



**TC00359**

**Appeal number LON/2005/0625**

*VAT – refusal of right to deduct input tax – Missing Trader Intra-Community (MTIC) fraud*

**FIRST-TIER TRIBUNAL**

**TAX**

**NEXT GENERATION INTERNATIONAL LIMITED**

**Appellant**

**- and -**

**THE COMMISSIONERS FOR HER MAJESTY'S  
REVENUE AND CUSTOMS (VAT)**

**Respondents**

**TRIBUNAL: JUDGE ROGER BERNER  
GILL HUNTER (Member)**

**Sitting in public in London on 7 – 11 December 2009**

**Kevin Andrews, Senior VAT Consultant, VAT Consultants Ltd, for the Appellant**

**Rupert Jones, instructed by the General Counsel and Solicitor to HM Revenue and  
Customs, for the Respondents**

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## DECISION

1. This is the appeal of Next Generation International Limited (“the Appellant”) against the decision of HMRC contained in a letter dated 21 February 2008 denying the Appellant the right to deduct input tax in the sum of £122,690.75 claimed in respect of the VAT accounting period August 2006 (08/06). HMRC’s grounds for this decision are that the input tax was incurred by the Appellant in two transactions connected with the fraudulent evasion of VAT and that the Appellant knew or should have known that the transactions were connected to fraud. In short this is one of the line of cases commonly referred to as MTIC (“missing trader intra-community”) fraud cases.

2. The Appellant was represented by Kevin Andrews, Senior VAT Consultant with VAT Consultants Ltd. Rupert Jones of Counsel appeared for HMRC.

3. We had witness statements, and heard oral evidence from, a number of witnesses. For HMRC we had evidence from its officers Michael Quartey, Fidelis Mayungbe, Peter Dean, Clive White and Roderick Stone, and from John Fletcher, a Principal Adviser of KPMG LLP. There was one witness for the Appellant, Robin Ramdane, who at the time of the hearing was the General Manager of the Appellant, but who at the date of the transactions in question in this appeal was one of its directors. We also received in evidence a substantial quantity of documents.

### **The law**

4. The legislation governing the recovery of input tax is contained in sections 24 and 25 of the Value Added Tax Act 1994 (“VATA”). There was no dispute on the application of those provisions, which we need not refer to in full.

5. The basis for the decision of HMRC to refuse repayment of input tax to the Appellant for the relevant period was the decision of the European Court of Justice in *Axel Kittell v Belgium* [2008] STC 1537. It was submitted by Mr Jones, and not disputed by Mr Andrews, that *Kittell* provides a legal basis for denying a taxable person the right to deduct input tax (and, in appropriate circumstances, to obtain repayment of input tax) in defined circumstances. At paragraphs [56] to [59] the ECJ set out the guiding principles:

“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.

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

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

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

This was echoed in paragraph [61] of the ECJ judgment.

6. In *Revenue and Customs Commissioners v Livewire Telecom Ltd* [2009] STC 643, Lewison J set out the following summary of the ECJ jurisprudence as follows (at [76]):

“I would summarise the current state of the jurisprudence of the ECJ on this subject as follows:

(i) The objective of preventing evasion of VAT is an objective encouraged by the Sixth Directive (see *Kittel* [2008] STC 1537, [2006] ECR I-6161, para 54 of the judgment);

(ii) This objective precludes the recovery of input tax where the tax is evaded by the taxable person himself (*Kittel*, para 53 of the judgment). In such cases where the right to deduct has been exercised fraudulently the deduction may be retrospectively disallowed (*Kittel*, para 55);

(iii) This objective sometimes justifies stringent requirements as regards suppliers' obligations, but any sharing of risk must be compatible with the principle of proportionality (*Teleos* [2008] STC 706, [2008] QB 600, para 58 of the judgment);

(iv) It is disproportionate and contrary to Community law to require a person who is a careful and honest trader to assume liability for the frauds of others (*Teleos*, para 77 of the opinion, footnote 26);

(v) It is also disproportionate to hold a taxable person liable for fraudulent acts of third parties over whom he has no influence (*Netto* [2008] STC 3280, para 23 of the judgment);

(vi) A trader who does take every precaution that could reasonably be required of him, and does not realise that he is participating in VAT fraud must be entitled to rely on the legality of his own transaction (*FTI* [2006] STC 1483, [2006] ECR I-4191, para 33 of the judgment);

(vii) A person who knew or should have known that by his purchase he was taking part in a transaction connected with the fraudulent evasion of VAT is to be treated in the same way as a person who fraudulently exercises the right to deduct (*Kittel*, paras 55 to 56);

(viii) It is not contrary to Community law to require a supplier to take every step that could reasonably be required of him to satisfy himself that the transaction which he is effecting does not result in his participation in tax evasion (*Teleos*, para 65; *Netto*, para 24);

5 (ix) Likewise a taxable person can be expected to act with all due diligence and care (*Netto*, para 45 of the opinion);

(x) Whether a taxable person knew or should have known that he was participating in a transaction connected with the fraudulent evasion of VAT must be determined having regard to objective facts or factors (*Kittel*, para 59 of the judgment);

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(xi) Community law does not prohibit presumptions, but presumptions must be rebuttable by evidence (*Garage Molenheide* [1998] STC 126, [1997] ECR I-7281, para 52 of the judgment; *FTI*, para 32).”

15 7. On this basis, and on the basis of the judgment of the Chancellor in *Blue Sphere Global Ltd v Revenue and Customs Commissioners* [2009] STC 2239 at [29], there was no dispute as to the questions the Tribunal must address. They are:

(1) Was there a tax loss?

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

20 (3) If there was a fraudulent evasion, were the Appellant’s transactions which are the subject of this appeal connected with that evasion?

(4) If such a connection were established, did the Appellant know or should the Appellant have known that its purchases were connected with a fraudulent evasion of VAT?

25 8. In *Livewire*, when considering the test, Lewison J made it clear that the trader in the position of the Appellant does not have to know, or be said ought to have known, the identity of the missing trader. He said (at [91]):

30 “Unless there is a missing trader somewhere further down the chain (or in a parallel chain) there is no fraud. I accept that the honest trader need not know the identity of the missing trader but unless he knows or should have known that there was (or was likely to be) a missing trader somewhere in the dirty chain, I do not see how it can be said that he knew or should have known that his transaction was connected with fraud.”

35 *Livewire* itself was of course a case on contra-trading, but it is clear from Mr Justice Lewison’s reference to a missing trader in the chain that he was speaking generally. As will be seen, this case does not concern contra-trading, but the principle that the trader need not know the identity of the missing trader is equally applicable here.

40 9. The test of the trader’s knowledge set out by Lewison J in *Livewire* requires at the least that the trader should have known that there was likely to be a missing trader somewhere in the dirty chain. Also in the High Court, in considering how to apply

the *Kittel* test, Floyd J in *Mobilx Ltd (in administration) v Revenue and Customs Commissioners* [2009] STC 1107 said (at [7]):

5 “In the light of the difficulties of making enquiries beyond the immediate supplier, there is a danger in reading para 51 of *Kittel* in a narrow sense and as suggesting that provided proper checks are carried out by the trader on a supplier, then the trader's claims to repayment of VAT are not capable of challenge. That is not, in my judgment, a correct view. Suspicious indications obtained by a trader from carrying out due diligence checks on its supplier are one, but not the only basis from which it may properly be inferred that a trader knew or should have known of its implication in VAT fraud. The test to be applied is that set out in para 61 of the judgment, and indeed in the ECJ's final determination at the end of the judgment. Paragraph 51 needs to be understood in the sense that 'all reasonable precautions' may, in some cases, involve ceasing to trade in specified goods in a particular market, at least in the particular manner in which the trader undertakes that trade. Such a situation may conceivably arise where, from other indications available to the trader, the trader knew or should have known that it is more likely than not that, despite all due diligence checking, any further goods traded in the same way will be implicated in VAT fraud.”

10. The standard against which the trader is to be measured is that of a person with the skill, experience of the ordinary competent trader. This can be found from the judgment of Lewison J in *Livewire* at [123] to [125]. The test must be applied to the taxable person, which in this case is the Appellant company, and not merely its director, Mr Ramdane. There may be others whose knowledge ought properly to be attributed to the Appellant.

