[2014] UKFTT 241 (TC)

TC03380

Appeal number: LON/2007/01027

VAT – INPUT TAX – ***HMRC denied input tax claims totalling £1,847,976.80 in respect of 16 transactions of mobile phones and CPUs – Was there a VAT Loss? – Yes – Was the loss fraudulent? – Yes – Were the Appellant's transactions connected with the fraud? – Yes - Did the Appellant know or should have known that its transactions were connected to fraudulent evasion of VAT? – Yes the Appellant knew – Appeal dismissed***

FIRST-TIER TRIBUNAL
TAX CHAMBER

TRICOR PLC **Appellant**
(FORMERLY PNC TELECOM PLC)

- and -

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

TRIBUNAL: JUDGE MICHAEL TILDESLEY OBE
MS HELEN MYERSCOUGH ACA

Sitting in public at 45 Bedford Square, London on 9 January 2012 to 27 January 2012, 9 September 2013 to 11 September 2013, and 19 and 20 September 2013

Ian Bridge, counsel, instructed by Morgan Rose solicitors (David Tunney appeared in January 2012) for the Appellant

Jeremy Benson, Queens Counsel, and Christopher Foulkes, counsel, instructed by the General Counsel and Solicitor to HM Revenue and Customs, (Christopher Foulkes in January 2012) for HMRC.

DECISION

The Appeal

1. On 31 May 2007 and 15 January 2008 the Appellant appealed against HMRC's decisions to refuse repayment of VAT in the following sums: £192,338.13 in respect of four transactions in the VAT period 12/05, £1,508,638.70 claimed in respect of 12 transactions in the VAT period 03/06, and £147,000.00 in respect of one transaction in the VAT period 06/06.

2. HMRC's reason for refusal was that it concluded that the Appellant's transactions were each connected to the fraudulent evasion of VAT and that the Appellant knew or should have known of the connection of its transactions with the fraudulent evasion of VAT.

3. The Appellant accepted that the disputed transactions were connected to the fraudulent evasion of VAT but denied that it knew or should have known of that connection.

4. The Appeal was heard on 9 to 27 January 2012 and adjourned part-heard until 9 May 2012 for closing speeches. During the intervening period the Appellant appointed new representatives who applied to recuse Judge Tildesley, which was refused by Judge Berner on 9 May 2012. The hearing was resumed before the original Tribunal on 9 September 2013. On 20 September 2013 the Tribunal reserved its decision.

5. The chronology of the proceedings and the evidence received are set out in Appendices 1 and 2 of the decision.

6. The Tribunal has issued three decisions on preliminary points: disclosure of evidence and documents (11 December 2012 and 5 February 2013), admissibility of evidence and leave to recall witnesses (5 May 2013), and the admissibility of Mr Fletcher's evidence (9 September 2013). These decisions form part of this decision.

Background

7. The dispute concerned 16 deals involving the wholesaling of mobile phones during the period from 2 December 2005 to 13 April 2006. HMRC broke down the 16 deals into 24 transactions because in some of the deals the consignment of mobile phones was broken down into smaller consignments with separate invoices[1]. The Tribunal, however, in this decision retained the integrity of the 16 deals structure.

8. The Appellant was a public company listed on the Alternative Investment Market in London. The Appellant had approximately 1,600 shareholders including members of the public. The Appellant was incorporated on 27 April 1992 and became a successful business supplying telephony services which included personal

[1] See HMRC's hearing note of 20 September 2013.

numbering, premium services, advance routing, and messaging. In June 2003 the Appellant, however, went into administration due to poor management and the collapse of shares in the dot.com boom.

9. In 2004 two former directors of the Appellant, Mr Leo Knifton and Mr Joe Case, decided to revive the Appellant's fortunes. On 30 January 2004 the Appellant came out of administration. On 24 August 2004, Messrs Knifton and Case took the place of the existing board of directors which were removed following a shareholders' vote. Messrs Knifton and Case decided that the Appellant should concentrate on just one of its varied activities which was the wholesaling of mobile phones in the UK and Europe. In this regard Mr Richard Andrews joined the Appellant as a consultant in June 2005.

10. Mr Case looked after the financial side of the mobile phone business, ensuring that the various transactions were paid for and funded. Mr Case also had the final say on whether a deal went ahead. Mr Andrews was responsible for negotiating the deals and creating the due diligence file. Mr Knifton took no role in the wholesaling of mobile phones.

11. The Appellant declared no sales until the 06/05 VAT accounting period, when the sales turnover was in excess of £830,000. This was the first complete VAT period for the Appellant following the Advocate General's opinion in *Bond House*, which called into question the validity of HMRC's stance in respect of non-economic activity. Turnover increased further during the following periods: 09/05 £8,957,137; 12/05 £9,993,794; and 03/06 £9,301,395. During the first 12 months for which sales were declared, the Appellant achieved a turnover in excess of £29 million from a standing start.

12. Mr Andrews described himself as a consultant. He received from the Appellant for his services commission of 35 per cent of the value of the deals struck. He invoiced the Appellant £231,226 for the deals he set up between 3 October 2005 and 16 December 2005; and £263,442.73 for those arranged between 10 January 2006 and 14 March 2006. In March 2006 Mr Andrews agreed to halve his commission to 17.5 per cent.

13. The Appellant ceased trading in mobile phones around April 2006. The Appellant then traded in other electronic products such as Sat Navs and Nintendo games. The company also opened new divisions: Specs and Lenses and Carbon Trading. These new ventures did not work out. Messrs Case and Knifton resigned their directorships in March 2011. Mr Case remained a shareholder. The Appellant is now a shell company. The Appellant has set aside a provision of £132,000 each for Messrs Case and Andrews in the event of a successful appeal. According to Mr Case, the sum of £132,000 represented salary in lieu for dealing with the Appeal.

The Law

14. A taxable person is entitled to deduct VAT paid in respect of supplies of goods made to him used for the purposes of his business (art. 168 Council Directive 2006/112/EC (formerly art. 17 Sixth VAT Directive)).

15. The Court of Justice in the joint cases of *Axel Kittel v Belgium & Belgium v Recolta Recycling SPRL* (C-439/04 and C-440/04) established an exception to the right to deduct when the trader knew its transactions were connected to fraud. The Court stated at paragraph 56:

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

16. The Court of Justice concluded at paragraph 59:

> "... 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."

17. The Court of Appeal in *Mobilx Limited & Others v The Commissioners for Her Majesty's Revenue & Customs* [2010] EWCA Civ 517 clarified the test in *Kittel*

> "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*.
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> 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."

18. Under the test in *Kittel* the requisite state of knowledge is that which existed at the time the Appellant entered into the disputed transactions. Further HMRC has the burden of establishing on the balance of probabilities the requisite state of knowledge for each of the disputed transactions. This, however, does not mean that the Tribunal must look at each transaction in isolation. The Tribunal is entitled to examine all the

available and relevant evidence when determining the Appellant's state of knowledge, otherwise termed as the big picture approach. The authority for this proposition is derived from Lord Justice Moses' endorsement[2] of Mr Justice Christopher Clarke's dicta in Red12 v HMRC [2009] EWHC 2563:

> "109 Examining individual transactions on their merits do 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.
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> 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.
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> 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."

19. The Appellant referred to the decisions of the European Court of Justice in *Mahegeben kft v Nemezeti Ado-es Vahmhivatal Del-dunatuli Regionalis Ado Foigazgatosaga* (C-80/11), and *Peter David v Nemezeti Ado es Vamhivital Eszak-alfodi Regionalis Ado Foigazgatosaga (*C-142/11). The Appellant accepted that these judgments did not make any direct change to the test laid down in Kittel and acknowledged the correctness of the conclusions reached by the First Tier Tribunal in S&I Electronics Ltd v HMRC [2013] UKFTT 296 (TC) on the effect of *Mahegeban* and *David*:

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[2] See *Mobilx para. 83.*

> "21….The measures the State could impose depended on the circumstances ([59]) and if there were indications of fraud ([60]) a trader could be required by the State to make further enquiries as a condition of getting his input VAT, but "as a general rule" ([61]) the State could not impose blanket due diligence requirements. Thus the formulation in the disposition "suspicion [of fraud] within the invoice issuer's sphere of activity" is not a recasting or refinement of Kittel, but the definition of a possible exception to the general rule precluding the imposition of due diligence tests.
>
> 22 Thus to my mind in neither its decision in *David* nor that in *Mahageben* did the CJEU intend to refine, limit or explain the knowledge test in *Kittel*, nor did its description of that test provide any new insight into it.
>
> 23 In my view *Kittel*, *Mahageben* and *David* indicate clearly that the relevant question is whether the trader knew or ought to have known (or should have known) that its transaction was connected with fraud by someone in the chain of supply."

20. The Appellant, however, relied on *Mahegeban* for its proposition that HMRC must adequately police the market to ensure that traders kept proper records and defaulters were pursued. According to the Appellant, HMRC acted unlawfully by effectively delegating its responsibility to police the market to exporters when it imposed a de facto blanket policy of denying exporters their input tax claims. The Appellant then appeared to link its proposition to its analysis of the facts which suggested that the prevalence of fraud in the mobile phone market at the time the Appellant was trading was so great that it was virtually impossible for an honest trader to avoid being caught up in a fraud.

21. The Tribunal agrees with HMRC that there was no evidence to substantiate a de facto blanket policy of denying input tax claims, and, in any event, the Appellant's assertion in this regard was irrelevant to the issue of knowledge. The Tribunal, however, considers the Appellant's analysis of the facts regarding the prevalence of fraud stands on its own, and may be a relevant factor when assessing the Appellant's knowledge.

22. The Tribunal is obliged to consider four questions in determining this Appeal, and answer them all in the affirmative if the Appellant is to be denied its right to repayment. The questions were approved in the High Court decision of *Blue Sphere Global Limited v HMRC* [2009] EWHC 1150. The four questions are:

(1) Was there a VAT loss?

(2) If so, was it occasioned by fraud?

(3) If so, were the Appellant's transactions connected with the fraudulent VAT loss?

(4) If so, did the Appellant know or should it have known of such a connection?

23. The Appellant accepted that HMRC had adduced evidence to substantiate affirmative answers to the first three questions. The sole issue in this dispute was whether the Appellant knew or should have known of the connection of its sixteen deals with fraud.

24. The individuals whose states of minds were attributable to the Appellant for the purposes of considering the issue of knowledge and means of knowledge were Mr Case and Mr Andrews. Mr Knifton who was a director with Mr Case had no involvement in the Appellant's deals in mobile phones. Mr Andrews was engaged as a consultant to the Appellant and played a major role in the conduct of the disputed deals. In the context of alleged Missing Trader frauds, the Upper Tribunal in *The Commissioners for HMRC v Greener Solutions* [2012] UKUT 18 (TCC) confirmed that an agent's knowledge of the fraud can be attributed to the company. The Appellant accepted that Mr Andrews' state of knowledge was central to its Appeal.

25. The Tribunal intends to summarise below the evidence in respect of the first three questions which were not disputed by the Appellant.

Was there a Tax Loss?

26. Each of the Appellant's 16 deals were traced to a tax loss occasioned by the following defaulting traders:

(1) **12/05 Deals 1, 2, 2b, 3:** ECS84.com Ltd which did not appeal an assessment £15.5million in unpaid VAT.

(2) **03/06 Deal 1:** Allied Jap Distributions Ltd which did not appeal an assessment of £914,568 in unpaid VAT.

(3) **03/06 Deals 2, 2b, 3, 4, 5:** Art Enterprise Ltd which did not appeal an assessment of £20.3 million in unpaid VAT.

(4) **03/06 Deals 6, 6b, 6c, 6d, 6e, 7, 7b:** Myco Telecom Ltd which did not appeal an assessment of £42.2 million in unpaid VAT.

(5) **03/06 Deal 8:** Puwar UK Ltd which did not appeal an assessment of £76 million in unpaid VAT.

(6) **03/06 Deal 9:** Aristaeus Ltd which did not appeal an assessment of £17.9 million in unpaid VAT.

(7) **03/06 Deal 10 &11:** K&S Xport Ltd which was compulsory wound up in respect of VAT debts owing to HMRC.

(8) **03/06 Deals 12&12b:** KSK Trading Ltd which did not appeal an assessment of £14.9 million in unpaid VAT.

(9) **06/06 Deal 1**: Apollo Communication Ltd which did not appeal an assessment of £51 million in unpaid VAT.

Was the Tax Loss Fraudulent?

27. The parties agreed a document entitled *Agreed Facts* comprising 111 paragraphs which sets out in detail the fraudulent nature of the tax losses occasioned by the defaulting traders[3]. The Tribunal does not intend to recite the contents of the document in the body of this decision. The Tribunal, however, incorporates the contents of that document as part of its decision.

Were the Appellant's 16 deals connected with the Fraudulent Tax Loss?

28. Officer Saunders traced back each of the Appellant's 16 deals to the defaulting trader identified above through a series of intermediate traders referred to as buffers. Officer Saunder's tracing exercise used material obtained from the Appellant and freight forwarders and involved the examination of deal listings and deal paperwork obtained or compiled by officers of HMRC from other traders. From his tracing exercise Officer Saunders compiled a deal sheet for each transaction.

29. In respect of 03/06 Deal 8, Officer Saunders initially traced the transaction chain back to the defaulting trader Ultimate Security Agency Ltd. Further analysis, prompted by the First Curacao International Bank FCIB evidence of Officer Japes, identified a further supply to the first line buffer trader (The Wireless Warehouse Ltd.) from another defaulting trader, Puwar Business Co-operation (UK) Ltd, although the buffer trader declared only one purchase. Officer Saunders identified Puwar as the defaulter in this chain, but it was clear that both purchases led to a fraudulent default.

30. Similarly, in respect of 03/06 Deal 6, Officer Saunders identified two possible supplies to the buffer trader, The Export Company Ltd. Both came from the buffer trader, Zeenom Trading Ltd, and both traced back through an additional buffer trader (Feathermore Trading Ltd.) to supplies from the same defaulting trader, Myco Telecom Ltd.

31. During the original hearing, the Appellant's previous representative challenged Officer Saunders' tracing exercise on the basis that, in some instances, the identified deal chains did not correspond with the money tracing exercise undertaken by Officer Japes in respect of the FCIB evidence. The Appellant's new representative did not pursue this point in its closing submissions and accepted the result of Officer Saunder's tracing exercise which was that each of the Appellant's 16 deals were connected with the fraudulent evasion of VAT.

32. The Tribunal agrees with HMRC's observation that an inconsistency between the *supply chain* as evidenced by commercial documents, and the *chain of money payments*, as evidenced by the FCIB material, was entirely common in, and consistent with, a scheme to defraud the Revenue. The VAT loss arose from the taxable supply, not the payment of money. The inconsistency between the two chains was generally a result of the appearance of third party payment in the *money chain.* The existence of

[3] The document was originally produced for the January 2012 hearing. The Appellant's new representatives subsequently agreed the contents of the document

such payments was a recognised feature in many MTIC fraud supply chains, and ensured that the defaulting trader did not have the funds to pay the VAT due on its supply.

Did the Appellant knew or should have known of the connection?

Outline Submissions

33. HMRC's primary assertion was that the Appellant had actual knowledge of a connection with fraud. In HMRC's view, the evidence clearly demonstrated that the Appellant's transactions formed part of an overall scheme to defraud the Revenue. According to HMRC, the scheme involved planning of the various deals with each party in the transaction chain knowing with whom it should trade. Such arrangements were not consistent with a legitimate market and had only one purpose, namely, defrauding the Revenue.

34. HMRC submitted the existence of an overall scheme to defraud carried the strong inference that the Appellant must have known of the connection of its deals with fraud. Further the Appellant performed a key role in the scheme by exporting the mobile phones and the scheme could not succeed without the Appellant's participation. HMRC relied on a wide range of objective factors derived from the evidence which in its view substantiated its assertion that the Appellant was an active and knowing participant in the fraudulent scheme.

35. HMRC in the alternative argued that the Appellant should have known of the connection of its transactions with fraud. In this respect HMRC contended that the alternative limbs of the *Kittel* test were not mutually inconsistent, and that there was an overlap in the evidence relied upon in respect of each limb.

36. The Appellant disagreed with HMRC's depiction of the overall scheme to defraud. In the Appellant's view, the evidence showed that the frauds in the Appellant's deal chains were organised in such a manner that they did not require the participation of the traders at the export end of the chain in order to be successful. In this respect the Appellant was inviting the Tribunal to draw the inference that alongside with the Revenue it was also a victim of the fraud.

37. The Appellant contended that the objective factors relied upon by HMRC to demonstrate knowledge did not come up to proof. The Appellant argued that there were inconsistencies in the evidence and insufficient regard had been given to the explanations of Mr Andrews and Mr Case.

38. The Appellant held similar concerns about HMRC's alternative case of constructive knowledge. The Appellant asserted that HMRC's case lacked clarity about what it might have discovered about the connection with fraud and what it left undone which would have revealed the existence of such a connection.

39. The Tribunal agrees with the Appellant's submission that the case turned on its own facts. Before the Tribunal embarks on its findings of fact in respect of knowledge

it is necessary to deal with two preliminary matters. The first concerns the weight to be attached to the evidence of Mr Fletcher and Officer Saunders. The second involves the issue of pleadings.

Preliminary Matters

40. The Tribunal said the following in respect of Officer Saunder's evidence in its interim decision released 3 May 2013 at paragraphs 51 and 52:

> "The Tribunal disagrees with the Appellant's assessment of Mr Saunders' evidence as statements of opinion. The Tribunal finds that Mr Saunders' testimony was predominantly factual which was relevant to the disputed issues. The Tribunal was satisfied of the admissibility of Mr Saunders' evidence.
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> The Tribunal acknowledges that Mr Saunders within his evidence made assertions that could be described as opinion or matters that were for the Tribunal to determine. The inclusion of such assertions in his statement did not justify the exclusion of the evidence. In the Tribunal's view, the assertions went to the probative worth of Mr Saunders' evidence"…..

41. The Appellant in its closing submissions repeated its assertion that a very large part of the evidence of the Officer Saunders was opinion evidence of the variety which the Officer was not qualified to give. The Appellant pointed out that Officer Saunders had no dealings with it and that he was parachuted in to deal with the Appellant upon the departure from HMRC of Officer Watson. The Appellant contended that Officer Saunder's evidence should be restricted to the formal production of documents. All other parts of his evidence, written and oral, were inadmissible opinion. Finally the Appellant asserted that Officer Saunders was simply following orders, and that his evidence was in effect replicating a pro-forma approach adopted in all cases involving allegations of MTIC fraud.

42. After making its overarching contention regarding the admissibility of Officer Saunders' evidence, the Appellant then cited specific aspects of his evidence upon which it relied or disagreed with. In this respect HMRC pointed out that the Appellant was itself seeking to rely repeatedly on opinions allegedly expressed by Officer Saunders.

43. The Tribunal maintains its position as expressed in its interim decision that Officer Saunders' testimony was predominantly factual. The preponderance of his evidence dealt with the tracing of the Appellant's deals, the contacts with HMRC and a description of enquiries made, and of various documents produced by the Appellant and other parties connected with the deals. The Appellant did not contest the tracing exercise conducted by Officer Saunders. The Tribunal has attached no weight to Officer Saunder's comments about whether specific facts were indicative of the Appellant's state of knowledge of the fraudulent connection. The Tribunal deals with particular aspects of Officer Saunder's evidence, such as cut outs, within the body of decision.

44. The Appellant stated that HMRC relied heavily on Mr Fletcher's evidence. The Appellant urged the Tribunal to treat his evidence with caution and to compare and contrast his experience as a trader in the market with that of Mr Andrews. HMRC devoted a considerable number of passages in its closing submissions to Mr Fletcher's evidence. HMRC, however, pointed out that it did this because of the approach adopted by the Appellant on the relevance of Mr Fletcher's evidence, which had consumed so much time in these proceedings. HMRC stated that it relied on Mr Fletcher's evidence but not heavily or lightly. According to HMRC, his evidence was one of the various strands of evidence which showed that the Appellant knew or should have known of the connection of its transactions with fraud.

45. The Tribunal in its interim decision released on 9 September 2013 ruled that Mr Fletcher's evidence was both admissible and relevant. The Tribunal observes that his evidence had two separate components. The first deals with his expert analysis of the grey market in the mobile phones. The second comprises his understanding of Nokia's wholesaling practices. The two components raise different questions in respect of the weight to be attached to his evidence. Mr Fletcher's analysis of the grey market depends upon the quality of his research and its appropriateness to the circumstances prevailing at the time the Appellant undertook its disputed transactions. Mr Fletcher's evidence on Nokia's practices was hearsay being based on conversations with key individuals, which in turn raised questions about its reliability.

46. The Tribunal found the Appellant's approach on the question of the weight to be attached to Mr Fletcher's evidence contradictory. The Appellant in its closing submissions as well as criticising Mr Fletcher's evidence relied on aspects of his evidence to substantiate its case. In view of the Appellant's approach, the Tribunal considers the best way to deal with the challenge on weight is on a piecemeal basis, as and when Mr Fletcher's evidence becomes an issue in the body of the decision.

47. The Appellant said that HMRC's pleadings in this Appeal were deficient in two material respects:

(1) HMRC relied on the same evidence in support of the two mutually exclusive alternatives of knowledge and should have known, which according to the Appellant, demonstrated an inherent weakness in HMRC's case. The Appellant argued that the alternative of constructive knowledge was not adequately pleaded and not put to the Appellant's witnesses in cross examination. The Appellant asserted that HMRC did not in its pleadings on constructive knowledge identify the means by which the connection with the fraud could have been discovered. Further HMRC did not put to Mr Andrews in cross-examination how he could have found out that his trades were connected to fraud. Given these circumstances the Appellant was of the view that it had not been given proper notice by HMRC of the case it faced.

(2) HMRC's allegation of fraud or dishonesty was not sufficiently particularised, in particular the facts relied upon by HMRC in its pleadings were consistent with the Appellant's innocence.

48. The Appellant cited various authorities in support of its propositions. Lord Millet in *Three Rivers DC & Ors v Governor and Company of the Bank of England* (No3) [2003] 2 AC encapsulated the Appellant's propositions when he said at paragraphs 183 and 184

> "Having read and re-read the pleadings, I remain of opinion that they are demurrable and could be struck out on this ground. The rules which govern both pleading and proving a case of fraud are very strict. In *Jonesco v Beard* [1930] AC 298 Lord Buckmaster, with whom the other members of the House concurred, said, at p 300:
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>> 'It has long been the settled practice of the court that the proper method of impeaching a completed judgment on the ground of fraud is by action in which, as in any other action based on fraud, the particulars of the fraud must be exactly given and the allegation established by the strict proof such a charge requires'.
>
> It is well established that fraud or dishonesty (and the same must go for the present tort) must be distinctly alleged and as distinctly proved; that it must be sufficiently particularised; and that it is not sufficiently particularised if the facts pleaded are consistent with innocence".

49. The Appellant also cited a passage from the judgment of Thesiger LJ in *Davy v Garrett* 7 Ch D 473, 489 which dealt with the rationale for the inadequacy of pleadings derived from facts consistent with innocence:

> "In the present case facts are alleged from which fraud might be inferred, but they are consistent with innocence. They were innocent acts in themselves, and it is not to be presumed that they were done with a fraudulent intent."

50. HMRC in response stated that that the Tribunal was not required to adopt the same course as the Civil Courts with regards to pleadings. Rule 25(2) of the Tribunal Procedure Rules 2009 sets out the requirements of a statement of case which of necessity is a summary of the evidence, and set out the essential propositions upon which HMRC relied to establish their case. HMRC had not departed from the propositions set out in its amended statement of case dated 14 February 2011. Further HMRC expanded upon these propositions in the statements of its witnesses and opening submissions. In this respect HMRC relied on the observations of Lord Woolf MR in *McPhilemy v Times Newspapers* [1999] 3 All ER 775:

> "The need for extensive pleadings including particulars should be reduced by the requirement that witness statements are now exchanged. In the majority of proceedings identification of the documents upon which a party relies, together with copies of that party's witness statements, will make the detail of the nature of the case the other side has to meet obvious. This reduces the need for particulars in order to avoid being taken by surprise. This does not mean that pleadings are now superfluous. Pleadings are still required to mark out the parameters of the case that is being advanced by each party. In particular they are still critical to identify the issues and the extent of the dispute between the parties. What is important is that the pleadings should make clear the general nature of the case of the

> pleader. This is true both under the old rules and the new rules. As well as their expense, excessive particulars can achieve directly the opposite result from that which is intended. They can obscure the issues rather than providing clarification. In addition, after disclosure and the exchange of witness statements pleadings frequently become of only historic interest."

51. HMRC asserted that its amended statement of case and opening submissions set out clearly the allegation in respect of the Appellant and the principal factors upon which it relied. The witness evidence supported and expanded upon this evidence. In HMRC's view the Appellant was left in no doubt as to the case against it and had ample opportunity to address it.

52. During closing submissions the parties referred to a recent decision of the Upper Tribunal in *Davis & Dann Limited v HMRC* [2013] UK UT 0374 (TCC) which discussed at paragraphs 47 and 48 the question of pleadings in the context of an alleged MTIC fraud.

> "Mr Kinnear's point illustrates, however, the importance of accurate pleading so that a party knows the case he has to answer and can ensure that the actual circumstances of the case are established by appropriate evidence. If the transaction is at a demonstrably low price (for which there would need to be evidence) that was then unexplained, an appropriate inference may be drawn; similarly, if the low price is explained but the explanation is not accepted or believed. Once the low price is satisfactorily explained, however, it may no longer be possible to draw that inference from the low price. The question that arises in relation to this is who must explain and what should the Tribunal say to demonstrate whether it has accepted or rejected the explanation.
>
> In this case HMRC have pleaded no wrongdoing in respect of Bristol and CEMSA and have made no disclosure in respect of them. If, for example, HMRC wanted the First-tier Tribunal to draw any inference adverse to the Appellants from the fact that Bristol sold the goods on credit terms to the Appellant then it would have been necessary for HMRC to plead that and to produce evidence in support".

53. The Tribunal finds that HMRC's amended statement of case dated 14 February 2011 and HMRC's outline submissions dated 5 January 2012 clearly alleged that the Appellant knew or should have known that the disputed deals were connected with the fraudulent evasion of VAT. HMRC in both documents supplied a detailed account of the primary objective facts upon which it relied to support its assertions about the Appellant's state of knowledge.

54. HMRC's outline submissions identified eleven sources of evidence with detailed explanation to substantiate the contrived nature of the Appellant's dealings, and an allegation of direct knowledge. The outline submissions then spent 35 paragraphs dealing with the evidence on constructive knowledge. In those 35 paragraphs HMRC was explicit about the alleged means by which the Appellant should have known of the connection of its deals with fraud.

55. The Tribunal considers that there will be an inevitable overlap in the evidence purportedly supporting the mutually exclusive states of direct and constructive knowledge. HMRC, however, in its outline submissions distinguished the facts relied upon to demonstrate its primary and alternative cases by placing a different emphasis on the factual matrix for each state of knowledge which was interpreted in accordance with the legal test for the respective knowledge states of either contrivance or the only reasonable explanation.

56. The Tribunal refutes the Appellant's assertion that Mr Andrews was not cross examined on HMRC's pleaded case. At the first hearing in January 2012 Mr Andrews spent three days in the witness box when HMRC's counsel went through HMRC's case in minute detail. At the recent hearing in September 2013 counsel with one exception which had no bearing on the question of pleadings challenged the extent of what Mr Andrews knew in relation to the individual deals.

57. The Tribunal is not convinced with the Appellant's contention that HMRC's case on constructive knowledge was derived from facts which were consistent with bona-fide trading. The Tribunal considers that the Appellant was confusing the question of pleadings with the legal test of only reasonable explanation to be applied once the Tribunal has determined the facts. In appeals of this nature the Appellant will inevitably challenge the facts relied upon by HMRC by offering a different explanation from that placed on the facts by HMRC. The mere fact that the evidence pleaded is capable of an alternative innocent explanation does not in the Tribunal's view undermine the integrity of the pleadings.

58. The Tribunal does not consider that the judgment in *Davis and Dann Limited* advances the Appellant's argument on pleadings. The Upper Tribunal has simply restated the law that HMRC cannot rely on facts which have not been pleaded. If the facts are pleaded then it is a matter for the Tribunal on the evidence to determine their probative worth.

59. The Tribunal concludes that HMRC's pleadings in this Appeal clearly alleged that the Appellant knew or should have known of the connection of the disputed transactions with the fraudulent evasion of fraud. The pleadings set out the primary facts relied upon by HMRC upon which to find an inference of the relevant state of knowledge. Finally the pleadings, particularly the outline submissions, distinguished the facts relied upon for each state of knowledge, which in turn defined the Appellant's extent of knowledge that HMRC intended to prove.

60. The Tribunal is, therefore, satisfied that there were not material irregularities in HMRC's pleadings. The Appellant would have been in no doubt as to the case it faced.

