier.

185. The invoicing paperwork for Deal 1 is unreliable. It showed two prices: £107,159 and £110,000. The seller (Parr Metals) invoice was for £107,159. Mrs Dunbar accepted (as she was bound to) that there was nothing to show that Parr was selling to the Company for £110,000. However, the Company paid Parr Metals £110,000 (two payments to Luciano's: both on 17 June 2013; £99,999 and £10,001). The wording of the Company's invoices did not make sense, since there was reference to pro-forma invoices and invoices on the same invoice number on the same day.

Deal 2 – 26 June 2013

186. On 26 June 2013, Parr Metals sold 47 metric tons of '96% copper birchcliffe' to the Company. On the very same day, the Company paid Parr Metals £100,000 via Luciano's. This was also a back-to-back deal. On the very same day, the Company then sold this on to Douglas Waste, albeit under two invoices: 24.598 metric tons, and 22.402 metric tons, each described as 'copper scrap'.

187. In relation to Douglas Waste, there was no letter of introduction until 3 July 2013, which postdates Deal 2. This adds to the overall impression that the letters of introduction were not genuine, but were produced simply as part of a 'paper trail'. The impression is that the intended trades had already been set up, and were the cause of the letters of introduction, and not vice versa.

188. We incorporate the general discussion and features above. We are satisfied that the circumstances of this deal were such that the Company should have been aware that the transaction was connected to fraud. This was a back-to-back deal. There was no insurance. There was no evidence that the goods had ever actually passed through the Company's hands.

Deal 3 – 15/16 July 2013

189. On 15 July 2013, Parr Metals sold 23.545 metric tons of 96% copper birchcliffe to the Company, and payment was made to Parr Metals on the same day. On 16 July 2013, the Company sold the same to Douglas Waste.

190. We incorporate the general discussion and features above. We are satisfied that the circumstances of this deal were such that the Company should have been aware that the transaction was connected to fraud.

***Actual* knowledge of connection to fraud**

191. We stop short of finding that the Company, through its directors, did *actually* know of a connection to fraud.

192. This for three reasons.

193. The first is that it arranged not only for its accountant, Mr Yewdall, but also for Chris Howard to be present at the meeting on 11 April 2013. We simply do not believe that the Appellant would have arranged for Mr Yewdall and Mr Howard to have attended if it was knowingly engaged in fraud. There was no suggestion that Mr Yewdall, or anyone at his firm, was knowingly involved in any fraud.

194. The second is that when the Appellant encountered payment difficulties with Yorkshire Metal Recycling, following Deal A, the Appellant instructed well-known solicitors – DWF – to put pressure on Yorkshire Metals, which they did, culminating in an email on 8 July 2013 threatening to petition for the compulsory liquidation of Yorkshire Metals. That email prompted a response, and payment by Yorkshire Metals. We do not consider that an appellant knowingly engaged in fraud would have taken those steps.

195. The third is that the Company was open and co-operative with HMRC in its inquiries.

Conclusion

196. For all the above reasons, the Appeal is dismissed.

Decision

197. This document contains full findings of fact and reasons for the decision. Any party dissatisfied with this decision has a right to apply for permission to appeal against it pursuant to Rule 39 of the Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules 2009. The application must be received by this Tribunal not later than 56 days after this decision is sent to that party. The parties are referred to "Guidance to accompany a Decision from the First-tier Tribunal (Tax Chamber)" which accompanies and forms part of this decision notice.

DR CHRISTOPHER MCNALL
TRIBUNAL JUDGE

RELEASE DATE: 4 SEPTEMBER 2018