11. Mr Andrews raised only one issue in relation to the applicable law. Based on an answer given to him in his cross-examination of Mr Stone, he argued that the missing trader or the defaulter must be the importer, and that HMRC had provided no evidence, such as EC sales lists, to prove that the alleged missing trader in connection with these transactions, UR Traders Ltd, had been the importer of the mobile phones in question. We do not agree. As Mr Jones pointed out, this issue has been determined by Clarke J in *Red 12 Trading Limited v HMRC* [2009] EWHC 2563 (Ch) where he states that the fact that descriptions of the classic or simplest form of missing trader habitually referred to the defaulter as the importer (or vice versa) did not mean that a right to deduct input tax on the ground of such fraud could only be denied if HMRC established that the defaulter was the original importer. He said (at [84]):

40 “In many cases of MTIC fraud the defaulter, i.e. the company which fails to account for VAT and beyond which HMRC will not have been able to trace the chain, will be the actual importer. But it need not be so. Y may be the actual importer who sells (or transfers possession of) the goods to A who sells to B. Both the actual importer and A may go “missing” and make no payment to HMRC at all (as was the case with deals 12–14: see para 21 (iv)). The goods may bypass the defaulter and

5 be allocated by the freight forwarder directly to one of the buffer  
companies (as happened in deal 1) although input and output tax is  
accounted for by a buffer company earlier in the chain. The buffer  
company serves its function of preventing HMRC tracing back to the  
original importer. Third party payments may be made by purchasers in  
the middle of the chain cutting out those above. What is needed for an  
MTIC fraud to work is an importation without payment of VAT, a  
trader who disappears without accounting to HMRC for the output tax  
it has received, and an export which generates an entitlement to claim  
back input tax. The original importer will make the most profit from  
failing to pay over output VAT. For that reason the defaulter is usually  
the original importer; but any company in the chain which defaults at  
any stage in the chain will make a profit from not accounting for the  
VAT, assuming that it has sold on at a profit. In order to justify denial  
of the right to deduct input tax there must be knowing participation in a  
transaction connected with fraudulent evasion of the tax. If that is  
established, the right is lost. It would be inconsistent with that  
principle, and an unmerited boon to fraudsters, to require the  
authorities to prove that the defaulter was the original importer.”

20 Accordingly it is not necessary for HMRC in this case to prove that UR Traders  
Limited was the importer of the mobile phones in question.

12. There was no dispute on the standard of proof. This is the ordinary civil standard,  
namely the balance of probabilities. However, as regards the burden of proof we  
should make some comments, as there are conflicting approaches in different High  
Court judgments. The position is summarised by Clarke J in *Red 12 Trading* at [44]  
to [49]:

“44 In *HMRC v Brayfal Ltd* (Unreported) CH/2008/App 082 Lewison J  
said that:

30 “In cases of this kind, the burden is on HMRC to establish a fraudulent  
tax loss and that the transactions giving rise to that loss are connected  
to the taxpayer's transactions. If that is established, then the taxpayer  
must show that it did not know and could not have known about the  
fraud.”

35 45 In *Calltell Telecom Ltd v HMRC* [2009] EWHC 1081 (Ch) Floyd J  
held that:

40 “7. The mere fact that a transaction forms part of a chain in which  
fraud occurred is not enough to justify the refusal of repayment of  
income tax. To justify such a refusal the tax authorities must prove that  
the taxpayer was himself being fraudulent, or knew or had the means  
of knowledge of fraud by others.”

45 46 On 22nd May 2009 the Chancellor handed down judgment in *Blue  
Sphere Global Ltd v HMRC* [2009] EWHC 1150 (Ch), in which he  
upheld a trader's appeal from a decision of the tribunal upholding the  
Commissioners' refusal to repay input tax. In the course of his  
judgment he held that the test used by the tribunal to determine

whether the trader had the requisite knowledge that it was participating in transactions connected with the fraudulent evasion of VAT was misleading. That test had been expressed by the tribunal *inter alia* as follows:

5 “We consider that the due diligence exercise relating to Universal [one  
of the trader's purchasers] was inadequate, as was the failure to follow  
up outstanding questions where matters did not appear to be in  
satisfactory order. The exercise was not sufficient to protect BSG from  
10 the risk of involvement in transactions which might turn out to have  
undesirable associations.”

15 47 That test was, the Chancellor held, misleading for two reasons.  
First, the burden was on the Commissioners to prove that the trader  
ought to have known that by its purchases it was participating in  
transactions connected with the fraudulent evasion of VAT. It was not  
for the trader to prove that it ought not. Secondly, it was not sufficient  
to demonstrate that the trader was involved in transactions which *might*  
20 turn out to have undesirable associations. The relevant knowledge was  
that the trader ought to have known that by its purchases it was  
participating in transactions which *were* connected with the fraudulent  
evasion of VAT; that such transactions *might* be so connected was not  
enough; paras 51 and 52.

25 48 The Commissioners also had to prove that the trader ought to have  
known that earlier transactions, with which the seller of the mobile  
phones to the trader was connected, were transactions involving the  
fraudulent evasion of VAT: paragraph 53.

30 49 The Commissioners, who are appealing the Chancellor's decision in  
*Blue Sphere*, contend that, insofar as the Court intended to alter the  
burden on HMRC in a simple MTIC case (*Blue Sphere* was a case of  
contra trading) the decision is in conflict with earlier domestic and ECJ  
authority not cited to the Chancellor.”

13. This is a simple MTIC, and does not involve contra-trading. In *Red 12 Trading Clarke J* found that it was not necessary to decide the incidence of the burden of proof, but said obiter at [53]:

35 “Were it necessary to reach a conclusion I should be in agreement with  
the Chancellor. The ECJ authorities emphasise the importance of the  
taxpayer's right to deduct input tax in respect of what, viewed  
objectively, are taxable supplies, whilst recognising the right of public  
authorities to refuse repayment if the taxpayer knew or ought to have  
known that its purchases had a fraudulent connection. In these  
40 circumstances it seems to me that, if the Commissioners seek to deny  
the taxpayer a right to repayment of input tax paid on taxable supplies  
on the grounds of the taxpayer's knowledge (actual or constructive) of  
a connection to fraud, it is for them to establish that. If, in the light of  
all the evidence, including that of the taxpayer, the tribunal is not  
45 satisfied that he had or ought to have had the requisite knowledge, the  
taxpayer will be entitled to recover. In practice before a tribunal the

5 stage may be reached at which the evidence calls for an answer, in the sense that, if the taxpayer gives no evidence that he made any inquiries, the tribunal could conclude that he had the requisite knowledge because he either had or ought to have had knowledge of the fraudulent nature of the transaction. But, at the end of the day, it remains for HMRC to convince the Tribunal that it should so conclude.”

14. In light of this we have concluded that we ought to follow the Chancellor’s test of the burden in *Blue Sphere*, as approved albeit obiter by Clarke J in *Red 12 Trading*.  
10 We do not consider that we can distinguish *Blue Sphere* from this case on the ground that this is a simple MTIC and does not involve contra-trading.

### **Background**

15. The Appellant is a limited company incorporated on 12 September 1995. It is registered for VAT having first applied for registration on 28 July 1996 and having  
15 been registered from an earlier date, namely 2 July 1996, to take account of earlier taxable supplies. The VAT1 registration form completed by the Appellant specified its business as “computer consultancy services”, and we heard from Mr Ramdane that this had been the nature of the initial business that had been undertaken by him and his partner in the business, Mr A K Bhardwaj.

20 16. On 16 August 2002 the Appellant was de-registered for VAT on the basis that it had failed to submit two previous VAT returns and that its principal place of business showed no sign of trading. However the Appellant was re-registered on 8 October 2002 on the footing that it was trading from a new principal place of business.

25 17. At the time of the transactions relevant to these appeals, the directors of the Appellant company were Mr Ramdane and Mr Bhardwaj. Mr Bhardwaj was also the company secretary. From 12 September 1995 to 19 August 2008, Mr Ramdane was the director of the Appellant and from that date, according to his witness statement, Mr Ramdane was, as general manager, involved in all administration duties for the day to day operations of the company and a six month handover period to the new  
30 director.

