

20883

INPUT TAX – MTIC – Mobile phones – Appellant claiming input tax on phones sold to Luxembourg trader – Direct chains – Whether acquisitions part of chains connected with VAT fraud – Yes – Whether Appellant a knowing participant – Yes – Appeal dismissed

LONDON TRIBUNAL CENTRE

EUROPEANS LTD

Appellant

- and -

THE COMMISSIONERS FOR HER MAJESTY’S REVENUE & CUSTOMS Respondents

**Tribunal: THEODORE WALLACE (Chairman)
MRS SHAHWAR SADEQUE (Member)**

Sitting in public in London on 15 to 19 and 22 to 24 September 2008

Kieron Beal, Counsel, instructed by BDO Stoy Hayward, chartered accountants, for the Appellant

Mark Cunningham QC and Daniel Margolin, instructed by Howes Percival LLP, for the Respondents

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DECISION

1. This was an appeal against a decision dated 24 April 2007 denying £1,256,675
5 input tax for period 07/06 on the acquisition in the United Kingdom of mobile phones
which then were sold to a Luxembourg trader.

2. There were five purchases, two on 14 June 2006, and one on each of 16 June,
20 June and 31 July 2006. In each case the phones were bought from Trade 247 Ltd
10 (“247”) being warehoused at the Feltham premises of Edge Logistics (“Edge”) and
were sold to 3G Trade SA (“3G”) in Luxembourg. There was no dispute as to the
existence of the goods, as to their removal to Luxembourg or as to the content of the
invoices.

3. The decision by Customs was based on the decision of the Court of Justice
15 *Kittel v Belgium* and *Belgium v Recolta Recycling SPRL* (Joined cases C-439/04 and
C-440/04) [2008] STC 1537, decided on 6 July 2006, to which we refer as *Kittel*, on
the footing that the acquisitions formed part of chains connected with the fraudulent
evasion of VAT and that the Appellant knew or should have known of that fact. This
20 type of fraud is known as “MTIC fraud”, MTIC standing for missing trader intra-
community. The missing trader in the first four chains was Astra Central Ltd, its
name being wrongly spelt as Astar on some documents; the missing trader in the fifth
chain purported to be Pearl Cosmetics Ltd but its VAT number had been hijacked.
Both missing traders had acquired the goods from EU traders. Customs’ case was
25 that these were direct chains: this was not a case of contra-trading.

4. There were over 3000 pages of exhibits. There were four witnesses for
Customs: Mrs Mia Stevenson, who made the decision under appeal; Andy Monk and
Kirsty Jolliffe, Customs officers, and Roderick Guy Stone, a Grade 7 officer, who is a
30 senior policy adviser with operational oversight for MTIC fraud. A statement by
Christopher Alan Solway was agreed with some exhibits being excluded. Terek
Meghrabi, managing director and sole shareholder, was the only witness for the
Appellant.

5. Mr. Cunningham opened the case and called his witnesses first. This was on
35 the basis that the burden was on Customs to establish the various chains, that there
was a default at the top of each chain and that the purpose of the default was
fraudulent and also that there was also an initial burden on Customs to establish that
the Appellant knew or ought to have known of these matters. Mr Cunningham
40 accepted that although the standard of proof is the civil standard the nature of the
allegations required a degree of cogency, see per Lord Hoffman at [55] in *Home
Secretary v Rehman* [2003] 1 AC 153. The allegations were serious. In fact his case
was that the Appellant had actual knowledge.

6. Mr Cunningham concluded his opening by saying that the transaction chains
45 were 90 per cent weighted in favour of the Appellant; that it was obvious that the
chains were contrived and orchestrated; that there must have been compliant

connivance certainly at the buffer level; that no orchestrator of a fraud would have permitted an unwitting interloper to come in and take 90 per cent; and that the only inference must be that the role of the Appellant and Mr Meghrabi went beyond “should have known” to “knew”.

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7. At the conclusion of Mr Cunningham’s opening Mr Beal said that the allegation that the entire transaction chain was contrived and pre-arranged was not in the Statement of Case served by Customs, apart from paragraph 30(viii) and (x). There was no distinct allegation against the Appellant of actual knowledge of matters in a transaction chain beyond his immediate customer or supplier. There was no allegation in the Statement of Case against the Appellant that it was all a pre-arranged scheme and that the Appellant knew of this or that it was masterminded by a puppet-master off stage. The opening thus differed substantially from the Statement of Case. The allegations of actual knowledge in the opening had not been properly pleaded and it was too late to raise them. He said that nowhere in Mrs Stevenson’s evidence did she allege that the Appellant was party to a pre-arranged scheme. He asked for a direction that the case against the Appellant be limited to the allegations contained either in the Statement of Case or in Mrs Stevenson’s statement and that Customs should not be allowed to allege knowing participation in a pre-arranged series of transactions.

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8. He referred to *Revenue and Customs Commissioners v Dempster* [2008] STC 2079 where Briggs J said at [26],

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“It is a cardinal principal of litigation that if serious allegations, in particular allegations of dishonesty, are to be made against a party who is called as a witness they must be both fairly and seriously pleaded and fairly and squarely put to that witness in cross-examination.”

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9. Mr Beal said that if the Statement of Case had been clearly pleaded the Appellant might have sought evidence from Edge Logistics Ltd.

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10. Mr Cunningham replied that it had always been clear on the Statement of Case and Mrs Stevenson’s evidence that one of the possible conclusions was that Mr Meghrabi was a knowing participant in the chains. In paragraph 33 it was pleaded that the Appellant knew or should have known that the assessed transactions formed part of chains in which one or more transactions was connected with fraudulent evasion of VAT. Actual knowledge was always in play. The words “in the premises” in paragraph 33 invoked the earlier matters pleaded, including paragraph 30. The contention that there were contrived chains was not new, it was in the Statement of Case.

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11. After a short recess we dismissed Mr Beal’s application. The allegation of knowledge was clearly contained in the Statement of Case albeit in an omnibus form. The Statement of Case alleged artificial contrivance in a context which was not limited to the Appellant’s immediate transactions. It was clear at the directions hearing that dishonesty was alleged, see Decision No.20796.

12. In the event Mr Cunningham put the allegation squarely to Mr Meghrabi in cross-examination that he was the ringmaster.

5 Facts not in dispute

13. Although there was no agreed statement of facts, many of the underlying facts were not in issue. The Appellant was incorporated on 9 October 2001 and registered for VAT from 15 October 2001.

10 14. Mr Meghrabi had previously operated a chauffeur driven car hire business as sole trader and transferred this to the Appellant in October 2001. The Appellant's business on registration was described as "performance and executive car hire". On 15 21 November 2002 the Appellant notified Customs that it would in addition be trading wholesale in mobile phones "on an export import and inland trading basis". The Appellant was visited on 3 December 2002 when the visiting officer was told that the Appellant had made sales of mobile phones to UK traders on 21 and 29 November. In letters on 5 December 2002 and 23 January 2003 the Appellant was told that there were problems in its trade sector and that it should verify the VAT 20 status of new suppliers and customers by fax at Dorset House VAT office.

15 15. On 16 November 2005 Mr Meghrabi wrote to Customs' Variation Unit at Newry, "The business have been approached by an overseas customer to export mobile phones. This trade will be an ancillary trade to our main business of car hire". 25

16. At some time before 2 February 2006 the Appellant took a tenancy of an office at 16 Hanover Square, W.1, consisting of one room on the first floor just large enough for three large desks.

30 17. Repayment returns had been made for six successive quarterly periods from 07/03 to 10/04, the largest being £29,127 for 10/03, and for 07/05. On 2 December 2005 the Appellant asked to change from quarterly to monthly returns. On 2 February 2006 writing from Hanover Square the Appellant informed Customs that 92.78 per 35 cent of sales would be zero-rated exports of mobile phones and that it would be in an ongoing refund position. Repayment claims of £291,165 for 01/06 and £747,104 for 04/06 were made before that now under appeal. All of the above claims were paid by Customs the repayment for 01/06 followed a visit by Mr Monk on 21 February 2006. The repayment claim for 04/06 was credited to the Appellant's account with Barclays on 8 June 2006.

40 18. On 28 July 2006 Customs wrote to the Appellant refusing the request to change to monthly returns.

45 19. On 2 August 2006 the Appellant submitted its VAT Return for 07/06 reclaiming £1,247,162; output tax was shown as £45,925 and input tax as £1,293,047; total sales were shown as £7.80 million of which £7.54 million was to other EU Member States. The output tax related to the car hire business.