The Facts

61. The Tribunal intends to start its factual analysis with an examination of the competing interpretations of the fraudulent scheme of which the Appellant's disputed transactions were part. The Tribunal will then consider various aspects of the factual

matrix. Finally the Tribunal’s findings will be considered against the legal tests in order to reach a determination.

The Fraudulent Scheme

62. The Tribunal sets out below in the following paragraphs its findings in respect of the fraudulent scheme. The Tribunal begins with its findings on Officer Saunder’s analysis of the *supply chain*. The Appellant, on the whole, did not challenge the analysis of the chain outside its immediate supplier and customer because it said those parts of the chain were not within its knowledge. The Appellant, however, sought to undermine the inferences that HMRC drew from the analysis about its knowledge.

63. The 16 disputed deals happened in the period 2 December 2005 to 13 April 2006. They were all traced back to a defaulting trader. The Appellant accepted that the activities of the defaulting traders were fraudulent. All the defaulting traders have been assessed for significant sums of VAT. None of the assessments have been paid Five defaulting traders have gone missing. Of the remaining four the directors have received lengthy disqualifications in three companies, whilst the other has been wound up.

64. The deals involved the import of mobile phones into the UK to the defaulting trader with the mobile phone consignments then passing through various UK traders (referred to as buffers) before being exported by the Appellant back to the European Union (EU) or to Switzerland.

65. There appears to be no plausible commercial rationale for these deal chains involving the import of mobile phones from mainland Europe into the UK, and their almost immediate export back to mainland Europe. In the Tribunal’s view, the Appellant’s European customer could have sourced the phones from mainland Europe at a cheaper price and without the additional cost of transporting them from the UK.

66. None of the deal chains was traced back to a manufacturer or authorised distributor.

67. Sprint Communication Services Limited was the Appellant’s supplier in all but one of the disputed deals. 3G Trade SA was the Appellant’s customer in 11 of the deals with Unicell being the customer in four of the deals. In deal 8 03/06 Cybacomms UK acted as the Appellant’s supplier with Mobile World GBH as the EU customer. Between the period of 17 January to 13 April 2006 the Appellant dealt solely with Sprint and 3G Trade except deal 8 03/06.

68. The mobile phones in all of the Appellant’s disputed deals were traded down a lengthy UK deal chain in a short space of time, having only recently entered the UK from mainland Europe. The 16 deal chains were split equally between having seven and six members respectively starting with the defaulting trader and ending with the Appellant. The deal chains were not hierarchical. The more established, larger traders bought sometimes from smaller less well-established traders.

69. The deal chains involved 23 separate buffers. The Export Company had a presence in all the deal chains involving Sprint. Zeenom acted as a buffer in nine of the deals.

70. Of the 23 buffers the following companies have subsequently been deregistered as missing traders, or have had VAT returns reassessed through a failure to substantiate the claims, or assessments made following a failure to declare sales. Some also persisted in making third party payments despite warnings from HRMC as to the significance of such payments in the context of VAT fraud. The companies were:

(1) Direct Billing Limited which has an outstanding VAT payment of £25,000, and been involved in the making of third party payments resulting in a VAT tax loss of £5 million.

(2) Euro Imports and Exports Limited which was deregistered from 30 March 2006 and has outstanding assessments for unpaid VAT

(3) Feathermore Trading Limited which was now a missing company and has subsequently been deregistered.

(4) Frontflex Limited which was deregistered with effect from 10 February 2006 and has outstanding assessments for unpaid VAT.

(5) Seymour Selections Limited which was deregistered from 24 May 2006 and has outstanding assessments for unpaid VAT.

(6) The Wireless Warehouse Limited which was denied input tax of £2.2 million and was subsequently de-registered from 24 November 2006.

(7) Zeenom Trading Limited, which was a missing company with VAT debts of almost £5.8 million. The company was de-registered from 25 May 2008.

(8) Excelsior Enterprise whose company director was disqualified for 14 years in 2009.

(9) Exhibit Enterprise Limited which was denied input tax of £2.7 million. The company was placed into compulsory liquidation in March 2009. The Official Receiver has not lodged an appeal against the denial of input tax.

71. The following buffer companies have had their input tax claims denied with appeals pending or dismissed:

(1) Blue Wire Connections which was denied input tax of £2.8 million.

(2) JD Group Limited which was denied input tax of £2.1 million.

(3) London Mobile Communications Limited which was denied input tax of £4.3 million.

(4) Rigcharm Limited which was denied input tax of £2.7 million. Appeal was dismissed by the Tribunal.

(5) Top Telecoms Limited which was denied input tax of £1.3 million. The Tribunal struck out the Appeal.

(6) Trade 24/7 Limited which was denied input tax of £257K.

72. Thus of the 23 buffer companies involved in the Appellant's deals at least 15 have been implicated in some way to VAT fraud.

73. The Appellant's principal supplier, Sprint had its input tax claim of £2.5 million for periods 04/06, 05/06 and 06/06 denied. The First Tier Tribunal struck out its appeal against the denial of input tax because of Sprint's failure to comply with directions.

74. The Tribunal heard evidence from Ms Ravleen Sharma, a director of Sprint. Ms Sharma told the Tribunal that she had been informed in September 2005 and March 2006 that the supplies to Chandi Diwar Ltd (CDL) (Sprint's sister company) from the Export Company were connected with fraud. Ms Sharma said that she did not advise the Appellant of this fact. Ms Sharma stated that Sprint did not carry out IMEI checks because they were of no benefit to the company. The sister company, CDL, traded in mobile phones alongside Sprint from the same premises. The two companies had the same directors and the same customers, and did trades between themselves. Both companies traded with Cybacomms and 3G Trade which were the Appellant's other supplier and principal customer in the disputed deals. Sprint exported mobile phones as well as doing UK to UK trades. Sprint also exported goods to Switzerland which they stopped doing after being advised by HMRC of the risks of carousel fraud in respect of deals with Swiss companies.

75. The Tribunal considers that Ms Sharma's evidence gave a clear indication that Sprint was involved in questionable trading. Appellant's counsel did not demur from that conclusion when it was put to him by the Tribunal in closing submissions. Ms Sharma's evidence together with the striking out of Sprint's appeal against the denial of input tax constituted persuasive evidence of Sprint being knowingly involved in VAT fraud.

76. In the first quarter of 2006, the Appellant's other supplier, Cybacomms, sold in excess of £17 million of stock to 3G Trade which was the Appellant's principal customer in the disputed deals. Cybacomms also sold in excess of £6.9 million of stock to Mobile World which was the Appellant's customer in the only deal in which Cybacomms was its supplier.

77. CDL, the sister company of Sprint, sold in excess of £25 million of stock to 3G Trade in the first two quarters of 2006.

78. The Appellant's principal customer, 3G Trade, was therefore known to its two suppliers during the period in dispute. Those suppliers could have made considerably greater margins had they sold direct to 3G Trade which questioned their commercial rationale for selling to the Appellant.

79. During 2005 the export trade of mobile phones from the UK to Switzerland increased dramatically. As a result HMRC conducted extensive enquiries into the

export trade to Switzerland which revealed a circular trade in mobile phones. The mobile phones would return in a very short time to the UK after being despatched to Switzerland either directly to the UK or through a freight forwarder in France.

80. Officer Saunders identified circularity with the mobile phones sold to Unicell, a Swiss company, from the Appellant in the three deals in the 12/05 period. For example the stock sold in Deal 1 had been removed from Paul's Freight Services Ltd. on or around 2 December 2005 and carried to General Logistics Services AG in Basel. Within an hour the same goods in the quantity and at the same weight were consigned back to Paul's Freight Services in the UK.

81. HMRC adduced evidence to demonstrate that the Appellant's customer, Mobile World was involved in the carousel of mobile phones. Officer Saunders exhibited a spreadsheet prepared by Mr Stone which analysed Mobile World's deals in 2006. The spreadsheet showed that the mobile phones were often consigned back to the UK shortly after having been received by Mobile World.

82. In the specific deal involving Mobile World (Deal 8 03/06), the Appellant supplied Mobile World GMBH on 16 February 2006, shipping from Hawk Logistics. On the same day Mobile World sent the goods back to Hawk Logistics, releasing them to Universal Systems SCS, which in turn released them to the defaulting trader K&S Communications Ltd.

83. The Luxembourg authorities stated that the Appellant's principal customer, 3G Trade, fitted the profile of large scale carousel fraud with many of the goods it purchased from the UK being returned to freight warehouses in the UK. In respect of the Appellants deal in the 06/06 period the mobile phones were collected from Edge Logistics on 12 April 2006 for delivery to 3G Trade's warehouse in Luxembourg. On 13 April, 3G Trade sold the goods, with others, to International Mobile, an Italian trader, adding a £1 per phone mark-up. The goods were then consigned back to Paul's Freight in the UK.

84. The Tribunal is satisfied that all of the Appellant's customers during the period in question were engaged in the carousel of mobile phone consignments on a wide scale. The Tribunal finds that it was more probable than not that the overwhelming majority of the Appellant's phone consignments were returned to the UK shortly after being exported to the EU.

85. In deal 4 03/06 the 2,000 handsets sold to the Appellant by Sprint were part of a consignment of 3,150 handsets purchased by Top Telecoms which sold the remaining 1,150 to CDL, Sprint's sister company. CDL then sold them on to Data Select, which in turn sold them to 3G Trade, the Appellant's customer in deal 4. 3G Trade paid £4.50 per unit more for the handsets from the Appellant than it did for those from Data Select.

86. In deal 11 03/06 the Appellant purchased 6,199 handsets from Sprint and sold them to 3G Trade. The 6,199 handsets were part of a larger consignment from Rigcharm. Sprint sold 2,199 units from the same consignment to Data Select, which

also sold them to 3G Trade. 3G Trade again was willing to pay £8.00 per unit more for the handsets from the Appellant than it was for those from Data Select. The remaining part of the consignment were sold through Amnico to another Luxembourg trader, Westcomm SA.

87. The existence of split consignments in the deal chains which ultimately end up with the same EU trader which was prepared to pay significantly different prices for them was in the Tribunal's view an indication of the fraudulent nature of the arrangements. Mr Andrews, although he denied knowledge of what happened earlier in the supply chain, accepted in cross-examination that it was highly unlikely that split deals would happen in an honest market.

88. A large number of the traders in the Appellant's disputed deal chains had accounts at FCIB, a bank based in the Netherlands Antilles until October 2006 when its banking licence was withdrawn and administrators were appointed. The Dutch authorities investigating its activities seized the bank's Dutch computer server, and the data it contained was later made available to the UK authorities. Subsequently the bank's Paris server was also made available, which provided further detail in respect of transactions, and in particular the narrative entries accompanying the transactions, as entered by the account holders.

89. The Appellant and its principal supplier, Sprint, did not have accounts with FCIB unlike the Appellant's customers which all held FCIB accounts during the relevant period.

90. Officer Japes analysed the relevant account data in respect of these deal chains. By comparing the amounts in the Appellant's National Westminster trading account with the date and value of the Appellant's sales and purchase invoices, he identified the Appellant's receipts and payments in relation to the disputed deals. Officer Japes then traced those funds to the accounts of the Appellant's customers and suppliers respectively, continuing where possible to show each payment / transaction in the chain until the payments returned to the initial company that had commenced the transaction. Most of the tracing involved FCIB accounts, but some traders used accounts at other banks.

91. According to HMRC, Mr Japes' exercise revealed circularity of funds in respect of the participating companies in all but two of the deals (deal 3 12/05 & deal 8 03/06). The Appellant disagreed stating that it was prepared to concede that circularity of funds was present only in deals 5 and 7 of 03/06 and, possibly, deal 1 of 04/06.

92. HMRC objected to the Appellant's submission that circularity of funds was present in only three deals. HMRC pointed out that the Appellant had not cross-examined Officer Japes on his evidence on circularity of funds. In those circumstances HMRC argued that the Appellant was not entitled to impugn Officer Japes' evidence. The Appellant retorted that its new representatives had not had the opportunity to put questions to Officer Japes. Further the Appellant contended that the question of whether the fund movements were circular was a matter of opinion and

not evidence. In which case the Appellant was entitled to venture an interpretation of the evidence in its closing submissions.

93. Officer Japes in his first witness statement dated 6 July 2010 identified eight deals where he said there was circularity of funds (deal 1, 12/05, deals 1, 4, 5, 6, 7 & 11, 03/06 and deal 1, 06/06). In his second witness statement dated 7 October 2011 Officer Japes revisited his initial analysis in the light of the additional information supplied by the Paris server. Officer Japes on the whole confirmed his original analysis, and did not give a different view on the number of deals affected by circularity of funds as stated in his first witness statement.

94. HMRC was in effect replicating the approach adopted by the Appellant towards Officer Jape's evidence by placing its own interpretation on the analysis of money movements. In those circumstances the Tribunal is not impressed with HMRC's objection to the Appellant's contention that it was entitled to form its own view on whether circularity existed.

95. In the Tribunal's view, the critical question is which of the two interpretations was correct. The Tribunal considers that the parties were approaching the issue of circularity from different standpoints. The Appellant adopted a strict stance by identifying circularity only when the money flows comprised effectively the same amount going round. HMRC, on the other hand, concentrated on the overall direction of the money flows.

96. HMRC recognised that it was not always possible to identify the sums of money, which exactly matched those shown on the invoices. In some instances there was more than one payment from one trader to another. In others the amount of the payment shown on the statement differed from the invoiced amount owing to the addition or deduction of transaction charges. Finally in a number of instances, individual payments made by participating traders were funded from other sources, in the sense that the credit balance in the trader's bank account at the time of a given payment arose as a result of a previous credit from a separate transaction which was not part of the chain of payments.

97. The Tribunal prefers the approach adopted by HMRC. In the Tribunal's view what counts is the overall direction of the funds provided there was a strong connection with the invoiced deal chains. With this in mind the Tribunal has carried out its own analysis of Officer Japes' evidence which was summarised in diagrammatic form for each deal. On the whole the Tribunal agrees with HMRC's interpretation that 14 deals were characterised by circular money flows with the caveat that deals 3 and 9 of 3/06 were not completely circular in that the money flow ended with the Appellant's customer for the next deal. A better description for these two deals would be a spiral rather than a circle.

98. The presence of circular movements in the overwhelming majority of the Appellant's deal chains cast further doubts on the commerciality of the deals. In the Tribunal's view the circular movements were a strong indication of the contrived nature of the transactions.

99. Officer Japes' tracing exercise uncovered the participation of a number of companies not apparent within the deal chains as traced on the available commercial documentation. Two of those companies were previously UK VAT registered but had been deregistered, one (Elanex Marketing) as a missing trader, and the other (A-Z Office Equipment) because it failed to provide evidence of the existence of the goods in which it purportedly traded.

100. Officer Japes' evidence also revealed that some accounts within the chains were held in the name of third parties. For example, the Elanex 02 account was held in the name Pak Shine, an EU company that appeared as an EU supplier in the deal chain documentation for some of the chains. This suggested that the same individual or individuals had control of a number of participating companies in the scheme and that those participants were included in the chains in order to mask their true nature.

101. Third party payment instructions to other EU traders were identified in each of the disputed deal chains. Pak Shine featured as third party recipient in eight of the deals with Westcomm and Sweetstorm each appearing as a recipient in four deals.

102. In 13 of the 16 deals third party payments were made to one of the following companies: Sweetstorm, Technology PLC and International Mobiles. Mr Vito Cardinale was a signatory of three of the four companies (not Technology PLC). Mr Sajeed Sadiq was a named signatory of three companies (excluding International Mobiles). Thus in 13 deals the third party payments went to the same individuals.

103. Deals 1, 2, 3 (12/05) and 2, 3, 5 (03/06) Sunico were a named party on the third party payment instructions but the payments actually went to Pak Shine, Westcom and Trading House.

104. Third party payments provided the means by which the output VAT which should ordinarily be accounted for on acquisition was expropriated. The payments starved the defaulting trader of funds with which to pay the VAT liability. The use of third party payments in each disputed deal was another indicator of the contrived and orchestrated nature of the transactions.

105. The margins achieved by the buffer traders on the individual handsets in the deals were small and generally of consistent amounts ranging from 25p to 50p Likewise the Appellant's principal supplier, Sprint, achieved either £1 or £2 except on transactions 6 and 6b 03/06 when mark ups of £3 and £4 were respectively secured. Cybacomms in deal 8 03/06 charged a £1.50 mark up.

106. The Appellant's margin was considerably more than the other traders in the deal chains ranging from £11 to £42 per handset. The mark ups for all deals except one were in the range 6.9% to 8.1%. The mark ups for 13 of the deals were in the range of 7.5% to 8.1%. One deal (08; 03/06) had a mark up of 3.8% which was considerably lower than the others.

107. Mr Andrews did not recognise the term "mark up". Mr Andrews stated that the low mark up for deal 8 was a commercial decision.

108. The Appellant pointed out that Mr Fletcher and Officer Saunders were unable to give evidence of what a reasonable mark up would look like. Mr Fletcher said that he did not know the usual mark up for an exporter in the mobile phone market in 2006. Officer Saunders stated that he was not qualified to give such an opinion. He also stated that he had seen wide ranging profit margins for deals connected with MTIC fraud.

109. The Appellant contended that HMRC was unable to provide a proper basis for comparison of mark up. In the Appellant's view, it was crucial for HMRC to adduce evidence of a baseline of what a proper mark up on a deal unconnected with fraud should be in order to draw an inference about there being something unusual or 'contrived' about the Appellant's profits or mark ups.

110. The Tribunal at the moment is considering the overall nature of the fraudulent scheme rather than addressing the specific issue of what the Appellant knew. Leaving aside the question of the margins achieved by the Appellant, the Tribunal finds the pattern of the margins achieved by the buffer traders and the Appellant's suppliers strikingly uniform, involving similar whole number amounts for a wide range of handsets. The question for the Tribunal is whether this uniformity was consistent with a market where both suppliers and customers were seeking the best prices for their deals. The Tribunal thinks not. In this respect the Tribunal's conclusion was supported by Mr Andrews' testimony of what he perceived to be the market in mobile phones in 2006[4].

111. The Tribunal does not agree with the Appellant's submission that HMRC has not provided a baseline for assessing the level of mark ups achieved by the Appellant. HMRC was relying on a relative baseline rather than an absolute one. The question posed by HMRC concerned the justification for the high level margin or mark up achieved by the Appellant in comparison with the other traders in the deal chains. The Tribunal will consider this question further on in the decision.

112. The matter that the Tribunal is deciding at this stage is the character of the fraudulent scheme. The Appellant accepted that there was a fraudulent scheme but that it was restricted to the acquisition end of the deal chains. HMRC, on the hand, argued that the scheme was more pervasive and involved the carousel of mobile phones. The distinction between the parties' conceptualisation of the scheme is significant in respect of the inferences to be drawn on the Appellant's knowledge. The potential inferences are not decisive and would need to be tested against the other evidence relied upon.

113. HMRC's position was that the whole scheme was planned with each party knowing with whom it should trade in respect of given consignments of mobile phones. HMRC's position carried the inference that within such a scheme it was very difficult for the Appellant to claim it was an innocent dupe. The Appellant played the key role of exporter and must have known that the transactions were connected with fraud.

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[4] See Transcript 10.9.2013 para. 13 to 3 pages 115 & 116.

114. The Appellant's position was that the success of the fraudulent scheme did not depend upon the participation of those traders further down the deal chains. The fraudsters had secured their ill-gotten gains when the defaulting trader did not meet its VAT liabilities. The inference to be drawn from the Appellant's position was that its trades alongside those of other traders had inadvertently been tainted with a fraud in which they played no part.

115. Although the Appellant expressed reservations about the nomenclature for the competing positions, the Tribunal intends to use the labels of acquisition fraudulent scheme (Appellant's position) and carousel fraudulent scheme (HMRC's position) to distinguish the parties' respective positions.

116. The Appellant argued that there were a very large number of parties involved in the disputed deal chains, which on its conservative estimate was in the region of 56 legal persons. In the Appellant's view, it was inherently unlikely for all those parties to be involved in the fraud. The Appellant stated that there was some evidence from Officer Japes of connections between those said to be trading in the chains at all points before the third party payer. There was, however, no evidence of connection further along the chain in the direction of the exporting broker.

117. The Appellant submitted that it was difficult to imagine how it would be possible to orchestrate a fraud involving unconnected parties in the chains of supply without any instance of a 'weak link' materialising amongst those who must, according to HMRC's position, have apparently fully collaborated with each other in order to make the fraud work. In the Appellant's view, it was much more likely that the frauds were organised without the involvement of those at the broker end of the chain. According to the Appellant, all that was required by an European based fraudster was a UK missing trader, and a UK third party payer. Once the goods were discounted by the value of the stolen VAT it was an easy task to find a UK buyer who because of the de facto discount brought about by the theft of the VAT would have a ready market into the EU.

118. The Appellant referred to the contents of a detailed letter dated 8 April 2013 sent to HMRC and the Tribunal where it set out its analysis of the perpetrators of the fraud. In that letter the Appellant referred to High Court proceedings taken by HMRC where it alleged that Sunico A/S and various connected individuals were involved in a substantial VAT fraud during the relevant period in the UK. In the High Court writ HMRC pleaded that Sunico were behind in excess of 700 fraudulent transactions in the period 2004 to January 2006.

119. The letter also identified that Sunico was a named party on third party instructions in this Appeal, and that Sunico had connections with other third party recipients, most notably Pak Shine.

120. The Judgement of Mrs Justice Proudman was handed down on the 19 April 2013 (*HMRC v Sunico A/S* [2013] EWHC 941 (ch)) which made a clear finding that Sunico was party to a fraudulent conspiracy.

121. The Appellant submitted on the evidence that it was a reasonable conclusion that an European business, Sunico S/A, was the principal beneficiary and originator of the fraud. Further there was no evidence of trading links between the Appellant and Sunico.

122. The Appellant pointed out that in the letter dated 8 April 2013 it asked HMRC to make clear whether and to what extent the allegation it levelled at the Appellant involved an allegation of fraud against a business referred to in the evidence as Sunico A/S (Sunico). Despite the request for clarification no clear case has been pleaded in respect of Sunico. According to the Appellant, HMRC has repeatedly stated that as a matter of law it need not particularise the nature of the fraud alleged. The Appellant considers HMRC's approach hypocritical particularly in view of its intention to rely upon Mr Andrews' admission that he knew, Mr Sunil Harwani, the director of Sunico from his trading in mobile phones. In the Appellant's view, HMRC was attempting to have its cake and eat it, which should not be allowed in the absence of a pleaded case on the involvement of Sunico in the fraud.

123. Turning first to the substantive issue of whether the fraudulent scheme is to be characterised as an acquisition or carousel fraud, HMRC made a telling observation that acquisition fraud was unlikely to be successful on a wide-scale because the perpetrators would run out of mobile phone consignments. According to HMRC, MTIC fraud depended upon a guaranteed supply of goods which was achieved by the carousel of the same mobile phone consignments.

124. The critical consideration, however, for the Tribunal is not the efficacy of acquisition fraud but whether the Appellant's description of the fraudulent scheme was supported by the evidence. The Tribunal's findings on the fraudulent scheme as set out in paragraphs 62 to 111 above are resoundingly against the Appellant.

125. The Tribunal's findings demonstrated that fraud was rife throughout the deal chains, and not restricted to the defaulting trader and the third party recipient. At least 15 of the 23 buffer traders were implicated in some way with VAT fraud. The Tribunal was satisfied on the balance of probabilities that the Appellant's principal supplier, Sprint, and its three customers, Unicell, 3G Trade and Mobile World were active participants in the fraud. In the Tribunal's view, the evidence demonstrated that the Appellant's customers were involved in the carousel of mobile phones back to the UK.

126. The findings showed there was no commercial rationale for the deal chains. They were unduly long and involved the import and export of goods which could be sold more profitably if they had remained in the European mainland. The findings on missing traders, third party payments, uniform mark ups, split deals, circularity of money flows, and carousel of mobile phone consignments demonstrated that the scheme was highly orchestrated and contrived.

127. The Tribunal is, therefore, satisfied that the fraudulent scheme matched HMRC's description of a carousel scheme. The Tribunal has already stated that the inference from such a scheme of each party carrying out a specific role is not decisive

in determining the Appellant's state of knowledge, and has to be tested against the rest of the evidence. The Appellant denied that it had knowledge of the wider scheme. The Appellant asserted that its knowledge should be judged on its dealings with its suppliers and customers.

128. There are various aspects to the questions raised by the Appellant in respect of the alleged involvement of Sunico.

129. First, the Tribunal agrees with HMRC that it cannot be expected to know precisely how the fraud was organised (see *Megtian Ltd v HMRC* [2010] EWHC 18 (Ch), per Briggs J). HMRC have always maintained that the Appellant's transactions formed part of an overall scheme to defraud. The applicable legal test, however, did not require HMRC to prove that the Appellant knew the identity of any of those responsible for orchestrating the fraud.

130. Second, contrary to the Appellant's assertions, HMRC have not placed weight on the role of Sunico in the fraud. Sunico did not feature in HMRC's outline submissions, and its appearance in the evidence was restricted to being a named party on some third party payment instructions. HMRC's cross-examination of the Appellant's witnesses on Sunico was limited, and principally in response to Mr Andrew's evidence on his knowledge of Sunico in his second witness statement.

131. Finally the Tribunal does not consider that HMRC was having its cake and eating it. HMRC was not placing significant reliance on Mr Andrews' relationship with Mr Harwani in respect of the Appellant's state of knowledge. HMRC's closing submissions were restricted to the observation that the Tribunal was entitled to note that Mr Andrews in fact knew, and had traded with Sunico previously, but seemed to have avoided them when trading on behalf of the Appellant. HMRC also considered Mr Andrews' knowledge of Sunico relevant in the context of the Appellant's potential trade with authorised distributors.

The Appellant's Knowledge of MTIC Fraud and its contact with HMRC

132. Mr Case started his first business in the early 1980s, with The Television Parlour and Network Video which he built up to become a chain of 20 shops competing with Dixons and Currys. His business ventures brought him into contact with the international market in electrical goods including the grey market. From 1986 Mr Case also sold mobile phones mainly through mail order under the company banner of KJC Limited. Mr Case eventually sold Network Video to the Blockbuster chain, and KJC Limited to the Appellant.

133. Mr Andrews had been in the mobile phone industry since 1994. At that time he worked for UniqueAir Limited which was a thriving mobile phone distribution company and also a service provider. Mr Andrews then moved on to work as Sales Director for 20/20 Logistics which was part of the Caudwell Group, widely regarded as the leading distributor of mobile phones in the UK. In 2000 former senior managers of UniqueAir invited Mr Andrews to join them in launching a new company, Unique Distribution which grew rapidly into a leading mobile phone

distributor with an extensive wholesale mobile telephone trading operation. Unfortunately in April 2005 Unique Distribution went into administration when its major funder decided to withdraw from the mobile telecommunications industry.

134. In 2002 HMRC assessed Unique Distribution for unpaid VAT in relation to sales to a company known as Total Telecom. In June 2004 HMRC refused to repay Unique Distribution VAT arising from mobile phone transactions which HMRC said constituted non-economic activities. Mr Andrews asserted that he did not know of HMRC's interest in Unique Distribution. According to Mr Andrews, he left the grey market team for Unique Distribution in mid-2002, and returned to it in 2005.

135. HMRC did not accept Mr Andrews' assertion that he was unaware that Unique Distribution had been involved in circular deal chains and chains connecting to defaulting traders. HMRC pointed out that as this information was a shock to Unique Distribution it would be remarkable that someone of Mr Andrews' seniority would have been unaware of something this significant.

136. Mr Case acknowledged there was fraud in the wholesale mobile phone industry which was facilitated by a VAT system across Europe. Mr Case pointed out that the Appellant had its own capital funding and was not reliant on VAT repayments to fund its operations.

137. Mr Andrews said that when he joined the Appellant he was conscious of the difficulties of fraud in the wholesale market for mobile phones. Mr Andrews, however, pointed out he had a good understanding of the precautions that should be taken to protect against fraud and of the requirements of Customs Notice 726.

138. Mr Andrews was a member of the steering group comprising representatives of the mobile phone wholesalers and HMRC which was set up to improve relations between themselves and address issues arising from missing trader fraud. Further Mr Andrews stated that he was involved in drawing up the Memorandum of Understanding on tackling fraud between HM Customs and Excise and the mobile phone industry.

139. Mr Andrews asserted that at the time of the disputed deals he did not know the extent of the fraud in mobile phone wholesale sector. Mr Andrews pointed out there were 3,000 traders in this sector, the Appellant was dealing with six of them. As far as Mr Andrews was concerned he picked the best but they all let him down. Mr Andrews with hindsight considered that the Appellant was a victim of widespread fraud.

140. Officer Stone stated the market in mobile phones reduced dramatically from June 2006 following the introduction of extended verification. When the reverse charge mechanism was introduced in June 2007 only one in 1,000 mobile telephone traders continued to trade.

141. Between June 2005 and February 2006, HMRC officers had regular contact with the Appellant when MTIC fraud was discussed, and in which Messrs Case and Andrews' understanding of the issues was confirmed.