18. In his evidence Mr Ramdane explained the background to the mobile phone trading entered into by the Appellant. An opportunity arose in Harlow, Essex for the Appellant to open a shop in the retail mobile phone business. Both Mr Ramdane and Mr Bhardwaj were working full-time for other businesses at this time, so they went  
35 into partnership with another local trader and hired staff. Mr Ramdane explained that this business was partially successful, but that it ended in disagreement with the partner. This led the company to enter the wholesale market through box-breaking, but this was not universally profitable, and the Appellant incurred losses.

19. This in turn led to the Appellant being introduced into the broking business by a  
40 third party, identified as Mr R Nagji, who became an agent and trusted adviser to the Appellant. After some initial, limited, activity in this market in 2004, because of the fact that the directors were in full-time employment, the Appellant was invited to

become an investor in New Order Exports Ltd (“New Order”), receiving a return described as a commission. No explanation was provided as to the agreement as regards the return to be obtained on the Appellant’s investments in New Order, but an examination of the commission statements produced in evidence by the Appellant shows that for each of the deals done in August 2005, the Appellant received a return equal to 75% of the net profit. Each of those deals also resulted in a gross profit for New Order, after recovery of input tax, of around 6% (the figures varying only between 5.82% and 6.17%).

20. Mr Ramdane’s evidence was that at the start of 2006 the Appellant’s agent told the Appellant that its investment was no longer required, but that the Appellant was to be given the opportunity to trade on its own account. The Appellant agreed to do so on the basis that the return (which the Appellant had seen was obtainable on the New Order transactions) was excellent. Mr Ramdane said that the agent introduced him and Mr Bhardwaj “to the party”, in the form of two trades. From deal logs produced in evidence by the Appellant, we find that the following deals were undertaken in this period:

(1) On 23 February 2006 the Appellant purchased 2,000 digital e-cards from Gulf Link FZE at £19 per unit, a gross value of £38,000. On 26 February 2006, the Appellant sold 2,000 digital e-cards to New Order at a unit price of £21, a gross value of £42,000 (exclusive of VAT).

(2) On 4 March 2006 the Appellant again sold 2,000 digital e-cards to New Order at £21 per unit.

(3) On 15 March 2006 the Appellant purchased 2,000 digital e-cards from Gulf Link FZE at £19 per unit. The customer name included against this transaction is again New Order.

(4) On 4 April 2006 the Appellant sold 3,500 mobile phones (no indication is given as to make or model) to Sunico A/S of Denmark at a unit price of £177.50, a gross value of £620,895. The matching purchase was dated 6 April 2006 from Jos UK Limited at a unit price of £167.50, and a VAT exclusive amount of £586,250. The Appellant’s profit margin, on a VAT-exclusive basis, was 5.9%.

(5) In May 2006, there were further transactions in digital e-cards, in each case the acquisition being from Gulf Link FZE, and the customer being Sinclair Data Systems Ltd.

(6) On 30 May 2006 the Appellant entered into four transactions in mobile phones of different unit prices. Its supplier was again Joe UK Limited and its customer Sunico A/S. The overall value of its purchases was £433,062.50, exclusive of VAT, and its aggregate sale price was £459,213.14, a mark-up, on a net of VAT basis, of 6%. For the individual phone consignments the mark-ups were between 5.93% and 6.15%.

### The July 2006 deals

21. In the VAT period 08/06 two transactions were identified by HMRC as appropriate for extended verification, and it is those transactions with which this appeal is concerned. There is no dispute on the facts of the transactions themselves, which were described in HMRC's evidence, and were included in the deal logs produced by the Appellant. On 11 July 2006 the Appellant purchased from Blue Star Trading Ltd 1,450 Nokia 8800 mobile phones at a unit price of £312.20 giving a value, exclusive of VAT, of £452,690 and 1,000 Nokia 9300i mobile phones at a unit price of £248.40 giving a value, exclusive of VAT, of £248,400. On the same day the Appellant sold to Sunico A/S the same quantity of each phone, in the case of the Nokia 8800 at a unit price of £330.90, giving a value of £479,805, and in the case of the Nokia 9300i at a unit price of £263.30, giving a value of £263,000. The mark up on each sale by the Appellant was a fraction short of 6%.

22. The evidence of HMRC, specifically that of Mr Mayungbe and Mr Dean, demonstrates that these transactions were part of a chain. The transactions were identified as separate deals in relation to the Nokia 8800 and the Nokia 9300i respectively, but it seems to us that, apart from one additional final link in the chain that relates only to the sale by Sunico A/S of the Nokia 9300i phones to a Netherlands company, the transactions in both phones were invoiced by each supplier in the chain as a single deal, and we therefore consider that, up to the purchase by Sunico A/S, we should regard the transactions as representing a single chain, and not two separate chains. On the basis of the documentary evidence before us, we find that the Appellant's transactions were part of the following chains, which identify separately the invoice chain, the money chain (that is, how payments were made notwithstanding the invoice chain) and the freight forwarder chain, that is how the ownership of the goods moved:

**Invoice chain:** UR Traders – Principle Traders – Carpa – Ultimate Wholesale – Bluestar Trading – the Appellant – Sunico

**Money chain:** Sunico – the Appellant – Bluestar Trading – Ultimate Wholesale – Alpha (Greece) – Imanse (France) – DRA Corp. (Cyprus) – Sunico

**Freight forwarder chain:** DRA – Imanse – Ultimate Wholesale – Bluestar Trading – the Appellant

23. This is the full extent of the chain in respect of the Nokia 8800 phones. The only difference in relation to the Nokia 9300i phones is that there is an additional link in the invoice chain at the very end, after Sunico, where Silus (Netherlands) appears.

24. As regards the fact that companies in the invoice chain, namely UR Traders, Principle Traders and Carpa, did not also feature in the money, or payment, chain, we had evidence from Mr Stone that such third party payments were often a feature of MTIC fraud. These third party payments are as a result of payment instructions given to either the trader dealing with the missing trader ("the first line buffer") or to another buffer trader further along the chain. The purpose is to ensure that the missing trader is unlikely to have assets available to meet its VAT liability.

25. Mr Stone also gave evidence regarding the possible reason for a difference between the invoice chain and the freight forwarder chain. The effect of this would be that the freight forwarder would not know the identity of the missing trader, thus making it more difficult for HMRC to identify such a trader at the freight forwarder level so as to de-register the missing trader.

26. One particular feature of the money chain merits further comment. As will be seen from the above description, Sunico A/S features both at the start and end of that chain. It paid £263,000 to the Appellant on 18 July 2006 and on the following day it received £275,000 from DRA Corporation Limited, a Cyprus company. There was accordingly a circularity of payments in the chain.

### **Was there a tax loss?**

27. The first question we have to address is whether HMRC have satisfied us, on the balance of probabilities, that there was a tax loss. As described above, we are satisfied that the transactions can be traced back to UR Traders Ltd (“UR Traders”). UR Traders has not submitted a VAT return since its first VAT return for period 10/05. Its registration was cancelled with effect from 26 July 2006. We were informed by Mr Quartey, and we accept, that various assessments have been raised against UR Traders in respect of which that company has defaulted in an amount, at the date of the hearing, of about £66 million.

28. We are satisfied that there was a tax loss.

### **Did the tax loss result from fraudulent evasion?**

29. Mr Jones argued that the evidence clearly demonstrated that the tax loss was attributable to fraud. He pointed to the tax loss on the default of UR Traders. The evidence of Mr Quartey showed that on its VAT registration form UR Traders had stated its business activities as “retail electrical items, crockery, computer parts” and its estimated taxable turnover as £200,000. The value of the expected purchases from the EU and sales to the EU was stated as nil. Based on the assessments raised against UR Traders, the total taxable supplies made by that company in the 12 months subsequent to registration would have been in excess of £366,385,579, inclusive of VAT. Given the estimated taxable turnover at the time of the VAT registration, this is a growth rate in excess of 183,000% in a period of less than one calendar year.