20. On 1 August the Appellant had sent by e-mail to Gary Saul deal sheets for the five transactions in dispute. These were summarised. The first transaction showed 4400 Nokia 8800 silver supplied by 247 on 14 June at £360 per unit at a cost of £1,861,200 including £277,200 VAT with payments in two tranches on 15 June at the
5 First Curacao International Bank NV (“FCIB”); the same quantity of the same type of phones were shown as sold to 3G also on 14 June at a unit price of £378 for £1,663,200 without any VAT, payment being made at the same bank on 15 June, the freight forwarder being Edge and the delivery address as Warehouse 3G Trade, Luxembourg; invoices with VAT numbers were provided. Similar details were
10 provided for the other four deals.

21. On 31 August the Appellant was informed that a period of time would be required for Customs to undertake verification before repayment could be authorised and that enquiries had started. This process is described as extended verification. On
15 6 September Mr Archibald, Higher Officer, wrote that he was the case officer responsible for conducting the verification. On 27 September Customs wrote to the Appellant stating that the first transaction which we have described in the preceding paragraph commenced with a defaulting trader and that the joint and several liability explained in Notice 726 could be applied if the Appellant knew or had reasonable
20 grounds to suspect that VAT would go unpaid. On 5 October Mr Archibald wrote to the Appellant stating that it was Customs’ view that the Luxembourg transaction chains involving 3G Trading (sic) “which pass through (Europeans Ltd) form an integral part of an overall scheme to defraud the Revenue”. This letter was given to Mr Meghrabi on 5 October at the outset of a visit to the Appellant by Mr Archibald and Mrs Stevenson at which Mr Meghrabi, Giovanni Leon, an employee of the
25 Appellant, and Andrew Lynch, of Chiltern plc were present.

22. Before the meeting the Appellant had already given to Customs the original deal material for deal 1 including invoices, declarations by the Appellant to 247, purchase order to 247, order confirmation, inspection report by 4G UK Ltd (“4G
30 UK”) to the Appellant with IMEI numbers, Companies House details on 247, VAT validation responses from Europa, purchase order from 3G, Intra Account Transfer notifications from FCIB and instructions to Edge to ship on hold and release the goods to 3G. Similar material was provided for the other four deals. At some point
35 which appears to have been after 5 October the Appellant provided due diligence material to which we return later. We also return later to the visit on 5 October.

23. Subsequently Customs obtained from Edge successive release notes for deal 1 from Marubo International SL (“Marubo”), a Spanish company, to Astra, from Astra
40 to RX Tech Solutions Ltd (“RX Tech”) and thence to RK Brothers Ltd (“RK”), thence to JD Group (“JD”), and from Team Mobile Int (“Team”) to 247 and from 247 to the Appellant; the only release note missing in the sequence was one from JD to Team or, alternatively, a release from RK direct to Team. They were all dated 14 June and were for 4400 Nokia 8800 models. There were further release notes for deal
45 2 also on 14 June covering 3300 Nokia 8800 (black) following the same sequence to JD, from JD to The Export Company UK Ltd (“TEC”) and then to 247 and to the Appellant. There were similar sequential release notes for the other deals involving

5 6600 Nokia 9300 on June 16 and 3400 Motorola V3X R on June 20. The release notes for the deal on 31 July involving 5000 Nokia 9300i started with a release from Koornmarkt in Belgium to Pearl Cosmetics Ltd (“Pearl”) and from Pearl to RX-Tech. Apart from the absence of any release note to Team in deal 1, all sequences were complete.

24. A diagram was produced by Mrs Stevenson showing the chains on which Customs relied. This is annexed to this decision.

10 25. Mr Beal accepted that Astra Central Ltd and the trader purporting to be Pearl Cosmetics Ltd had not accounted for the VAT on the onward sale following acquisition.

Witnesses for Respondents

15 26. Mrs Stevenson confirmed witness statements dated 24 October 2007 and 9 January 2008. She has been a Customs officer since 1997 and since July 2006 has been attached to the MTIC team at Redhill, which collects, collates, monitors and verifies repayment claims.

20 27. On 24 April 2007 she notified the Appellant that the claim for period 06/07 was denied. She wrote that “the transactions form part of an overall scheme to defraud the Revenue” and that:

25 “there are features of those transactions, and conduct on your part, which demonstrate that you knew or should have known that this was the case, in that you either deliberately, or recklessly, ignored factors which indicated that those transactions may have formed part of such an overall scheme.”

30 28. On 5 October 2006 Mr Archibald and Mrs Stevenson visited the Appellant’s premises at 16 Hanover Square, W1. The visit lasted 2hrs 20 minutes. Mrs Stevenson exhibited two A4 pages of manuscript notes. She noted that the Appellant was advertising on three websites and was looking for retail customers but had not started yet. The notes continued,

35 “Supplier Trade 247 – see K.C. Cico – Director MD Deals

40 - looked for customers first negotiated the prices then contact 247 for stocks

- £10-20 margin depending

45 - confirmed the stocks and got paid by the customer within hours, by fax, check on line of the bank a/c to ensure the payment received.

- insurance policy hold by 247. Europeans has not insurance policy. Paid 247 directly on line.
- how to see the stock. Eur instruct independent A1 as good agents in scanning everything or 10%, send by email and sent a hard copy.”

She noted the address of A1 at Feltham, Middlesex. She recorded that no goods had been returned but 247 would be liable. She noted,

“- Contract for freight forwarder to store goods : a copy of the Edge Logistics Ltd.

Europeans would use the same freight forwarder as 247 depending on the location of the goods.”

Under “Customers” she noted

“You meet once year Mr Bulent in the UK office.

- checked with Redhill by phone. Noted a call reference No of the call with before the deal completed. Check Europa.

- it took too long to check Redhill for the commercial process because the line is too busy.

Confirmed the Europa’s verification is not enough.”

Later she noted

“English Bank took too long.

Barclay Bank

- car hire overheads

Overseas bank mobile.

- Tax adviser asked when i/t to be paid, but will inform you.”

29. Mrs Stevenson produced a typed summary of the visit from an electronic folder which was much more extensive than her notes. She said that she had telephoned Mr Meghrabi on 9 October; the notes included material from the telephone conversation and other material from Customs’ records; it may have taken more than a day to write it up; she asked Mr Archibald to look at the report before she finalised it. She was not sure whether Mr Archibald had taken notes but she did not look at any

other notes. We observe at this point that apart from the manuscript notes we derive little help from the visit on the issue of what the Appellant knew or ought to have known.

5 30. She produced Job-pack records provided by Edge for the five deal chains showing either Astar Central Ltd (sic) or Pearl as the UK acquires leading up to the Appellant. These were stamped as received by Customs on 19 December 2006. The release notes showed that Edge was initially instructed by fax to allocate and release stock to Astar (sic) or Pearl and then allocated and released the same quantities of
10 stock to successive customers according to the faxed instructions from the relevant suppliers until the stock was dispatched by the Appellant to 3G. In each case the successive releases were on the same day. She produced CMRs provided by the Appellant showing Edge removing the goods for the Appellant to Warehouse 3G Trade, Luxembourg.

15 31. On 20 November 2006 Mr Archibald wrote asking for extensive documentation including the original CMRs, relevant business records, additional inspection reports, due diligence records, bank statements, proof of payments to freight forwarders and inspection agents and a copy of the insurance policy.

20 32. Mrs Stevenson produced a letter from Mr Meghrabi dated 29 November 2006 in response to the request by Mr Archibald for the insurance policy in which he stated,

25 “With regard to insurance, we were under the impression that the goods were insured through our freight forwarders (Edge Logistics) in light of the size of their charges; however it appears that this is capped by limited liability. We therefore cannot provide insurance certificates.”

30 33. Mrs Stevenson produced deal logs provided by 247 which showed 247 as making supplies to 3G Trade on 27 January 2006 and 19 April 2006. 247 was also shown as making supplies to the Appellant on the first of those dates.

35 34. Cross-examined as to whether the Appellant was the target of the enforcement activity rather than the buffers, she said that she was only responsible for the Appellant. She would not be in a position to say whether the buffers were more likely to know about the defaulting trader. She said that there were instructions for third party payments elsewhere in the chains.

40 35. Asked about a progress log, she said that “MS” was herself and “IA” was Mr Archibald. She was involved at the same time as Mr Archibald, being his working partner to take over the case. Mr Archibald had been in court all week but was not giving evidence.