142. On 27 June 2005 the HMRC sent the Appellant a copy of VAT Notice 726 (Joint and Several Liability).

143. On 13 July 2005 HMRC carried out an unannounced visit on the Appellant. At that meeting Mr Case stated that the Appellant was interested in electrical goods and would deal with any items should the opportunity arose. Mr Case suggested that a large number of suppliers and freight forwarders were used. HMRC officers stressed the importance of due diligence and the risks of involvement in MTIC chains.

144. On 1 August 2005 HMRC conducted another visit on the Appellant and took the records relating to the 06/05 period. The mainstay of the Appellant's repayment claim was down to two deals involving the sales of mobile phones to Ireland which had been purchased in the UK from Wizard Trading (Europe).

145. In the first instance HMRC received little information from the Appellant on due diligence checks undertaken. The Appellant supplied further information, the majority of which had been compiled after the event. In a letter dated 12 August 2005 Officer Watson recommended that the Appellant verify VAT registration numbers via the HMRC Redhill office prior to instigating transactions. Officer Watson also referred the Appellant to examples of due diligence checks set out in Notice 726.

146. On 18 August 2005 HMRC held another meeting with the Appellant at which Mr Case, Mr Andrews and the Appellant's accountant were present. The notes of the meeting showed that the Appellant's market research was based on its experience of the trade. The Appellant did not then do credit-checks on the companies with which it traded. Mr Andrews doubted the value of such checks as they were historical. Instead Mr Andrews and Mr Case preferred to rely upon their personal knowledge of the companies and whether they had met their debts in the past.

147. On 18 August 2005 the Appellant explained that prices were negotiated hard on each deal. In the Appellant's view, it was commercially viable for the price of goods to increase a number of times within the short duration of a supply chain because of fluctuations in the market. The Appellant did not carry out checks of the freight forwarders because they had been in business for a length of time. Mr Andrews also pointed out that whilst he was at Unique Distribution insurance companies would carry out audits of the freight forwarders.

148. On 26 August 2005 HMRC sent the Appellant Notice 700/52 (Notice of requirement to give security) and the Statement of Practice concerning invalid invoices.

149. On 7 October 2005 HMRC wrote to the Company's accountant seeking further information including details of due diligence checks undertaken. HMRC pointed out that a Redhill check had been made after a deal had been concluded, and that there was little point in undertaking due diligence checks if the outcome of those checks was to be disregarded.

150. On 26 October 2005 HMRC wrote again to the Appellant's accountant setting out its concerns about the adequacy of the due diligence checks. HMRC also

questioned why the specification of some mobile phones in a particular deal had been changed between purchase and sale, of which no mention had been made on the purchase invoice.

151. On 22 November 2005 HMRC informed the Appellant that it refused on review the Appellant's request to move to monthly VAT returns. HMRC also told the Appellant that two of its deals in the 06/05 period were linked to defaulting traders.

152. On 29 November 2005 HMRC held another meeting at the Appellant's premises. Messrs Andrews and Case were both present. Due diligence checks were again discussed, and it was recommended that Dun and Bradstreet checks were undertaken, and enquiries made of the freight forwarders as to how long goods had been on their premises and the number of times the goods had been traded since arriving in the warehouse. HMRC pointed out[5] that a typical feature of supply chains involved in VAT fraud was that ownership of goods changed rapidly whilst in the same freight forwarders' premises. According to HMRC, the length of time in the premises and the frequency of change in ownership were good indications of the likely presence of fraud. Mr Case agreed that such checks would be undertaken, which was confirmed in a letter from the Appellant dated 5 December 2005.

153. At the Appellant's request, HMRC informed it of the two particular deals which wer related to defaulting traders. HMRC said that they were two supplies to BPI in Ireland at the very end of the June quarter. The notes for the meeting on 21 November 2005 recorded that Officer Watson stated that from memory he told the Appellant of the identity of the Appellant's immediate supplier in these deals. Mr Case asked if HMRC had any particular concerns about the particular supplier in these deals (*Wizard)* with which he had a long business relationship. HMRC advised that it could not disclose details of other registered businesses nor confirm that the businesses were legitimate.

154. On 3 February 2006 HMRC wrote to the Appellant regarding its VAT return for the period ending 12/05. In the letter HMRC questioned the accuracy of the Appellant's letter of introduction regarding its years of trading in the mobile phone industry. Further HMRC identified discrepancies in the stock inspection reports on hardware and software issues, manuals and warranties.

155. On 16 February 2006 HMRC advised the Appellant that, of the 19 transactions verified for the 09/05 claim, 11 commenced with defaulting traders resulting in the loss to the Revenue of £753,587.59. HMRC supplied full details of those sales which included the name of the customer but not that of the supplier. HMRC also supplied details of the two suspect transactions in the 06/05 claim.

156. On 23 February 2006 HMRC advised that the number of questionable deals in the 09/05 quarter had increased to 12 with the loss to the Revenue rising to £811,098.99. On 24 February 2006 HMRC notified the Appellant of a further increase

[5] In the follow up letter of 1 December 2005.

of transactions connected to a defaulting trader in the 09/05 quarter to 13. This deal involved the Appellant's supplier, Cybacomms.

157. After he received the letters informing the Appellant of the connections with the defaulting traders, Mr Andrews stated the Appellant had been wrong with its assumption of trusting suppliers because of his and Mr Case's long association with them. Mr Andrews also believed that the due diligence done by the Appellant was not good enough[6]. Mr Andrews, however, was prepared to do a deal with Wizard in February 2006 because HMRC had not confirmed conclusively that Wizard had been involved in suspect transactions.

158. Mr Case found HMRC's response obstructive[7]. According to Mr Case, HMRC was not prepared to disclose details of the suppliers to the Appellant's suppliers. Mr Case stated that Wizard and Cybacomms were still trading which brought into question the validity of HMRC's criticisms of the Appellant's transactions. Mr Case pointed out that in any event the Appellant had stopped dealing with Wizard and Cybacomms.

159. The Tribunal makes the following findings of fact:

> (1) The incidence of fraud in the mobile telephone wholesale market was rife during the period of the Appellant's trading.
>
> (2) Mr Andrews and Mr Case were aware of the risks of fraud when the Appellant entered the market in 2005. They both had extensive experience of the trade. Although Mr Andrews denied knowledge of the specific instance when Unique Distribution was refused input tax because of the connection of its trades with circular deals, the Tribunal is satisfied that a person of his seniority would have known at the time about HMRC's concerns with the legitimacy of mobile phone trading as a whole. It is no coincidence that the Appellant's entry in the market was after the European Court judgment in *Bond House*
>
> (3) Although Mr Andrews stated that he did not know the extent of the fraud in the market back in 2005 and 2006, the Appellant knew from 22 November 2005 that two of its deals in the 06/05 period were contaminated with fraud. On or around the 16 February 2006 the Appellant knew that the majority of its deals in the 09/05 period had been traced back to defaulting traders. After 16 February 2006 the Appellant still carried out five more deals.
>
> (4) Throughout the period July 2005 to February 2006 HMRC advised the Appellant of the risks of fraud and ensured that Mr Andrews and Mr Case understood the risks. Officer Watson, during this period, carried out a thorough analysis of the Appellant's trading practices, and gave repeated and explicit warnings about inadequacies in the Appellant's due diligence.

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[6] See Transcript 24 January 2012 page 178 20-23.

[7] For example see Transcript 27 January 2012 page 48 paras 15-25.

(5) The Appellant stated that it followed Mr Watson's advice despite reservations about his approach. The Tribunal, however, observes that on 3 February 2006 Mr Watson was still raising real concerns about discrepancies in the stock inspections reports for the Appellant's deals.

(6) Mr Case asserted that the Appellant stopped dealing with certain suppliers because of warnings given by HMRC. The timelines for the Appellant's changes in suppliers: Wizard[8] and Aircall (27 June to 22 August 2005), MNR (2 to 15 September 2005), Cybacomms[9] (22 September to 8 November 2005) and Sprint from 23 November 2005 did not correspond with the dates of HMRC's warnings about contaminated trades.

(7) The Appellant was aware of and alive to potential indicators of fraud well before the commencement of the disputed deals**.**

The Appellant's Trading Operations

160. From 27 June 2005 to 12 April 2006 the Appellant concluded 55 export deals in mobile phones and two UK deals[10]. The latter involved the sale of 250 prepaid mobile phones to Recycled 4U purchased from Unique on 27 June 2005, and on 13 July 2005 the sale of 100 Nokia 8800 mobile phones with full English specification manual to Frequency 3G at £470 per handset. The Nokia 8800 were purchased from Brightpoint International, (BPI (Ireland)), at £465 per handset.

161. The 55 export deals involved five different suppliers: Wizard, Aircall (2 deals), MNR (4 deals), Cybacomms and Sprint, and six different customers: BPI (Ireland), Mobile World (Germany), France Affairs (France), LPDC (France), Unicell (Switzerland) and 3G Trade (Luxembourg). From 22 September 2005 37 deals were concluded with Cybacomms and Sprint being the only suppliers, and with Unicell and 3G Trade being the only customers except for one deal involving Mobile World. In respect of the 16 disputed deals Sprint was the supplier in all but one, and 3G Trade was the customer in 12 of the deals. From 17 January 2006 to 13 April 2006 all deals involving Sprint as the supplier had 3G Trade as the customer.

162. Mr Andrews stated that the key to avoiding fraudsters was for the Appellant to know exactly with whom it was dealing. Messrs Case and Andrews decided to trade only with parties known to them.

163. Mr Case stated that the Appellant operated in the grey market which according to him was a perfectly lawful activity. According to Mr Case, the grey market referred to trade in goods acquired outside the normal distribution channels by manufacturers. Mr Case asserted that the factory imposed price differences between markets could never precisely match the actual demand in that market to which goods were assigned in the first instance by the manufacturer. Mr Case stated that with free title and

[8] Wizard was the supplier in the aborted deal with Mobile World in February 2006.

[9] The Appellant did one further deal with Cybacomms on 16 February 2006.

[10] On the Appellant's schedule four of those deals were split deals 1, 3, 7 and 9.

movement, goods could readily be bought and sold at a profit in a market with a shortage.

164. Mr Andrews stated that the Appellant concentrated on sourcing mobile phones from within the UK for sale to customers in Europe. The reason for adopting this business was that UK was the leading mobile phone market in Europe. This meant that prices were lower in the UK which created the opportunity for making profitable sales to other European countries. Mr Andrews asserted that a drop in the price charged by manufacturers for mobile phones was not always reflected in an equivalent drop in price in other European countries.

165. According to Mr Andrews, the task of the Appellant was to tease out stock. Mr Andrews asserted that the Appellant conducted real business in real goods which were physically inspected and carried to the customer.

166. Mr Andrews disagreed with the premise that Nokia’s pricing policy limited trading opportunities for the Appellant. In Mr Andrew’s view such a premise ignored the reality of what an authorised distributor may do in practice to sell their stocks.

167. Mr Andrews pointed out that he had been a salesman in the wholesaling of mobile phones for most of his adult life. He knew that sales teams in this industry were expected to sell hard, which was why the grey market did so well. Mr Andrews considered the grey market to be a tough place to earn a living but the mobile phone boom created really exceptional opportunities for profit.

168. Mr Andrews stated that authorised distributors were reluctant to deal with the Appellant because it was newly back in a crowded market. The Appellant did not have the necessary track record to open an account with an authorised distributor.

169. Mr Andrews had hoped to turn the Appellant into a real market player after several years and for it to operate as an authorised distributor.

170. Mr Andrews’ agreement with the Appellant and Mr Case was that he would get commission of 35 per cent on gross profit. Mr Andrews received commission totalling £494,668.26 for the deals he set up between 3 October 2005 and 14 March 2006. According to Mr Andrews, he had been offered more by other companies but preferred to work for the Appellant for a variety of reasons. Mr Andrews acknowledged the commission was a substantial sum of money but at one time in his career he had eight traders working for him and was aware of the huge sums of monies that could be earned. He cited an example of one trader at Unique Distribution earning about £40,000 a month. Mr Andrews stated that his annual salary at Unique was about £60,000 to £70,000 and around £120,000 at Cauldwell.

171. Mr Case disagreed with HMRC’s assertion that all Mr Andrews did was to make a few phone calls to trusted customers and suppliers. According to Mr Case, there was a lot of paperwork to do which was why he had his daughter and Mr Andrew’s wife to assist Mr Andrews. Mr Case did not accept that the commercial documentation was fairly straightforward. Mr Case disagreed that Mr Andrew’s pay

was excessive. He pointed out that when the mobile phone business first started there was one company where the profit shared between partners exceeded £750,000.

172. Mr Case accepted that he had invested in Unistar which was a competitor to the Appellant in the wholesale trading of mobile phones. Likewise Peter Scrancher, a director of Deluni Mobile, another competitor, had invested in the Appellant. Mr Case saw no inconsistency of competitors investing in each other with his view of an open and competitive market for mobile phones. Mr Case stated that Unistar was not in direct competition with the Appellant. Unistar had its customers; the Appellant had its own. Mr Case had no idea how Deluni Mobile ran its business. Mr Case pointed out that Peter Scrancher was a director of several companies. Officer Saunders accepted that Mr Case had been open with HMRC about his interests in Unistar.

173. The Appellant’s margin was considerably more than the other traders in the deal chains ranging from £11 to £42 per handset. The mark ups for all deals except one were in the range 6.9% to 8.1%. The mark ups for 13 of the deals were in the range of 7.5% to 8.1%. One deal (08; 03/06) had a mark up of 3.8% which was considerably lower than the others. The mark ups did not appear to vary with the model of phone traded.

174. Mr Case asserted that the Appellant used its own funds to finance the disputed deals. The analysis of the Appellant’s payments for the individual deals is summarised in the table below:

Appellant (A) paid supplier after payment from customer.	**A paid supplier before payment from customer.**	**A paid deposit to supplier with overnight credit. Customer normally paid in full before A discharged the overnight credit.**
Deal 1 12/05; Deals 1, 2, 3, 4 & 8 3/06, (**Total 6**)	Deals2,3 12/05; Deal 12 03/06: Deal 1 06/06 (**Total 4**)	Deals 5, 6.7, 9, 10, & 11 3/06: (**Total 6**)

175. Mr Fletcher’s evidence comprised three elements:

(1) A description and analysis of the nature and scope of the authorised (“white”) market in mobile handset distribution.

(2) A description and analysis of the grey market for mobile phone handsets during 2006 (this being the market within which the Appellant and those with whom it traded claimed to operate), including the opportunities in and scope of the grey market trading, forms that grey market trading would take, and an explanation of whether it was possible to identify when grey market trading was taking place.

(3) An analysis of the Appellant's deal chains in January to April 2006, the statements of Messrs Andrews and Case, and their claim that the Appellant was operating in the legitimate grey market.

176. According to Mr Fletcher, the grey market in mobile phones arose from the failure of the authorised market to meet fully the needs of all participants in the market. There were two categories of market failure:

(1) Price related market failures; which provided two forms of trading opportunities: arbitrage and box breaking.

(2) Volume related market failures which occurred when mobile network operators and large retailers underestimated demand (volume shortages), or when distributors overestimated demand or purchased surplus stock in order to receive additional volume rebates from originating equipment manufacturers (dumping).

177. Mr Fletcher concluded that if the Appellant operated in the grey market it was in arbitrage. Mr Fletcher identified that the Appellant's dealings exhibited three characteristics that would be expected to be found in rational and profitable arbitrage, namely: minimal stock-holding periods, repeating profitable transactions with customers so long as a price differential was maintained, and trading close to release dates.

178. Mr Fletcher, however, decided that there were specific behaviours and characteristics of the Appellant's trade during the disputed period which were not indicative of rational profit-maximising behaviour, and included:

(1) Trading in Nokia handsets, which constituted a large proportion of the Appellant's deals (16 of the 24 transactions[11]). Mr Fletcher said that Nokia had a homogenous pricing policy which involved setting identical prices for its wholesale customers in all geographical markets. Mr Fletcher was of the view that this policy limited the opportunity for the Appellant to profit from arbitrage involving such handsets. Mr Fletcher also stated that the Sterling to Euro exchange rate fluctuations at the time of the disputed deals would not have been sufficient to yield the profit margin achieved by the Appellant.

(2) Supplier selection: no evidence that the Appellant attempted to source the goods from the manufacturer or authorised distributor.

(3) Supply chain length: Mr Fletcher would have expected the parties at the ends of the deal chains to advertise their stock offerings or requirements, such as, through widely used internet-based phone trading websites. The Appellant, however, had no familiarity with these websites, saying instead that it relied on building a network of contacts. Mr Fletcher considered that the flow of information within such an open market was likely to be such that the Appellant would be unable to make its

[11] The 16 deals included 24 transactions of individual phone consignments)

consistently high mark-ups without the other traders in the chain becoming aware of the Appellant's margin and taking steps to eliminate the Appellant from the chain. Mr Fletcher concluded that the lengthy deal chains in which the Appellant operated were implausible, and inconsistent with rational and profitable grey market trading.

(4) Market share: Given the highly fragmented and "national" nature of the handset distribution market, it was unusual, in Mr Fletcher's opinion, for the European (plus the UAE) market share of any one company to exceed 5% in any particular month. The Appellant's market share of the total European market for handsets exceeded 5% on four occasions (two handsets in January, one in both March and April) representing 54% of the handsets in the deals considered by Mr Fletcher. In two of these instances, the Appellant's market share exceeded the addressable market opportunity for all distributors in a particular month (115% of the distributed Nokia 9300i handsets in March 2006[1] and 27,000% of the distributed NEC E616 handsets in January 2006).

(5) Mr Fletcher accepted as a possibility that, given the particular age of the NEC E616 handsets, they could have been dumped onto the market and were ultimately retailed in a territory which would not have been covered by the data used by Mr Fletcher to calculate the market share. Mr Fletcher, however, considered it highly unlikely that the Appellant was involved in dumping. Mr Fletcher refuted the alternative market share calculations advanced by Mr Andrews for the other phone models, but noted that even if Mr Andrew's calculations were correct, the Appellant's market share remained unusually high and implausible.

(6) The lack of detail on the Appellant's purchase orders, invoices and inspection reports

(7) The discrepancies between the purchase orders and the inspection reports held by the Appellant for the disputed deals.

179. Mr Fletcher concluded that, on balance the Appellant's transactions in January to April 2006 were extremely unlikely to be part of the rational and profit-maximising arbitrage market, or any other rational and profitable white or grey mobile phone handset trading market.

180. The Appellant originally challenged Mr Fletcher's evidence on the basis that profitable deals were in fact made. Mr Andrews and Mr Case did not recognise the word '*arbitrage*'. They did not think *arbitrage* when they set about their daily business. Instead they saw themselves as simple people who get on the phone every day to try and conduct business. Many days they did not succeed but some days they did.

181. Mr Fletcher denied that his analysis of the grey market in the wholesaling of mobile phones was purely theoretical. He made the following points in cross examination:

> "The reason why these terms and explanations appear in my statement is that there must ultimately be some mechanism available in the market by which a profit can be made".
>
> "Through my knowledge of the market I have set out arbitrage as being one of the four main opportunities that I would see could be exploited by a grey market trader. …I don't accept that that's a theoretical view".
>
> "I think that's what's observed in almost any market where there is a wholesale and retail relationship. Each person in the market will seek to profit from their participation, but in order to profit they must be able to do something which is considered to be of value by their customer".
>
> "Therefore, the more people who are participating: the more people who are seeking profit. Where you have a market where profits are going to be thin, then the best thing to do is to buy from as close to the point of manufacture and sell as close to the eventual point of retail".

182. Mr Fletcher did not recognise the description of simple market trading. In his view it was not good enough for the Appellant to state that by buying goods at one price and selling them at a higher price allowed it to make a profit. According to Mr Fletcher, there must be behind the Appellant's statement a rationale from which that profit opportunity stemmed.

183. The Appellant argued that the Tribunal should attach no weight to Mr Fletcher's evidence. The Appellant referred to Mr Fletcher's absence of direct experience in the grey wholesale market of mobile phones. The Appellant pointed out that Mr Fletcher had never sat down with a grey market trader and discussed his business. Finally, the Appellant relied on Mr Fletcher's admission that he did not know if the behaviour of authorised distributors and mobile network operators were the same now as they were in 2006, as an indication of his lack of expertise in this area.

184. The Appellant highlighted what it considered to be inconsistencies in Mr Fletcher's evidence. The Appellant believed that Mr Fletcher undermined his evidence regarding Nokia's homogenous pricing policy with his acknowledgement that once the handset had left Nokia's authorised distributors, traders were free to set the price they wished.

185. The Appellant pointed out that Mr Fletcher had accepted that mobile network operators and authorised distributors would dump mobile phones via an export sale in a market where there would be demand for those phones. In the Appellant's view, Mr Fletcher's acknowledgement corroborated Mr Andrews' evidence of the Appellant taking advantage of the dumping of mobile phones by mobile network operators and authorised distributors in the grey market for export. Mr Andrews said that mobile network operators and authorised distributors did this to avoid scrutiny by the mobile phone manufacturers.

186. The Appellant considered the nefarious activities of Data Select, an authorised distributor, weakened Mr Fletcher's proposition that the Appellant in pursuit of rational profit maximising behaviour would have actively sought opportunities to source mobile phones from authorised distributors. The Appellant said the evidence

on Data Select also sourcing stock from the grey market, and having its input tax claims disallowed gave lie to Mr Fletcher's assertion that the safest and most profitable rational route to obtain mobile phone stock was from an authorised distributor.

187. The Appellant reinforced its argument on the unreliability of Mr Fletcher's assertion on authorised distributor by reference to Mr Case's evidence of the conditions and strings attached to the Appellant having direct commercial relationships with authorised distributors and mobile phone manufacturers.

188. The Appellant's principal argument on the weight to be attached to Mr Fletcher's evidence was that in reaching his conclusions on grey market trading opportunities he failed to take account of the volume of fraudulent trading that was occurring in the grey market in 2006. Mr Fletcher stated that he excluded the fact of fraudulent trading because it was not relevant to his analysis of the grey market as it existed for the rational pursuit of profit.

189. The Appellant asserted that as fraudulent trading was such a significant factor in the market in 2006, which was corroborated by Mr Stone's evidence, the exclusion of this variable by Mr Fletcher rendered his analysis of the 2006 market unreliable. In short, the Appellant contended that Mr Fletcher's report was a theoretical exercise which had no practical application to the facts.

190. The Appellant argued that the existence of widespread fraud in the mobile phone wholesale market created another profit making opportunity not considered by Mr Fletcher. The Appellant postulated that in the 2006 market the preponderance of fraudulent behaviour occurred at the point where the defaulting trader acquired the phones. This in turn created a supply of low cost mobile phones which could be exploited by genuine traders. In support of its proposition the Appellant relied on Mr Fletcher's evidence that a mobile phone consignment which had been subject to a VAT default still had intrinsic value in the market.

191. The Tribunal starts its consideration on the Appellant's trading operation by assessing the weight to be attached to Mr Fletcher's evidence. The Appellant repeated its arguments on Mr Fletcher's expertise advanced at the hearings on 25 February and 13 March 2013 when the Tribunal determined that Mr Fletcher's evidence was admissible. The Tribunal heard nothing new from the Appellant when the substantive hearing resumed on 9 September 2013 to persuade it to depart from its conclusion reached in the decision released 9 September 2013 that Mr Fletcher had the requisite expertise to give an opinion on the wholesale mobile telephone market in the UK and overseas in 2006.

192. In the Tribunal's view, the facts that Mr Fletcher had no direct experience of the grey market and had not sat down with a grey market trader did not devalue the reliability of his conclusions. As HMRC pointed out, Mr Fletcher was assisted by a research team, members of which had worked with companies operating in the grey market. The study conducted by Mr Fletcher incorporated recognised and standard research methods. The Tribunal found his report to be thorough and supported by a

significant volume of underlying materials which were exhibited with his witness statements.

193. At the hearings on admissibility the Appellant complained that Mr Fletcher was unable to identify the precise contribution made by each team member. The Appellant pointed out that without this information it was unable to deal with Mr Fletcher's findings, and in any event his opinion on the advice given to him by team members was hearsay. In this respect the Tribunal accepted Mr Fletcher's evidence that he would not have introduced matters into his report that he was not satisfied with, and that the team acted under his supervision. The Tribunal agrees with HMRC's submission that Mr Fletcher's report was his opinion and the evidence presented was his evidence.

194. The Tribunal was not convinced for the reasons elaborated upon later that Mr Case and Mr Andrews were better placed than Mr Fletcher to give evidence on the grey market in the wholesaling of mobile phones. Essentially the Tribunal found that there was a disconnect between the Appellant's actual trading and Mr Case and Mr Andrews assertions about how the grey market in mobile phones operated.

195. The Appellant's contentions on inconsistencies in Mr Fletcher's evidence carried no truck with the Tribunal's evaluation of his evidence. Mr Fletcher was adamant about the existence of Nokia's homogenous pricing policy which meant that Nokia set identical prices for its wholesale customers in all geographical markets. The Appellant at the substantive hearing did not pursue its concerns aired at the admissibility hearings about how Mr Fletcher discovered the existence of this policy. The Tribunal in any event was satisfied of the existence of and the rationale for the policy from the various disclosures made by Mr Fletcher as a result of the Appellant's challenges. The policy was necessary to avoid allegations from regulatory authorities that Nokia was taking advantage of its pre-eminent market position by applying predatory pricing policies.

196. The significance of the homogenous pricing policy was that it severely limited the profit-making opportunities for grey market trading in Nokia mobile phones, which was the position that Mr Fletcher maintained throughout his evidence. The Appellant sought to undermine Mr Fletcher's stance on the effect of the homogenous pricing policy by reference to his answer to a question posed by the Tribunal regarding the freedom of grey market traders to fix the price of Nokia mobile phones once they left the authorised distributor. The Tribunal is not convinced with the correctness of the Appellant's challenge. The fact that grey traders were free to set their prices was insufficient on its own to provide a coherent rationale for a profit marking opportunity arising from deals in Nokia phones. In short there had to be an opportunity first in order for a grey market trader to fix a competitive price for Nokia phones.

197. The Appellant suggested various scenarios for profit making opportunities from Nokia phones. The Appellant referred to the existence of Nokia's system of rebates and discounts based on volumes shipped to authorised distributors which according to the Appellant, would create an incentive for authorised distributors to buy more than

they needed and dump excess stock into the grey market. The Appellant asserted that Mr Fletcher accepted that this was a possibility with his reference to the importance of cash flows to companies which might cause them to put volumes out into the grey market.

198. The Tribunal considers that the Appellant had been selective with Mr Fletcher's evidence. The Appellant failed to refer to Mr Fletcher's statements on the unlikelihood of an authorised distributor purchasing stock in order for it to be dumped, and if an authorised distributor dumped stock it would not normally be in the UK market but to a market where the mobile phone's age or obsolescence was less of a concern.

199. The Appellant also overlooked Mr Fletcher's evidence that he did not understand how the Appellant took advantage of purported dumping of mobile phones by authorised distributors. In Mr Fletcher's view, Mr Andrews' assertions about grey traders teasing stock from authorised distributors which operated differently from grey traders, made no sense to him because it implied that certain deals of authorised distributors were not governed by supply and demand.

200. Finally the Appellant made no reference to its cross examination of Mr Fletcher on the allowances given by Nokia to authorised distributors for marketing. The Appellant suggested that these allowances were used to discount the price of Nokia mobile phones when they entered into the grey market. Mr Fletcher disagreed. As far as he was concerned Nokia did not permit authorised distributors to use such allowances for discounting prices of mobile phones.

201. The Tribunal is satisfied that the Appellant had failed to undermine Mr Fletcher's evidence on the effect of Nokia's homogenous pricing policy in limiting the profit making opportunities for grey market trading in Nokia mobile phones.

202. Equally the Tribunal is not persuaded by the Appellant's attempts to devalue Mr Fletcher's evidence that a grey market trader would gravitate towards an authorised distributor and cut out intervening traders in pursuit of profit.

203. The Appellant asserted the involvement of Data Select, an authorised distributor, in suspect grey market deal chains, gave lie to Mr Fletcher's claim that a grey market trader would see an authorised distributor as the safest and most profitable rational route to obtain mobile phone stock. The Tribunal agreed with HMRC's observation that the Appellant's argument was misconceived. Mr Fletcher was concerned with the rational and profitable grey market not with fraud and fraud avoidance. In that case Mr Fletcher's conclusion that seeking out an authorised distributor was the best route for maximising profit in a rational grey market still held.

204. The Tribunal considers the reasons advanced by Mr Andrews and Mr Case for the difficulties facing the Appellant in doing business with an authorised distributor

contradictory. Mr Andrews supplied differing unconvincing accounts[12] as to why the Appellant did not trade with Mr Andrews' former employer, Unique Distribution, or with Data Select with whom Mr Andrews had established business connections. Mr Andrews emphasised that authorised distributors would not do business with the Appellant because they were new players in the market. Mr Andrews' assertion did not make sense to the Tribunal in the context of Mr Andrews' claims of his contacts in the business and of being well known in the wholesaling sector.