30. On 26 July 2006 Mr Quartey visited UR Traders at its principal place of business at 5 Campbell Road, London, E6 1NP. The address was a rented room in a residential address. Mr Quartey was informed by the occupant that the business was no longer at that address. In cross-examination, Mr Andrews put it to Mr Quartey that it was not possible to conclude that the size and nature of the premises necessarily proved that the business carried on by UR Traders was not legitimate. Mr Quartey was unable to clarify how many transactions had been entered into by UR Traders, but agreed that it had been relatively few. Mr Quartey’s evidence was that, based on his experience, the only businesses generating such an increase in turnover from such an infrastructure were those associated with MTIC fraud. We do not regard the type of

premises occupied by UR Traders as decisive, but we do consider it relevant. It is apparent that in a commercial business counterparties would be concerned to check the credentials of a trader before conducting business with that trader. In the case of UR Traders, not only was the turnover vast, it had been generated by only a relatively few transactions, and so a number of those transactions must have been sizeable. It seems to us that the fact that counterparties were prepared to deal with UR Traders despite its evident lack of infrastructure at least raises a question as to whether it can be regarded as a bona fide trader, a question that must be considered along with other factors.

31. Also on 26 July 2006 Mr Quartey sent a letter to UR Traders notifying it of the removal of its VAT registration from the VAT register. Subsequently, on 1 February 2007, Mr Quartey visited 240A Helly Road, Manor Park, London E12 6UD, the address listed at Companies House as the residential address of the company director Ahmad Janjuva and the company secretary Khalid Nawaz. There was no response. Despite leaving a calling card, Mr Quartey has not been contacted by either the company director or the secretary.

32. On 30 August 2007 mail addressed to UR Traders was returned to HMRC marked RTS (return to sender). Mr Quartey attempted to contact UR Traders on two telephone numbers given in its application to register for VAT, but neither is in service. A National Telephone Unit (“NTU”) check shows that one of the numbers was registered to NPower Yorkshire Ltd, Top Rank Club, 79 High Street North, London E6 1HZ, and the other to a person other than the named company director or secretary. Finally no VAT return has ever been rendered by UR Traders since its first VAT return for the period 10/05.

33. As well as the facts surrounding UR Traders itself, Mr Jones also referred us to the chains of transactions as themselves evidencing fraud. We received evidence from Mr Fletcher as to the “grey market” in mobile phone handset distribution and the limited opportunities to enter that market. It was submitted on behalf of HMRC that the transaction chains were not consistent with profitable grey market trading. We accept the evidence of Mr Fletcher in this respect. According to his evidence the grey market exists because of market failures occurring in the authorised distribution market. These market failures fall into two distinct categories: those relating to volume failures, and those relating to price failures. Volume failures (or forecast failures) are caused by the authorised distributor holding too much or too little stock. This failure creates the two grey market trading opportunities of volume shortages and dumping. Price failures are caused by differentials arising in the price of particular handsets in different markets. These differentials can be caused by a variance in the level of the handset subsidy applied to the handset by the mobile network operator in different countries. This leads to the grey market opportunity of box-breaking. The differential can also be caused by the original equipment manufacturer (“OEM”), in this case Nokia, setting a different price for the same handset in different markets. This leads to the grey market opportunity of arbitrage.

34. Mr Fletcher identified a number of negative indicators in respect of each of these grey market opportunities that would suggest that profitable grey market trading was

not being undertaken. In relation to box-breaking, trading in handsets that did not originate in the UK indicates that box-breaking is unlikely to be taking place, since handsets in the UK are amongst the most heavily subsidised in Europe. The presence of a two-pin plug means that the phone was not originally intended for use in the UK.  
5 A lack of infrastructure to support profitable box-breaking, such as storage and warehousing facilities, and not holding stock, would also be negative indicators, as well as absence of sufficient specification on purchase orders and invoices.

35. In relation to arbitrage, Mr Fletcher's evidence was that trading in Nokia phones excludes traders from pursuing arbitrage opportunities as Nokia sets homogenous pricing for its customers across all territories. Whilst currency arbitrage would remain possible in theory, Mr Fletcher's evidence was that, having regard to the fluctuations in the sterling to euro exchange rate during 2006, it was unlikely that these would have been sufficient to support arbitrage opportunities other than at enormous volumes, and they appeared insufficient to generate opportunities that would cover even the fixed costs.  
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36. Mr Fletcher said that profitable volume shortage opportunities in the grey market required very specific phone descriptions on order forms and invoices. Furthermore, a trader would be unlikely to be able to compete in the market without its own stock, or rapid access to the exact stock required, due to the rapid response expectations of its customers. Advantages of price and reliability of supply could be obtained through dealing with an authorised distributor. Failure to do so, despite selling sufficient numbers of phones to establish trade terms with an authorised distributor, would be a negative indicator in respect of profitable grey market trading in respect of volume shortages.  
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37. Mr Fletcher explained the "dumping" takes place where distributors have excess stock that they cannot trade for a suitable level of profit in their own operating territory. A distributor is unlikely to purchase stock that is being dumped, as the distributor would be expected to have the requisite market knowledge to know that the phone is being dumped and would be commercially unpopular.  
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38. Mr Fletcher also explained that in a profitable grey market the most profitable position is for the distributor to be supplied by an authorised distributor or mobile network operator and for them in turn to sell directly to the retailer or end customer. This works best if there are relatively short deal chains. Profitability and margins are likely to be reduced in longer deal chains, which therefore suffer from the risk of disintermediation, that is where traders are cut out of the chain.  
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39. In cross-examination by Mr Andrews, Mr Fletcher said that he was not arguing that the negative indicators to which he had referred would suggest fraud. They merely suggested that it was highly unlikely that the transactions entered into with those indicators would be a profitable or profit-driven grey market trade. We accept Mr Fletcher's evidence, and we find that the long chain of traders, the lack of specificity on the orders and invoices we have seen, the fact that the phones were Nokia phones and that there was no warehousing of stock by any of the parties, taken together indicate that it was more likely than not that the trades were not being carried  
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out in pursuit of profitable grey market trading, but were, as Mr Jones submitted, contrived for the purpose of fraud on the VAT system.

40. We are satisfied that HMRC have discharged the burden of showing that the tax loss resulted from fraud. We accept that UR Traders was a missing trader, and we regard its failure to make VAT returns and to account for VAT, its disappearance and the disappearance of its director and secretary, its false contact details, and the fact that it must have given a third party payment instruction to exclude itself from the payment chain and was also excluded from the freight forwarder chain as showing, in the context of a chain of transactions that cannot be accepted as representing profitable grey market trading, on the balance of probabilities that it was engaged in fraud and that the tax loss resulted from that fraud.

41. Mr Jones also argued that the circularity of payments in the money chain that we have described earlier showed a clear tax loss attributable to fraud because the payments must be orchestrated in such a way that the person who makes the first payment receives it back in a circle and that the payment chain is never broken. HMRC's argument was that such a circle could not realistically occur by chance, or at least that the chances of it occurring by chance are so small as to be disregarded. We agree that this is strong evidence of an orchestrated design, and we find that the transactions were contrived, were not in themselves commercial transactions, and were designed for the purpose of VAT evasion.

42. As well as circularity of payments, Mr Jones referred us to the IMEI checks that HMRC had carried out on the inspection reports obtained by the Appellant from A1 Inspections Limited on the consignments of the two phones concerned in the Appellant's trades. The IMEI, or International Mobile Equipment Identity, numbers are unique identifiers attached to each phone and they can be scanned and recorded each time the phones enter and leave the United Kingdom. The IMEI numbers were taken and recorded by A1 Inspections. HMRC found, and we accept as a fact, that a high percentage of each of the two makes of phone had been scanned at either the same or different locations on previous occasions before the sales by the Appellant to Sunico A/S. This conclusion was drawn from batch reports from a NEMESIS database to which HMRC (but not, we should record, the Appellant or A1 Inspections) had access and which were produced in evidence. Mr Jones argued that the number of hits on the NEMESIS database indicates the presence of fraud (generally termed "carousel fraud"), as there could be no commercial rationale for a phone to enter and leave the UK on a number of occasions. In our view, although this would not of itself be conclusive, this represents a further factor pointing towards the transactions being connected to fraudulent evasion of VAT.