45 36. She said that Mr Meghrabi had produced the Edge contract at the meeting on 5 October but they did not go through the contract at the meeting. Asked about a note in the visit summary “supplier declaration by Trade 247 Ltd (not signed)”, she said that some deal pack documents were signed and some not; she said that she did not

know who “Jay Roach” (whose name appeared on the declaration under a signature) was and she neither interviewed him nor contacted 247. She did not ask Mr Meghrabi about it at the meeting. They did not go to specific documents during the interview which was simply to assess the company’s background and get a picture of the business.

37. Mrs Stevenson agreed that the Appellant had carried out a verification with Redhill as to 247 in January 2006, the request being on 19 January and the response on 23 January. She said that Redhill was overwhelmed with enquiries and had to conduct a certain kind of verification before sending confirmation backup; they had four, five, six faxes operating at the same time. Asked about a Europa validation response from the European Commission she said that she did not think this was the VIES system; when it was pointed out by Mr Beal that “VIES” appeared on the response, she agreed that Redhill uses the VIES system but said that Redhill had far more details in VIES, but she did not know to what extent. She said that she was not familiar with the VIES system, She said that the Appellant had been specifically required in writing to verify with Redhill and should do so even if it made no difference.

38. She agreed that a fax verification request by the Appellant as to VIP (Scotland) Ltd on 15 March 2006 had been answered on 8 May, whereas a telephone verification for the same company was given on 15 March.

39. She agreed that 247 and 3G Trade were still registered for VAT when her statement was made and that she had no information to suggest that either was not an existing company.

40. Mrs Stevenson said that her witness statement was closely related back to the visit report. Asked about paragraph 41.12 where she stated that Mr Meghrabi said that Europeans had no uniform terms of business, she said that he did say that although it was not in the visit report; she remembered because it was the first time she had visited the business and she could still remember. The supplier’s declaration by 247 “this purchase order is only valid once the attached supplier declaration is signed” did not say “contract”. She said that they had asked about terms of business at the interview; sometimes she asked a question when Mr Archibald had not done so; possibly she forgot to make a note. After the interview she wrote asking for a contract.

41. She said that Mr Meghrabi said that Edge was the freight forwarder but did not say “who also acted as the exclusive freight forwarder for all the transactions in the deal chains carried out in the UK” as she stated in paragraph 41.26 of her statement. She accepted that Mr Meghrabi did not comment on the deal chains or indicate that he knew anything about the freight forwarder acting further up the chains.

42. Mrs Stevenson said that the price she had included on a spreadsheet for Deal 1 for the sale by Marubo to Astra was not derived from an invoice but was her best judgment, assuming a margin of 35 pence from later deals; RK had produced invoices

from RX Tech. She accepted that the documents preceding those between 247 and the Appellant were not obtained from the Appellant. She agreed that the Nemesis batch report which she had exhibited as produced by the Appellant was Customs' document; she accepted that Nemesis reports are not available to traders. She said that traders could check with the Home Office database of stolen numbers.

43. She said that Edge had sent the release notes to David Maud, at Wolverhampton, on 19 December 2006. She said that she had not asked Mr Maud to give evidence.

44. Asked by Mr Beal whether it was possible for the Appellant to know that Astra was deregistered before she deregistered it on 15 December 2006, she said that she did not know.

45. She said that, although it was not in her notes, Mr Meghrabi had said that the inspection agency and the freight forwarders were the same people; this was in the subsequent telephone conversation which was more than half an hour long. She had telephoned him when she was typing. When Mr Beal put it to her that the telephone conversation was about 10 minutes, she said that it would not be a surprise.

46. Mrs Stevenson said that the first indication Customs had of concern about trade with 3G was in an intelligence report from Brussels on 31 August 2006. The report dealt with April 2006. This was produced for the first time on the fourth day of the hearing.

47. She said that Edge had told Mr Maud that the goods had come in on the same day as they went out again although the CMR had been lost by Edge. Mr Maud had told her this over the telephone.

48. She accepted that the Appellant was paid by 3G before the goods were supplied to Luxembourg.

49. Mr Monk, Higher Officer, who had been doing full-time MTIC work since 2003, gave evidence of a visit to the Appellant on 21 February 2006 to verify the large repayment claim for 01/06. He produced a page from the Appellant's electronic folder. He did not have his notebook but it was produced later during the hearing.

50. He said that he was shown the CMR evidence and was satisfied that the goods had been despatched. He discussed due diligence but did not go into great depths. He saw the invoices. He had no reason to believe that he was not shown the supplier's declaration. It would be normal practice to take copies of documents but he did not know if he had done so. The due diligence appeared to be adequate on the basis of the discussions. He said that it appeared that they were ticking the adequate boxes to protect themselves from the joint and several liability provisions. It was just a cursory interview. Normally two officers would go to discuss the activities in greater depth at a later date. At the time, which was shortly after the decision in the ECJ *Optigen v*

Customs and Excise Commissioners (Case C-354/03) [2006] STC 419, Customs were flooded with large repayment claims and simply did not have the resources.

51. He was asked about a passage in his report stating,

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“Discussed due diligence at meeting which, on basis of initial interview, appears adequate. Checked VAT numbers of customers and suppliers, all valid. Checked export evidence all satisfactory ... will subsequently line check deals and advise trader if any defaulters identified.”

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He said that it was one of his last visits before leaving Dorset House in March 2006. The case was passed to another officer. He had no idea what the Appellant’s future reclaims might be. He said that everything he saw and heard was consistent with the trading activities of the Appellant facilitating MTIC fraud. Asked why he did not include this in his report, he said that Customs had established a VAT user interest; when resources were available they would be checked thoroughly, as was the case. From April and May 2006 a large number of assurance officers were seconded to MTIC. He had recorded “No departmental delay. No grounds to delay repayment further.” This was because of the guidelines at the time : in MTIC terms £290,000 was a very small amount.

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52. He said that he had passed the paperwork to Mr Saul who passed it to Mrs Stevenson.

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53. Kirsty Jolliffe stated that Pearl was incorporated on 2 November 2004 and was registered for VAT from 5 November 2004. For the periods up to 11/05 there were no unusual trading patterns. The return form for 02/06 was returned undelivered. Another letter was returned to Customs marked “addressee moved out on 30/11/05 please return to sender.” Two officers called on 23 November 2006 at the principal place of business shown on the registration application and were told that the director had moved next door; a lady next door said that the director, Khuram Saeed, did not live there and that she knew about the company and believed it had finished about a year or two ago. Pearl was deregistered and assessments were raised, including one for £208,994 on a sale on 31 July 2006 to RX-Tech of 5000 Nokia 9300i.

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54. Subsequently, following a meeting with Mr Saeed, Customs concluded that the VAT number of Pearl had been hijacked. The assessments on Pearl were withdrawn and an assessment was raised for £208,994 against the Trader Purporting to be Pearl in respect of the supply to RX-Tech. That figure was a best judgment assessment.

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55. Mr Stone stated that data on HMRC’s trade statistical website showed the value of mobile phones exported to the EU and to non-EU countries was approximately £21 billion for the period January to June 2006. In July 2006 a reverse charge was announced in a Business Brief: the value of mobile exports fell back to £2.1 billion in the next 6 months. He said that approximately 34,000 transaction

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chains verified by Customs in 2006 were found to be connected to MTIC fraud. Approximately 5 per cent of those verified were not connected to fraud.

56. He accepted that it is possible for a trader in the UK to sell mobile phones to a trader in the EU. Asked about price differences between Member States in the prices of mobile phones, he said that Nokia and Motorola had been quoted as saying that they have a consistent pricing structure. He accepted that parallel trading could be beneficial to the consumer, that it is legal and that the potential for parallel importation between Member States should not be stifled. Customs could not insist on purchases from authorised distributors.

57. Mr Stone said that the joint and several liability powers have only been used on a very limited basis. The decision of the Court of Justice in *Customs and Excise Commissioners v Federation of Technological Industries* (Case C-384/04) [2006] STC 1483 was only given in May 2006. There was no enforcement until then. As to the number of MTIC appeals outstanding, he suspected that 700 accounting periods were involved with in the region of 350 to 500 traders. Approximately 1500 firms had been subject to extended verification.

58. He said that he was aware that the Federation of Technological Industries had complained at pressure by Customs on banks to refuse to give new accounts to mobile phone traders. He did not find it strange that the Federation had suggested to traders that they use FCIB. He agreed that traders were given no warning of joint action against FCIB before September 2006.

59. He said that currently there are not long waiting times for Redhill verification. After the ECJ decision in *Optigen* and *Bond House* in January 2006 the nature of the trade exploded. He said that Customs at Redhill largely got its details of EU traders from VIES (the VAT Information Exchange System). Traders could conduct checks through the Europa website, entering the number of the trader they are looking at and getting an answer whether it was valid or not. Customs get the name and address of the trader and the date of registration or deregistration, and thus get more information on the VIES system than traders do; this was why traders were told to do their verification with Redhill. The Europa website can also be used to check UK traders.