205. Mr Case produced an agreement from Data Select to suggest that the terms for doing business with an authorised distributor were prohibitive for the Appellant. Mr Case maintained that under the agreement the Appellant would have to open up a credit account. HMRC, however, pointed out that the agreement exhibited by Mr Case showed no such thing. The principal requirement of an authorised distributor appeared to be payment up front for large wholesale orders which was within the Appellant's financial capacity, if Mr Case's claim that the Appellant used its own capital to fund deals was correct.

206. The Tribunal also observes that the Appellant in one of its earlier deals had actually purchased mobile phones from Brightpoint International, an authorised distributor, which makes the Appellant's claims regarding the difficulties of doing trades with authorised distributors even more perplexing.

207. The Appellant's principal submission on Mr Fletcher's evidence was that it was a theoretical exercise because he disregarded the existence of fraud in the market as at 2006. The Tribunal accepts the validity of HMRC's position as to why it did not ask Mr Fletcher to consider the effect of fraud on the market in 2006. HMRC's rationale was that Mr Fletcher's expert opinion of the rational and profitable grey market acted as a benchmark against which the Appellant's transactions could be assessed in order to make inferences on the Appellant's knowledge of the connections of its transactions with fraud. The Tribunal considers HMRC's rationale for the relevance of Mr Fletcher's evidence legitimate.

208. The Tribunal, however, believes that the Appellant's submission is flawed in two material respects. First the Appellant has overlooked the essential proposition upon which Mr Fletcher based his evidence. Second the logic of the submission ran contrary to the Appellant's case.

209. Mr Fletcher's expert opinion is founded on the premise that there must be a rational explanation for a deal in mobile phones. Profit on a deal does not simply happen. There must be some opportunity to create that profit. A successful grey market trader understands the market, and recognises an opportunity when it arises. In short, the successful grey market trader is able to give a rational and coherent explanation for the profit made in the deal.

210. From the Tribunal's perspective the value of Mr Fletcher's expert opinion is that he could discover no rational and commercial explanation for the Appellant's

[12] See the summary in pages 39 and 40 of HMRC's Closing Submissions dated 19 September 2013.

deals. Equally the Tribunal finds that Mr Andrews and Mr Case did not offer a persuasive commercial explanation for the success of the Appellant's trades in mobile phones. Their stance at the beginning of the hearing was that the Appellant was successful because it made a profit. They provided no insight on the opportunities that created those profits other than generalised statements about their extensive knowledge of the market and that Mr Andrews worked hard in securing deals. The Appellant's position was that there was a grey market because it did successful deals.

211. The Appellant's submission on the fraudulent market gave the Appellant an alternative explanation for why its deals were caught up with fraud without its knowledge. The Appellant appeared to suggest that it was operating in a bubble of bona fide trading which had been created after the fraudsters had made off with their ill-gotten gains on the acquisition of mobile phone consignments. In Mr Andrews' words the Appellant was also a victim of the fraud.

212. The Tribunal considers the logic of the Appellant's submission is against the Appellant. The Tribunal is concerned with the Appellant's state of knowledge at the time it transacted the deals, not with the Appellant's rationalisations after the event. The Appellant knew of the prevalence of fraud in the market at the time it did the deals. The Appellant adduced no evidence that at the relevant time it asked the question: *Is this transaction connected with fraud?* The Appellant's lack of reflection was typified by Mr Andrews exhortation of being victims which displayed his surprise at the Appellant being caught up in the fraud. A trader in the legitimate grey market at the time of making the deal would have a rational explanation for it, and an answer for why it was not connected with fraud. The Appellant, on the other hand, did the deal but did not reflect about whether the deal made sense knowing of the prevalence of fraud in the market.

213. The themes of failure to reflect, and contradictions with what was done and said to be done, were evident in the wider facts on the Appellant's method of trading at the time of the transactions.

214. Mr Andrews and Mr Case described the grey market as highly competitive, and a hard place in which to work where commercial confidentiality about suppliers and customers was sacrosanct. Mr Case, however, expressed no surprise that a competitor was investing monies in the Appellant, and he was investing in a competitor, which ran counter to his description of a competitive market founded on commercial confidentiality.

215. Similarly the fact that the Appellant's transactions throughout its short trading history was on the whole restricted to a select group of customers and suppliers did not sit comfortably with the assertions of Mr Andrews and Mr Case that they had to work hard to secure deals in a tough environment. Mr Andrews and Mr Case said that they adopted this form of trading to minimise the risk of fraud by working only with suppliers and customers known to them and were in fact following HMRC's advice. Mr Andrews and Mr Case, however, offered no insight as to why its favoured suppliers, Cybacomms and Sprint, were giving this opportunity to the Appellant to make profits.

216. Mr Andrews and Mr Case did not consider the size of Mr Andrews' commission on the deals unusual. Mr Andrews said that his commission was in line with that paid to traders working with him in Unique. Mr Case said it was justified because of the paperwork involved. The Tribunal takes a different view. The commission of £494,668.26 earned by Mr Andrews for six months work was seven times his annual salary at Unique. The Tribunal's assessment of the work done by Mr Andrews on the evidence was that he was simply reacting to a known customer's demands which required him to make and receive calls, and if a deal was struck to complete a series of pro-forma documents. The entries in Mr Andrews' trading day books did not reveal extensive activity on his part. The Tribunal finds no rational basis for the size of Mr Andrews' commission.

217. The Appellant's margins on the deals were considerably higher than their suppliers and remarkably consistent as measured by the percentage rate of mark up except for deal 8 in the 03/06 VAT period which was significantly lower at 3.8 per cent. The Appellant argued there was no evidence from HMRC to suggest that its mark up was odd. The Appellant was not aware that its mark up was greater than that of other traders in the chain. The Appellant, in any event, as an exporter bore higher costs of sale than its suppliers. Finally the Appellant pointed out that Mr Fletcher and Mr Saunders could offer no view as to what the correct mark up was for the disputed transactions.

218. The Appellant was incorrect to state that there was no evidence substantiating potential oddities with the level of margin achieved by the Appellant. First the margin was significantly higher when compared with that achieved by the other traders in the deal chain. The size of the Appellant's margin was simply not due to the higher costs borne by the exporter. The analysis done by the Appellant's first representative showed that the transport costs for the disputed deals were generally in the region of £1,500 to £2,000[13]. Second, the Appellant secured a strikingly similar mark up in percentage terms for all the deals except one. The mark up for 13 of the deals was in the range of 7.5% to 8.1%. The mark up did not vary with the model of the mobile phone.

219. The Appellant asserted that it did not know about the profits made by the other traders in the deal chain. The Appellant, however, knew about the scale of profits it had made in a short period of time from a standing start. Further the Appellant knew about the rate of margin achieved for each deal and that the rate was consistent across a range of different models of phone. The Appellant's response was that it achieved a turnover commensurate with the experience of its staff and with the level of funding available to it. The response begged the question about whether Mr Andrews and Mr Case gave any thought to the possibility that the profits and margins made were a result of the connection of the Appellant's transactions with fraud.

220. The Appellant referred to the 3.8 per cent margin for deal 8 in the 03/06 VAT period as evidence for its assertion of involvement in genuine negotiations. Deal 8

[13] Notable exceptions were deals 5 and 12 (03/06) which were £6,372 (5 vans) and £4,592 (3 vans) respectively.

was the only one of the disputed transactions which involved Cybacomms as the supplier and Mobile World as the customer. Given those circumstances the Tribunal views the significance of the 3.8 per cent margin in a different light from the Appellant. The Tribunal considers the lower margin should have put the Appellant on notice about the bona fides of the consistently higher rates achieved with its normal supplier and customer (Sprint and 3G Trade) particularly in view of its knowledge of prevalence of fraud in the market.

221. Mr Andrews and Mr Case maintained that the Appellant funded the deals from its own capital, and was not dependent upon VAT repayments to finance future deals. The analysis of the timing of the Appellant's payments and receipts for the disputed transactions presented a more nuanced picture from that portrayed by Mr Andrews and Mr Case.

222. Although there is evidence of a loan from Leo Knifton which was used to ease the cash flow situation at one stage, the Appellant's available funds arose largely as a result of the payments received and profits made from the disputed transactions, or earlier transactions in mobile phones that were not the subject of extended verification. The Appellant, however, paid its supplier before receipt from its customer in only four of the deals. In six deals the Appellant was obliged to request overnight credit arrangements from its supplier, Sprint. Mr Andrews in his later witness statements mentioned Mr Case awaiting VAT repayments in order to finance deals. Thus the Appellant did not have a substantial capital base to support its trading activities which was the implication of Mr Case's assertion on the Appellant's funding arrangements. Rather the Appellant was reliant on the revenue stream flowing from its trades to fund future deals.

223. The Tribunal concludes the following on the Appellant's trading operation:

(1) Mr Fletcher's evidence on the rational and profitable grey market in the wholesaling of mobile phones in 2006 was reliable. His expert opinion was relevant to the issues in the Appeal. Mr Fletcher's evidence provided a benchmark against which the Appellant's transactions could be assessed in order to make inferences on the Appellant's knowledge of the connections of its transactions with fraud.

(2) Mr Fletcher's premise that there must be a rational explanation for a deal in mobile phones and that profit on a deal did not simply happen was sound.

(3) The Tribunal was not convinced with the Appellant's argument that Mr Fletcher's analysis of the grey market was rendered a theoretical exercise because he did not consider the incidence of fraud. The Tribunal decided that the submission went against the Appellant, highlighting the absence of reflection on the Appellant's part about whether the deal made sense knowing of the prevalence of fraud in the market.

(4) Mr Case and Mr Andrews did not present a rational and coherent explanation for the profits made by the Appellant with its deals in the wholesaling of mobile phones. They assumed the grey market existed

because the Appellant made profitable deals. They did not question why the Appellant was able to make the profits it did on the individual transactions. The Appellant's actual trading practices were inconsistent with the portrayal of the grey market by Mr Andrews and Mr Case as highly competitive, and a hard place in which to work where commercial confidentiality about suppliers and customers was sacrosanct.

(5) The Appellant's transactions in January to April 2006 were inconsistent with the rational and profitable legitimate grey market in the wholesaling of mobile phones. The majority of the Appellant's transactions involved Nokia handsets, the profit opportunities in which were severely curtailed by Nokia's homogenous pricing policy. The Appellant made no attempt to source the phones from authorised distributors, and its reasons for not doing so were contradictory.

(6) The Appellant did the deal but did not reflect about whether the deal made sense knowing of the prevalence of fraud in the wholesale market for mobile phones.

The Individual Deals

224. In this section the Tribunal examines first the Appellant's documentation for the disputed deals. The Tribunal then goes on to consider each deal highlighting the purported discrepancies relied upon by HMRC to prove its case. Finally the Tribunal gives its view on the purported discrepancies.

Documentation

225. Mr Andrews prepared a front sheet for each deal known as the *Trade Deal Check List*. The essential details of the deal were recorded on this document together with a check list for each stage of the deal which Mr Andrews ticked off on receipt of the relevant piece of documentation.

226. The check list set out the following steps for each deal:

(1) A purchase order from the Appellant's customer.

(2) A declaration from the customer stating, amongst other things, that goods would be sold at market price; the transaction involved no third party arrangement; no grounds to suspect that VAT would go unpaid, reasonable checks had been made on suppliers; and that the goods would not be sold to a UK customer.

(3) The Appellant's purchase order which set out the Appellant's terms and conditions which included the supplier confirming that it had exclusive ownership of title; and the order would be subject to full inspection of the goods being sold and their satisfactory checking, and confirmation of the IMEI serial numbers.

(4) The supplier transaction declaration which had 13 conditions including that the supplier had full legal title to the goods and that they had been subject to examination by the supplier.

(5) Pro-forma invoice and invoice received from supplier

(6) Verifications of the supplier's VAT number; the Appellant conducted two forms of verification: one with the VAT national enquiry helpline, and the other with Redhill.

(7) The Appellant's request for inspection of the goods by its agent. The Appellant's request specified 12 requirements including a 100 per cent count of the boxes; 100 per cent IMEI scan; 100 per cent check of the contents of the box and to power up a proportion of the mobile phones.

(8) A copy of the inspection report from the agent. Two agents, A1 Inspection Limited and 4G UK Limited were used for the disputed transactions. The report from A1 was more detailed and dealt with 25 different items (type of units colour, type of charger etc and provided a report on the individual items checked). The report from 4G was more general.

(9) The Appellant's invoice giving the specification of the mobile phones. The invoice also included a statement that the goods were for permanent removal from the UK.

(10) Freight forwarder documentation: stock allocation form which permitted the Appellant's customer to inspect the goods but the form stated that the goods still belonged to the Appellant. Further under the stock allocation form the freight forwarder was only able to release the goods on receipt of official documentation and verbal confirmation from the Appellant. *Confirmation of Title Ownership* signed by the freight forwarder that the supplier had full title to the goods. *Transport Booking Request*: authorising the freight forwarder to arrange transport ship on hold until confirmation. Release instruction which, according to Mr Andrews, would only be given if payment was made for the goods.

(11) Payment made to supplier

(12) Payment made to customer

(13) Release document sent to forwarder or shipper

(14) Phone call to verbally confirm release

(15) Original invoice received from supplier

(16) Proof of shipment (CMR) received from shipper

(17) Deal notes.

227. Mr Andrews stated that he compiled the check list and the supporting documentation to protect the Appellant. The completion of the checklist was his way of ensuring that everything was done. Mr Andrews denied HMRC's allegation that it was simply window dressing. Mr Andrews accepted that the check list contained no

assessment of the financial viability of the Appellant's trading partners. According to Mr Andrews, Mr Case was responsible for the financial aspects of the transaction. Mr Case expressed in cross examination[14] mild surprise of Mr Andrew's assertion that he had nothing to do with the financial viability of the Appellant's trading partners.

228. Mr Andrews accepted that the Appellant carried out no independent checks of the declarations made by its suppliers and customers. HMRC asserted that such declarations were entirely contingent upon the integrity of the very party whose integrity they were designed to ensure. In short, according to HMRC, the declarations lacked independent verification.

229. The Appellant had written terms and conditions for the dealings with its suppliers which formed the basis of Appellant's business with them. The terms were referred to in the section for *Special Instructions* at the foot of the Appellant's purchase orders. The Appellant had separate terms and conditions with its customers. These were not printed on the Appellant's sales invoices but the terms and conditions were apparently sent separately to its customers.

230. HMRC identified the following contradictions in the customer's terms and conditions with the manner in which the Appellant conducted its business

(1) The terms and conditions specified that delivery of goods would take place at the Appellant's place of business which did not happen in practice. All the disputed transactions took place at the premises of the freight forwarder. Mr Case accepted in cross examination that the term requiring the transaction to take place at the Appellant's premises was rather a strange term. Mr Case pointed out that the terms and conditions were written by a firm of lawyers with whom Mr Case had extensive meetings. Mr Case accepted that the position of freight forwarders should have been covered in the standard terms and conditions.[15]

(2) Mr Case accepted that the Appellant did not always apply the term that *quantity and description of goods should be set out in the company's quotation or acknowledgement of order*. Mr Case, however, insisted that Mr Andrews informed the customer of the change in specification.[16]

(3) Mr Case acknowledged that the Appellant did not have a price list which was a specific term and condition.[17] Mr Case considered the price information was found on the invoice. Mr Case explained that the terms and conditions were designed for an expanding situation, and, therefore, did not reflect the current business practices for the Appellant.

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[14] Transcript 27 January 2012 para 4-9 page 149

[15] Transcript 27 January 2012 para 2-15 page 192

[16] Transcript 27 January 2012 para 8-22 page 193

[17] Transcript 27 January 2012 para 5-13 page 195

The Individual Deals

Deal 1 (2.12.05; 12/05 VAT period)

231. Deal 1 involved a sale of 1,175 Motorola phones to Unicell in Switzerland. The deal had been traced back to a tax loss of £35,490.88 with ECS 84.Com.

232. The documentation revealed that

(1) A phone specification of silver, whereas the inspection report showed that the handsets were coloured soft white and pearl white. Mr Andrews pointed out that soft white was Motorola's description of the colour, similar to pearlescent silvery white, which, according to Mr Andrews looked like silver to ordinary people on street.

(2) Cut outs on three cartons.

(3) The phones had two pin chargers.

(4) Manuals were either Spanish or English (Central Euro language software).

(5) The inspection agent was asked to power up one per cent (12 units) of the phones but only powered up two units.

(6) The phones were sent from Paul's Freight Services on 2 December 2006 and sent back to the UK almost immediately.

233. Mr Andrew's entry in day book for 29 November 2005 indicated that Unicell was in the market for Nokia 8800 and 7610, Samsung D600 and D500, and Motorola ROKR E1 mobile phones. The entry also showed that Wizard, Aircall, Sprint, and Cybacomms were selling. Wizard was selling Samsung D500 Model for £156 per unit, some £4 cheaper than Aircall and £6 cheaper than Cybacomms. According to Mr Andrews, the price negotiations for the Motorola mobile phone were primarily around £189 with price agreed at £187.

234. Unicell made the payment of £220,312 at 0930 on 2 December 2005. Appellant paid Sprint £241,609.38 at 1250 on 2 December 2012. The net amount to Sprint was £205,625 which gave the Appellant a gross profit of £14,687.50.

Deal 2 (12.12.05; 12/05 VAT period)

235. There were two sale invoices each selling 1,100 Nokia 9300 mobile phones to Unicell in Switzerland which were traced back to a tax loss of £93,016 with ECS 84 Com Ltd.

236. The documentation revealed that

(1) The inspection reports revealed 35 cut outs.

(2) The phones had two and three pin chargers. (Unicell's purchase order stipulated that only original, boxed and badged 2 pin plug was acceptable).

(3) The sample taken for the stock inspection report showed that there were three different language mixes of manuals, three different software languages, some phones had Italian keypads, and a number of phones had no warranty details.

(4) The inspection company was asked to power up one per cent (22) of the phones but only powered up six units.

(5) The purchase orders from Unicell were dated 12 December 2005. The Appellant's invoices were dated 28 November 2005 and 2 December 2005 respectively.

(6) The phones were sent from Pauls Freight Services warehouse on or around 12 December 2005 and consigned back to the UK.

(7) The freight forwarder refused to provide information about the number of days the goods had been held at the warehouse to the Appellant.

237. There was no specific entry in relation to the deal in Mr Andrew's day book. Mr Andrews, however, asserted that he negotiated the deal.

238. Unicell paid on 13 December 2005 two separate amounts of £291,500. The freight ticket was dated 12 December 2005 indicating that the goods had been sent before payment.

239. The net transaction cost of the Appellant's purchase was £539,000 which gave the Appellant an overall profit of £44,000. The VAT inclusive price paid by Sprint was £633,325.

Deal 3 (13.12.05; 12/05 VAT period)

240. Deal 3 involved the sale of 1,700 Samsung D600 to Unicell in Switzerland traced back to a tax loss of £75,741.75 with ECS 84 Com Ltd.

241. The documentation showed that

(1) The phones had two pin chargers.

(2) The inspection company was asked to power up one per cent (17) of the phones but only powered up two units.

(3) The inspection report was dated 10 December 2005. The order from Unicell was dated 12 December as was the purchase order from PNC.

(4) The phones were sent from Paul's Freight Services on or around 12 December 2005 and were consigned back to the UK within a short period of time.

(5) No cut outs and no customs stamps recorded

242. The NEMESIS database[18] showed that all these phones had been previously scanned on 24 November 2005.

243. There were few notes in Mr Andrew's day book for this deal. Mr Andrews, however, reconstructed the events of the deal from his memory and other entries in the daybook. Mr Andrews, however, stated that Samsung D600's were in popular demand at the time. He referred to an entry in the day book of Unicell not prepared to take all 3,400 phones and Sprint declining the offer of £208.

244. Appellant's payment request for Sprint was recorded at 1333 on 13 December 2005. Unicell paid the Appellant (£382,500) at 0921 on 13 December 2005

245. Mr Andrews pointed out that the Appellant had at the time £1.4m in the bank. Further the Appellant did not need to rely on the payment from its customer before meeting its supplier's debt. The net transaction with Sprint was £354,450 (£416,478.75 with VAT) giving the Appellant an overall profit of £28,050.

Deal 1 (11.01.06; 03/06 VAT period)

246. This involved a sale of 3,400 Samsung D600 to 3G Trade SA traced back to a tax loss of £122,867.50 with Allied Jap Distributions Limited.

247. The documentation revealed that

(1) The phones had two pin chargers.

(2) The inspection report stated that *all cut outs have destination cartons*. Mr Andrews pointed out that *destination cartons* was poor English, and meant that the cutouts were of destination/shipping labels.

(3) The inspection report stated that in the small sample taken there were 10 different language codes, five different manual types, and three different software language configurations.

(4) The inspection team was asked to power up one per cent (34) of the phones but the team only tested 10.

248. The NEMESIS database showed that some of these phones had been previously scanned on 1 December 2005.

249. According to Mr Andrews, the 9 January 2006 entry in his day book indicated that Sprint would have available tomorrow Samsung D600's, Nokia 8800, 9300s but no price. Unicell was looking for a range of phones. 3G Trade on 5 January 2006 was seeking Samsung D600 at £227 in quantity.

250. The Appellant paid Sprint £838,950 at 0255 on 10 January 2006 before receipt of payment of £771,000 on 11 January 2006. The net cost of the purchase was

[18] The NEMESIS database was compiled by HMRC, and consisted of IMEI numbers of mobile phone consignments which had been scanned by HMRC when the consignments entered and left the UK. Traders, such as the Appellant, did not have access to the database.

£714,000 which provided the Appellant with a profit £57,800. The Appellant paid £210 for each phone and sold each mobile phone at £227.

251. The documentation showed that the goods were released on 10 January 2006 at 1148 before the Appellant supplied Edge, the freight forwarders, with a stock/ allocation from at 1339. The inspection report was dated and timed at 1427 on 11 January 2006.

Deal 2 (16.01.06; 03/06 VAT period)

252. This deal involved the sale of 2,800 Samsung D600 to Unicell in Switzerland on two invoices which were traced back to a tax loss of £101,234 at Art Enterprises Limited.

253. The documentation showed that

(1) The phones had two pin chargers.

(2) The Appellant's request for inspection specified black phones, whereas the inspection report variously described the colours of the phones as charcoal black and noble blue.

(3) The inspection report stated that in the small sample taken there were 11 different language codes, seven different manual types, and three different software language configurations. Unicell specified in its purchase order Central European although Mr Andrews asserted that Unicell would take French manuals

(4) IMEI numbers were not checked.

(5) The inspection team was asked to power up one per cent (28) of the phones but the team only tested 11 mobile phones.

254. An entry in Mr Andrew's day book on 9 January 2006 referred to a price of £224.50 for Samsung D600's. It was not clear to the Tribunal whether the entry related to the price at which Unicell was offering to buy.

255. The Appellant's payment request to Sprint was timed at 0216 on 13 January 2013. Unicell paid on 16 January 2006 after the payment to Sprint. The net cost of purchase to the Appellant was £588,000 (£690,900 with VAT) which produced a gross profit of £40,600. The Appellant bought the mobile phones at £210 per item and sold at £224.50.

Deal 3 (17.01.06; 03/06 VAT period)

256. This deal involved the sale of 1,050 Nokia 9300 to 3G Trade SA traced back to a tax loss of £41,729.63 with Art Enterprises Limited.

257. The documentation showed that

(1) The phones had a mixture two and three pin chargers.

(2) There were 175 cuts outs on the cartons.

(3) The inspection report stated that in the small sample taken some of the phones had no warranties. Further there were four different language codes, three different manual types including Arabic, and two different software language configurations. Some of the phones had Italian keypads with English manuals.

(4) The inspection team was asked to power up one per cent (10) of the phones but the team only tested four.

(5) Hawk, the freight forwarder indicated that the consignment had only been in the warehouse for one day and that there had been no previous transactions with the consignment. This statement was not true when viewed against the transaction chain for the deal.

258. The NEMESIS database showed that some of these phones had been previously scanned on 2 December 2005.

259. Entries in Mr Andrews' day book for 16 January 2006 recorded prices for Samsung D500's and Nokia 9300's. The Tribunal was not clear from the entries whether Mr Andrews was obtaining the prices from 3G Trade. There was also a reference to Sprint selling at £230.

260. The Appellant paid £283,762.50 to Sprint on 17 January 2006 before 3G Trade paid £260,925 on 18 January 2006. The cost of purchase was £241,500 giving a gross profit of £19,425. The price paid for individual phone was £230 and sold at £248.50.

Deal 4 (19.01.06; 03/06 VAT period)

261. This deal involved the sale of 2,000 Nokia 9300 to 3G Trade SA traced back to a tax loss of £80,185 with Art Enterprises Limited.

262. The documentation showed that

(1) The phones had a mixture of two and three pin chargers.

(2) The inspection report stated that only 575 phones were scanned. The Appellant had asked for 100 per cent scanning of the mobile phones. Mr Andrews recalled that the inspection agent (A1) had to wait an hour and the customer was very keen to have the stock shipped out that evening which meant that A1 did not have time to complete the scanning. The Appellant, however, provided HMRC with 2,000 IMEI numbers.

(3) The inspection report stated that in the small sample taken some of the phones had no warranties. Also there were 3 different manual types.

(4) The inspection team was asked to power up one per cent (20) of the phones but the team only tested three.

263. Mr Andrews referred to the entries in his day book for 16 January 2006 from which he said that he had spoken to a number of companies. There were no specific

entries in the day book relating to this deal. According to Mr Andrews, he rang Lucky at Sprint on 19 January to find out the available stock.

264. The Appellant paid Sprint £545,200 on 19 January 2006. 3G Trade paid the Appellant £501,000 on 20 January 2006. The Appellant purchased at £232 per item and sold at £250.50. The net purchase cost was £464,000 which gave the Appellant a profit of £37,000. The Appellant had at the time £912,000 in bank.

Deal 5 (24.01.06; 03/06 VAT period)

265. This deal involved the sale of 5,885 NEC 616 to 3G Trade SA traced back to a tax loss of £187,591.73 with Art Enterprises Limited. The number of 5,885 represented the stock available

266. The documentation revealed that

> (1) The phones had three pin chargers even though the Appellant dispatched them to Luxembourg. Mr Andrews suspected that the mobile phones were for eventual export outside Europe. The Appellant's customer, 3G Trade, however, specified Euro Stock not three pin chargers. Mr Andrews accepted in cross examination that the description on the Appellant's invoice as three pin EU charger was incorrect. A European charger would have two round pins[19].
>
> (2) The inspection team was asked to power up one per cent (58/59) of the phones but the team only tested one.
>
> (3) The inspection report revealed that the phones had an English manual with a number of European languages.
>
> (4) The report also recorded the existence of some loose stock. Mr Andrews considered that it was not a deal breaker if some of the stock was not in the original manufacturer's cartons. Mr Andrews had indicated earlier that stock was more saleable if in original cartons.

267. The NEMESIS database showed that the phones were a mixture of NEC E616 and NEC E616V. The model E616V had additional features and functionality. Finally the Appellant's record of IMEI numbers contained 1,012 duplicated entries.

268. Mr Andrews had recorded no notes of this deal in his day book. He apparently had left the book in the Southampton Office. Mr Andrews recollected NEC 616 was coming to the end of its production life. There was, however, no knowledge at the time that NEC was pulling out of the mobile phone market. Mr Andrews pointed out that Sprint's headquarters was close to NEC's factory in Birmingham. Sprint's warehouse was, however, in West London.

269. The Appellant paid Sprint in two amounts: £800,000 on 24 January 2006 and £486,166.75 on 25 January 2006. 3G Trade paid £1,182,000 on 24 January 2006. Mr

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[19] Transcript 10 September 2013, para 12-25 page 29.

Case agreed with Sprint a deposit of £800,000 and credit overnight. According to Mr Andrews, Mr Case would not have paid a deposit if he had known that 3G Trade would pay £1,182,000 on 24 January 2006. This was the Appellant's largest deal of the disputed transactions.

270. The net purchase price paid was £109,461,000 which gave a profit of £88,275. Individual phones bought at £186 and sold at £201

Deal 6 (27.01.06; 03/06 VAT period)

271. The deal involved sales of 1,600 Nokia 6230i, 121 Nokia N90, 832 Samsung D500, 360 Motorola PEBL and 500 Nokia 8801 to 3G Trade SA. The deal was traced back to a tax loss of £123,314.18 at Myco Telecom. Mr Andrews did not consider the size of some of the consignments odd. In his view the numbers represented the available stock.

272. The documentation revealed that

(1) The phones had two pin chargers.

(2) The colour of the Nokia 6230i mobile phones was stated on the trading deal check list and sales invoices as silver, whereas the inspection report showed that they were black. Mr Andrews asserted the colour described in the invoices was an administrative error. The Appellant had in fact wanted black mobile phones. Likewise the colour of the Samsung D500 was said to be blue black but the deal check list and sales invoice showed the phones as black. Mr Andrews said that he did not change the invoice as he wanted continuity through the documents.