43. Mr Andrews argued, by reference to a reply of Mr Stone given to him in cross-examination, that it would be necessary that the defaulting trader was shown to have been the importer, and that this had not been shown by HMRC, either having regard to EC sales lists or otherwise. Mr Stone had said that "on paper ... [the defaulter] would have to be the acquirer". This is a question of law, and not of evidence, and as we have noted earlier it is not necessary for HMRC to show that UR Traders was the acquirer of the phones in the intra-community trade.

44. Mr Andrews also argued that the three traders in the chain that did not receive payment, namely Carpa, Principle Traders and UR Traders, could themselves be regarded as “fiscal victims”, and unable to pay their VAT liabilities simply through themselves not being paid. He suggested that it might have been possible for these companies to claim bad debt relief. As regards UR Traders, we do not accept this as a credible explanation. In our view UR Traders was not a fiscal victim as described by Mr Andrews, but the tax loss occasioned by its default was the result of a fraud, for the reasons we have given.

**Were the Appellant’s transactions connected with that fraudulent evasion?**

45. We have examined the evidence regarding the chain of deals including both UR Traders, the missing trader, and the Appellant. For the reasons we have given we are satisfied that the Appellant’s transactions were connected to the fraudulent evasion of UR Traders.

**Did the Appellant know or should the Appellant have known that its purchases were connected with a fraudulent evasion of VAT?**

46. In relation to the burden of proof on this question, Mr Jones said that the primary submission of HMRC was that, having heard the evidence, the Tribunal need not consider the issue of the potentially conflicting authorities on where the burden of proof lies. If, contrary to the position of HMRC on the law, the burden of proof lies fully upon HMRC, he submitted that the evidence heard by the Tribunal was more than sufficient to discharge that burden. We indicated earlier that we prefer the approach of the Chancellor in *Blue Sphere* and the obiter comments of Clarke J in *Red 12 Trading*, and we accordingly approach this question on the footing that, having due regard to the evidence given by the Appellant, or the absence of it, the burden lies on HMRC.

47. As regards the evidence, the Tribunal heard only from Mr Ramdane. It heard no oral evidence from Mr Ramdane’s business partner and co-shareholder in the Appellant, Mr Bhardwaj, nor from the Appellant’s agent, Mr Nagji, nor from Bluestar, from which company the Appellant bought the phones in question, nor from Sunico A/S, the Danish company to which the Appellant sold the phones.

*The deal chains*

48. Mr Jones referred us first to the deal chains, which we have found to be connected to the fraudulent evasion of VAT. He said that there were two deals – one for the Nokia 8800 phones and one for the Nokia 9300i phones – that showed two perfect carousels with the money flowing in a circle through numerous FCIB bank accounts (and Jyske bank in the case of Sunico A/S) within the course of two days. He argued that it was inherently implausible that both transactions could have occurred by chance. Mr Jones said that in order for MTIC fraud to be carried out successfully, the transactions had to be directed. The fraud cannot operate successfully unless the orchestrators of the fraud know that the funds will pass through the hands of each of the nominated European exporter, UK buffer traders, UK broker (here the Appellant)

and European importer. He argued that there was no reasonable explanation as to how the Appellant happened to purchase from exactly the right supplier and sell to exactly the right customer the precisely correct number of phones on each separate occasion, thereby ensuring that the orchestrators of the fraud received the money injected at the start of each carousel.

49. By “carousel” here, Mr Jones was not, as we understand it, describing a typical carousel fraud of the nature we have described above in relation to the scanning of the IMEI numbers, where goods are exported from the UK as part of a scheme for fraudulent evasion of VAT, and are then re-imported so that the fraudulent process can begin again. He was merely referring to the circular nature of the money chain which, we have found, shows that the transactions were contrived, and we accept therefore that they must have been orchestrated.

50. We do not consider that any conclusions can be drawn from the fact that these transactions have been analysed as separate for the purpose of identifying the relevant chains. As we have set out above, in our view, certainly from the perspective of the Appellant, this was a single trade, covering both the Nokia 8800 phones and the Nokia 9300i phones. These were not, contrary to Mr Jones’ submission, separate transactions. We do, however, accept that the single deal chain was orchestrated.

#### *The Appellant’s brokerage business*

51. The burden of Mr Ramdane’s evidence on the July deals was that the entry of the Appellant into the brokerage business in mobile phones was made after extensive study and hard work in related fields, leading to an acceptance into the market place. We found his evidence in this regard unconvincing. He referred extensively to the research that had been carried out prior to trading, but was unable to recall, or provide to the Tribunal, any significant detail of this. Of the tens, or hundreds, of potential suppliers said to have been researched in the period of about a month prior to these transactions, Mr Ramdane could not recall a single name. He told us that he might have fax logs to evidence the contacts made, but these were apparently archived and we did not receive any in evidence. His reason for lack of detail in this period was that he had been interested in watching the football World Cup. We formed the view that Mr Ramdane was an opportunist who relied on others to provide the opportunities to trade, whether this was Mr Nagji, or New Order, or some other person; he told us that he had received advice from others but could not tell us from whom.

52. Our conclusion that the Appellant carried out less than extensive research was reinforced by Mr Ramdane’s own evidence in cross-examination. He was asked by Mr Jones how many suppliers and customers he spoke to before he arrived at Bluestar as the supplier. His answer was: “They were the first.” Furthermore, in relation to the trade with Sunico A/S he said: “I believe Sunico was my first port of call as well.” Mr Ramdane’s explanation for the fact that the Appellant was able to deal with Bluestar and Sunico was that this was “a lot of luck”. We do not accept this evidence. Also in cross-examination Mr Ramdane was asked about certain transactions carried out by New Order Exports Limited, the company in which the Appellant had

previously invested in return for a share of its profits from mobile phone trading. He was asked if there was any coincidence in the fact that New Order had bought from the same supplier – Bluestar – and sold to the same customer – Sunico A/S as the Appellant did shortly afterwards. His answer was that he was not privy to New Order’s records. He claimed that he did not carry out any checks in relation to the Appellant’s substantial financial investment in New Order except to verify its existence on the Companies Register, and that he did not look at New Order’s trading records. He said that he did not obtain any information about Bluestar and Sunico from New Order, saying: “No, it was through my agent”, and confirming that this was Mr Nagji. We find that the Appellant did not make contact with Bluestar or Sunico A/S through its own research or marketing activity. It was directed towards those traders by Mr Nagji.

*The nature of the July 2006 deals*

53. Mr Jones submitted that the Appellant was not involved in the genuine grey market and that it knew or should have known that it was not involved in genuine commercial trading. We accepted Mr Fletcher’s evidence that the trades carried out are unlikely to have been for the purpose of profitable grey market trading. Mr Andrews argued that the business the Appellant was in was of pure broking which had different characteristics to those referred to by Mr Fletcher. Thus it was to be expected that deals would be back-to-back and that stock would not be held. We accept that broking is different from wholesale and that neither the mere fact that trades are back to back or stock is not physically held are of themselves indicative of fraud, but the trade must nevertheless be explicable in commercial terms. Mr Jones argued that Mr Ramdane’s evidence showed that he was not concerned with the commercial rationale for the Appellant’s business activity. We agree. Mr Ramdane referred to the profit motive, and to supply and demand as the reasons for the trade. Supply and demand is of course a basic principle of economics, but we consider that a reasonable businessman would seek a deeper understanding of the economics of the business, and would be expected to appreciate that, in the circumstances of these transactions, the market itself would not produce the profit. Mr Ramdane did demonstrate an awareness that one of the roles of the exporter in these deals, indeed probably the principal role, was the financing of the VAT element of the price paid to the UK supplier. There is a VAT cash flow delay between the exporter being required to pay its supplier the VAT-inclusive price, having received only the VAT-exclusive price from its EU customer. He put this forward as a reason why it had been possible for the Appellant to have dealt with both Bluestar and Sunico A/S, despite those companies already having had their own business dealings.