Mr Meghrabi's evidence

60. Mr Terek Meghrabi confirmed his witness statement dated 31 October 2007 with two amendments. He became a director in January 2003. He said that paragraph 5 which stated that his father runs a successful money services bureau should be in the past tense.

61. He said that he looked for a minimum mark-up of 5 per cent, there being a lot of overheads such as transportation and office expenditure; the mark-up on UK sales was lower, because exports affected cashflow.

62. He identified documents in the Bundle onwards as being from the Appellant's due diligence file, starting with a VAT Validation Response from Europa for 247 dated 23 January 2006 and Companies House material for 247, including accounts to April 2004. He met the director Mr Cicopalus when he visited 247; on the site visit which was around 25 January he was quite impressed by the company which had 10 or 11 traders. The Appellant never actually gave 247 any credit. He produced a check list showing the due diligence required by the Appellant from suppliers; he had obtained every single item on the check list but did not know where they were; they were all given to Chiltern. He said that Mr Monk had been shown the due diligence folder on his visit, it was the first thing he had asked for. The reply to a verification request to Redhill for 247 faxed on 19 January was on 23 January. Payments to 247 were online to FCIB where both the Appellant and 247 had accounts; this was quicker and charges were lower. The Appellant had received a letter of introduction from 247 on 16 January. On 24 January Giovanni Leon obtained a report on 247 from Equifax. The Appellant provided information to 247 for a site visit by 247 to the Appellant on 29 March. Mr Meghrabi produced some other due diligence material in relation to 247.

63. Mr Meghrabi said that 3G contacted the Appellant through the IPT website and Mr Bulent came to the Appellant's office. The Appellant sent an introduction letter to 3G on 19 January 2006 and obtained a Validation Response from Europa on 20 April. He produced a certificate of incorporation and a VAT certificate for 3G.

64. He produced due diligence material for various other companies, saying that it was standard to check any companies interested to work with the Appellant and to verify them with Redhill. Sometimes enquiries to Redhill took days, sometimes months. One enquiry as to Goldex International Ltd on 26 April was validated by Redhill on 25 May. An enquiry on 15 March as to VIP (Scotland) Ltd was validated on 8 May; an enquiry as to the same company by telephone was verified on 15 March.

65. Mr Meghrabi next produced documents relating to Edge: an introductory letter from the Appellant dated 15 March, a credit application form to Edge filled in by Mr Meghrabi, an Edge document headed "General Lien", a certificate of incorporation showing Edge as incorporated on 1 December 2005 and a letter setting out various requirements by Edge. The letter stated that Edge required a deposit of £1000; it gave the address of the warehouse at Feltham, Middlesex (adjoining London Airport). It set out warehousing charges, including Warehousing 20p, Allocation/Releases £10, Inspection 10p, Check-counting 10p and Scanning 10p. Quotations for transport and freight were on request. As to insurance, the letter read,

"We are not regulated by FSA. As such we are unable to offer 'all risk' marine cargo insurance for your stock. Should you require cover in excess of our limited liability you will need to arrange adequate insurance cover ..."

Mr Meghrabi said that no officer had asked him to do due diligence on freight forwarders.

66. He produced some documents relating to 4G UK. The Appellant had a few problems with A1 Inspection and 4G UK was recommended by Edge. He produced a list of 4G UK's standard charges carrying an address at Weybridge. These included 10 pence per unit plus VAT for scanning.

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67. He said that 4G UK inspected phones, scanning 10 per cent of the phones to obtain the IMEI numbers and counting the number of boxes. He produced an inspection report for deal two dated 14 June 2006 showing 825 boxes of four as counted. Usually 4G UK telephoned that the inspection was satisfactory, sent the IMEI numbers by e-mail and sent the hard copy of the report by post. He produced IMEI numbers for deal one. He said that the first five IMEI numbers show the model, the rest identify the phone. The Appellant usually tried to check these against previous numbers to see whether any were repeated. He said that checking was a tedious job; the Appellant never had a database to tell whether a number had been repeated. Giovanni used to do this. In answer to a question by the Tribunal whether this was manual, not using computer data, he said that it was tedious; he had asked Customs many times if they had a system they could help with but they said no. 4G UK gave the data by e-mail. He said that it was not in digitised form. It was necessary to check the columns manually, working down the columns.

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68. Mr Meghrabi said that the telephone conversation with Mrs Stevenson on 9 October was around 10 minutes.

69. In his statement Mr Meghrabi said that Customs officers visited the Appellant on several occasions and they established a good rapport. They discussed problems in their trade sector. He was advised: "Know your customer, know your supplier and do not make third party payments." At no time did HMRC ever express any concerns with the Appellant's trading partners, or methods of trading.

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70. He said that the Appellant is in constant contact with its suppliers and customers, enquiring about availability and demand, in an attempt to identify matches in supply and demand to provide a reasonable profit. The profit from arbitrage is only realised if the supplier and customer cannot deal directly, otherwise they would cut the Appellant out.

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71. He produced the files for the transactions in dispute. He stated that once an opportunity was identified the Appellant negotiated prices with both the supplier and customer to maximise the profit; once prices were agreed the Appellant asked the supplier to complete and return a supplier's declaration. The supplier's declaration for deal 1 was apparently faxed to 247 at 1213 hours and returned at 1239 hours signed by Jay Roach. The declaration stated that the goods were brand new with full manufacture warranty, that 247 had full title and that the goods had been inspected by 247 or the freight forwarder and IMEI numbers were available on request.

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72. He stated that once the prices were agreed, the Appellant checked the VAT numbers of 247 and 3G on the Europa website. This was a provisional go ahead. He stated at paragraph 50 of his statement,

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“I can categorically state that no transaction is completed until the full verification is received from HMRC.”

5 Presumably, although, it is not clear from the statement, the supplier’s declaration already described came next.

73. The Appellant then contacted Edge to confirm that the goods were at the warehouse and that 247 had title. Next the Appellant faxed an inspection request to
10 4G at Weybridge asking for 10% to be scanned. He stated that the Appellant was provided with an inspection report for 4400 Nokia 8800 silver phones. The IMEI numbers were also produced.

74. He stated that having received a satisfactory inspection report the Appellant
15 decided to ship the goods and issued the purchase orders. The purchase order for deal 1 to 247 was dated 14 June and was for 4400 Nokia 8800 Silver SIM free handset (euro) at £360 per unit making £1,584,000 plus VAT. An order confirmation to 247 containing specifications was signed by Giovanni also on 14 June; at the bottom of the form appeared “Edge Logistics”; this appears to be timed 1004 hours. The
20 purchase order from 3G was dated 14 June at a unit price of £378 and a total cost of £1,663,200; it provided for delivery on 15 June to Warehouse 3G Trade, “Transport Intra-communitarian” and stated “full payment after inspection of the goods”. The invoice by 247 dated 14 June bears the specific time “12:10”.

25 75. Fax instructions by the Appellant to Edge were to “Ship on hold” to 3G and then to release; both dated 14 June. On 15 June 3G paid the Appellant and the Appellant paid 247, the payments being at FCIB. The invoices were stamped as paid on 15 June.

30 76. The CMR gave the sender as the Appellant, the consignee as Warehouse 3G Trade SA, Luxembourg, the place and date of taking over the goods as “Feltham 16/06/2006”. The carrier was Edge and the vehicle number and drivers were given. The cargo was 4 pallets of mobile telephones, weighing 1115kgs.

35 77. Documents produced to Customs by Edge included a stock release instruction from 247 to the Appellant on 15 June at 1314 hours, an illegible CMR, an export invoice from Edge to the Appellant for £1250 freight and £55 packing plus VAT.

40 78. The preceding paragraphs were for deal 1. Similar documentation was exhibited for the other four deals.

79. Mr Meghrabi was cross-examined for six hours. He said that he was aged 37
45 having been born in Damascus. His mother tongue is Arabic but he has a clear command of English, having come to the UK aged twelve. He started Eurostyle in 1998, hiring out top of the range cars with his father’s help. He had helped his father with various businesses. His father’s conviction of four offences relating to the business and sentence to 10 years imprisonment was a matter of grave

disappointment. His statement that his father “runs” a successful Money Service Bureau should have been in the past tense. He accepted that “runs” gave a completely wrong impression.