(3) There were three different manual types as well as two different software languages.

(4) The inspection team powered up a lesser number of phones than the one per cent requested.

273. The NEMESIS database showed that around 10 per cent of the phones were in fact Sony Ericsson phones. A1 scanned them against the database held for the Appellant.

274. The goods were sent on 27 January 2006 before the date of the inspection report. Mr Andrews thought that the inspection report was probably e-mailed the day before.

275. Mr Andrews relied on references in his day book for 16 January 2006 which recorded the price of 500 Nokia 8801 at £520 and 832 Samsung D500 at £158 for the deal.

276. The Appellant paid Sprint £840,958.08 by means of a deposit of £500,000 with the balance payment on 30 January 2006. 3G Trade paid the Appellant £772,552.50 on 30 January just before the balance was paid by the Appellant to Sprint. Gross profit

on the deal was £56,813.50. The Appellant had at the time an opening balance of £719,592.03 in its account.

Deal 7 (03.02.06; 03/06 VAT period)

277. This deal involved sales of 105 Nokia 8800 and 995 Nokia 8801 to 3G Trade SA which were traced back to a tax loss of £100,140.49 with Myco Telecom Limited.

278. The documentation showed that

(1) The phones had two pin chargers.

(2) 25 of the boxes of Nokia 8800 were in a factory seal.

(3) The Nokia 8800 only had English manuals.

(4) The inspection team only power tested one Nokia 8801 mobile phone.

(5) According to the inspection report, the Nokia 8801 mobile phone which was designed for the North American market had two pin EU chargers and a European warranty

279. The IMEI numbers provided by the Appellant showed that 509 of the phones in this deal were repurchased from Sprint Communications Services in deal 9 at £17 less than in this deal.

280. There were no comprehensive notes in Mr Andrew's day book on deal. There was, however, a record regarding the financing of the deal and the balances required to pay for the stock. According to Mr Andrews, Nokia 8800 and 8801 were in high demand at the time.

281. The Appellant paid Sprint £492 (8800) and £527 (8801) per phone. The Appellant sold the phones at £531 for 8800 and £569 for 8801. Mr Andrews recalled that the high sale prices made 3G's owner's eyes water.

282. The Appellant paid the purchase amount of £676,829.38 by means of a deposit of £500,000 at 1439 on 2 February 2006 with the balance on 3 February 2006 which was not transferred by the Appellant's bank until 6 February 2006. 3G Trade's payment was credited to the Appellant's account on 2 February 2006 at 1533. The net cost of the deal to the Appellant was £ 576,025 which gave a gross profit of £45,885.

Deal 8 (16.02.06; 03/06 VAT period)

283. This deal involved the sale of 691 Nokia 8800 to Mobile World GmbH which was traced back to a tax loss of £64,281.26 with Puwar UK Limited.

284. The documentation revealed that

(1) The phones had two pin chargers

(2) 129 of the boxes were in factory seal.

(3) The inspection report showed that the sample of mobile phones had three different language codes, three different manual types and two different types of warranties. There was note on inspection report from Mrs Andrews *not all manuals English and Jurgen of Mobile World was okay with that.*

(4) A1, the inspection agent, had noted that a number of the phones were in scuffed boxes. On receipt of this information Mr Andrews said he complained to Cybacomms and spoke to Jurgen of Mobile World about whether he was prepared to accept a reduced phone consignment. According to Mr Andrews, Jurgen accepted the smaller consignment. Mr Andrews noted the word *amended* on Mobile World's purchase order but made no record of the purported conversation with Cybacomms and Jurgen.

(5) The inspection team was asked to power up one per cent (6) of the phones but the team only tested three.

(6) The trading deal check list revealed that Hawk, the freight forwarder, had stated that the goods had changed ownership eight times in three days. Mr Andrews denied that this fact regarding change of ownership had put the Appellant on notice of potential fraudulent deals. According to Mr Andrews, he would have expected a lot more trades for a product which was in high demand. The Appellant had requested the freight forwarder to supply this information because Officer Watson had requested it. Mr Andrews at the time disagreed with Officer Watson about the reasons for requiring such information from the freight forwarder.

285. The Appellant's customer, Mobile World shipped back the goods on 16 February 2006 to Hawk Logistics in the UK. The goods were released to Universal Systems, which in turn released them to the defaulting trader in deal 12, K&S Communications Limited.

286. The mobile phones were despatched before payment was made. Mr Andrews stated that the Appellant had allowed this to happen despite making no enquiry about the financial standing of Mobile World.

287. This deal had a low mark up 3.8 per cent when compared with the Appellant's mark ups for the other deals. Mr Andrews maintained that it was a commercial decision to accept the deal.

288. Mr Andrews referred to entries in his day book on 8 February 2006 which covered the period up to 16 February 2006. This showed that Jurgen of Mobile World was looking for various models of phone including Nokia 8800's at a price of £470. Cybacomms was selling at £452.50.

289. Mobile World paid the Appellant after it had paid Cybacomms. The Appellant at the time had a balance of £980,000 in bank. Net cost £367,396.06 yielding a gross profit of £12,092.50. Apparently Mobile World had instructed its bank to pay for the mobile phones on the 16 February 2006. The Appellant's bank, however, did not

inform Mr Andrews or Mr Case that the payment from Mobile World had been made on the 16 February 2006. According to Mr Andrews, this confusion about when Mobile World made its payment resulted in Mobile World canceling another deal.[20]

Deal 9 (02.03.06; 03/06 VAT period)

290. This deal involved the sale of 2,000 Nokia 8801 to 3G Trade SA which was traced back to a tax loss of £177,660 with Aristaeus Limited.

291. In this and subsequent deals Mr Andrews used 4G as the inspection agent. According to Mr Andrews, the price charged by 4G was significantly less than that charged by A1. Mr Andrews also stated that A1 was too busy to do the inspection in any event on that day. A1 was, however, content to carry out the IMEI check for the Appellant against its database.

292. The documentation revealed that

(1) The phones had two pin chargers.

(2) The manual was stated to be in English.

293. Mr Andrews considered the quality of 4G's inspection reports sufficient despite the general comment on 4G's report "*everything all-right*".

294. The IMEI numbers of 509 phones in this deal matched those transacted in deal 7. Mr Andrews believed 4G were sending the numbers to A1 to check against the database. Mr Andrews believed A1 were still doing the IMEI checks even though it had been replaced by 4G. The Appellant produced no invoices from A1 for carrying out these checks after A1 had been replaced by 4G.

295. There was no record in Mr Andrews' day book of any deals from 27 February to 14 March 2006. Mr Andrews believed he was keeping notes elsewhere. Mr Andrews, however, stated that he was aware on 2 March 2006 that Sprint had 2000 units of Nokia 8801 available for sale. According to Mr Andrews, he negotiated a price of £551 with 3G. The phones were bought at £510 per item.

296. Appellant sold the goods at £551 which was around twice the sales price of US$ 501.52 quoted by Nokia. Mr Andrews did not think that this was odd.

297. The Appellant had insufficient capital in the bank to pay for this trade. In order to finance this deal the Appellant agreed to pay a deposit of £700,000 on 2 March 2006 to Sprint against a sales invoice of £1,198,500. 3G Trade paid the Appellant £1,102,000 at 0857 on 3 March 2006. The Appellant then at 1232 on 3 March 2006 transferred £998,523 to Sprint: £498,500 balance for this deal and £500,000 deposit for next deal. The net cost of this deal to the Appellant was £1,020,000 which produced a gross profit of £82,000.

[20] See paragraphs 387 to 403 which deals with the cancelled deal.

Deal 10 (03.03.06; 03/06 VAT period)

298. This deal involved the sale of 1,901 Nokia 9300i to 3G Trade SA which was traced back to a tax loss of £122,457.67 with K & S Xport Limited.

299. The documentation showed that

(1) The phones had two pin chargers.

(2) The manual languages were English and Dutch compared with the software languages of English and Spanish.

(3) 4G's inspection report was limited. 4G supplied no information about cut outs or Customs stamps. 4G did not investigate whether the IMEI numbers matched. According to Mr Andrews, he was not concerned with 4G's apparent failure to comply with the Appellant's inspection request. Mr Andrews said that these matters would have been considered in his discussion with 4G about the report.

300. There were no notes on this deal in Mr Andrew's day book. Mr Andrews stated that he was aware that 3G Trade was enquiring about Nokia 9300i which was in high demand..

301. In this deal the Appellant's supplier, Sprint, agreed to take deposit of £500,000 with the balance at a later date. 3G Trade paid for the goods on 6 March 2013. On 6 March 2006 Mr Andrews sent a revised instruction to Mr Case's Personal Assistant to pay the balance of £328,693.43 for this deal and further £440,000 for next deal. According to Mr Andrews, the Appellant received £500,000 from an investor on 7 March 2006.

302. The Appellant purchased the phone at £371 per unit and sold at £400.50. Net cost of the purchase to the Appellant was £705,271 (£828,693.43 with VAT) yielding a gross profit of £56,079.50.

Deal 11 ((06.03.06; 03/06 VAT period)

303. This deal involved the sale of 2,000 Nokia 9300i to 3G Trade SA which was traced back to a tax loss of £138,985 with K & S Xport Limited.

304. The documentation showed that the phones had two pin chargers. The inspection reports confirmed no duplicate IMEIs; all IMEIs matched in and out of box. Further the report showed no Customs' Stamp and no cut outs.

305. There were no notes in Mr Andrews' daybook about this deal. Mr Andrews was aware that the Nokia 9300i model was in high demand. According to Mr Andrews, the market price of £400 per unit for the phones had soared to £435, which was partly due to Customs holding onto substantial numbers of these phones at Heathrow. Mr Andrews said he negotiated a price of £432 for one unit with 3G trade.

306. The Appellant paid a deposit to Sprint on 6 March 2006 with the balance on 7 March 2006. 3G Trade paid £863,986.14 by electronic transfer on 7 March 2006. The net cost to the Appellant was £800,000 which produced a gross profit of £65,000.

Deal 12 (16.03.06; 03/06 VAT period)

307. This deal involved the sales of 1,100 Nokia 8801, and 2,070 Nokia 9300i to 3G Trade SA which were traced back to a tax loss of £241,743.60 with KSK Trading Limited.

308. The documentation showed that

(1) The phones had two pin chargers

(2) The manuals for the Nokia 8801 models were in English. The Nokia 8801s were designed for the American market.

309. Mr Andrews referred to the 14 March 2006 entry in his day book which mentioned Wizard selling, and Sprint having Nokia 6680. Mr Andrews said he phoned Lucky at Sprint for stock and was given the following prices for the various Nokia models: £ 400 for 9300i, £510 for 8801, £551 for 8801 and £432 for 9300.

310. The Appellant had no credit in the bank but was aware of the potential VAT repayment of £1,456,000 for 12/05. The Appellant arranged with the bank for payment to be made to Sprint on 16 March 2006 of £1,632,075 but due to an administrative error on the part of the bank payment was not made until 17 March 2006. Mr Andrews' daybook recorded problems with the bank. As a result of the bank's error 3G Trade paid for the goods before the Appellant transferred electronically the sum amount to Sprint in two batches £606,086.08 and £894,226.08. The net cost to the Appellant was £1,389, 000 which produced a gross profit of £111,340.

Deal 1 (13.4.06 06/06 VAT Period)

311. This deal involved the sale of 2,100 Nokia 8800s to 3G Trade SA which was traced back to a tax loss of £146,430.38 with Apollo Communications Limited.

312. The documentation showed that the mobile phones had two pin chargers and an English manual.

313. On 13 April 2006 the Appellant's customer sold the phones to International Mobile, an Italian trader, who consigned the phones back to Pauls Freight in the UK.

314. Mr Andrews' daybook entry for 10 April 2006 indicated that the Appellant was doing business with P at Global Star. The entry also showed that Mr Andrews had an appointment on that day with Lucky of Sprint who assured Mr Andrews that he was doing full diligence. Further Bulent of 3G Trade was looking to buy Nokia 8800s for £430 per unit. Mr Andrews said that he agreed a buying price of £400 per unit from Sprint and sold to 3G at £428 per unit.

315. At the time the Appellant only had £15,000 in bank because Mr Case had put £1,500,000 in the overnight money market. The Appellant had agreed with Sprint a split payment of £493,500 on 12 and 13 April 2006 respectively. 3G paid the full amount £898,786.06 at 1506 on 12 April 2006.

316. The Appellant's net cost of the deal was £840,000 which produced a gross profit of £58,800.

Issues Arising from the Appellant's documentation and the Individual Deals

Discrepancies between Specification and Trade

317. The Appellant placed stock on the thoroughness of its documentation in relation to each deal which Mr Andrews recorded on a *Trading Deal Check List.* In the table on page [R1-320], Mr Fletcher analysed the level of detail on the purchase orders of the Appellant and its customer, the sales invoices of the Appellant and it supplier, and the inspection reports provided to the Appellant, and concluded that in several instances the documentation was missing important specifications. In Mr Fletcher's opinion without this information it would be impossible to know what phones were being ordered.

318. According to Mr Fletcher, the failure of the Appellant and its trading partners to specify handsets correctly had potential disastrous financial consequences, with a trader incurring additional costs such as adapting the handset for additional languages, inserting new software CDs or sourcing an instruction manual in the appropriate local language. Mr Fletcher noted that, while these were relatively trivial tasks, the combined cost of adaptation could easily exceed £5 per unit. Worse still, the delays could result in the intended trade failing to complete, leaving the trader with ruinous levels of unwanted stock.

319. Mr Andrews disagreed with Mr Fletcher's opinion saying that traders knew what was contained in a particular pack: manufacturer habits were known through their own advertising, and that in a high speed world it only took 20 seconds on the phone to specify the key data for a potential deal; "brevity was, in Mr Andrew's opinion, a matter of common sense and not at all a negative indicator." Mr Fletcher disagreed, pointing out the likelihood of many different variants of an individual handset, and that it was a matter of commercial necessity to specify the products which were being bought and sold.

320. HMRC relied on the fact of insufficient specification of the phones traded as a pointer of the artificiality and the contrivance of the transactions. The Appellant, on the other hand, considered that such discrepancies were minor and accepted as part of grey market trading. In the Appellant's view such minor variations did not come close to satisfying the knowledge threshold.

321. The Tribunal's starting point is that it was accepted by Mr Andrews that in virtually every deal there were inconsistencies between what the Appellant had asked

for from its supplier and what it had been given[21]. Mr Andrews was not concerned by the inconsistencies because they involved the accessories to the handset, such as manuals and chargers, and that it had always been like that in the grey market. Mr Andrews stated that it was completely normal for him to be given something that he had not asked for.

322. The Appellant presented its difference of view with HMRC as a conflict between Mr Fletcher's expert opinion and Mr Andrews' significant experience in grey market trading. The Appellant argued that the Tribunal should favour Mr Andrews' evidence because it was based on what actually happened in the grey market. The Tribunal has difficulties with the Appellant's argument. In the Tribunal's view, Mr Andrews' depiction of custom and practice was highly irrational and carried considerable risk in the trading of high value and low margin goods. But if the Tribunal is wrong in preferring Mr Fletcher's rational exposition of the grey market, the Appellant has still not given an adequate explanation why it specified in the first place the requirements in its documentation if they did not matter.

The Inspection Reports

Cut-Outs

323. There were four deals (1 & 2 12/05 period and 1 & 3 03/06 period) where the inspection reports showed cut outs on the cartons containing the mobile phones. In respect of these four deals there was evidence that the mobile phones were being carouselled. In the 12/05 deals the mobile phones were immediately consigned back to the UK after being despatched by the Appellant. In the 03/06 deals the NEMESIS database showed that the phones had been previously scanned by HMRC.

324. HMRC maintained that cut outs were an indication that attempts had been made to conceal the fact that the goods were being carouselled by removing evidence of previous Customs stamps. In contrast, the Appellant claimed that the cuts outs related to the removal of labels belonging to the suppliers of the mobile phones. According to the Appellant, the removal of labels was common practice so as to prevent the Appellant from knowing from whom its supplier purchased the mobile phones.

325. Officer Saunders gave evidence that he did not witness the removal of labels when he inspected freight forwarder warehouses. He concluded that the cut outs were connected with the extinguishment of previous Customs stamps.

326. The Appellant, on the other hand, relied on the evidence of Mr Cummings, Mr Andrews and Mr Poulton who said that labels were routinely cut out in order to preserve commercial confidentiality. The Appellant also introduced a short video clip which demonstrated the ease with which labels were removed with the use of a Stanley knife. Further the Appellant pointed out that Officer Saunders had never seen a Customs stamp removed and that ink from a stamp might soak through and be visible if the outer skin alone was removed.

[21] See transcript 26.1.2006 pages 40 -42.

327. HMRC was equally critical of the evidence of Mr Cummings and Mr Andrews. According to HMRC, Mr Cummings' evidence was inconsistent and of very limited value. Mr Cummings admitted he had no experience of freight forwarders and of exporting goods. Mr Andrews had not seen a Customs stamp, and had contradicted Mr Cummings' evidence by stating that Mr Cummings had shipped goods to a freight forwarder for export.

328. The Tribunal concluded that whether labels were routinely removed by suppliers was not the correct question to address in the circumstances of this case. The inspection reports commissioned by the Appellant revealed cuts outs in four of the sixteen deals. The Tribunal is satisfied that the cut outs in these four deals were, in all probability, connected with Customs stamps, which was supported by the undisputed evidence that the mobile phones in these deals had been either previously scanned or consigned back immediately to the UK. The correct question, therefore, is whether the existence of the cut outs put Mr Andrews on notice of irregularities with these four deals.

329. Mr Andrews said that the cut outs did not put the Appellant on notice of irregularities because he assumed that they were to do with the supplier's labels. Further, if they were not related to the supplier's labels he would have expected the inspection agent to have alerted the Appellant of the possibility that the cut outs were somehow connected with Customs stamps.

330. The Tribunal is not convinced with Mr Andrews' explanation because:

(1) If Mr Andrews was correct that the cut-outs were removed labels and that removal of such labels was standard throughout the industry, the Tribunal would have expected the inspection reports for virtually all the deals to have revealed cut outs. The fact that cut outs were present in only four of the 16 deals suggested that it was an unusual event which would have put the Appellant on notice.

(2) In those four deals not every box in the same supply had cut outs. In deal 1, 12/05, there were only three cartons which had cut outs.

(3) A1's proforma reports contained a box entitled, *Customs Stamps*, which was immediately followed by a box entitled, *Cut-outs*. The Tribunal considers this juxtaposition strongly suggested that the reference to cut-outs was a reference to removed Customs stamps.

(4) The 4G inspection reports were also instructive in this regard. Although they did not include boxes for Customs stamps or cut outs, they did provide for *Other Comments*. The Tribunal is satisfied that the connection between cut outs and Customs stamp was clear in its report relating to Deal 1 06/06 in which 4G said:

> "No duplicate IMEIs were found all IMEIs matched outer and inner boxes.

> No customs *stamp*[22] found on box
> No cutting or scratched stamps were found
> Stock was new and in good condition"

(5) The Appellant's purchase orders stated that it would not accept consignments with *"no stamps or removed stamps or labels"*.

331. The Tribunal is satisfied from the above findings that Mr Andrews knew that cut outs referred to removed Customs stamps. The Tribunal is not convinced by Mr Andrews' excuse that he relied on the Inspection agent to tell him whether the cut out was suspicious. There was no need for the Inspection agent to contact Mr Andrews again. The report itself was explicit about the existence of cut outs which should have prompted Mr Andrews to ask questions about the bona fides of the particular deal.

Two Pin Chargers

332. The inspection reports showed that the mobile phones had two pin chargers in 12 of the disputed deals, a mixture of two and three pin chargers in three deals, and three pin chargers in one deal.

333. HMRC contended that the existence of two pin chargers in almost all the mobile phone consignments indicated that the stock was not intended for the UK market. In those circumstances the Appellant must have been aware that there was no commercial rationale for the presence of such consignments in the UK. It also followed that their importation into the UK served no legitimate purpose which in turn should have raised questions on the Appellant's part about the integrity of its supply chain.

334. Mr Andrews disagreed, stating that the cost of replacing a charger was minimal when compared with the value of the handset. Mr Andrews described a number of situations where an authorised distributor might have substituted a two pin charger in place of a three pin charger, namely where it could get a better price for the goods in the EU or it decided to dump back mobile phones into the EU. Mr Cummings confirmed that on occasions at Unique Distribution a three pin charger was replaced with a two pin charger and vice versa.

335. The Tribunal considers Mr Andrews' explanations for the preponderance of two pin chargers in the overwhelming majority of the Appellant's deals as highly improbable when set against the particular circumstances of this Appeal. The Appellant did not trade with authorised distributors, and it knew there was at least one UK grey market trader in the supply chain. That being so, if there was an authorised distributor in the chain substituting two pin chargers Mr Andrews should have known that it would have made no commercial sense for that authorised distributor to sell to another UK trader, particularly as it would get a better price by selling direct to an EU customer.

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[22] The Tribunal has inserted the *m* in *stap* to correct an obvious spelling mistake.

336. Finally the Appellant adduced no persuasive evidence of UK traders actively replacing the chargers in the mobile phone consignments. In this respect Mr Cumming's evidence was contradictory. He did not know why Unique substituted the chargers. He also changed his evidence by stating that it was wrong to say that he frequently substituted two pin chargers.

337. The evidence of the supply chains for the Appellant's deals revealed the true reason why the consignments had two pin chargers which was that they had been imported into the UK for the sole purpose of effecting a VAT fraud. Mr Andrews on his own admission ignored this possibility as a potential explanation for the predominant presence of two pin chargers in the Appellant's deals.

Inconsistencies between the Appellant's documentation and Inspection Reports

338. The Tribunal identifies below the following inconsistencies:

> (1) The inspection reports showed three deals with mixed consignments of two/three pin chargers. The Appellant's customer had specified two pin chargers.
>
> (2) In deal 5 03/06 the Appellant's customer required Euro stock but the consignment had three pin chargers. Mr Andrews originally argued that Euro stock included three pin chargers but under cross-examination accepted that this was not the case. Mr Andrews then suggested that his customer had bought them for eventual export outside the EU.
>
> (3) A1's reports showed that the samples of mobile phones inspected for each deal had on the whole a variety of different language manuals, different software languages and different keypads. This wide variety represented a wide departure from the Appellant's specification of *Central European* or *European*.
>
> (4) In three deals the inspection report showed a different colour for the handset from that specified in the documentation. Mr Andrew's explanation for the variations in two of those deals was that the colour identified by the inspection agent was similar to that specified.

Power Up

339. The Appellant required the inspection agent to power up one per cent of the mobile phones. A1 failed to power up the requisite percentage of mobile phones in every deal that it was instructed to do so. Mr Andrews was content with the lower number tested. According to Mr Andrews, the powering up of just one mobile phone was sufficient to demonstrate that it was not a dummy trade. He also said that the lower number powered up avoided grubby finger-marks on the new phones. Mr Andrews offered no plausible explanation for why he did not alter the instructions to the inspection agent. He simply said it was laziness on his part.

Warranties

340. In deals 2, 12/05; 3, 03/06; and 4, 03/06 some or all of the stock had no warranty. Further a number of inspection reports for Nokia handsets specified that the handsets came with an European and African warranty.

341. Miss Clarke of Nokia and Mr Fletcher gave evidence that Nokia handsets had regional warranties which applied to the region where the handset was intended for sale. The European and African warranty as recorded by the inspection agent did not exist.

342. At first Mr Andrews insisted initially that all Nokia handsets enjoyed the benefit of a global warranty. When challenged with the evidence of Miss Clarke and Mr Fletcher, Mr Andrews said that warranties were not particularly important to him because the retailer would be responsible for the warranty. At the September 2013 hearing Mr Andrews stated that the limited regional warranty would ensure that the mobile phone would be covered in another region.

343. The Tribunal finds Mr Andrew's explanations for the absence of appropriate warranties for some of the mobile phone consignments contradictory and unconvincing. The Tribunal agrees with Mr Fletcher's evidence that the warranty was important and fundamentally affected the value of the mobile phone. It gave the customer some assurance that a fault would be dealt with, not at the customer's expense. The Tribunal is satisfied the absence of a warranty was a matter that the Appellant should have had regard to in assessing whether to go ahead with a particular transaction.

Other Discrepancies with the Inspection Reports

344. The inspection reports involving Nokia phones suggested there were a total of six different language combinations on the phones that the customer received. Of these only one combination corresponded to one of the language packages within the specification for Nokia phones.

345. The inspection reports for deals 7 and 8 03/06 indicated that 25 and 129 of the boxes of Nokia 8800 respectively were in their factory seals which indicated that the Appellant's suppliers, Sprint and Cybacomms had not inspected the goods. This did appear to bother Mr Andrews despite the fact that the declarations signed by the suppliers stated that they had examined the goods.

346. In deal 5 03/06 the report revealed the existence of loose stock which again ran contrary to the Appellant's requirement for the mobile phones to be in the original manufacturer's cartons.

347. In deal 2 03/06 the IMEI numbers for the mobile phones were not checked by the inspection agent.

348. In deals 1 and 6 03/06 the Appellant received the inspection reports after the goods had been released or sent to its customer.

Overall Conclusions on the Inspection Reports

349. HMRC argued that the inconsistencies identified by the inspection reports, and the Appellant's failure to address them was highly significant and demonstrated the artificiality of the Appellant's deals. The Appellant, on the other hand, contended that the inconsistencies were minor and a normal feature of the wholesale trade which Mr Andrews had been dealing with as a trader without difficulty for many years.

350. If the Appellant's position was correct, the Tribunal does not understand why the Appellant commissioned inspection reports in the first place, particularly as it would appear that the reports had no value because, according to Mr Andrews, the Appellant's customer would take the goods regardless. The fact that in two of the deals the Appellant released the mobile phones before receipt of the inspection report was indicative of the Appellant placing no value on the reports.

351. The Tribunal finds that the inconsistencies and the Appellant's disregard of the inspection reports relevant to the question of the Appellant's state of knowledge. The discrepancies concerning the cuts outs, the preponderance of two pin chargers, and the absence of appropriate warranties were indicators of potential fraud, whilst the others demonstrated the lack of serious commercial intent on the parts of the Appellant and its trading partners.

352. Mr Andrews claimed that he resolved some of the discrepancies by speaking either to the inspection agent or to the particular trading partner on the phone. There was no documentary evidence to substantiate Mr Andrews' assertion except for deal 8, 03/06, where the purchase order was marked *amended*, and Mrs Andrews had recorded that *Jurgen of Mobile World was content with all the manuals not being in English.*

353. The Tribunal is satisfied that at the time of making the deals Mr Andrews did not address the various concerns highlighted by the inspection reports. In the Tribunal's view, this was clear from his evidence, where Mr Andrews was dismissive of the inconsistencies. His explanations for not addressing them had the character of rationalizations after the event. The Tribunal found his explanations implausible. In short, the Tribunal holds that the Appellant should have addressed the inconsistencies in the inspection reports, and its failure to do so was relevant to the state of its knowledge about the fraud.

The Inspection Agents

354. From deal 9 on 2 March 2006 the Appellant used 4G instead of A1 as its inspection agent. Mr Andrews acknowledged that the reports produced by 4G were less detailed than those of A1 and that the Appellant was not getting the service it expected from 4G.

355. Mr Andrews gave conflicting accounts for changing from A1 to 4G. First he suggested that the Appellant used 4G because it operated out of Edge Logistics, the freight forwarders, where the Appellant was carrying out the majority of its business. When it was pointed out that the Appellant had used A1 at Edge Logistics in previous

deals, Mr Andrews offered another explanation which was that 4G was considerably cheaper than A1. After further questions on this topic Mr Andrews finally stated that the Appellant had probably switched from A1 to 4G when he learnt in February 2006 that the Appellant's deals with MNR in September 2005 had been traced to a defaulting trader. A1 and MNR were owned by the same person, which Mr Andrews knew at the time of the disputed deals.

356. After the change to 4G, A1 still retained the Appellant's database of IMEI numbers. According to Mr Andrews, A1 on behalf of 4G, continued to check the Appellant's IMEI numbers against the database. Mr Andrews, however, was unable to corroborate the continuing engagement of A1 with documentary evidence of invoices from A1 about charges for data storage and comparison.

357. The Tribunal considers the Appellant's relationship with its inspection agents lacked transparency. Mr Andrews was unable to give a definite answer on A1's continuing involvement with the Appellant after instructing 4G in relation to the keeping of the IMEI database. The Tribunal also did not understand Mr Andrew's willingness to accept what he termed as unsatisfactory service from 4G.

Freight Forwarders

358. Officer Watson recommended that the Appellant request the freight forwarders to provide details of the changes of ownership of the mobile phone consignments involving the Appellant. Officer Watson advised the Appellant that frequent changes in ownership were an indication that the transaction was tainted by fraud.

359. The Appellant followed up on Mr Watson's recommendation but received negative responses from Pauls Freight, which said it would not co-operate for reasons of security and confidentiality, and from Edge Logistics which said that it was not company policy to divulge details of transactions other than to a party directly involved.