54. We do not accept Mr Ramdane’s evidence that the price agreed with Sunico A/S was a negotiated price. For both of the consignments of mobile phones the mark up was just short of 6%. Of itself it seems to us to be an unlikely coincidence that the Appellant had managed to obtain prices with Bluestar for each type of phone that enabled a uniform mark up to be achieved on its own sale. The only discernable added value provided by the Appellant in the transaction is the financing of the VAT cash flow. But that is not something that adds value as far as an EU customer is concerned, and not therefore something that an EU customer would expect to pay for

15 55. Mr Jones argued that there were other clear indicators that the Appellant was not  
involved in genuine commercial trading which would have alerted the reasonable,  
honest and competent trader to the fact that the transactions were connected with  
fraud. He pointed to the fact that all the phones in the export transactions had two-pin  
charger plugs. Mobile phones are not manufactured in the UK, and the UK does not  
have a two-pin plug system. This should have alerted the Appellant to the likelihood  
20 that the phones had been imported into the UK, and were being exported. There  
would be no commercial reason why this would be done. We accept this is another  
factor that the Appellant failed to take account of, but ought to have done.

25 56. Mr Fletcher's evidence was that the longer the deal chain the greater the risk of  
disintermediation, and the less likely that this could be part of profitable grey market  
trading. Mr Ramdanee claimed that he did not know at the relevant time that there  
were at least five participants in the chain. Apart from the Appellant itself, he knew  
of Bluestar and Sunico A/S, but he ought also to have been aware that Bluestar would  
have acquired the phones from another trader, which could have been an authorised  
distributor, and that Sunico A/S would on-sell the phones as it was not itself a retail  
customer. Mr Jones argued that the basic premise which underlies the Appellant's  
30 trading activities is that two European companies dealing in the same market as the  
Appellant, using the same websites and notice boards as the Appellant, one looking to  
buy and one looking to sell a particular quantity of a particular mobile phone on a  
given day, are unable to find each other and the seller therefore has to export to the  
UK (with all the export costs that entails), whereby the goods pass through a number  
35 of different traders before being re-exported to Europe by the Appellant. We agree  
that this is a factor that should have been considered by the Appellant. It ought to  
have led to the conclusion that the trade was inherently implausible as a genuine  
commercial trade.

40 57. Mr Jones argued that the Appellant was trading a substantial volume of Nokia  
phones, which represented an obviously unrealistic market share of the total volume  
of phones available from authorised distributors. He submitted that, as someone who  
claimed to have undertaken considerable research into the mobile phone market, Mr  
Ramdanee should have known, at least in approximate terms, the size of the market in  
which the Appellant was dealing. He said the fact that a company such as the  
45 Appellant was able to command such astonishing market share in such a short space

of time is an indicator of fraud that would have been apparent to any honest and careful trader. We do not accept Mr Jones' argument in this respect. Mr Fletcher's evidence was that the Appellant's trades amounted to a sizeable share of the market. We were referred to calculations of the market share for the two mobile phones in question. In the case of the Nokia 8800, the Appellant's trade involved 1,450 units and the total market in 07/06 identified from Mr Fletcher's evidence was 44,435. Mr Fletcher's evidence was that 36% of this market would be satisfied by phones that were neither sold through the mobile phone network's direct sales channels nor through the large specialist multiples such as Carphone Warehouse. The grey market would itself be only a proportion of this 36% share because the white market would meet the larger proportion of the wholesale demand for that sales channel. Taking these figures, and accepting that the grey market would itself be a smaller percentage than 36% of the total market, it was said that the Appellant's trade would represent 3.26% of the total market and 9.06% of the available market, only a part of which would be satisfied through the grey market itself. The corresponding percentages for the Nokia 9300i were 6.86% of the total market and 19.06% of the available market.

58. In calculating market share Mr Fletcher referred to market data obtained from GfK Marketing Services Ltd, part of the GfK group of market research companies. GfK are recognised as a leading market research provider. Data is collected from over 26 countries worldwide by use of links to electronic point of sales systems located in retail outlets. The outlets covered are solely retail; the wholesale market is not tracked in this research, and so there is no figure for the number of phones manufactured or released for sale against which to compare the Appellant's trades. Mr Fletcher was challenged in cross-examination by Mr Andrews as to the value of the comparison that had been made. His response was that it added value to the discussion because the grey market exists, as does the rest of the wholesale market, to supply the retail market. A comparison of the retail and wholesale markets in this way was relevant because it allows a view to be taken as to the proportion of the phones that have been traded in the grey market as against those that are actually being sold.

59. Mr Fletcher accepted, however, that the GfK numbers were not entirely comprehensive. Only 92% of retail sales of its "tracked universe" were included, and the tracked universe excluded corporate (or business to business) sales and a number of other outlets, such as offshore islands, petrol stations, newsagents, black market, exports and toy shops. Business to business (or B2B) sales were explained by Mr Fletcher as the sales of phones by mobile network operators to large corporate customers who would provide phones to their employees. A corporate buyer would not source phones from the grey market, and so this exclusion did not affect the market share calculations.

60. In our view the exclusions from the "tracked universe" against which these comparisons have been made are such that the precise percentages extrapolated are not themselves of material evidential value. It is not possible, in our view, on the basis of this evidence as presented, to conclude to the standard required that the Appellant's trades in the mobile phones in question did represent such a sizeable proportion of the overall market as to be a factor in determining whether the

Appellant either knew, or should have known, of the fraud. We also note that the GfK data is not readily available to an ordinary trader. It may be available at a cost, but we do not consider that a reasonable trader would be expected to have access to this information. For these reasons we do not place any reliance on the market share information.

*The transaction risks*

61. Mr Jones' next point was that the legal risks involved in the transactions undertaken by the Appellant were either not properly analysed or were ignored, in particular with respect to being sued for the contract price in the event of the deal chains collapsing and, in such a scenario, having to pay the cost of retrieving the goods which had been forwarded abroad. This, it was argued, was indicative of non-commercial trading. Mr Ramdanee's evidence showed that he was not really concerned with the contractual position. His evidence was that he expected that if there had been any problems those problems could have been resolved verbally, without recourse to any legal contract, and including the ability to back out of the deal.

62. We were shown the terms and conditions of purchase that covered the purchase order made by the Appellant in relation to its purchase from Bluestar. These were not bespoke or even drafted with this particular type of transaction in mind; Mr Ramdanee said in evidence that the terms and conditions had been downloaded from the internet. Those conditions include the following as regards cancellation of the contract:

“7. In the event of force majeure, strike, riot, civil commotion, war, epidemic, quota, embargo, interruption or congestion of transportation, inability to obtain shipping space, or other causes or circumstances beyond the control of the Purchaser, which interfere with the completion of this contract, the Purchaser on giving notice to the Vendor shall be entitled to cancel this contract without paying to the Vendor any damages or compensations. The Purchaser reserves the right to postpone the shipment.”

The Appellant also reserved the right under these conditions to withhold payment on any delivery in settlement of outstanding claims and on any shipments made that were not to the appellant's satisfaction.

63. There was nothing in these purchase conditions that would have enabled the Appellant simply to unwind its transaction with Bluestar if its own customer, Sunico A/S had defaulted. Nor did the conditions make reference to the passing of legal title, a matter which, according to Mr Ramdanee's evidence, was crucial in determining that the goods would only be released upon payment. The Appellant remained liable to pay Bluestar, and could not simply unwind the contract or return the goods (assuming it could have recovered them once shipped to Denmark). This was a risk for the Appellant which Mr Ramdanee refused to acknowledge in evidence. No written contractual protection was put in place in respect of the sale to Sunico A/S. The Appellant took no steps to identify its risks despite Mr Ramdanee having

obtained informal litigation advice from his partner, a solicitor. Mr Ramdane's assertion that there was no risk indicates to us that the Appellant was likely to have been aware that this was not a normal business transaction, that the risks had in practice been eliminated and that consequently no contractual protection was required. We did not accept as an adequate explanation that all the deals were based on trust. That serves merely to indicate further that the deals were not in the ordinary course of commercial trading.

64. Mr Jones submitted that a key aspect of any genuine, high value transaction that a business undertakes is to ensure that the product is properly identified, so that the product matches the customer's order and to avoid any potential disputes, after the event, as to the subject matter of the contract. He argued that this was clearly lacking in the Appellant's business, and that this provided a strong indication that the specification of the products simply did not matter either to the Appellant or its customer. From the evidence before us Mr Jones identified the following points in support of his argument:

(1) The Appellant failed to identify the phones properly on both purchase and sale, leaving it open to the likelihood of disputes. The Appellant did no more than list the make, model, quantity and price, and the generic term "Central European specification". This information was insufficient to establish the true specification of the phones, their true value, and whether the phones would meet a customer's specifications. The generic product description on the purchase orders and invoices left traders at risk of dealing in handsets which were not adequately enough specified to meet customer requirements. Mr Fletcher's evidence was that such descriptions did not include a range of matters which a purchaser would expect.