5 80. He said that he was a conscientious businessman who did everything possible
to avoid being involved in fraud or anything dishonest. He was unaware of any fraud
in the chains of the transactions in which the Appellant was involved. He knew that
there was fraud in the secondary or grey mobile phone market. He had received
various letters from Customs and had been given a clear and explicit instruction to
10 check before every deal. He knew that the problem was “all around”, it was talked
about by everybody. He knew about Customs’ Notice 726 introduced in 2003 and
was familiar with it : it was on the Appellant’s due diligence check list for customers.
He said that the Notice did not tell him not to be involved in the sector, just to be
careful. He agreed that one of the options open was to have nothing to do with it. He
15 said that he believed that he was vigilant.

81. He said that he knew that Customs were under resourced and were taking a
long time to reply to verification requests. He was aware of the possibility of joint
and several liability or disallowance of input tax.

20 82. Mr Meghrabi said that he knew that he was dealing in the grey market and that
the Appellant was not an authorised dealer. The Appellant was dealing with its
supplier and customer. He did not know how many transactions were in the chains.
He knew in 2006 and before from paragraphs 2.4 and 3.3 of Notice 726 that the stated
25 requirement was to verify the integrity of all the components in the chain. He
understood that this referred to the whole chain and that he had to make a judgment as
to the whole chain. However he knew that it was not possible to check the integrity of
the whole chain. He said that *Bond House Systems Ltd v Customs and Excise
Commissioners* [2003] V&DR 210 made everybody nervous but when Notice 726
30 came out with clear rules and guidance he was happy to get back in. Before Notice
726 there was a lot of mayhem in the industry. It was a good business to be in with
high profits; mobile phones were a commodity that everyone used. He spoke to
Customs officers about Notice 726 and they agreed that there was no way of knowing
up the chain.

35 83. Mr Meghrabi said that his due diligence as to 247 was 100 per cent. He said
that not all the due diligence material was in the bundle, although it was all in the file
which he had given to Chiltern. When making his statement he thought all the
documents were there; the exhibits were prepared by Chiltern. He said that there were
40 lots of missing documents : he did not know they were missing until the hearing
started. He disagreed when Mr Cunningham put it to him that he could not care less
about due diligence. He denied that it was woeful or completely useless. The
Appellant’s first trade with 247 had been on 27 January 2006. It did not mean
anything that the accounts of 247 were overdue; the Appellant was not giving credit to
45 247. He had looked at the balance sheet of 247 but had not expected 247 to be
making a large profit in its first year to April 2004. On the site visit he had seen how
large they were; their name in the market was quite huge. Although the reference

from Interken Freighters (UK) Ltd as to 247 was dated 20 February 2006, he had a verbal conversation with them in the January. He did not consider a performance bond from 247 to be necessary as recommended by Equifax because 247 was not being given credit. He felt comfortable with 247. He had asked about one of the directors of 247 having been a director of a company which was struck off the Register of Companies but had been given a valid answer although he could not remember what.

84. Mr Meghrabi was then asked about the due diligence for 3G. He said that Mr Bulent came to the Appellant's office and gave him the documents on the check list. There was a file which had been misplaced by Chiltern. He said that Mr Monk and Mr Gary Saul had definitely seen it and were happy with the due diligence. He believed that he obtained a bank reference for 3G. Asked about a Redhill check, he said that he was under the impression that Redhill could not verify traders outside the UK. He did check with the Europa site. He said that it was impossible trying to do a deal, waiting for Redhill to verify.

85. He said the Appellant asked around about Edge and got a positive reply. The Appellant had Edge's certificate of incorporation and looked at its website. The check list was not sent to freight forwarders. He was told that Edge was a reputable company and had been in the market since 1999.

86. He said that 4G UK had been critically vetted. The Appellant was provided with its certificate of incorporation and VAT registration. 4G UK was in the market; he did not realise fraud was coming from inspectors or freight forwarders. He had obtained verbal references by telephone. The Appellant was happy with the inspection reports provided by 4G UK; the Appellant received verbal confirmation, the numbers were e-mailed and the report came by post afterwards. He agreed that he asked 4G UK to include the following matters: make and model, quantity, colour, country of manufacture, language of manuals, software language, type of charger, warranty and a ten per cent scan. He agreed that the inspection report on deal 1 indicated that the boxes were not counted and "Other comments – quantity inspected" was blank. The page before showed stock as 4400 and packing as 1100 boxes of four. "Charger" was left blank. Mr Meghrabi said that the Appellant used to speak to 4G UK all the time and they confirmed the type of charger; there was no note of the call. He said that when 4G UK inspected they checked that all the contents of the boxes were there including phone, charger and manual. He agreed that the bill dated 20 June 2006 only charged for a 10% scan at 10 pence a unit, with no charge for inspection and box count. Mr Meghrabi said that he was under the impression that 4G UK always did the box count. He agreed that the report on the second deal gave the wrong colour.

87. Mr Meghrabi said that the most important aspect of the whole exercise was to look at the IMEI numbers. He said that the order to ship was given when the Appellant received a completed report verbally on the telephone. The Appellant got the telephone confirmation; they got the stock numbers by e-mail and checked them; then they got the full inspection report by post. He denied that this was a pack of lies.

He said that previously the Appellant did obtain a 100% scan but it was expensive and time consuming.

5 88. He said that they tried to do a trade every day but it was not possible. The market was volatile but they always made substantial net sales : there were overheads. Edge and 4G UK's costs came to some £1,600; there was office rent, employees, telephone packs and many other expenses. He agreed that the gross profit in June was nearly £300,000; he said that 25 per cent should be deducted for expenses. There was no loss because he always sourced what was asked for.

10 89. He denied a suggestion that there was never a loss because it was all pre-arranged and that he was the ringmaster.

15 90. He agreed that the negotiation, inspection, reports and payments were all in one or two days. Asked whether he needed to look beyond one supplier, he said they had numerous calls every day from different people and called them. They felt comfortable with 247 but, although 247 was the only supplier in 07/06, it was not the only supplier the Appellant deal with. He was not surprised looking back that there was only one supplier and one customer in the quarter. He said that the Appellant never broke down larger consignments. The Appellant's phone records would show that they called many people. They used 247 because 247 had a lot of stock. Customers would ring up and ask for 4400 Nokia 8800s; all were SIM free with European specification. Most of the time 247 had the stock.

25 91. Asked about paragraph 4 of Mrs Stevenson's second statement where she said that analysis of deal logs provided by 247 showed that 247 was in direct contact with 3G in January 2006, Mr Meghrabi said that he was surprised. He said that maybe 247 did not want to export itself. He denied that it was all orchestrated and contrived and he was "in on it".

30 92. Mr Cunningham then went through with Mr Meghrabi his evidence as to 14 June 2006 as a typical day.

35 93. Mr Meghrabi said that Stage 1 was an enquiry from 3G as to whether the Appellant had 4,400 Nokia 8800 mobile phones.

94. Stage 2 was to try to source them. 247 stated on the telephone that they had them and would sell at £360 each.

40 95. Stage 3 was to go back to 3G and quote £378 including the Appellant's 5 per cent margin. He did not know that 247 and 3G knew each other.

45 96. Stage 4 was to check the files to ensure that due diligence was up to date and in order. After knowing them for some time, this was not necessarily done each time. He could not remember every detail from two and a half years ago; he had another employee and did not do everything himself.

97. Stage 5 was to check the VAT numbers of 247 and 3G on Europa.

98. Stage 6 was to try to check with Redhill. He tried to send a fax. He could not remember if the line was busy. If unsuccessful he called the national helpline.

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99. Stage 7 was to contact Edge to confirm that the goods were there. The Appellant knew the goods were there from the order confirmation issued by 247. These came after the purchase order from 3G. 247 also told them verbally that the goods were at Edge. Giovanni Leon signed the order confirmation and returned it to 247.

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100. Stage 8 was the supplier's declaration in which 247 confirmed that it had legal title. The declaration was faxed by Mr Meghrabi to 247 at 1213 hours and returned by 247 at 1239 hours.

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101. Stage 9 was that the Appellant instructed 4G by telephone and then by fax to do their inspection. The instruction was to their office at Weybridge. Most of the time 4G UK had a wide range of staff. He did not know where Edge's warehouse was, having never visited it. 4G UK may have had staff at Edge's premises at Feltham; usually staff were there checking other stock. It would take 4G UK about an hour to do the 10 per cent scan. 4G UK telephoned to say that everything was all right and e-mailed the IMEI numbers.