360. Hawk Logistics, however, supplied change of ownership details in two deals. In deal 3, 03/06 Hawk advised that the consignment had only been in the warehouse for one day and there had been no previous transactions with the consignment. In deal 8 03/06 Hawk advised that the goods had changed ownership eight times in three days.

361. Mr Andrews did not consider Hawk's revelation in relation to deal 8 put him on notice of fraudulent dealing. According to Mr Andrews, he would have expected alot more trades for a Nokia 8800. Mr Andrews referred to his experience of observing the fishermen at Ullapool to demonstrate his point that the wholesaling of goods involved frequent changes of ownership. Mr Andrews stated that he had disagreed with Officer Watson at the time when the recommendation was made.

362. The Tribunal is not convinced with Mr Andrew's reason for ignoring the information supplied by Hawk on the changes in ownership in deal 8. The Tribunal is satisfied on the evidence that Mr Andrews took no action at the time he received this information from Hawk. Whatever Mr Andrew's personal views on the significance

of the frequent changes in ownership, he knew at the time that HMRC considered it to be an indicator of fraud but he chose to ignore it.

Nokia 8800 & 8801

363. Six of the disputed deals involved the purchase and sale of Nokia models 8800 and 8801. Deals 6, 9 and 12 03/06 involved only Nokia model 8801, deals 8 03/06 and 1 06/06 concerned Nokia model 8800, and deal 7 03/6 involved the sale and purchase of both models 8800 and 8801.

364. Nokia took the decision to produce two virtually identical phones, the 8800 model which was designed for regions outside the Americas and the model 8801 designed solely for the Americas. The 8800 had three frequencies, 900, 1800 and 1900 megahertz. The 8801 had two of those three frequencies, 1800 and 1900 but used the 850 megahertz frequency instead of the 900. Model 8801 would also have had two flat pin chargers and warranties for Americas.

365. The GfK data of retail sales for these two models showed that in 2006 570,884 Nokia 8800 handsets were sold in retail sales in Europe and the UAE, whereas only 299 Nokia 8801 handsets were sold in those markets. During 03/06 period the Appellant purportedly exported 4,595 8801 models to the EU.

366. Mr Andrews knew at the time the deals were made that model 8801 had been manufactured for use in the Americas, and that it could not be used on all service providers in Europe. The Appellant, however, insisted it was a fallacy to say that model 8801 would not work or would require significant adaptation for use outside the Americas and that there was a market for model 8801 in Europe. In this respect Mr Case in his fifth witness statement exhibited documentation which he said showed that the 8801 could be used widely in Europe, and that it was being sold in 2006 on the *alibaba* website by a UK trader which was not an authorised distributor. Finally Mr Case produced an article dated 2 November 2005 reporting that Nokia was restricting the amount of models 8800 and 8801 entering the market, which he said generated the demand in Europe for model 8801.

367. The Gfk data for 2006 showing only 229 sales of Nokia 8801 handsets in Europe and the UAE undermined Mr Case’s assertion that there was a European market for Nokia 8801 models. The Tribunal considers the Appellant’s justification for there being an European market for a model 8801 was an afterthought and did not constitute its state of mind at the time of entering the disputed transactions.

368. The Tribunal is satisfied that the Appellant disregarded the following warning signs present at the time of purchasing model 8801 which would have put the Appellant on notice of the suspicious nature of the deals.

> (1) The documentation for all the Appellant’s deal chains in which Nokia 8801s were traded suggested that the phones were of European specification. The Appellant’s customer, 3G Trade, raised purchase orders specifying that goods must be of Original Euro stock. The Appellant’s

purchase orders addressed to its supplier, Sprint, for 500 and 995 handsets of Nokia 8801 chrome 2-pin CE with Central European Languages manuals and software, and 2,000 and 1,100 Nokia 8801 2-pin with European or Central European languages and software. Mr Andrews knew that model 8801 was not designed for the European market but did not question why the deal documentation described the model 8801 as Euro-stock.

(2) In deal 7 03/06 the Appellant sold the 8801 at a higher price than the 8800 (£569 v £531), despite the fact that the latter was designed for the European market. Mr Andrews' explanation was that models 8800 and 8801 were in such high demand that customers would buy whatever they could get hold of. Mr Andrews' explanation defied common sense. The Tribunal agrees with HMRC's observation that it was perfectly obvious that in any circumstance, the model 8800 would attract a higher price than that for model 8801 in the EU. Further in deal 7, both models were being sold to the same customer at the same time. In such circumstances the model 8800 would attract a higher price. Finally, if as Mr Andrews asserted, models 8800 and 8801 were in such demand it would also make it unlikely that any models 8801s would be available outside their intended market.

(3) It was improbable that a retailer in EU would buy a model of a phone (8801) which he knew that some of his customers would have no interest in because it would not work on occasion or not work at all on the network his European customers have subscribed to, particularly as there was an identical model (8800) available specifically designed for the European market.

(4) During January to March 2006 the Appellant sold the model 8801 at prices which varied between £551 and £569. This was almost double the Nokia list price of US$501.52 (£285.12) for this handset. Ms Clarke's evidence was that the price at which the Appellant sold the phones wholesale was approximately £100 more than what she would have expected.

IMEI numbers

369. Mr Andrews accepted that the Appellant kept a copy of the A1 database of IMEI numbers of the mobile phones traded by the Appellant. In three deals HMRC identified from NEMESIS that the mobile phones had been previously scanned which suggested that they were involved in circular trades. The Tribunal acknowledges that the Appellant did not have access to NEMESIS, and may not have been aware of the adverse findings in respect of these three deals. The Tribunal, however, considers that the Appellant should have known of the following anomalies from its own records:

(1) In deal 4, 03/06 the Appellant supplied 2,000 IMEI numbers to HMRC. The A1 report showed that only 575 IMEI number were scanned, although A1 invoiced for 2,000 scans. Mr Andrews in cross examination

stated[23] that A1 must have arrived late at the freight forwarders and did not have time to scan all the boxes. The Tribunal observes that Mr Andrews failed to identify the discrepancy at the time he received the invoice from A1 and that he gave no explanation for the supply of 2,000 numbers when only 575 were taken.

(2) In deal 05, 03/06 the IMEI numbers provided to HMRC contained 1,012 duplicated entries. Mr Andrews did not notice this at the time the records were taken nor when they were subsequently supplied to HMRC.. Mr Andrews said it was a clerical error on the part of A1, the inspection agent, but he only discovered that after it was brought to his attention by HMRC. NEMESIS also showed that the phones scanned comprised two NEC models E616 and E616V instead of the one model E616 specified in the deal documentation. Mr Andrews was not interested in the variation because he considered that both models effectively had the same functionality. The inspection report revealed that the agents powered up an E616V which Mr Andrews failed to spot at the time the report was supplied.

(3) In deal 6, 03/06 the check of the Appellant's IMEI numbers against NEMESIS revealed that 10 per cent of the consignment consisted of Sony Ericsson K750i phones which were not specified in the deal documentation. Mr Andrews said that he had no idea how the Sony Ericsson phones were included in the consignment. A1, the inspection agent, suggested that there may have been an error when the phones were scanned. 3G, the Appellant's customer, had not got the IMEIs for that batch of phones but said that it bought Sony Ericsson K750i phones from another UK supplier on that day. Mr Andrews accepted his inspection agent, was not doing a good job. Mr Andrews said that he did not have the time and skills to carry out spot checks on his inspection agents. Mr Andrews relied on the Appellant's customers getting back to him on discrepancies.

(4) The IMEI numbers provided by the Appellant showed that a large proportion of the stock purchased from Sprint in deal 7 03/06 was purchased again from Sprint in deal 9, 03/06. In both deals the Appellant sold the mobile phones to 3G. The trading check list for the deal compiled by Mr Andrews indicated that IMEI numbers had been checked and approved. The duplicated entries related to the Nokia 8801, the model designed for the Americas.

(5) Mr Andrews disagreed that the same stock had been purchased again in deal 9. In March 2007 he said he carried out his own check of the IMEI numbers for both deals and found no duplication of IMEI numbers. Even if Mr Andrews' checks were correct, he has still not explained why there was duplication with the IMEI numbers supplied to HMRC. The Tribunal observes that deal 9 was the first deal where the inspection was carried out

[23] Transcript 25.1.2012 Pages 207 & 208 para 14-17

by 4G. The Tribunal has already highlighted Mr Andrews' inability to give a definite answer on how 4G checked the IMEI numbers against the Appellant's database held by the Appellant's former inspection agents A1. In the Tribunal's view, the particular circumstances of deal 9 suggest that the Appellant failed to check the IMEI numbers for deal 9 against its database.

Daybook

370. Mr Andrews produced in evidence three notebooks known as daybooks: RA15 which covered his time with the Appellant, RA 16 which started on 4 December 2001 and ended with 23 April 2002, and RA17 for the period 8 August 2002 to 27 November 2002. RA16 and 17 related to Mr Andrews' employment with Unique Distribution.

371. According to Mr Andrews, he always kept such books on his desk to record his work activities. Mr Andrews stated that most of the books had been thrown out when he and his wife moved home but three books were found in a box brought down from the loft around 19 December 2011.

372. Mr Andrews stated that RA15 which covered the Appellant's trades showed his daily activity in searching the markets for business deals. Mr Andrews considered the book recorded a vast amount of information about prices, margins, discounts and calculations of profitability. The book also contained personal and domestic information. Mr Andrews said in evidence that in addition he would record conversations on *Post Its* and scraps of paper.

373. Mr Andrews was cross-examined in detail by Mr Foulkes on the information contained in notebook RA15.[24]

374. HMRC observed that on the Appellant's own account Mr Andrews' notebooks included no details whatsoever in respect of Deals 4, 5, 6 and 12, 03/06. Further the detail for others was far from complete. According to HMRC, there was nothing inconsistent with the existence of Mr Andrews' notebooks and the knowing participation of the Appellant in a contrived scheme in which it knew with which companies it should trade.

375. The Appellant, on the other hand, submitted that the notebooks constituted a contemporaneous record of Mr Andrews' efforts to source and supply phones in the market during the relevant period. The Appellant referred to Officer Saunders' evidence who described the book as *a warts and all* record of phone specifications and prices. Further the Appellant contended that such a record would be unnecessary if the deals were contrived as alleged.

376. The Tribunal makes the following findings on the notebook RA15:

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[24] See transcript 26.1.2012 para 1 page 43 to para 2 page 104

(1) The notebook was not a continuous and comprehensive record of Mr Andrews' dealings on behalf of the Appellant. Although the notebook recorded dates, there was not a note for every day of the year. There were often considerable gaps between the dates with some pages having lots of information whilst other pages had no or little information. Mr Andrews also stated that the information recorded under a particular date may not have happened on that date, as he did not always record dates.

(2) Mr Andrews accepted that the notebook did not contain details of specific deals (4, 5, 9, and 12 03/06). The Tribunal also considers that Mr Andrew's analysis of his notebook in relation to the deals as set out in paragraph 11 of his fourth witness statement did not show that specific deals had been brokered. Instead the analysis comprised random pieces of information that might relate to the deal in question, such as, the buyer seeking stock or price differences between buyers and sellers.

(3) Only one date in the notebook corresponded with the dates for the disputed deals.

(4) The notebook revealed that Mr Andrews talked to a limited number of companies about prices. The majority of these companies were either authorised distributors or companies (such as Wizard) that the Appellant was no longer doing business with.

(5) Mr Andrews did not record discrepancies between the documentation and the actual deals in his day book.

377. The Tribunal concludes that Mr Andrews' notebook (RA15) was not a comprehensive and contemporaneous record of his dealings on behalf of the Appellant. The book was no more than a collection of random notes covering his personal and business life. There was no direct relationship between the contents and the deals in question. Further the entries contradicted Mr Andrews' evidence that he would not deal with certain companies. Having regard to the above findings the Tribunal decides that the contents of notebook (RA15) did not support the Appellant's claim of not being involved in contrived trading.

Negotiating and Agreeing the deals in question

378. Mr Andrews in his fifth, sixth, seventh and eighth witness statement gave a detailed account of negotiating and agreeing each deal in question. Mr Andrews' account of each deal in question was based on his recollection of the events in question and his entries in the notebook.

379. HMRC did not cross examine Mr Andrews in detail on his evidence in relation to negotiating and agreeing deals as set out in his later witness statements. Counsel took the view that he could not take instructions on those matters. In his opinion it was not possible to say on a particular day whether Mr Andrews spoke to a particular trader. Counsel pointed out that HMRC had put to Mr Andrews that the deals were contrived, and that Mr Andrews clearly knew HMRC's case against the Appellant.

380. Appellant's counsel took a different view. He stated that Mr Andrews had painstakingly set out every detail about the deals in his later witness statements. In counsel's view, cross-examination was required of every relevant entry in Mr Andrews' witness statement. Further it was not open to the Tribunal to find against the Appellant on evidence not challenged by HMRC. Counsel pointed out that he clearly articulated the Appellant's position at the beginning of Mr Andrews' evidence on 9 September 2013, and that HMRC has not been taken by surprise[25].

381. HMRC considered that Mr Andrews had been cross examined on each and every deal at the January 2012 hearing, and it was relying on that evidence. The questions put by HMRC at the resumed hearing in September 2013 on the circumstances surrounding the making of Mr Andrews' later statements[26] were as follows

Questions by Mr Benson for HMRC	**Mr Andrews' response**
I suggest that in relation to each and every deal, you either knew or you certainly should have known that they trace back to a fraudulent default of VAT?	I did not and I have -- maintain that I had no idea of anything within my evidence that would have led me to thinking that.
Mr Andrews, you said that you found those books just before Christmas of 2011, it would have been.	I would have to refer to the statement exactly when it was. I think it was about the 19th.
If we have a look at your fourth witness statement, which is in A1/87. So this is the statement dated 2 January 2012?	Yes.
So that is when you actually make the statement. You had all the exhibits available to you, did you not, before the hearing started in January of 2012?	Yes, I did, yes.
So you had all the deal packs?	Yes.
And if you have a look at paragraph 11 -- so you would have done this before the 2 January 2012 -- you went	Yes.

[25] Transcript 9.9.2013 page 71 para 8

[26] Transcript 9.9.2013 pages 74 -79.

through your book trying to identify each deal which was the subject of the appeal.	
So you did have an opportunity, didn't you, to have a look at your day book and all the exhibits well in advance of giving evidence?	I would say that I had sight of them but not enough to do the detailed work that we carried out. It too probably -- I think it was four or five weeks to prepare the last witness statements that I have submitted, and it was a real forensic analysis job to try and put myself back in the mind that I was back at the time of doing the deals, which was some six years before.
You knew you were going to give evidence at the end of January 2012, didn't you?	Yes.
You knew it was important that you could give as much detail as possible about these 16 deals? It is just 16 deals you had to deal with.	I think it's clear to everybody here that I was woefully under-prepared and the representation that I had hadn't prepared me sufficiently for the depth of what I was expected to be going through within the Tribunal. That's why we were grateful to be able to be given the opportunity to present the statements as they were as a detailed analysis, and if you'd like to go through each point, detail by detail, within those, I would welcome it, because the amount of hard work I've put into it, every single sentence requires an answer or a question if you require. I'm quite happy to do that.
You had the opportunity to have a look at the material involving the 16 deals, yes?	Yes.
You knew you had to give evidence about the 16 deals and how they came about?	Yes, and if I can take you to this page that's A1/89, paragraph 11, that's the sort of depth that I was advised to go through to support the transactions that were part of the Tribunal's -- part of this tribunal.
You see, what I am going to suggest, very simply, is that your memory as far as what actually happened is suspect, is	Suspect before or after or what are you saying?

it not, now?	
You were asked questions by Mr Foulkes as to the detail of each of these deals. About telephone conversations, for example. Do you remember being asked those questions?	Yes.
You had no notes of telephone conversations, did you, in your day books?	Yes, I did.
There are perhaps one or two, but there are very few notes of what was actually said in your day book?	That's true.
For example, there are no notes, are there, of conversations you had with the person who carried out the inspections at the warehouse in your day book, are there?	I couldn't take you to any that I know of immediately, no. There may be, there may not be. I still haven't managed to go to that level of detail, but --
-- sorry, go on.	I put myself in the mind of each deal, and that must have taken three days or so, to look at each day and refresh my mind what had happened before, what was going on in my personal life, all that sort of thing, so I could be as absolutely accurate and helpful to the Tribunal as possible. may have been omissions, of course, of conversations. I didn't make a written note of every conversation I had with every inspecting agent or every customer, supplier. I certainly didn't keep an accurate record of everything like that. I wasn't expecting to have to present myself in this sort of situation, to justify those comments. Otherwise I would have taken every single note from every single conversation.
I am not talking about every single conversation. There are hardly any notes of any conversation in your day book?	It was primarily a day book for drawing in who was selling what, who was buying what, and what was likely to be going on in the market at the time.
And so when you come to write your	Sorry, I am waiting for the question.

fifth, sixth, seventh witness statements, you have in mind, don't you, the cross-examination of Mr Foulkes?	
You had that in mind, didn't you, when you came to sit down and write your fifth, sixth and seventh witness statements?	but it is not contrived. Of course it's in my mind, because I've just got out of the tribunal, and
So -- sorry.	And there are things in there that I'm thinking: oh, of course, I wish I'd remembered that, or I'd written that, and I may have said that wrong in the first tribunal because my memory hadn't been refreshed to the level that it is now for each and every single deal. So...
Or is it simply that in your witness statement you said, "Well, the person who was dealing with the inspections phoned me up and told me this, that and the other because when you were cross-examined by Mr Foulkes you realised that that's what you should have done?	No that’s incorrect
So you have tailored your account in your fifth, sixth and seventh witness statements, having been cross examined by Mr Foulkes?	I refute that. As I say, the sixth, seventh, eighth witness statements are the best of my knowledge. There may be inaccuracies in there as well. I can't be sure because it is a very long time ago but it has been done from memory and from what brief notes I do have available to me.
You had an opportunity to have a look at your day book and all the exhibits before you gave evidence in January 2012.	Albeit a brief review of it. The books were with Mr Tunney for some time as well.

382. The Tribunal considers from the above extract of the transcript on 9 September 2013 that HMRC challenged Mr Andrews’ evidence in his later witness statements. Mr Benson focussed his questioning on the overall circumstances surrounding the making of those witness statements rather than cross examining on every point of detail. Mr Benson referred to the fact that the notebooks and the deal packs were available to Mr Andrews when he gave his evidence in January 2012. In Mr Benson’s view, the only feature that had changed from Mr Andrews’ testimony in January 2012 and the making of the additional statements in May 2012 was that Mr Andrews had

been subjected to detailed cross-examination by Mr Foulkes. Mr Benson with his questioning was inviting the Tribunal to infer that Mr Andrews' description of the individual deals in his fifth, sixth and seventh witness statements was an attempt to put on a gloss on his answers to Mr Foulkes' questions at the January 2012 hearing.

383. The Tribunal is satisfied that Mr Benson's cross examination was sufficient to undermine the credibility of Mr Andrew's evidence in his fifth, sixth and seventh witness statements. The Tribunal, therefore, did not accept Mr Bridge's contention that HMRC had not challenged the evidence given by Mr Andrews in these witness statements. In the Tribunal's view, the approach of asking a question on every point of detail was not the sole means for casting doubt on Mr Andrews' evidence. Mr Benson's choice of concentrating his questions on what had changed from the January 2012 hearing was an effective way to contradict Mr Andrews' testimony.

384. The Tribunal now turns to the substance of Mr Andrews' fifth, sixth and seventh witness statements which gave Mr Andrews' account for each deal. Mr Andrews adopted the same format for describing each deal, starting with *negotiations and agreeing the deal, financing the deal, processing the deal, inspection of goods, review of the inspection reports, payments to supplier and from customer.*

385. The Tribunal concludes from the examination of statements that Mr Andrews' description of the deals under the various headings except *negotiations and agreeing the deal* added nothing new to his January 2012 testimony, and the identified anomalies with his evidence and discussed in detail in the preceding section on *Issues arising from the Individual Deals* still remained.

386. Mr Andrews' evidence under the *negotiations and agreeing the deal* heading gave a fuller account of how he brokered the deal including details of purported telephone conversations with suppliers and customers. The Tribunal, however, was not convinced with Mr Andrews' explanation. The Tribunal questions the reliability of Mr Andrews' recall of events that occurred some six years before. Also the Tribunal did not consider that Mr Andrew's entries in his day books substantiated the assertions made in his statement about the negotiations. The Tribunal has already found that the day book was no more than a collection of random notes covering Mr Andrews' personal and business life. In short the Tribunal holds that Mr Andrews' descriptions of *negotiating and agreeing the deal* in his later statements were no more than unsubstantiated assertions which carried minimal evidential weight.

Cancelled Deal

387. Mr Andrews in his eighth witness statement gave evidence on a deal which the Appellant said was cancelled.

388. The cancelled deal involved the potential sale of 3,000 Nokia 6230i mobile phones to Mobile World at £142.50 per unit which gave a total sale price of £427,500. The Appellant purchased the mobile phones from Wizard at £135 per unit giving a net transaction cost of £405,000 (excluding VAT). If the deal had gone through, the Appellant would have made an overall gross profit of £22,500.

389. Mr Andrews supplied various exhibits to demonstrate the existence of the cancelled deal. The exhibits included, amongst others, a *Trading Deal Check Sheet,* purchase orders, inspection requests and reports and bank instructions.

390. According to Mr Andrews, the prices for and the various formalities associated with the cancelled deal had been agreed on 16 February 2006. As a result of which Mr Andrews issued a *Transport Booking Confirmation* for delivery of the phones by 9am on 17 February 2006 to Mobile World at the freight forwarders, MBS, in Frankfurt, Germany. Mr Andrews also on 17 February 2006 gave instructions via Mr Case's daughter to the Appellant's bank to pay £475,875 to Wizard

391. Mr Andrews said that the deal did not take place because late in the day on 17 February 2006, Mr Case could not find a payment from Mobile World for deal 8 03/06. The Appellant decided that it could not progress the new deal with Mobile World in case it would not get paid for the mobile phones.

392. Mr Andrews apparently had heated exchanges with Jurgen of Mobile World about deal 8 on 17 February 2006. Mr Andrews told Jurgen that he would not release the phones in deal 8 until the Appellant had been paid for them with Jurgen telling Mr Andrews that he had instructed his bank to make payment for them on 16 February 2006. Mr Andrews said that Mr Case later found out that Mobile World had in fact paid for deal 8 on the day stated by Jurgen, and that the Appellant's bank was at fault in not communicating the payment. Mr Andrews said once he was informed of the payment he authorised release of the mobile phones in deal 8 to Mobile World on 20 February 2006.

393. Mr Andrews stated that Jurgen of Mobile World took offence with the Appellant's handling of deal 8, and cancelled the new deal. Mr Andrews also believed that Jurgen was aware that the market price for Nokia 6230i was falling and used the Appellant's mishandling of deal 8 as an excuse to get out of a loss-making deal.

394. Mr Andrews asserted that as soon as Mobile World cancelled the deal he instructed Mr Case's daughter to cancel the payment to Wizard for the supply of the goods. According to Mr Andrews, Wizard was not prepared initially to release the Appellant from its contract. Mr Andrews said that he eventually persuaded Wizard to drop their claim, provided the Appellant paid Wizard compensation in the sum of £18,000 plus VAT for loss of profit. On 21 February 2006 the Appellant issued instructions to its bank to make the payment to Wizard.

395. The Appellant argued that the existence of a cancelled deal was inconsistent with contrived trading. HMRC, on the other hand, questioned the legitimacy of the deal. HMRC also pointed out that even in contrived trading, things can go wrong, such as the phones might not have arrived back in the UK in time or the money was not available at the right moment when it was expected.

396. The Tribunal is not satisfied with the bona fides of the cancelled deal for the reasons set out in the following paragraphs.

397. At the January 2012 hearing Mr Andrews responded to a question put by Mr Foulkes that the Appellant as at 5 January 2006 had no intention of trading with Wizard because the Appellant had been informed in November 2005 of problems with the supply chains involving Wizard[27]. Mr Case was also explicit about not doing business with Wizard[28]. At the September 2013 hearing Mr Andrews qualified his earlier answer by denying that the Appellant had completely stopped trading with Wizard. Mr Andrews stated that it was a commercial decision to do business again with Wizard, particularly as the Appellant had heard nothing official from HMRC about the previous suspect deals involving Wizard.

398. Mr Andrews' explanation for changing his evidence at the September 2013 hearing was that he had not been prepared properly for the earlier hearing and that the Appellant had been let down by its previous representative. The Tribunal is not persuaded by Mr Andrews' explanation. The Tribunal is perplexed by Mr Andrews' inability to recall details of the cancelled deal at the January 2012 hearing, particularly as it purportedly involved the payment of compensation. Further Mr Andrews' answer at the January 2012 hearing was consistent with one of the Appellant's principal arguments was that it changed suppliers in response to HMRC's concerns. Further Mr Andrews' change of tack at the September 2013 hearing had wider repercussions for the Appellant in that it undermined critical aspects of its case of adhering to HMRC's advice, by only trading with known and trusted suppliers.

399. On 16 February 2006 HMRC informed the Appellant that 11 of the 19 Appellant's transactions in the 09/05 quarter had commenced with a defaulting trader. HMRC identified Mobile World and Wizard as being parties to the transactions. HMRC produced in evidence at the September 2013 hearing[29]a record of a telephone conversation between Mr Andrews and Officer Watson dated 20 February 2006 at 1225. The record showed that Mr Andrews had contacted Officer Watson raising concerns about the 16 February 2006 letter, and informing him that the Appellant had recently put a deal through with Wizard as the supplier.

400. Mr Andrews stated in evidence that the deal with Wizard had been cancelled by the time he made the phone call to Officer Watson. Mr Andrews was, however, unable to give a convincing answer in cross-examination as to why he did not inform Officer Watson of the cancelled deal involving Wizard. Mr Andrews said that the Appellant did not want to forewarn HMRC of the cancellation because the Appellant hoped that HMRC would declare Wizard as bad eggs which would give the Appellant a reason not to pay Wizard compensation. The Tribunal considers that if this was the case, the Appellant already had the necessary ammunition in the form of the 16 February 2006 letter to challenge Wizard's bona fides.

[27] See the 26 January 2012 transcript at page 89 paragraph 12 onwards and Mr Andrew's cross examination & re-examination on 10 September pages 65 to 70 and pages 94 -101.

[28] See the 27 January 2012 transcript at page 189 paragraph 22.

[29] The Appellant did not object to the late admission of this evidence.

401. The Tribunal finds Mr Andrews' evidence on the details of the cancelled deal confusing and contradictory. The Tribunal was not clear when Mobile World purportedly cancelled the deal. Mr Andrews appeared in his evidence to fluctuate between Friday 17 and Monday 20 February 2006 as to when the cancellation took place. There was no documentation from Mobile World cancelling the transaction. Mr Andrews' reason for not seeking compensation from Mobile World for breach of contract was weak, particularly as the Appellant was more than ready to pay Wizard compensation in relation to the same transaction. The Appellant's transport booking confirmation indicated that the mobile phones would have been in Germany by the 17 February 2006. The Tribunal considers that the Appellant's documentation for the cancelled deal suggested that the deal was actually concluded on 16 February with delivery on 17 February 2006.

402. The Tribunal agrees with HMRC's observation that if this deal had been cancelled legitimately it would be reasonable to have expected the following additional documents:

(1) Correspondence with Mobile World cancelling the deal.

(2) Correspondence with Mobile World claiming the loss or negotiating the same.

(3) Correspondence with the Bank about its error in respect of Mobile World's payment in deal 8.

(4) Written instructions to the freight forwarder not to ship the goods, or documents in response from them;

(5) An entry in the deal logs.

403. The Tribunal finds that the evidence points to a deal being struck between Wizard, the Appellant, and Mobile World on 16 February 2006. When the Appellant received HMRC's letter of the 16 February 2006 which was most likely on the 20 February 2006 it cancelled the transaction. In contrast to the Appellant's assertions, the Tribunal considers that the circumstances surrounding the cancelled deal suggest contrivance on the Appellant's part.

Deal 8 03/06

404. The Appellant also relied on Mr Andrews' evidence that he agreed with Cybacomms and Mobile World a reduction in the order by 128 phones on the grounds that the packaging was defective. The Appellant argued that this would not happen if the trading was contrived. HMRC did not cross-examine Mr Andrews on this particular point, HMRC asked questions on other aspects of this deal with the intention of demonstrating its contrived nature.[30]

Insurance

405. The Appellant appeared to have insured the goods in only three of the deals.

[30] See transcript 26.1.2012 pages 17 to 24; and 10.9.2013 pages 53 to 56.