(2) The purchase orders from Sunico A/S in no way matched the phones that are said to have been inspected on behalf of the Appellant by A1 Inspections. Mr Jones produced for the Tribunal a summary of the specifications requested by Sunico A/S as compared against the phones despatched. We have considered the evidence in this respect and it is apparent from this comparison that there were significant differences, particularly in relation to software language and warranty that in a normal commercial transaction would have given rise to issues, for example as to price. Mr Ramdane ignored the fact that the phones did not fully come up to specification as being the customer's problem; the customer could inspect the goods and choose to accept them. Mr Jones noted that this could have led to the wholesale rejection of the consignment with the attendant transport costs of returning the goods from Denmark and finding a new customer in a rapidly changing market. As we have seen, there were no contract terms to protect the Appellant's position in such an event.

(3) Inspection of the goods sold by the Appellant only took place after the goods had been delivered "ship on hold". Mr Jones argued that it was remarkable that, given the non-correlation of the phones with Sunico

A/S's specification, none of the phones were queried and none were returned. Nor was the price questioned or renegotiated by Sunico A/S. Mr Ramdaneé did say in evidence that Sunico A/S had told him that three phones were missing, a fact that A1 Inspections had not noted. Mr  
5 Ramdaneé initially said in evidence that he thought he might have paid Sunico A/S a refund, but there was no evidence of this and he later claimed that he gave them a discount. But there was no evidence of a discount either.

65. Mr Ramdaneé's evidence was that there was nothing in the inspection report  
10 carried out by A1 Inspections that caused him any real concern. He said that his interest was in the IMEI numbers, and whether they were repeated (which, as we have earlier described, could indicate that the phones were part of a "carousel fraud"). As regards the IMEI numbers we accept that neither the Appellant nor A1 Inspections had access to the NEMESIS database, and that a check by A1 Inspections could only  
15 reveal duplicates in their own records. However, aside from the question of the IMEI numbers, it was evident from the inspection report that in a number of material respects the actual phones did not meet the specification set out by Sunico A/S in its purchase order. Mr Ramdaneé said that in the business world there would be some room for manoeuvre on this, and it would come down to negotiations. His view was  
20 that it was for the customer to inspect the goods and if not satisfied to return them. But this fails to take account of the fact that, unless there had been some breach by Bluestar, the Appellant would have remained liable to pay the price to Bluestar and would not, as we have described, have any right simply to return the goods to Bluestar. Mr Ramdaneé was asked by Mr Jones why he did not seek to obtain  
25 confirmation from Bluestar that the phones would match those specified by Sunico A/S. His response was to the effect that this was not possible given the pressure of time to do the deal and that in any event even if the goods did not accord with the purchase order they may in practice be accepted. This to our minds is another example of Mr Ramdaneé not being concerned as to the contractual position or any  
30 form of risk. If, as Mr Ramdaneé contended, this had been a fully-negotiated sale and purchase it is quite evident that a purchaser would agree a particular price on the assumption that the goods would meet a particular specification. In such a case it is not credible, and we do not accept, that any reasonable businessman would rely on such a purchaser not enforcing the actual contract and simply saying, in Mr  
35 Ramdaneé's words: "OK, we can use those goods."

66. It follows from this that we agree with the submission of Mr Jones in this respect that these factors, taken together, should have alerted the Appellant to the fact that the transactions in which it was participating were connected to fraud. An honest and careful trader would in our view have reached that conclusion.

40 *Reasonable precautions?*

67. We now move to consider if the Appellant took all reasonable precautions to avoid entering into transactions that were connected to fraud. Mr Ramdaneé, and consequently the Appellant, was clearly aware of the prevalence of MTIC fraud in the mobile phone industry at the time the deals in question were undertaken. In his

evidence he accepted that he had knowledge of MTIC fraud generally, through meetings with HMRC officers and VAT Notice 726 over the period. He knew therefore of the importance of due diligence in relation to the Appellant's transactions. His witness statement says that the Appellant performed all the due diligence checks outlined in all the relevant notices sent by HMRC.

68. In his evidence Mr Ramdane claimed that his understanding was that he only needed to be satisfied that the Appellant's own supplier was the missing trader. We do not accept this. Mr Ramdane is an intelligent man who is fully capable of understanding the information that had been given to him, both in meetings with HMRC officials and in VAT Notice 726. Notice 726 itself refers to the fact that it concerns VAT unpaid not only on the direct supply to the trader, but on any previous or subsequent supply, and explains that a trader is not necessarily expected to know its supplier's supplier or the full range of selling prices through its own supply chain. This clearly indicates that the supply chain may be longer than the individual purchase and sale carried out by the trader, and Notice 726 goes on to state clearly, in this connection: "... we would expect you to make a judgment on the integrity of your supply chain." Even if we could conclude that Mr Ramdane did not appreciate that he was expected to consider the integrity of the supply chain beyond his own, we find that this would not have been reasonable, and a failure to consider the wider picture would mean that the Appellant did not take reasonable precautions.

69. As regards the Appellant's due diligence in relation to its own supplier, Bluestar, the Appellant did not inspect the premises of that company. Instead, Mr Ramdane and one other, whom we infer was Mr Bhardwaj, travelled to a service station on the M1 motorway to meet the directors of Bluestar. No documents were inspected at that meeting. A Company History Questionnaire was completed by Bluestar on 10 July 2006, to which it was said that references were attached from S M Accounting Services and Dass, solicitors. However, no references were produced in evidence. The Appellant undertook a credit check on Bluestar on 11 July 2006, the date of the purchases of the mobile phones from that supplier, undertaken by a company called Checksure. The "checkSCORE" on the report was recorded as "L – Accounts which should have been filed are late., and the report also records that "the last filed accounts at Companies House are those to 31/01/04", some 2½ years prior to July 2006. The credit check report was timed at 17.27. Mr Ramdane's evidence was that he telephoned Bluestar's accountants on 11 July 2006 who clarified that the late filing had been their error and that the accounts would be filed shortly. But he was unable to provide any further detail. If Mr Ramdane did telephone the accountant then it appears to us that this was probably already too late. The credit report shows a balance sheet with a total asset figure of £4,000 at 31 January 2004, with a total liability figure of £3,000, leaving net current assets of £1,000. Mr Ramdane said that he was not concerned with this, relying on the fact of earlier deals and the business relationship that had been built up. However, we do not consider that the Appellant's checks in this respect, and the fact that contra-indications were present but not fully followed up, were reasonable.

70. The verification check of Bluestar's VAT registration with the HMRC office at Redhill was also done after the deal, on 12 July 2006. Mr Ramdane's explanation of

this was that it was difficult to contact Redhill, and he suggested that HMRC were making verification difficult for traders. He was not concerned that no verification had been received at the time of the deal. He saw the transaction purely in terms of risk and reward. The Appellant had traded with Bluestar on a previous occasion, and  
5 Mr Ramdanee's view was that as payment for the phones had not as at 12 July 2006 been released it would have remained possible for the deal to have been unwound. As we have indicated, we consider that Mr Ramdanee is wrong on this point, and in our view a reasonable businessman would have known that.

10 71. Mr Jones referred us to certain documents relating to due diligence on the directors of Bluestar provided by the Appellant in the course of this appeal. These were a British gas bill, a BT bill and photocopies of passports of the directors, Nahim Tasin and Zahid Mahmood Karim. The British Gas bill was dated 10 August 2006 and the BT bill had an issue date of 9 October 2006. Both documents have a fax header at the foot of the page which purports to confirm that the documents were sent  
15 by Bluestar on 13 July 2006 at 12:02 and 12:03 respectively. It can be inferred from this that all these documents were not obtained as part of the Appellant's due diligence. Mr Ramdanee was unable to give any explanation as to the apparent discrepancy between the dates on the bills and the date on the fax. In any event the fax date of 13 July 2006 was after the deal with Bluestar had been struck.