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102. Stage 10 was to check the numbers. He said that Giovanni had told him over the weekend that he did this using an Excel spreadsheet; Giovanni sorted the sequence of numbers numerically first and then copied and pasted them onto the old numbers before printing them off and checking manually whether there were any repetitive numbers. Mr Meghrabi said that he himself was not an IT person. Giovanni checked manually against the old numbers : this was tedious for him. Mr Meghrabi could not remember how long this took. Giovanni might get Denise to do it. It could take half an hour, it could be an hour. He agreed that it had to be done twice on 14 June because there was a second deal.

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103. Stage 11 was for the Appellant then to issue a purchase order to 247. Mr Cunningham asked him about the fax header on the purchase order giving the time at 1232 hours saying that it could not have been before 1339 hours (an hour after the supplier's declaration was returned). Mr Meghrabi said that he could not really comment on the paperwork, Giovanni, his trader, did that. He denied that this was a pack of lies. He agreed that 247 could not know the number of the purchase order, 200600012, before the order was sent. Mr Cunningham pointed out that 247's invoice bearing the number of the purchase order, gave a time of 1210 hours in the body of the invoice.

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104. Mr Meghrabi said that the payment from 3G was on 15 June to the Appellant's FCIB account. The payment to 247 was also on 15 June.

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105. Re-examined, Mr Meghrabi said that the Appellant always tried to get verification from Redhill by fax but it was always busy; they did not succeed they telephoned the national advice number. They also did a Europa check.

5 106. He said that he spoke to Gary Saul numerous times on the telephone. Mr Saul asked for all the documents when the 04/06 return was put in. The Appellant had sent the whole deal pack to Mr Saul's office and Mr Saul had confirmed receiving them.

107. He said that he knew nothing about Marubo, Astra or Astar, RX Tech
10 Solutions, RX Brothers or TM Global.

108. He said that once the Appellant was paid for the goods Edge were instructed to release them. The CMR was stamped as received by Warehouse 3G Trade on 19 June, the same day as the Norfolk Line ticket.

15

109. He said that the fax header on the order confirmation from 247 was timed at 1004 hours.

110. Mr Meghrabi said that the time on the 247 invoice for deal 2 was shown as
20 1201 hours, whereas the fax header time was 1504 hours. The supplier's declaration for deal 2 was sent at 1214 hours and returned at 1416 hours; the purchase order by the Appellant also had a fax time of 1214 hours, being sent with the supplier's declaration.

25 Submissions

111. Mr Cunningham said that it was not credible that six or seven conniving fraudsters in the chains would allow Mr Meghrabi having nothing to do with the fraud to walk away with much the largest part of the cake.

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112. The test under *Kittel* at [61] gives rise to two issues: whether the five transactions by the Appellant were connected with the fraudulent evasion of VAT having regard to objective factors, the factual element; and whether the Appellant knew or should have known, the mental element.

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113. As to the first issue, there had been no serious challenge to the tax loss in the chain; Pearl had been hijacked and Astra was missing and the balance of probabilities was that the defaults were fraudulent; it was clear from the deal chains that there was an unbreakable connection between each of the various transactions in each chain.

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114. As to the mental element, it is necessary to ask whether it was or should have been apparent to Mr Meghrabi that the Appellant's transactions were "more likely than not to be connected with fraud," see *Mobilx Ltd v Revenue and Customs Commissioners* (2008) Decision 20687 at [108]. If a trader fails the *Kittel* test then he is an accomplice, see *Calltell v Customs and Excise Commissioners* (2007) Decision
45 at [63] and (64). He said that at the lowest Mr Meghrabi should have known; Customs put it higher and submitted that he was the ring leader, or had actual

knowledge or was guilty of Nelsonian blindness. The lowest threshold would however suffice.

5 115. Mr Cunningham said that in some ways Mr Meghrabi was an attractive witness, being unfailingly polite, giving considered answers and, despite provocation, not being in the least aggressive. However his words belied the reality. His description of his father's business as successful was thoroughly misleading. He blamed Chiltern for misplacing documents. He invented telephone calls as to inspections by 4G. He did not check the language of his witness statement or his
10 exhibits.

116. He said that Mr Meghrabi knew that there was fraud all around the sector, that Customs were trying to tackle it, that his suppliers were not manufacturers or authorised dealers so that there were chains, that under Notice 726 he had to verify the integrity of the whole chains and that he could not verify the whole chains. He said
15 that there was no human right to embark on this trade.

117. Mr Cunningham said that it is quite difficult and probably impossible for an honest trader to operate in this sphere, namely the grey market.
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118. He said that 247 and 3G had traded with each other. The chains were contrived. If they were contrived, by definition there were no Chinese walls. All of the participants were knowingly, contrivingly playing the game, including Mr Meghrabi. He asked whether it was likely that Mr Meghrabi alone was a beacon of rectitude, but that the orchestrators let him take £18 a phone. He submitted that at
25 best he was catastrophically stupid; an honest bona fide trader who knew that he could not do the Notice 726 checks would not have taken the risk.

119. He said that the Appellant's due diligence was a perfunctory, box ticking, window dressing exercise to try to keep Customs at bay. The searches by 4G UK had all been described as satisfactory but the reports were cursory or perfunctory. The Appellant went through the motions of due diligence because Mr Meghrabi knew exactly what was going on.
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120. Turning to the actual trading, Mr Cunningham said that there were only five deals in the whole quarter, four of them in eight days; it was a volatile business but was always profitable for the Appellant; on every occasion complicated deals were completed in one day; in a highly populated sector all deals were with one supplier and one customer; 247 always had what was required; 247 and 3G did not deal with each other directly. On any view the Appellant knew of these matters, apart from 247
40 and 3G knowing each other. He said that the eleven stages in deal 1 described by Mr Meghrabi were not sustained by the documents. He submitted that Mr Meghrabi's initial evidence as to tedious time consuming manual checks on the IMEI numbers was not credible and that his later evidence was not correct.
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121. He said that the time shown on the purchase order by the Appellant to 247 was not consistent with the searches which were said to have been carried out by 4G UK

and the time consuming search when the IMEI numbers were received. Stage 11 could not have been at the time stated because some earlier stages were carried out after that time.

5 122. Once it was shown that the transactions were connected to fraudulent chains a substantial explanation was called for. He adopted the observations of Pumfrey J in *Softwarecore Ltd v Pathan* [2005] EWHC 1845 (Ch) at [52] where he said,

10 “The factors are to be viewed as a whole. They reveal at best a pattern of trading from which, without substantial explanation, a judge could draw an inference of dishonesty.”

15 123. Mr Cunningham said that arguments by the Appellant based on legal certainty are trumped by the objective of preventing tax evasion, avoidance and abuse, see per Burton J at [45] in *R (Just Fabulous (UK) Ltd) v Revenue and Customs Commissioners* [2007] EWHC 521 (Admin).

20 124. In opening Mr Beal said that Customs targeted traders removing goods to another Member State, who they called brokers, because they were the traders making repayment claims as the Appellant was here. A joint and several liability approach could have been adopted against the co-called buffers in the transaction chain under section 77A of the VAT Act 1994 but this had not been done although they were closer to the defaulting traders.

25 125. Paragraph 2.4 of Notice 726 refers to reasonable checks to verify the supply chain, however none of the specific checks recommended went to the supply chain itself. In *Mobilx* at [287] it was recognised that in practice none of the checks could go beyond the immediate suppliers and customers. At paragraph 3.3 of Notice 726 it is said that the measure is aimed at those who know of the fraud or choose to turn a
30 blind eye. None of the specific checks recommended were directed to the customers. Paragraph 4.8 is significant because Customs accept the burden of establishing on the balance of probabilities knowledge or reasonable grounds to suspect that the VAT would go unpaid. This was the regime considered in *Customs and Excise Commissioners v Federation of Technological Industries* (Case 384/04) [2006] STC
35 1483 where section 77A was considered. In that case the Court of Justice said at [29] that when Member States exercise the powers conferred upon them by Community directives they must comply with general principles of Community law including legal certainty and proportionality, see also *Teleos v Revenue and Customs Commissioners* (Case C-409/04) [2007] ECR I-7797 at [45], [48] and [50].

40 126. In *Garage Molenheide BVBA v Belgium* (Case C-286/94) [1998] STC 126 the Court said that measures to ensure the proper collection of VAT must not “have the effect of systematically undermining the right to deduct VAT”. Measures must be proportionate. He said that in *Kittel* the Court did not say that if a trader does not take
45 every reasonable precaution he is complicit in fraud : that would be completely at odds with the UK concept of complicity in fraud. He submitted that Customs must show that Mr Meghrabi was complicit in fraud. The phrase “should have known” in

Kittel is to be interpreted in the light of equivalent UK domestic law and practice. Customs must show something that put Mr Meghrabi on notice of the fraud to which he turned a blind eye. Negligence is not enough. He cited a number of decisions of the Court of Justice.