406. Mr Case in his fourth witness statement dated 4 January 2012 supplied an e-mail from Beddis, a commercial insurance broker, of 17 June 2005 giving a quotation for marine insurance. Beddis quoted a minimum premium and deposit of £40,000 per annum and a premium of £50,000 per annum if the expected value of the exports reached £9.2 million. The policy covered all risks of loss or damage whilst anywhere in the world subject to a £5,000 excess and limits of £500K any one vessel, aircraft or conveyance or location, £1million any one accident or occurrence, and £500K at premises of Hawk, the freight forwarder. Cover was also subject to confirmation of no claims in the past five years from previous insurers.

407. Mr Case's rationale for insuring in three of the deals was that Mr Andrews had informed him that there had been a hold up of a vehicle on the route the goods of those deals would be taking. Mr Case considered that insurance was not a commercial necessity in respect of the remaining deals. Mr Case said that he had been trading in electrical goods without insurance for 30 years, and that by not taking out insurance on the remaining deals there was a notional saving to the Appellant.

408. Mr Andrews took the view that insurance was a matter for Mr Case.

409. HMRC pointed out that the Appellant still made healthy profits on the three deals for which it took out insurance. In HMRC's view, the taking out of insurance on the remaining deals did not have had an adverse effect on the Appellant's profit margins. HMRC, therefore, contended the Appellant's failure to insure in the remaining deals was a significant indicator of knowledge having regard to the high value of the transactions.

410. The Appellant took a contrary view saying that it was a commercial decision not to take out insurance, and that HMRC adduced no evidence to show that grey market traders routinely purchased insurance.

411. The Tribunal considers that the Appellant adopted a high risk strategy by not insuring the remaining deals. Both Mr Case and Mr Andrews acknowledged that there was a real possibility that mobile phone consignments might attract the interest of criminals. Also the value of the consignments was high ranging from £263K to £1.2 million. Further the Tribunal was not convinced that the Appellant had the wherewithal to fund such a loss if it happened[31]. Finally the Tribunal finds that the purported cost of insurance of £50,000 per annum was minimal in the context of the Appellant's annual turnover of £29 million, and Mr Andrews' commission of £494K for six months.

412. In view of the above findings the Tribunal considers the Appellant's decision not to insure the remaining deals irrational and commercially unsound.

[31] See paragraph 220 on the Tribunal findings on the Appellant's funding arrangements.

Due Diligence

Appellant's suppliers

Cybacomms

413. The Appellant's documentation comprised an introductory fax, Cybacomms Trading application form, Certificate of Incorporation, VAT Certificate, an old Redhill request, PNC supplier due diligence declaration, trade application form, bank details (including FCIB) and a Veracis report, although dated 21 January 2006, was apparently received by the Appellant two days before the single deal with Cybacomms in February 2006.

414. The Veracis report stated that Cybacomms had good due diligence but provided no evidence of it. Mr Andrews agreed that Veracis relied on what Mr Whisson, the main director of Cybacomms, told it.

415. The Veracis report indicated that Cybacomms was prepared to take on new trading partners which was contrary to the Appellant's position of only doing business with companies with which it had long trading relationships. Mr Andrews stated that it did not occur to him at the time of reading the report that Cybacomms operated differently from the Appellant.

416. The Veracis report made no mention of the Cybacomms undertaking stock inspections or recording IMEI numbers as a matter of routine. Mr Andrews was not too concerned about Cybacomms not carrying out these tasks because of the Veracis statement that Cybacomms had good due diligence in place. Mr Andrews, however, was forced to concede that Veracis had not said what Cybacomms did to earn the description *very good due diligence.*

417. The Veracis report referred to an abbreviated balance sheet at 30 June 2004 for Cybacomms which showed net current assets as £17,585. A Dun & Bradsheet report gave Cybacomms a maximum credit rating of £8,500. Mr Andrews said that he glazed over when faced with financial information and expected Mr Case to carry out the financial appraisal.

418. Mr Case held different expectations of Mr Andrews, pointing out that it was Mr Andrews' job to highlight reasons for not doing business with a company. Mr Case could not recall whether he saw the due diligence material on Cybacomms. Mr Case, however, added that the financial information would not have concerned him because he knew Cybacomms to be a long standing dealer with no criminal record.

419. Cybacomms sent a supplier declaration form to the Appellant despite that fact that it was a customer. Mr Andrews accepted with hindsight the sending of a supplier declaration form was rather strange. Mr Andrews acknowledged that he gave no thought to why Cybacomms did this at the time of the Appellant receiving the declaration.

Sprint

420. Mr Andrews had known Sprint since 1994. Mr Andrews originally stated that the Appellant was not the obvious trading partner for Sprint because of the size of its deals. Mr Andrews, however, acknowledged that the Appellant was doing big enough deals in June 2005 to trade with Sprint. Mr Andrews then said he was too embarrassed to trade with Sprint initially because his former employers, Unique Distribution, owed Sprint monies.

421. According to Mr Andrews, the Appellant stuck with Sprint from December 2005 because the Appellant believed that it would reduce the risk of its deal chains leading back to fraud.

422. The Appellant's due diligence of Sprint comprised a bank details form, certificate of incorporation, VAT certificate, trade application form, a Redhill request, a Dun & Bradstreet report, and a Veracis report dated 13 September 2005.

423. The Dun & Bradstreet report was prepared for a Mark Ley, a colleague of Mr Andrews previously from Unique Distribution. Mr Andrews did not have a Dun & Bradstreet account himself. Mr Andrews thought Mr Case held such an account but he decided to ask Mr Ley despite apparently wanting to have nothing to with Unique Distribution.

424. The Dun & Bradstreet report on Sprint dated 28 November 2005 revealed a credit limit of only £60,000, and described the company's business as general retailing. Mr Andrews was not cross-examined on the financial information contained in the report in view of his earlier assertions that he did not analyse financial information.

425. The Veracis report dated 13 September 2005 had no covering letter to indicate that it was prepared for the Appellant. The report made reference to a separate report for Chandi Diwar Limited which Mr Andrews could not remember procuring. Mr Andrews accepted the possibility that the report exhibited was not prepared for the Appellant but insisted that he asked Veracis to do a report on Sprint.

426. The Veracis report mentioned that the office used by Sprint was shared with Chandi Diwar Limited. Mr Andrews said that he knew that the office was used by two companies. Mr Andrews said he was not surprised by the office share. He believed Chandi Diwar Limited traded in accessories and the retail side.

427. The Veracis report on Sprint stated that the director "*relies on gut instinct rather than robust due diligence procedures"*. The Veracis report made broad assertions about Sprint's supplier base: "*all with good track records*", but did not provide any basis for saying this. The report also noted that IMEI numbers were downloaded as time permitted, but that "*Many trades are completed on the same day thereby limiting the practical use of this element of checking*". Mr Andrews accepted that this indicated that Sprint did not routinely take IMEI numbers but he did not consider it to be a negative factor.

428. Sprint gave The Export Company, its supplier, as a trade reference. Mr Andrews accepted that this appeared to be extraordinary. Further the Appellant would have got to Sprint's main supplier had he taken up trade references. Mr Andrews, however, was not particularly bothered about such references. He also acknowledged that Sprint's action of giving its supplier as a referee rendered confidentiality a waste of time[32].

429. Mr Andrews accepted that Sprint had filled out supplier declarations to him during the period when they were being repeatedly warned of fraud in their deal chains, but did not inform the Appellant.

430. Mr Andrews accepted that his decision to trade with Sprint was a gut instinct based on his previous experience with Sprint[33].

The Appellant's customers

Unicell

431. The Appellant's due diligence consisted of a trade application form dated the day before the first deal (with a bank as a trade referee), an official document in German, bank details including FCIB, freight forwarder details, a letter of introduction again the day before the deal. The other documents provided were after the event. Mr Andrews said he was trying to get historical material from a colleague at Unique Distribution because the Dun & Bradstreet report had been mislaid. The purpose of obtaining this information was to provide Officer Watson with a complete due diligence file.

432. The Appellant also exhibited a letter dated 24 March 2006 to Unicell informing it of the outcome of HMRC's enquiries which showed that Unicell had returned the mobile phones sold to them by the Appellant to Paul's Freight in the UK. Unicell responded four days letter saying that it never sold goods to the UK. Mr Andrews on receipt of Unicell's reply considered the company to be *thieving crooks.*

Mobile World

433. The Appellant originally provided HMRC with no due diligence material on Mobile World. The Appellant later supplied official documents in German, a letter of introduction undated, a Redhill request in August 2005, a trading application form, and bank details. There was no Veracis report, no financial information and no third party referees.

434. Mr Andrews knew Mobile World, having visited the company in 2003/04. In view of his prior knowledge Mr Andrews did not do any extensive checking. He obtained the basics including up to date VAT registration. The Appellant did the February deal because Mr Case thought the Appellant should do business with Mobile World, after meeting its director, Jurgen, in London.

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[32] Transcript 25 January 2012 page 59 paragraph 6.

[33] Transcript 25 January 2012 page 74 paragraph 23.

3G Trading

435. The Appellant's due diligence on 3G comprised a letter of introduction, bank details, trade application form completed 7 December 2005 with no trade reference, a Redhill check dated 7.December 2005, and a Veracis report dated 15 December 2005. The due diligence post dated the Appellant's first deal with 3G on 6 December 2005.

436. Mr Andrews said that he was not anticipating any issues with 3G because he had done business with 3G in the past. Mr Andrews said he would have done the basic due diligence before the first trade with 3G.

Freight Forwarders and Inspection Agents

437. The Appellant carried out no checks on the freight forwarders and inspection agents. Mr Andrews took this course because the freight forwarders and inspection agents had been in business for some time. Mr Andrews believed that the insurers for the freight forwarders would have carried out their own checks on them. Mr Andrews also stated that he may have done some due diligence on the freight forwarders when he was at Unique Distribution.

438. If the Appellant had conducted due diligence on freight forwarders and inspection agents it would have discovered that

> (1) Edge Logistics Ltd.(freight forwarder) was not registered for VAT until 10 January 2006.
>
> (2) A1 (inspection agent) had an issued share capital of £10, only ever submitted accounts up to 30 September 2004, which showed a balance sheet surplus of £24,869.
>
> (3) 4G (inspection agent) had an issued share capital of £1. It was engaged in textiles until changing its name in June 2005 when it began goods inspection.

The Submissions on Due Diligence

439. HMRC argued the fact that Mr Andrews and Mr Case claimed to know the individuals behind its trading partners for a considerable time did not negate the need for proper checks to be made on the Appellant's trading partners. HMRC further argued that the information obtained by the Appellant on its trading partners was limited, and when such information was obtained Mr Andrews and Mr Case chose to ignore it believing that there was no point to due diligence except to satisfy HMRC's document keeping requirements.

440. HMRC also pointed out that Mr Andrews and Mr Case received visits and lengthy correspondence from Officer Watson on the extent and quality of the Appellant's due diligence. By the time of the disputed deals, Officer Watson had told them that previous transactions had been traced to defaulting traders, and that others were believed to be similarly connected with fraud. According to HMRC, Mr Andrews and Mr Case were under no illusion as to the inadequacy of the Appellant's

due diligence previously undertaken. Thus before the Appellant commenced the disputed deals the Appellant knew that the approach that it had taken to due diligence and fraud avoidance had failed. The Appellant, however, elected to carry on with its existing practices whilst at the same time increasing its trading.

441. The Appellant disagreed with HMRC. The Appellant asserted that it complied with requests to alter its approach to due diligence made by Officer Watson as far as it was able. The Appellant followed Officer Watson's advice not to trade with unknown counterparties and to restrict its trading with parties which it knew and trusted. The Appellant undertook full VAT checks with Redhill and with the VAT helpline.

442. Further the Appellant argued that greater due diligence would not have revealed the extent of fraud in the market. The Appellant stated it could never have discovered that the market was awash with mobile phones on which there had been a default in the payment of VAT.

Tribunal's conclusions on due diligence

443. The reality was that Mr Andrews and Mr Case did not carry out substantive due diligence on its trading partners before the Appellant carried out its transactions. The evidence showed that the majority of the Appellant's due diligence was collected after the event to satisfy HMRC's enquiries. The evidence also indicated that Mr Andrews obtained Dun and Bradstreet reports from a former colleague at Unique Distribution and that the various Veracis reports were not commissioned by the Appellant. Mr Andrews and Mr Case gave no plausible explanation why they considered it necessary to dress up their due diligence in response to HMRC's enquiries.

444. The Appellant's insistence that it followed Officer Watson's advice was open to question. The Tribunal has already found that on 3 February 2006 Officer Watson was still raising real concerns about discrepancies in the Appellant's stock inspection report. Further the timelines for the Appellant's changes in suppliers did not correspond with the dates of HMRC's warnings about contaminated trades[34].

445. Mr Andrews and Mr Case instead preferred to rely on their personal knowledge of the Appellant's trading partners as their acid test for doing business. Officer Watson's findings on the connection of the Appellant's deals with defaulting traders demonstrated the weaknesses of their approach. Of more significance, Mr Andrews and Mr Case knew that such reliance of personal knowledge was flawed before the Appellant entered into the disputed deals, but they still continued to trade.

446. The Tribunal considers the Appellant's assertion that due diligence would not have revealed the extent of fraud misguided in two respects. First, the principal purpose of due diligence was to provide the Appellant with information in order to assess the bona fides of their trading partners, not the extent of fraud in the wholesale mobile phone market. Second, the Tribunal's analysis of the limited due diligence

[34] See paragraphs 159(5) & (6).

material produced by the Appellant raised significant doubts about doing business with their trading partners, had Mr Andrews and Mr Case asked the right questions.

Did the Appellant Knew or Should it Have Known of the Connection of Transactions with Fraud?

447. HMRC's principal position was that the Appellant knew that its transactions were connected with fraud. HMRC relied on various sources of evidence which demonstrated that the disputed deals were part of a fraudulent contrived scheme. HMRC contended there was clear evidence that the contrived scheme was one of carousel fraud. Further the scheme was highly orchestrated with the deal chains having either six or seven members in order to distance the Appellant from the missing trader. Further the Appellant played a key part as broker in the scheme and must have been aware of the traders with whom it must trade.

448. HMRC also placed emphasis on the fact that in the relevant period of five months the Appellant bought mobile phones solely from Sprint except on one occasion. The Appellant's profit was, therefore, entirely dependent on its customers not finding Sprint which was highly unlikely particularly in view of the Appellant's acknowledgement that Sprint was well-known in the mobile phone industry. Further the Appellant added no value to the deal which meant there was no persuasive commercial reason for the Appellant to make the profits it did. The only plausible explanation for the profits was that it represented the Appellant's share of the gains from the fraudulent trading.

449. In the alternative HMRC argued that the Appellant should have known of the connection of its transactions with fraud. According to HMRC, the Appellant had available to it information which would have led a reasonable trader ultimately to conclude in respect of the disputed deals that the only reasonable explanation was that they were connected with fraud.

450. The Appellant, on the other hand, contended that it was carrying out legitimate trading. The Appellant asserted that organisation of the entire chain of supply was not necessary for a fraud to function. The Appellant said that given the sheer numbers of parties involved in the disputed deals, orchestration of the entire chain was highly impractical. The Appellant argued that the fraudsters had achieved their ill-gotten gains when the missing trader disappeared from the scene. There was no need for the fraudsters to involve the Appellant in their misdeeds. The Appellant also cited various aspects of its trading which it said demonstrated the bona fide nature of its mobile phone business.

451. In addition the Appellant challenged HMRC's argument by highlighting what it saw as weaknesses in HMRC's case on direct knowledge. In the Appellant's view, the evidence relied upon by HMRC was consistent with the Appellant's innocent involvement. HMRC's alternative case of *should have known* was equally flawed. None of the factors relied upon by HMRC passed the test of the *only reasonable explanation*.

452. The Tribunal starts with the law on the question of knowledge. The Court of Appeal in *Mobilx Limited & Others v The Commissioners for Her Majesty's Revenue & Customs* [2010] EWCA Civ 517 clarified the test in *Kittel*

> "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."

453. The Upper Tribunal in *Davis & Dann Limited v HMRC* [2013] UK UT 0374 at para 38 (TCC) emphasised that the only reasonable explanation test was a high hurdle for HMRC:

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

454.The decision for the Tribunal is whether at the time the Appellant entered into each of the disputed transactions it knew or should have known that the particular transaction was connected with fraud. In order to arrive at that decision the Tribunal is required to have regard to all the available and relevant evidence and is not restricted to consideration of the evidence for each transaction in isolation (see Christopher Clarke J in *Red12 v HMRC* [2009] EWHC 2563). Thus the Tribunal should look at the given transaction and the circumstances in which the transaction took place. The Tribunal should then build a picture from the accumulation of detail and form a view on whether the detail proves that the Appellant had the requisite state of knowledge at the time of entering into each transaction.

455.The parties agreed that the Appeal turned on its own facts. The Tribunal now considers its findings of facts starting with HMRC's proposition that the Appellant's deal chains were highly contrived and orchestrated involving the carousel of mobile phones. The Appellant disagreed with HMRC's depiction of the scheme, arguing that the evidence on circularity of money flows was contradictory and that it was perfectly possible to carry out legitimate trading even though the deal chain had been contaminated by missing trader fraud.

456. The Tribunal's findings on the character of the Appellant's deal chains are set out in paragraphs 62 to 111 above and supported HMRC's depiction of being contrived and highly orchestrated.

457. The Tribunal is satisfied that its findings demonstrated that fraud was rife throughout the deal chains, and not restricted to the defaulting trader and the third party recipient. At least 15 of the 23 buffer traders were implicated in some way with VAT fraud. The Appellant's principal supplier, Sprint, and the Appellant's three customers, Unicell, 3G Trade and Mobile World were active participants in VAT fraud. The customers were also actively involved in the carousel of mobile phones back to the UK. Further, the Tribunal found there was no commercial rationale for the deal chains. They were unduly long and involved the import and export of goods which could be sold more profitably if the goods had remained outside the UK. In short, the findings on missing traders, third party payments, uniform mark ups, split deals, circularity of money flows, and carousel of mobile phone consignments demonstrated that the disputed deal chains were highly orchestrated and contrived.

458. The Appellant's suggestion that the fraud was restricted to the acquisition end of the deal chain was not borne out by the facts found. The finding that the Appellant's principal supplier and customers were engaged with fraudulent trading undermined the Appellant's assertion that it was involved in bona fide trading.

459. The Appellant argued that various features of the deal chains relied upon by HMRC did not demonstrate that it knew of the fraudulent connection. The Appellant referred to some traders in the chains having VAT issues; goods returning to the UK; split deal chains; and associations between traders in the Appellant's chains. The Tribunal considers the Appellant's challenge misguided because it examined the features in isolation. The Tribunal's finding that the deal chains were contrived and orchestrated was derived from the cumulative effect of these features existing together alongside with other features, which justified the inference that the Appellant knew of the connection of its transactions with fraud.

460. The Appellant relied on specific aspects of its trading which it said negated its active participation in the orchestrated and contrived deal chains. The Appellant stated there was no evidence of it being involved in third party payments. The Tribunal accepts that this was the case. The Tribunal, however, places no weight on it because third party payments were generally associated with the acquisition end of the deal chain rather than the exporter end. The role played by third party payments was to ensure that the missing trader had no funds. The Appellant operated as a broker/exporter and it was essential for the fraud to be perpetrated for the broker/exporter to remain on the scene and be sufficiently distanced from the missing trader.

461. The Appellant referred to the fact that it held a bank account with National Westminster and did not use an FCIB account to transfer monies. The Appellant asserted that if it was an active participator, its co-conspirators would have insisted the Appellant used an FCIB account so that monies could always be kept under control to facilitate the fraud. The Tribunal is not convinced with the Appellant's argument. The fact that the Appellant did not have an FCIB account pales into insignificance when contrasted with all the other features demonstrating the contrived and orchestrated nature of the deal chains. Next according to HMRC, the Appellant required a UK bank account to receive the VAT repayments from HMRC[35]. Finally the Appellant's principal supplier, Sprint, also did not have a FCIB bank account. The Tribunal found that Sprint was an active participant in deal chains involving fraud.

462. The Appellant asserted that it had varying margins on the deals it transacted and that there was nothing odd about the margins achieved by it. The Tribunal's findings at paragraph 177 above were somewhat different, deciding that the Appellant's margin was considerably more than the other traders in the deal chains. The mark ups for all deals except one were in the range 6.9% to 8.1%. The mark ups for 13 of the deals were in the range of 7.5% to 8.1%. Finally the mark ups did not appear to vary with the model of phone traded.

463. The Appellant contended that the occurrence of two deals during the relevant period which were either cancelled in entirety or in part indicated that they were carrying on legitimate trading. The Tribunal found there were serious question marks over the deal cancelled in its entirety. The said deal involved the supply of mobile phones from Wizard to the Appellant in February 2006. Mr Andrews at the January 2012 hearing said that the Appellant had ceased trading with Wizard in November 2005. Further in the Tribunal's view, the cancellation was prompted by receipt of HMRC's letter confirming that Wizard was the supplier to the Appellant in previous deals which had been traced back to a defaulting trader. The Tribunal decided that the circumstances surrounding the cancelled deal suggested contrivance on the Appellant's part (see paragraphs 396 -403 above).

464. The Tribunal acknowledged that Mr Andrews was not cross examined on the specific circumstances surrounding the part cancellation of the mobile phones in deal 8 03/06. The Tribunal, however, considered there were other aspects of deal 8 which questioned its integrity.

465. HMRC placed weight on the awareness of Mr Case and Mr Andrews of the nature and the prevalence of MTIC fraud within the wholesale mobile phone market, and that they knew some of the Appellant's mobile phone deals before the disputed transactions were connected with missing traders.

466. The Tribunal's findings on the Appellant's awareness of MTIC fraud are found at paragraph 159 above. In summary, the Tribunal was satisfied that both Mr Andrews and Mr Case were aware of the risks of fraud when the Appellant entered the wholesale mobile phone market in 2005. Of more significance, the Tribunal found

[35] See hearing note of 20 September 2013 proceedings.

they knew from 22 November 2005 that two of its deals in the 06/05 period were contaminated with fraud. Further on or around the 16 February 2006 Mr Andrews and Mr Case knew that the majority of its deals in the 09/05 period had been traced back to defaulting traders but still carried out five more deals.

467. The Appellant acknowledged that Mr Andrews and Mr Case were aware of MTIC fraud but denied that they knew the true extent of it with the implication that it was virtually impossible for a bona fide trader to avoid being enmeshed in a fraud, albeit innocently. The Tribunal is not convinced with the relevance of the Appellant's argument when set against the facts of this case. The reality was that Mr Andrews and Mr Case knew before they entered the disputed deals that the Appellant's transactions had already been traced back to a defaulting trader. Mr Andrews and Mr Case did not act upon this but carried on as before, transacting more deals.

468. Further the Tribunal considers that the logic of the Appellant's submission was against the Appellant. The Tribunal is concerned with the Appellant's state of knowledge at the time it transacted the deals, not with the Appellant's rationalisations after the event. The Appellant knew of the prevalence of fraud in the market at the time it did the deals. The Appellant adduced no evidence that at the relevant time it asked the question: *Is this transaction connected with fraud?* The Appellant's lack of reflection was typified by Mr Andrews exhortation of the Appellant being a victim which displayed his surprise of the Appellant being caught up in the fraud. A trader in the legitimate grey market at the time of making the deal would have a rational explanation for it, and an answer for why it was not connected with fraud. The Appellant, on the other hand, did the deal but did not reflect about whether the deal made sense knowing of the prevalence of fraud in the market.

469. Mr Andrews and Mr Case asserted that they followed Officer Watson's advice in particular not to trade with unknown counterparties and confine the Appellant's trading to parties they knew and trusted. The Tribunal found otherwise:

(1) Throughout the period July 2005 to February 2006 HMRC advised the Appellant of the risks of fraud and ensured that Mr Andrews and Mr Case understood the risks. Officer Watson during this period carried out a thorough analysis of the Appellant's trading practices, and gave repeated and explicit warnings about inadequacies in the Appellant's due diligence.

(2) The Appellant stated that it followed Mr Watson's advice despite reservations about his approach. The Tribunal, however, observes that on 3 February 2006 Mr Watson was still raising real concerns about discrepancies in the stock inspections reports for the Appellant's deals.

(3) Mr Case asserted that the Appellant stopped dealing with certain suppliers because of warnings given by HMRC. The timelines for the Appellant's changes in suppliers: Wizard[36] and Aircall (27 June to 22 August 2005), MNR (2 to 15 September 2005), Cybacomms[37] (22

[36] Wizard was the supplier in the aborted deal with Mobile World in February 2006.

[37] The Appellant did one further deal with Cybacomms on 16 February 2006.

September to 8 November 2005) and Sprint from 23 November 2005 did not correspond with the dates of HMRC's warnings about contaminated trades (paragraph 159 above).

470. HMRC relied on Mr Fletcher's evidence to demonstrate the inconsistency of the Appellant's transactions with rational and profitable grey market trading. The Appellant challenged Mr Fletcher's evidence on two levels. The Appellant said that Fletcher was not qualified to give expert evidence on grey market trading and that his analysis had no relevance to a market which was rife with fraud.

471. At paragraph 223 the Tribunal concluded, amongst other matters, that Mr Andrews and Mr Case were unable to provide a rational explanation for the profit they made on deals. The Tribunal agreed with Mr Fletcher's proposition that a genuine trader would be able to articulate how the opportunity for profit arose. In contrast, Mr Andrews and Mr Case assumed the grey market existed because the Appellant made profitable deals. They did not question why the Appellant was able to make the profits it did on the individual transactions.

472. Further the Appellant's trading practices were not only inconsistent with Mr Fletcher's view of profitable grey market trading but also with Mr Andrews and Mr Case depiction of the grey market as highly competitive, and a hard place in which to work where commercial confidentiality about suppliers and customers was sacrosanct.

473. HMRC built upon its portrayal of the wider circumstances of the Appellant's deal chains by highlighting a range of discrepancies with the individual deals which the Appellant was aware of at the time of making those deals. HMRC said the Appellant's disregard of those discrepancies in the context of the other evidence demonstrated that it knew of the connection of its transactions with fraud. The Appellant's position was that the discrepancies were minor and fell within custom and practice of grey market trading.

474. The Tribunal has made detailed findings on the discrepancies with the individual deals in the body of the decision: *discrepancies between specification and trade* (317-322), *inconsistencies between the appellant's documentation and inspection reports* (323-353), *inspection agents and freight forwarders* (354-362), *Nokia 8800 and 8801*(363-368) and IME*I numbers* (369). The Tribunal found the discrepancies significant, and the Appellant's failure to act on those discrepancies was a strong indicator that the Appellant knew that the disputed deals were connected with fraud.

475. The Tribunal highlights the following points arising from its findings on the matters arising from the individual deals:

(1) These were matters which Mr Andrews and Mr Case knew about at the time of entering the transactions. The evidence on the discrepancies was not susceptible to the argument of having no direct knowledge which was used by the Appellant against the evidence on the wider circumstances of the deal chains.

(2) The scale of the discrepancies was high. Mr Andrews accepted that in virtually every deal there were inconsistencies between what the Appellant had asked for from its supplier and what the Appellant had been given. All the inspection reports produced by A1 highlighted anomalies which Mr Andrews disregarded. The level of anomalies fell off when the Appellant appointed 4G. Mr Andrews, however, acknowledged that 4G provided an unsatisfactory service but did nothing about it.

(3) The discrepancies were material to the issue of knowledge. The inconsistencies with the specification together with Mr Andrews' disregard of them made no commercial sense. Similarly with the inspection reports, the presence of cuts outs, the preponderance of two pin chargers, and the absence of appropriate warranties were indicators of potential fraud. Other anomalies, such as the inspection agent not following the instruction on powering up the required number of mobile phones, and the multiplicity of software languages and manual types demonstrated the lack of serious commercial intent on the part of the Appellant. The circumstances of the Appellant's trading in Nokia 8801 were artificial and had no commercial logic.

(4) The Tribunal was satisfied that Mr Andrews did not question the discrepancies at the time of making the deals. Mr Andrews' evidence that he would raise these discrepancies with the supplier and or inspection agent was uncorroborated by documentary evidence except for deal 8 03/06 and contradicted his other testimony where he accepted that he did not pursue specific discrepancies (for example, see Mr Andrews' answer on power ups and his willingness to accept whatever Sprint supplied the Appellant).

(5) Mr Andrews' reasons for not following up on the discrepancies had the character of rationalisations after the event. It was clear to the Tribunal that Mr Andrews gave no thought to the discrepancies at the time of entering the transactions which begged the question: why?

(6) The Appellant presented its difference of view with HMRC on discrepancies as a conflict between Mr Fletcher's expert opinion and Mr Andrews' significant experience in grey market trading. The Tribunal preferred Mr Fletcher's view of the market and found Mr Andrews' depiction of custom and practice as highly irrational which carried considerable risk in the trading of high value and low margin goods. Even if the Tribunal was wrong in preferring Mr Fletcher's rational exposition of the grey market, Mr Andrews did not provide an adequate explanation why it insisted on specifications and inspection reports in the first place if he was not going to follow through on them. Mr Andrews' disregard of his own procedures which he put in place raised yet further questions.