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127. In closing Mr Beal said that the evidence was a far cry from the best evidence for a very serious allegation. Mr Archibald was not called as a witness although he was the front line officer for much of the time. Mrs Stevenson on a number of occasions relied on documents which Mr Archibald had written, being only a signpost. Key documents had been produced very late. The paper folder referred to by Mr Monk had not been produced and Mr Saul had not been called although he must have had the deal documents for 04/06. Fax headers had been omitted from the trial bundles. It was inappropriate for a panoply of new points to be raised which were not either in the Statement of Case or witness statements.

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128. He said that, if indicia of fraud were staring the Appellant in the face, they must have stared Mr Monk in the face and that it was inconceivable that he would have sanctioned repayment.

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129. Mr Beal said that the allegations against Edge and 4G UK had not been specifically set out. If the Appellant had understood how the case for Customs would be put, evidence from Edge could have been called.

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130. He said that Notice 726 contains no requirement to undertake any specific checks. The principles of proportionately, legal certainty and fiscal neutrality are relevant to the means by which Customs establish fraud on the part of a trader. If Customs were correct, Notice 726 could close the whole grey market.

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131. He said that Customs must prove the underlying fraud. The tax loss should be capable of being particularised. Customs must show that the same goods were involved : the only evidence here was the release notes.

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132. Mr Beal said that 247 and 3G are still VAT registered and trading. Edge is still in business as is 4G UK. He said that if these freight forwarders and inspection agents were effectively a conduit to an organised fraud it was inconceivable that Customs would not have stepped in.

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133. He said that in his evidence Mr Meghrabi had dealt with the points of criticism insofar as they were of substance in a measured way.

Conclusions

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134. We start by considering whether Customs have established that the transactions giving rise to the disallowed input tax were connected with the fraudulent evasion of VAT having regard to objective factors. Mr Cunningham accepted that he must show a loss in each chain, that this was the result of fraud and that the acquisition by the Appellant was factually connected with the chain. We then consider

whether the Appellant in the person of Mr Meghrabi knew or should have known of the above matters.

5 135. It was common ground that the standard of proof is the balance of probabilities but that cogent evidence was required commensurate with the serious nature of the allegations, see *Home Secretary v Rehman*. Although these are not criminal proceedings, knowing participation in fraud is an allegation of the utmost gravity.

10 136. Our decision was rendered much more difficult because of the nature of the evidence, most of which was purely circumstantial being based on documents a large number of which were obtained by Customs from sources other than the Appellant. The most important documents relied on by Customs were the release notes and the third party payment instructions. There was no direct evidence as to how these were
15 obtained. There was no evidence of visits at the relevant time to Edge, RK, Venus or Easy MSI Ltd.

137. The main direct evidence in relation to Mr Meghrabi's knowledge was the meeting on 5 October 2006. Although most of the questions were put by Mr
20 Archibald he was not called as a witness although present at the hearing. Although the meeting was part of the extended verification process it appears that he asked remarkably few questions about the actual transactions although he had the original deal material provided by the Appellant, see paragraph 22 above. The notes taken by Mrs Stevenson were very brief for a meeting of over two hours. We would have
25 expected Mr Archibald to have had a check list of matters to be covered at the visit and for this to have been produced. Mrs Stevenson's note contained no mention of 4G UK, referring only to A1, although criticisms of the inspection were an important part of the case for Customs. Mrs Stevenson was relatively inexperienced, this being her first MTIC verification and for the most part she acted as a signpost for the
30 documents.

138. There were also shortcomings in the evidence for the Appellant. In particular Giovanni Leon who played an important part in the transactions was clearly available
35 as a witness because Mr Meghrabi asked him during the hearing about the IMEI numbers, however he was not called.

139. The task of the Tribunal is, however, not to decide the appeal on evidence which was not given, but on the material before us although in doing that we are entitled to draw inferences in relation to evidence which was or ought to have been
40 available.

140. We return now to the initial factual issue. Mr Beal put Customs to proof of the underlying fraud in the chains and the connection through to the Appellant. He pointed to the lack of invoices for many transactions in the chains and said that the
45 release notes contained no values.

141. We accept the submission by Mr Cunningham that Customs do not have to dot every “i” and cross every “t”. The Tribunal Rules provide expressly for evidence which would be inadmissible in a Court of law. The weight to be given to hearsay evidence is another matter and Mr Beal pointed out that much of Mr Stevenson’s evidence was second or third hand hearsay and was often far from best evidence.

142. The evidence of the chains consisted mainly of the release notes provided to Customs by Edge. There was no evidence of a visit by Customs to Edge after January 2006 and no correspondence was exhibited by Mrs Stevenson as to the production of the deal logs. We do however accept that the release notes were provided by Edge to Customs with the covering lists. Apart from the absence of any release to Team in deal 1, the release notes show successive instructions to Edge to release the relevant models and quantities to the successive traders shown on the diagram annexed to this decision. The release notes are all dated and the dates coincide with the Appellant’s invoices. It would be an extraordinary coincidence if any of the release notes related to other identical models and quantities on the same days.

143. In each chain instructions were exhibited for payments by traders further down the chain from the UK importer direct to the EC supplier, Marubo in the case of deals 1, 2 and 4, Universal Systems SCS in deal 3 and BVBA Koornmarkt in deal 5. In deal 1 RX Tech invoiced RK for £1,577,400 plus £276,045 VAT, making £1,853,445 and instructed RK to pay £1,853,186.50 to Marubo and £285.50 to RX Tech. Deals 2, 3 and 5 involved similar instructions by RX Tech to RK, although in deals 3 and 5 the third party payments were to Universal Systems SCS and BVBA Koornmarkt respectively. In deal 4 Astra instructed Venus Computers Ltd (“Venus”) to make payments of £971,783.75 to Marubo and £199.75 to Astra and Venus instructed Easy MSI Ltd to pay £971,983.50 to Marubo and £199.75 to Venus; the invoice by Astra to Venus was for £827,220 plus VAT making £971,983.50.

144. In deal 1 the invoice from 247 to the Appellant was for £1,584,000 plus £277,200 VAT making £1,861,200, settled in two debits at FCIB on 15 June 2006. The invoice from the Appellant to 3G was for £1,663,200, also settled in two payments on 15 June.

145. There was no proper evidence as to how Customs obtained those documents. Mrs Stevenson’s evidence was that RX Tech was a missing trader. There was however no dispute as to the authenticity of the third party payment instructions, which we accept, observing that they are consistent with the release notes.

146. The instructions for payments to Marubo and the other two EC suppliers involved small payments to the immediate suppliers, RX Tech in four deals, and successive split payment instructions in deal 4. In each case the combined payments equalled the sums due to the immediate supplier inclusive of VAT. The amount payable to Marubo and the other two EC Suppliers was substantially greater than the amount excluding VAT payable to the immediate supplier. The clear inference must be that the £1,853,186.50 which RX Tech instructed RK to pay Marubo was the amount which Marubo charged Astra on deal 1 and that since RX Tech invoiced RK

in the sum of £1,584,000 excluding VAT, Astra sustained a substantial paper loss on selling to RX Tech. Similarly, in the other three deals where Astra was the UK acquirer, the payment to the EC Supplier substantially exceeded the tax exclusive amount for which the goods were sold on. The same goes for deal 5 where the hijacked Pearl was the UK acquirer.

147. In each of the chains the onward sales to 247 were at a nominal profit.

148. In view of the pattern of release notes in deals 2 to 5, and that in deal 3 RK released to TM, and that RK made a third party payment in deal 1, we conclude that the release in deal 1 to JD was an error for TM.

149 We regard the release notes and third party payment instructions as clear and cogent evidence that in respect of each deal the acquisition by the Appellant was causally connected with the fraudulent evasion of VAT and we find accordingly.

150. This brings us to the issue whether it has been established by objective factors that the Appellant knew or should have known that the transactions into which it entered formed part of chains connected to the fraudulent evasion of VAT.

151. We do not accept the submission by Mr Cunningham that the Appellant took or would have taken 90 per cent of the proceeds and must therefore have been the ringmaster. That submission failed to take account of the third party payments to the EC suppliers all of which were substantially greater than the sums obtained by the Appellant from 3G. In deal 1, if the Appellant recovered its input tax, its gross profit would be £79,200 before other expenses. Marubo on the other hand received £189,986.50 more than the Appellant obtained from 3G. Far from being 90 per cent, the Appellant's share was under 30 per cent before taking account of the time taken to reclaim VAT and the Appellant's other expenses. Until and unless the Appellant recovered its input tax it made a loss. The obvious inference is that Marubo and the other EC suppliers were the ringmasters or that they were acting for a common ringmaster.