476. The Appellant asserted that Mr Andrews gave clear evidence, which was not contradicted on the circumstances, in which the Appellant came to use the freight forwarders and the inspection companies. The Tribunal considers the Appellant's assertion regarding inspection companies inaccurate, in that Mr Andrews was cross-

examined at length on the Appellant's change of inspection agents from A1 to 4G. The Tribunal concluded that Mr Andrews gave contradictory evidence on the reasons for the change, and that his relationship with the inspection agents lacked transparency. Furthermore, Mr Andrews accepted that the Appellant had undertaken no effective due diligence on the freight forwarders and the inspection agents. Had it done so, the Appellant would have been alerted to circumstances which would have led to concerns about their continuing engagement.

477. The Appellant relied on Officer Saunder's evidence that a deal chain may be made up in the freight forwarders which carried the suggestion that a fraud could be perpetrated without some of the parties involved in the transactions knowing about the fraudulent scheme. In this respect the Tribunal refers to its finding on the information supplied by Hawk, the freight forwarder, on the changes in ownership in deal 8 03/06. Mr Andrews ignored this information knowing full well that HMRC considered frequent changes of ownership an indicator of fraud.

478. The Appellant asserted that it paid for the scanning and checking of IMEI numbers on all trades. The significance of this for the Appellant's case was undermined by the facts that Mr Andrews did not verify the information when it was received from the inspection agents. Further Mr Andrews failed to give a plausible account on how the IMEI numbers scanned by 4G were checked against the Appellant's database of IMEI numbers which would have required the co-operation of A1, the inspection agent the Appellant sacked in favour of 4G. Finally, HMRC uncovered anomalies in some of the IMEI scans which have not been adequately explained by Mr Andrews.

479. HMRC relied on the Appellant's failure to insure the mobile phones in all but three deals as an indicator of knowledge. The Appellant dismissed HMRC's concern, by saying the decision not to insure was a commercial one. The Tribunal found the Appellant's decision not to insure the remaining deals irrational and commercially unsound (see paragraphs 411 & 412 above).

480. HMRC contended that the Appellant's due diligence was poor, and that the absence of adequate diligence was itself a relevant feature in assessing whether the Appellant had actual knowledge of a connection with fraud. The Appellant said that it complied with HMRC requests to alter its approach to due diligence and that it carried out two VAT checks on its trading partners. Further the Appellant maintained that greater due diligence would never have revealed the extent of fraud in the mobile phone market.

481. The Tribunal decided that Mr Andrews and Mr Case did not perform substantive due diligence on its trading partners before the Appellant carried out its transactions with them. Further the Appellant's insistence that it followed Officer Watson's advice on due diligence was open to question. Finally the Tribunal considered the Appellant's assertion that greater due diligence would not have revealed the extent of fraud misguided in two respects. First, the principal purpose of due diligence was to provide the Appellant with information in order to assess the bona fides of their trading partners, not the extent of fraud in the wholesale mobile

phone market. Second, the Tribunal’s analysis of the limited due diligence material produced by the Appellant raised significant doubts about doing business with their trading partners, had Mr Andrews and Mr Case asked the right questions.

482. The Appellant argued that the contents of Mr Andrews’ notebook indicated that he was actively involved in the negotiation of deals, which was compelling evidence that the Appellant was not involved in contrived trading. Further Mr Andrews provided in his later witness statement a coherent and persuasive account of the making of the disputed deals. The Appellant submitted that HMRC had not challenged Mr Andrews’ account in the later witness statements, which meant that the Tribunal was obliged to accept Mr Andrews’ evidence.

483. The Tribunal reached a different conclusion on the notebook from that advocated by the Appellant. The Tribunal found that Mr Andrews’ notebook (RA15) was not a comprehensive and contemporaneous record of his dealings on behalf of the Appellant. The book was no more than a collection of random notes covering his personal and business life. There was no direct relationship between the contents and the deals in question. Further the entries contradicted Mr Andrews’ evidence that he would not trade with certain companies. Having regard to the above findings, the Tribunal decided that the contents of notebook (RA15) did not support the Appellant’s claim of not being involved in contrived trading (see paragraph 377 above).

484. The Tribunal disagreed with the Appellant’s submission that it was obliged to accept Mr Andrews’ description of the deals in his later witness statements. The Tribunal was satisfied that HMRC had challenged Mr Andrews on the new witness statements. The Tribunal concluded that Mr Andrews’ description of the deals in the later witness statements under the various headings except *negotiations and agreeing the deal* added nothing new to his January 2012 testimony.

485. Mr Andrews’ evidence under the *negotiations and agreeing the deal* heading gave a fuller account of how he brokered the deal including details of purported telephone conversations with suppliers and customers. The Tribunal, however, was not convinced with Mr Andrews’ explanation. The Tribunal questioned the reliability of Mr Andrews’ recall of events that occurred some six years before. Also the Tribunal did not consider that Mr Andrew’s entries in his day books substantiated the assertions made in his statement about the negotiations. In short the Tribunal held that Mr Andrews’ descriptions of *negotiating and agreeing the deal* in the later statements were no more than unsubstantiated assertions which carried minimal evidential weight (see paragraphs 385/386 above).

486. The Appellant relied on other aspects of its trading in support of its assertion that it had acted in good faith when making the disputed deals. The other aspects were that it did not use online market facilities such as IPT.com; the involvement of Mr Andrews’ wife with the administration of some of the deals; and that no goods were released until it had paid its supplier.

487. The Tribunal did not consider the above aspects of the Appellant's trading advanced the Appellant's case. The non-use of online market facilities was contrary to the Appellant's depiction of a highly competitive market which would demand the most up to date information on prices. The evidence indicated that Mr Andrews' wife played a peripheral role in the Appellant's business. The Tribunal accepts that the Appellant did not release the goods before it had paid its supplier. The Tribunal, however, notes that in three of the disputed deals goods were prematurely released by the Appellant before all the steps had been completed. They were deal 2,12/05, goods sent before payment from the customer; deal 1, 03/06, goods released before the Appellant supplied the freight forwarder with a stock allocation form, and deal 6, 03/6 goods sent before the date of the inspection report.

488. HMRC contended that the accounts given by the witnesses called by the Appellant lacked credibility in material respects. In HMRC's view, the Appellant's witnesses did not give a full and honest account to the Tribunal. HMRC stated that Mr Andrews' evidence was riddled with inconsistency and incredibility. HMRC also submitted that Mr Andrews shifted his position a number of times in respect of his evidence on the inspection reports. HMRC stated that large parts of Mr Case's evidence may properly be described as an exercise in avoiding the question.

489. The Appellant disagreed with HMRC's assessment of the credibility of the evidence given by Mr Andrews and Mr Case. The Appellant argued that Mr Andrews gave evidence about the nature of the market in mobile phones with obvious deep knowledge and understanding having been active as a trader for a number of years. The Appellant pointed out that Mr Andrews was painstakingly cross-examined over several days, and, in the Appellant's view, he was frank and honest with his answers.

490. The Appellant also stated that if HMRC was correct in its case, it followed that Mr Andrews and Mr Case were willing to enter into a criminal agreement where they would carry all the risk not only of the company being denied its input tax reclaim, but also of arrest and prosecution for a multi- million pound fraud for no advantage beyond what an exporter would expect by way of profit/mark up in any event.

491. The parties have presented the issue of credibility of the Appellant's principal witnesses in the starkest terms in direct opposition to each other. HMRC invited the Tribunal to decide that Mr Andrews and Mr Case were not telling the truth. The Appellant, on the other hand, argued they gave their evidence honestly, and that if HMRC was believed the Tribunal was obliged to conclude that they had acted criminally.

492. The Appellant's contention that the Tribunal would have to conclude that Mr Andrews and Mr Case had acted criminally if it rejected their evidence was misguided. In appeals on the denial of the right to VAT repayments the Tribunal is not concerned with the subjective intention of the alleged participants. Instead the Tribunal has to decide whether the objective criteria which limit the scope of VAT and the right to deduct have been met. Lord Justice Moses in *Mobilx* explained the correct test at paragraphs 47-49:

> "47. Accordingly, the objective criteria which form the basis of concepts used in the Sixth Directive form the basis of the concepts which limit the scope of VAT and the right to deduct under ss. 1, 4 and 24 of the 1994 Act. Applying the principle in *Kittel*, the objective criteria are not met where a taxable person knew or should have known that by his purchase he was participating in a transaction connected with fraudulent evasion of VAT. That principle merely requires consideration of whether the objective criteria relevant to those provisions of the VAT Act 1994 are met. It does not require the introduction of any further domestic legislation.
>
> 48. The traders contend that to enlarge the category of participants in the fraud to those who should have known that by their purchase they were taking part in a transaction connected with fraud is to impose a new accessory liability for fraud which does not exist in domestic law; it imposes, so they assert, a negligent standard for fraud by the back door.
>
> 49. It is the obligation of domestic courts to interpret the VATA 1994 in the light of the wording and purpose of the Sixth Directive as understood by the ECJ (*Marleasing SA* 1990 ECR 1-4135 [1992] 1 CMLR 305) (see, for a full discussion of this obligation, the judgment of Arden LJ in *Revenue and Customs Commissioners v IDT Card Services Ireland Limited* [2006] EWCA Civ 29 [2006] STC 1252, §§ 69-83). Arden LJ acknowledges, as the ECJ has itself recognised, that the application of the *Marleasing* principle may result in the imposition of a civil liability where such a liability would not otherwise have been imposed under domestic law (see *IDT* § 111). The denial of the right to deduct in this case stems from principles which apply throughout the Community in respect of what is said to be reliance on Community law for fraudulent ends. It can be no objection to that approach to Community law that in purely domestic circumstances a trader might not be regarded as an accessory to fraud. In a sense, the dichotomy between domestic and Community law, in the circumstances of these appeals, is false. In relation to the right to deduct input tax, Community and domestic law are one and the same".

493. The Tribunal considers the topic of credibility is not limited to the stark choice between truth and untruth. It is possible for a witness who has been discredited to give, on the whole, truthful evidence. A correct assessment of credibility involves ranking the testimony against the material issues in dispute. In this respect the Tribunal is concerned in this Appeal with the Appellant's state of knowledge at the time it entered the transactions. The Tribunal found that when Mr Andrews and Mr Case made the deals they either ignored a wide range of circumstances which suggested the transactions were connected with fraud or they failed to do what reasonable traders would have done in a market beset with fraud. These findings were largely based on the admissions of Mr Andrews and Mr Case. A good part of the Tribunal's evaluation was devoted to their explanations for not heeding the warnings or not taking the appropriate actions. The Tribunal found their explanations implausible, rationalisations after the event and in conflict with other parts of their evidence, and with each other's evidence. The Tribunal concludes that the testimonies

of Mr Andrews and Mr Case on the material issues in this Appeal were not reliable and contradictory, which supports a finding they were not credible witnesses.

494. In the preceding paragraphs the Tribunal has summarised its principal findings. Essentially the Tribunal found that

(1) The Appellant's deal chains were highly contrived and orchestrated.

(2) Mr Andrews and Mr Case were unable to provide a rational explanation for the profit they made on deals.

(3) Mr Andrews and Mr Case did the deal but did not reflect about whether the deal made sense knowing of the prevalence of fraud in the market, and knowing that previous transactions of the Appellant had been traced to defaulting traders.

(4) The discrepancies and anomalies within the individual deals were significant, and the failures of Mr Andrews and Mr Case to act on those discrepancies undermined their assertions that they were involved in the bona fide trading of mobile phones.

(5) Mr Andrews and Mr Case were not credible witnesses.

495. In determining what it was that the Appellant knew or ought to have known when it entered the disputed transactions the Tribunal is entitled to look at the totality of the deals effected by the Appellant (and their characteristics), and at what the Appellant did or omitted to do, and what it could have done, together with the surrounding circumstances in respect of all of them. Having regard to its findings, the Tribunal is satisfied that when the Appellant entered into each of the disputed transactions it knew that the particular transaction was connected with fraud.

496. In view of its finding that the Appellant knew of the connection with fraud, it is unnecessary for the Tribunal to consider the alternative case of *should have known*. For the sake of completeness the Tribunal is satisfied that HMRC also made out its case for *should have known*. The Tribunal's findings supported HMRC's submissions in paragraphs 274 to 334 of its closing submissions dated 19 September 2013.

Decision

497. The Tribunal finds the following:

(1) There was a VAT loss in each of the Appellant's disputed transactions.

(2) The loss in each of the Appellant's disputed transactions was occasioned by fraud.

(3) Each of the disputed transactions was connected with the fraudulent evasion of VAT.

(4) The Appellants knew at the time of entering the disputed transactions that each of those transactions was connected with the fraudulent evasion of VAT.

498. The Tribunal, therefore, dismisses the Appeal and confirms HMRC denial of input tax in the total sum of £1,847,976.80 claimed in the VAT quarterly accounting periods 12/05, 03/06 and 06/06 in respect of 16 deals.

499. The Tribunal invites the parties' representations on the question of costs within 56 days from the date of the decision.

500. In the absence of agreement leave is given to parties within 56 days of release to apply for a determination of the amount of the costs order under rule 10(1)(b) of the 2009 Rules.

501. 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.

MICHAEL TILDESLEY OBE
TRIBUNAL JUDGE

RELEASE DATE: 3 March 2014

APPENDIX ONE

THE EVIDENCE

1. The Appellant called the following witnesses:

(1) Mr Richard Andrews

(2) Mr Joe Case

(3) Mrs Ravleen Sharma director of Sprint

(4) Mr Sanjay Parmar, Chartered Accountant who audited the Appellant's accounts.

(5) Mr David Cummings, employee of Unique Distribution.

2. HMRC called the following witnesses

(1) Mr Nigel Saunders, HMRC Officer who gave evidence on the deal chains and the Appellant's business practices

(2) Officer Simon Japes dealt with the FCIB evidence

(3) Officer Roderick Stone: evidence on missing trader fraud generally

(4) Mr John Fletcher, expert witness

(5) Ms Catherine Clark, solicitor employed by Nokia in its litigation team

(6) Mr Roger Mercott, HMRC Officer dealing with Aristaeus, one of the defaulting traders.

(7) Mr Simon Vincent , HMRC Officer dealing with ART Enterprises, one of the defaulting traders.

(8) Mr Damian Parsons, HMRC Officer dealing with Puwar, one of the defaulting traders.

(9) Mr Terence Mendes, HMRC Officer dealing with Ultimate Security Agency Limited, one of the defaulting traders.

(10) Ms Smita Parikh, HMRC Officer dealing with Apollo Communications, one of the defaulting traders.

(11) Mr Robert Ross, HMRC Officer dealing with ECS84.Com, one of the defaulting traders.

(12) Mr Stewart Yule, HMRC Officer dealing with K & S Xport Limited, one of the defaulting traders.

(13) Mr Pankaj Mandalia, HMRC Officer dealing with Apollo Communications, one of the defaulting traders.

(14) Mr Barry Patterson, HMRC Officer dealing with KSK Trading, one of the defaulting traders.

(15) Mr Julian Cook, HMRC Officer dealing with Allied Jap one of the defaulting traders.

(16) Mrs Susan Okole, HMRC Officer dealing with Myco Telecom, one of the defaulting traders.

3. The following witness statements were received in evidence:

(1) Ms Judith Swainson, HMRC Officer line manager for Officer Watson, the assurance officer for the Appellant. traders.

(2) Mr Patrick Wood, HMRC Officer who checked the Appellant's repayment claims prior to November 2004.

(3) Mr Stephen Smith, HMRC Officer who accompanied Officer Watson on a visit to the Appellant.

(4) Mr Derek Gardner, employee of Nokia

(5) Mr William Gardner, HMRC Officer who accompanied Officer Watson on a visit to the Appellant.

(6) Mr Mark Adrian Wood, HMRC Officer who dealt with Unique Distribution

(7) Mr James Poulton for the Appellant (see transcript of 9 September 2013 on the extent of the Tribunal's leave to admit the statement).

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APPENDIX TWO

CHRONOLOGY OF THE PROCEEDINGS

1. On 31 May 2007 and 15 January 2008 the Appellant appealed against HMRC's decisions to refuse repayment of VAT in the following sums: £192,338.13 (VAT period 12/05), £1,508,638.70 (VAT period 03/06), and £147,000.00 (VAT period 06/06). HMRC alleged that the Appellant's transactions were connected with the fraudulent evasion of VAT and the Appellant knew or should have known that its transactions were so connected.

2. HMRC served its statement of case, consolidated statement of case and amended statement of case on 12 July 2007, 28 February 2008 and 14 February 2011 respectively.

3. From 9 to 27 January 2012 the Tribunal heard evidence in relation to the above Appeal which included testimony from Mr Fletcher on his first and second witness statements. On 27 January 2012 the Tribunal concluded the evidence but had insufficient time to receive the parties' closing submissions. The Tribunal adjourned the hearing part-heard to 9 and 10 May 2012 to hear closing submissions. Directions were issued for the exchange of written submissions and other matters.

4. On 24 February 2012 hMRC e-mailed the Tribunal advising that LEXLAW had been appointed to act in place of the Appellant's previous representative, Mr David Tunney, and that the Appellant would shortly be filing an application that would impact on HMRC's submissions. On 24 February 2012 HMRC indicated that it would not be serving its final submissions until the Appellant's application had been filed.

5. On 15 March 2012 HMRC advised the Tribunal that Morgan Rose, the Appellant's new representative, would update the Tribunal on how it intended to proceed on or before 20 March 2012. HMRC indicated that it had no objection to the Appellant's request.

6. On a date unknown the Appellant's representative requested additional time until 4.00pm on 30 March 2012 to allow the Appellant to advise the Tribunal how it wished to proceed with the Appeal. The Appellant indicated that it was examining whether it was appropriate to make an application to the Tribunal seeking leave to recall some of the Appellant's witnesses and/or some of HMRC's witnesses for cross-examination.

7. On 26 March 2012 the Tribunal indicated that it intended to retain the dates of 9 and 10 May 2012. Further the Tribunal stated that if the Appellant made an application it would be heard on 9 May 2012, and if granted the Tribunal would fix a new timetable. If, however, the Tribunal refused the application, the Tribunal would expect the parties to make and conclude their submissions by close of business on 4.30 pm on 10 May 2012. The Tribunal made amendments to the directions issued 27 January 2012

8. On 12 April 2012 the Appellant applied for

(1) Leave to recall Mr Saunders of HMRC for further cross-examination.

(2) Leave to adduce further evidence of Mr Case for the Appellant.

(3) Leave to adduce further evidence of Mr Andrews for the Appellant.

(4) A Tribunal direction on the admissibility of the evidence of Mr Fletcher.

(5) A Tribunal direction on the admissibility of the evidence of Mr Birtwhistle of HMRC.

(6) Further directions consequential on the applications at 1 to 5 above in particular the admissibility of expert evidence given by non-experts.

9. On 13 April 2012 the Tribunal indicated that it would not vary the directions issued on 26 March 2012.

10. On 24 April 2012 the Appellant gave notice that it would be making an application on 9 May 2012 for the recusal of Judge Tildesley from hearing the Appeal on the basis of a real danger of apparent and or perceived bias on two grounds:

(1) In *Edgeskill Ltd v Revenue and Customs Commissioners* [2011] UKFTT 393 (TC) the Judge ruled that the evidence of Mr John Fletcher qualified as expert evidence. The same issue fell to be determined in this Appeal and the Judge would have closed his mind to this issue, or not be impartial in this respect.

(2) Also in *Edgeskill*, the Judge heard evidence from a Mr Plowman, the director of Veracis Limited, and reached "certain unfortunate conclusions" about him. The Appellant relied upon "due diligence" reports from Veracis Limited in this case and the Judge may therefore take an unfavourable view of this evidence.

11. Having regard to the decision in *El-Farargy v El Farargy and others* [2007] EWCA Civ 1149 Judge Berner heard the Appellant's application to recuse Judge Tildesley. Judge Berner refused the Application stating in respect of the first ground concerning Mr Fletcher:

> "In summary, I see no basis for concluding that Judge Tildesley had anything other than an open mind as regards the issue of whether Mr Fletcher is an expert witness, and the admissibility of Mr Fletcher's evidence. The fact of the judge's earlier decisions in *Edgeskill* does not, in my judgment, amount to pre-determination of the issue. At most those earlier decisions might give rise, in the mind of the fair-minded observer, to a risk that the Judge might be pre-disposed to the earlier conclusion but, on the evidence of the Judge's conduct of the January hearing, the fair-minded observer would conclude that the Judge would not only be prepared to hear argument and submissions to the contrary, but to actively require the Respondents to make submissions and to encourage the Appellant to argue against those submissions. There is in my judgment no suggestion in the evidence before me that the Judge

> had a closed mind or approached the question of Mr Fletcher's evidence with anything other than impartial consideration".

12. The proceedings were stayed generally pending an appeal against Judge Berner's decision. On 16 August 2012 Judge Bishopp refused the Appellant permission to appeal Judge Berner's decision. On 9 October 2012 Judge Herrington following an oral hearing confirmed the refusal stating that Judge Berner applied the correct legal test.

13. On 11 December 2012 the Tribunal reconvened to progress the Appeal. At the hearing the Appellant renewed its application dated 12 April 2012 regarding the admission of new evidence and recall of witnesses. The Appellant also requested disclosure of various documents.

14. At the hearing on 11 December 2012 the Tribunal informed the parties that it had changed its view about the process for hearing arguments on the admissibility of Mr Fletcher's and Mr Birtwhistle's evidence. The Tribunal agreed with the Appellant that the question of admissibility should be dealt with as a separate matter and before final submissions, which was consistent with the ruling of Lightman J in *Mobile Export 365Ltd and another v Revenue and Customs Commissioners* [2007] STC 1794

15. On 8 January 2013 the Tribunal released its decision on the Appellant's disclosure requests. The Tribunal observed that the status of Mr Fletcher's evidence was a current and developing issue in MTIC appeals before the First Tier Tribunal, and in all probability would require a determination by the Upper Tribunal. In the First Tier Tribunal decisions of *HT Purser Ltd* [2011] UKFTT 860 and *JDI Trading* [2012] UKFTT 642, the expert characterisation of Mr Fletcher's evidence and his impartiality were called into question.

16. The Tribunal decided that there was merit in the Appellant's request for further information in order to mount its challenge in respect of the admissibility of Mr Fletcher's evidence but that the terms of the proposed application were too wide and lack specificity. There was also the added complication that Mr Fletcher and his employers, KPMG, had not been given the opportunity to make representations on the application. Given those circumstances the Tribunal issued a draft order in the following terms and gave Mr Fletcher and KMPG the right to comment on it.

> (1) By no later than 4pm on 1 February 2013 Mr Fletcher of KPMG shall provide the parties to this Appeal and the Tribunal with the following information and documents:
>
> a. The identities of the KPMG staff referred to in paragraph 1.4.1 of his witness statement dated 12 December 2008.
>
> b. The identities of the KPMG staff undertaking the work for *Dragon Futures.*
>
> c. The witness statements of Mr Simmonite of KPMG supplied on behalf of *Dragon Futures* to the VAT and Duties Tribunal (decision number 19186).

d. A copy of the Full Survey Report on the Grey Market produced by KPMG in co-operation with the Anti-Gray Market Alliance.

e. Mr Fletcher's knowledge and involvement with KPMG's engagements for *Dragon Futures* and the Anti-Gray Market Alliance.

(2) Mr Fletcher and or KPMG are given the opportunity to make representations to the Tribunal, which must be received by no later than 1 February 2013 if they have difficulties with complying with the Tribunal's directions.

17. On 25 February 2013 the Tribunal heard the parties' representations on the Appellant's application regarding the admission of new evidence and recall of witnesses. The Tribunal decided that

(1) Leave to recall Mr Saunders of HMRC for further cross-examination was refused**.**

(2) Leave given to adduce further evidence of Mr Case for the Appellant. The leave applied to the evidence identified as the sixth and seventh witness statements dated 19 April 2012, and subject to Mr Case attending the resumed hearing for cross examination.

(3) Leavegiven to adduce further evidence of Mr Andrews for the Appellant. The leave applied to the evidence identified as the fifth, sixth, seventh and eighth witness statements dated 9 May 2012, and subject to Mr Andrews attending the resumed hearing for cross examination.

(4) The parties agreed that the Tribunal should disregard the evidence of Mr Birtwhistle for HMRC

18. As at 25 February 2013 there was an ongoing dispute between the Appellant, HMRC and KPMG regarding the draft disclosure order referred to at paragraph 19 above, and a new disclosure request and application of the Appellant dated 12 and 21 February 2013 respectively.

19. Mr Fletcher supplied a fourth witness statement dated 21 February 2013 in which he dealt with points a, d and e of the draft disclosure order dated 8 January 2013. The Tribunal established at the hearing on 25 February 2013 that the Appellant accepted the assurances of Ms Vanessa Sharp, Solicitor and General Counsel for KPMG LLP, given on points b and c of the draft disclosure order[38].

20. The disclosure request of 12 February 2013 concerned the identity and qualifications of KPMG staff who either undertook work for or on secondment to Data Select Limited and or 20/20 Logistics. In this respect Mr Fletcher supplied a fifth witness statement dated 21 February 2013. The request also required further information from HMRC and KPMG regarding instructions and contacts with Mr Fletcher, and details of the retainer entered into between KPMG and Data Select

[38] Transcript 25 February 2013 para 5 page 69 – para.9 page 72.

Limited. These further matters have subsequently been either resolved or not pursued by the Appellant.

21. The Application dated 21 February 2013 requested the Tribunal to issue a summons to Mr Fletcher requiring him to attend as a witness to answer questions generally in respect of his evidence to the Tribunal and in particular in relation to those matters which were the subject of the Appellant's application dated 12 February 2013. At the hearing on 25 February 2013 HMRC agreed to call Mr Fletcher to answer the Appellant's questions directed at the admissibility of his evidence.

22. On 13 March 2013 the Tribunal received evidence from Mr Fletcher relating to his expertise, independence, and the expert nature of his evidence. At the end of the hearing the Tribunal directed that

> (1) The Appeal shall be adjourned part-heard to 5 September 2013 with the hearing commencing on 9 September 2013 at 10.30am at Bedford Square London.
>
> (2) A window of ten days will be set aside for the hearing (9 – 20 September 2013) with the 5 and 6 September 2013 reserved for reading.
>
> (3) The Tribunal will reconvene on 9 April 2013 in the absence of the parties to determine the applications heard on 25 February 2013 (applications to recall Mr Saunders and admit additional evidence of Mr Andrews and Mr Case).
>
> (4) By no later than 4pm on 22 April 2013 HMRC uses its best endeavours to provide copies of the letters of instruction to Mr Fletcher in connection with these proceedings to the Tribunal and the Appellant.
>
> (5) By no later than 4pm on 13 May 2013 the Appellant to provide the Tribunal and HMRC with its written submissions on the admissibility of Mr Fletcher's evidence.
>
> (6) By no later than 4pm on 13 June 2013 HMRC to provide the Tribunal and Appellant with its response on the admissibility of Mr Fletcher's evidence.
>
> (7) By no later than 4pm on 1 July 2013 the Appellant to have a right of reply on the admissibility of Mr Fletcher's evidence which if exercised must be served on HMRC and the Tribunal.
>
> (8) The Appellant to advise KPMG that its request for disclosure is at an end.

23. The dates for the exchange of written submissions on the admissibility of Mr Fletcher's evidence were subsequently extended in anticipation that the Upper Tribunal decision in *Edgeskill* would be released. The Tribunal had been advised subsequently that the likely release date of the *Edgeskill* decision would not be until the end of 2013. In those circumstances the parties agreed that the Tribunal should proceed to make a determination on the admissibility of Mr Fletcher's evidence, and

conclude the hearing of the Appeal with an end date of 20 September 2013 for the receipt of final submissions.

24. Since the hearing on 13 March 2013 there have been further exchanges between the parties regarding the disclosure of documents. HMRC supplied the Appellant with a copy of the letter of instruction dated 11 November 2008 from Howes Percival, solicitors acting for HMRC, to Mr Fletcher, and copies of e-mails dated 20 and 21 January 2010 regarding the preparation of Mr Fletcher's second witness statement. HMRC also provided the Appellant with a copy of the Non-Disclosure Agreement between Nokia UK Limited and KPMG LLP dated 20 October 2008 referred to in Mr Fletcher's evidence on 13 March 2013.

25. The Appellant also requested documents relating to the High Court proceedings involving HMRC Sunico which was refused by the Tribunal in directions released 23 August 2013.

26. The Tribunal held a case management hearing on 21 August 2013 to deal with outstanding matters. One of those matters concerned the provision to the Tribunal of the transcripts in the *EES* Appeal recording Mr Fletcher's testimony. HMRC did not object to the Appellant's request provided the Tribunal exercised care having regard to the fact that Mr Fletcher had not been given the opportunity in these proceedings to give an explanation on his testimony.

27. The Tribunal's decision on the admissibility of Mr Fletcher's evidence was released on 9 September 2013

28. The Tribunal resumed the hearing on 9 September 2013 and reserved its decision on 20 September 2013.