152. The next question is whether it has been shown that the Appellant albeit not the ringmaster was a knowing participant with actual knowledge. On this aspect the fact that the Appellant would potentially make a substantial profit is clearly a factor, however a share of under 30 per cent is much less compelling than one of 90 per cent.

153. Mr Cunningham placed substantial reliance on the inadequacy of the due diligence carried out by the Appellant which he described as woeful. In particular he said that Notice 726 required the Appellant to verify the integrity of the entire transaction chains, which Mr Meghrabi said was not possible. He also stressed the failure to verify with Redhill before the deals.

154. It is important to note that there is no legal obligation to verify the entire transaction chain, indeed any such an obligation would appear to contravene

Community law since it is impractical for a trader to comply. Similarly, verification with Redhill was unrealistic because of the time in obtaining a reply.

5 155. We accept that there were material weaknesses in the Appellant's due diligence, but we do not consider that they are more than a factor in deciding whether the Appellant had actual knowledge. We note that the weaknesses were not so apparent to Mr Monk as to cause him to delay repayment of the 01/06 reclaim. We consider however that the Appellant's due diligence was not strong enough to assist in countering the allegation of actual knowledge.

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156. This brings us to the actual trading transactions in issue.

15 157. During his evidence in chief Mr Meghrabi said that the 4G UK e-mailed the IMEI numbers to the Appellant and that Giovanni checked them against previous numbers, a tedious job which had to be done manually working down the columns since there was no database, see paragraph 67 above.

20 158. In cross-examination he said that Giovanni had told him over the week-end that he did this using an Excel spreadsheet and that he sorted the numbers numerically before pasting them onto the old numbers and printing them off to check manually whether there was any repetition; Mr Meghrabi said that this might take half an hour or an hour, see paragraph 102 above.

25 159. We have real difficulty with the evidence of Mr Meghrabi as to this. The Appellant's office in Hanover Square consisted of one room in which there were three large desks. Mr Meghrabi must have known what Giovanni was doing. His evidence in chief contained no suggestion that Giovanni sorted the numbers on the computer and married them with the old numbers before printing them off and checking manually for repetition. Since there had been a series of earlier deals, in particular in the preceding two quarters, this would have been an incredibly time-consuming task particularly since 4G UK did not provide the numbers in numerical order. If the whole process apart from checking for repetition was carried out on the computer, it seems to us inconceivable that Mr Meghrabi would not have realised what Giovanni was doing until he asked him over the weekend. We do accept that checking manually for repetition even after the numbers had been sorted and pasted would have taken a considerable time. It is clear that the Appellant did not have a computer programme similar to Nemesis which is used by Customs; Nemesis does not involve sorting into numerical sequences. Although Mr Meghrabi's witness statement said at paragraph 52 that the 10% can was "to guard against repeat buying of the same phones", the statement contained no mention of a tedious and time consuming check by the Appellant. We note that Giovanni Leon was not called as a witness and no print out was produced to confirm that the check described had taken place.

45 160. A further difficulty arises in relation to Mr Meghrabi's evidence as to receipt of inspection reports. At paragraphs 53 and 54 of his statement he said this,

- “53. We were then provided with an inspection report which we found to be satisfactory.
54. Having received the completed inspection reports, we took the decision to ship the goods.”

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This contained no mention of a confirmatory telephone call before receipt of the actual report in the post. We do not see how an oral report on the telephone could be found to be satisfactory unless it covered all items which 4G UK had been asked to cover, see paragraph 86 above. The completed reports could not have been received by post before the Appellant instructed Edge to ship the goods on 14 June. We do not find Mr Meghrabi’s answer in cross-examination that the Appellant got a completed report on the telephone to be credible. Even if 4G UK had said that everything was in order, that would only have been possible if 4G UK had been told what to look for.

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161. Mr Cunningham also relied on the timings shown on the fax headers. These however involve the difficulty that the fax headers did not appear on a number of documents in the bundles for the hearing and that we do not know which documents had no header or on which the header was not on the copy in the bundle because of misalignment in photocopying. Further some dates and times were not clearly legible.

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162. In those circumstances we can only draw limited conclusions from the fax headers. The first is that deals 1 and 2 were dealt with concurrently, since faxes emanating from the Appellant in relation to both deals show times very close together. Another conclusion is that the Appellant faxed the purchase order to 247 19 minutes after sending the supplier’s declaration to 247 for signature. This latter conclusion does not square with Mr Meghrabi’s evidence in cross-examination that 4G UK were instructed after the receipt from 247 of the signed supplier’s declaration, that 4G UK took about an hour to do the 10 per cent scan and that the purchase order was issued by the Appellant after checking the IMEI numbers (see paragraphs 100 to 103 above). We note however that the time shown on the fax header on 247’s order confirmation sent to the Appellant was some two hours earlier. If the Appellant was confident as to 247 making the supply, it would not be surprising if the instructions to 4G UK were in fact given before receipt of the supplier’s declaration. This was not however what the Appellant said.

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163. We do not find the dates of the deals significant. Although there were only five deals in period 07/06, the Appellant did not receive the £747,104 repayment for 04/06 until 8 June; prior to that there would no doubt have been a problem in financing the VAT element in the deals. The fifth deal was on the last day of the accounting period and the Appellant no doubt hoped for an early repayment. Given that the Appellant dealt back to back, it is hardly surprising that the deals were always profitable.

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164. We do not consider the fact that all five deals were profitable to be significant. Given that the Appellant sourced the goods to meet the customer’s requirements dealing back to back it is hardly surprising that the deals were profitable. We find nothing inherently improbable in such deals of themselves.

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165. We do however regard it as significant that in all five deals the specific mobile telephones in the specific quantities which 3G requested were always available from 247 without a single consignment having to be broken down or amalgamated since each consignment had been acquired in the same quantities by 247. There was no suggestion that 3G asked for different models or quantities and that any deal was adjusted to what 247 could supply. Nor was there any suggestion that 247 sourced goods to meet the Appellant's requirements. Given the chains of release notes any such suggestion would not have been credible. We are satisfied that 3G knew of the prior chains and that the Appellant would acquire the goods from 247.

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166. Although Mr Cunningham did not take this point, we consider the fact that the IMEI numbers, while all appropriate to the models in question, were random numbers bearing no apparent relationship to each other to be significant. We would have expected consignments being sold on the grey market as surplus to requirements to be in batches of adjoining numbers. Deal 1 consisted of 1100 boxes of 4 according to the report, of which 440 phones were scanned. The scatter of numbers suggests that they must have come from a very large number of different batches possibly hundreds. We can think of no satisfactory reason why goods should have been circulating in the grey market in this way. A sample of 10 per cent could not be representative of a whole of such consignment. Every single box would have to be checked for the matters referred to in paragraph 86. It may be that this goes primarily to the chains being fraudulent, however it is also relevant to the Appellant's knowledge.

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167. We have already recorded our concerns as to Mr Meghrabi's evidence as to checking the IMEI numbers and the receipt of the inspection reports. We do not accept his evidence that missing due diligence papers had been given by him to Chiltern; he suggested that there might have been lost when Chiltern became part of BDO Stoy Hayward, however he had already signed his witness statement omitting those papers while Chiltern was still independent. We accept Mr Cunningham's submission that Mr Meghrabi's reference to his father's business in the present tense was thoroughly misleading; in our judgment this was not accidental.

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168. We do not find it credible that Mr Meghrabi was an innocent dupe. He is both articulate and intelligent. His reference to the initial *Bond House* decision in the Tribunal shows that he was aware of the problems in the sector as far back as 2003.

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169. We have concluded that on the central matters in this case, Mr Meghrabi did not give truthful evidence. In particular we find that he did know when entering into the five transactions that they were part of a fraudulent chain.

170. In view of this finding the question of whether the Appellant should have known is not relevant. The submissions by Mr Beal as to legal certainty, proportionality and fiscal neutrality depended on the premise that the Appellant did not have actual knowledge. A trader who participates in fraud cannot in our judgment
5 rely on the principles of legal certainty, proportionality and fiscal neutrality in avoiding the consequences laid down by the Court of Justice in *Kittel*.

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**THEODORE WALLACE
CHAIRMAN**

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RELEASED: 26 November 2008

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The following additional cases were cited in argument or in written submissions.

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