20 72. Mr Jones argued that there were similar question marks over the due diligence undertaken by the Appellant on Sunico A/S. A credit check was undertaken on Sunico A/S on 26 April 2006 by D&B Inc. Whilst the report indicates Sunico's rating as "AA – good credit worthiness" and its history as being "well-established", Mr Jones submitted that the pertinent question for the Appellant, as Sunico's supplier,  
25 would be its ability to pay. The figures in the finance section of the report are recorded in Danish krone (DKK). It appears from Mr Ramdanee's evidence that there was no attempt on the part of the Appellant to translate the DKK figure into sterling. If it had done, this would have revealed that Sunico A/S had a credit limit of £2,874.96, a turnover of £623,350 and a net income of £4,468. Given that the two  
30 deals were for an aggregate price of £823,780.75, Mr Jones submitted, having regard to the risks attaching to non-payment for the goods, that it was not reasonable for the Appellant not to have made further enquiries as to the financial position of Sunico A/S. We agree. We consider that a reasonable businessman would have made such further enquiries and by not doing so the Appellant failed to take reasonable  
35 precautions.

73. The lack of any rigorous due diligence in respect of Bluestar or Sunico A/S is to our minds all the more unreasonable given the fact that the Appellant knew, from its earlier dealings, that Bluestar had requested a third party payment to Sunico A/S, and that the Appellant was aware, as Mr Ramdanee confirmed in evidence, that third party  
40 payments were considered by HMRC to be an indicator of fraud.

#### *The FCIB account*

74. The Appellant had an account with the First Curacao International Bank ("FCIB") in the Netherlands Antilles, as did the Appellant's supplier, Bluestar. Evidence of Mr

Mayungbe suggested that the use of FCIB accounts could be regarded as helping the perpetrators of the fraud to conceal information from the UK authorities and to keep the proceeds out of the authorities' hands. It was suggested that the location of FCIB in the Netherlands Antilles should have given rise to doubt in the case of a legitimate trader who "would have found it unusual if they were asked to pay in to an account in a bank located in an obscure place". Mr Andrews argued that the mere use of an FCIB account was not indicative of fraud. We agree, and we disagree with the suggestions made by Mr Mayungbe. However, we do regard the circumstances of the opening by the Appellant of its FCIB account as relevant.

75. The evidence of Mr Ramdane with respect to the opening of the FCIB account was less than satisfactory or convincing. Mr Ramdane recalled that Mr Nagji, the agent, had advised the use of FCIB as a bank, and said that other traders had also recommended it. He was asked if New Order was one of those traders, and he said that this was possible, but he could not recall. He was also unsure whether he had completed the application form, or particular parts of it, or whether Mr Bhardwaj had participated in that exercise and to what extent. From Mr Ramdane's evidence it appears that the formalities were completed at a meeting with Third Dimension Limited, a company that he and Mr Bhardwaj met for the first time on that occasion. Despite the fact that this was the first meeting, Third Dimension Limited supplied the Appellant, for the purpose of its application to open the FCIB account, with a reference from a Mr Anthony Elliot-Square, a director, that stated:

"I have known him [sic] in the capacity of him being known within the trading industry and current user of our www.ipt.cc, www.icb.cc and www.igt.cc web sites.

I enclose all the Due Diligence material, plus the Enhanced Due diligence material required for this industry."

Mr Ramdane could not remember sending or giving any documents to Third Dimension Limited, though he said that the Appellant must have done so.

76. There were two other references given to support the Appellant's application. One was from New Order, dated 25 November 2005. It said:

"This is confirmation that Next Generation Computing Limited is a company known to us, we have successfully traded with them on many occasions."

Although Mr Ramdane gave a somewhat confused account of his dealing with New Order, and the Appellant's transactions in digital e-cards with New Order took place later, in 2006, we are satisfied that, having regard to the investments made by the Appellant with New Order, for which the Appellant received commissions that we have found were shares of net profit, there was nothing inherently wrong with the reference given by New Order.

77. The same cannot be said for the other additional reference from Puwar Ltd. According to his evidence Mr Ramdaneer himself had had no dealings with Puwar, but he said that his partner, Mr Bhardwaj had. Puwar's reference said:

5                                "We have worked with the Directors of the organisation below [the Appellant] for five years, and consider them to be trustworthy and honourable individuals who are well respected within the general business community."

10 Puwar Ltd was incorporated on 9 May 2002, and so it would not have been possible for it to have given this confirmation. The Puwar reference was therefore, as Mr Ramdaneer accepted in cross-examination, both inaccurate and misleading.

15 78. We find that the circumstances of the opening of the Appellant's FCIB account were unusual and in our view not consistent with ordinary commercial dealings. The Appellant was aware of MTIC fraud at this time, and we consider that these circumstances were such as to necessarily have given rise to questions as to the nature of the trades that would be conducted through the account, and any advice and recommendations that the Appellant might receive in this connection. As part of the context in which the transactions were undertaken, the fact that the FCIB account had been opened on the basis of two false references should have given the Appellant a heightened sense of awareness that any indications that the transactions themselves had features that suggested they were outside the expected ordinary course of business ought to be regarded with the utmost caution. In fact, as we have found, the Appellant ignored those signals, and did not undertake reasonable precautions in respect of the trades in question.

### Conclusions

25 79. From all the evidence before us we have reached the following conclusions:

- (1) There was a tax loss.
- (2) That tax loss resulted from the fraudulent evasion of VAT.
- (3) The Appellant's transactions were connected with that fraudulent evasion.
- 30 (4) The Appellant should have known that its purchases were connected with the fraudulent evasion of VAT.

35 80. As regards our final conclusion, we have considered whether we are satisfied that HMRC have discharged the burden of proof that the Appellant knew that its purchases were connected with the fraudulent evasion of VAT. There is some evidence, along with certain of our own findings, that indicates that this is indeed the case. In particular, we did not accept Mr Ramdaneer's evidence as regards his identifying Bluestar as a supplier and Sunico A/S as a customer, nor his evidence as to negotiation of the price. On the contrary, we found that Mr Ramdaneer was presented with the deal by another party or parties. Mr Ramdaneer paid scant attention to the contractual position and due diligence and ignored clear indications that the trades were not ordinary transactions in the commercial market for mobile phones. His

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attitude to risk also suggests that he was confident that in practice there would be no risk, and this could indicate that he was aware of the contrived nature of the transaction.

5 81. It appeared to us that Mr Ramdane, and through him the Appellant, was driven  
by profit, and the opportunity presented to him to do a deal, to the extent that it  
blinded him to the true nature of the transactions the Appellant was entering into, and  
the numerous indicators that this was not a commercial deal in the real market, but a  
contrived transaction associated with VAT fraud. However, although it is clear to us  
10 that the chains of transactions must have been contrived, this of itself does not lead to  
the conclusion that every participant in the chain must have known that the  
transactions were connected with fraud. That depends on the circumstances of each  
such participant. In the case of the Appellant we are not satisfied that HMRC have  
discharged the burden of proof that, on the balance of probability, the Appellant did  
15 know that its transactions were connected to the fraud. On the other hand, we are  
fully satisfied that the Appellant should have known that its purchases were connected  
to the fraud.

20 82. The recent decision of Briggs J in *Megtian Limited (in administration) v Revenue  
and Customs Commissioners* [2010] EWHC 18 (Ch) in the High Court describes the  
distinction between a person who knows that a transaction is connected with  
fraudulent tax evasion and one who merely ought to have known of that connection in  
terms of the different states of mind of those persons. The judgment in *Megtian* was  
issued after the hearing of this appeal, and consequently we heard no argument on it.  
We do not base our decision on anything in that judgment. We do, however, consider  
that it encapsulates the dividing line between the two concepts. Mr Justice Briggs  
25 said (at [41]):

30 “It is important to bear in mind, although the phrase “knew or ought to  
have known” slips easily off the tongue, that when applied for the  
purpose of identifying the state of mind of a person who has  
participated in a transaction which is in fact connected with a fraud, it  
encompasses two very different states of mind. A person who knows  
that a transaction in which he participates is connected with fraudulent  
tax evasion is a participant in that fraud. That person has a dishonest  
state of mind. By contrast, a person who merely ought to have known  
of the relevant connection is not dishonest, but has a state of mind  
35 broadly equivalent to negligence.”

40 83. In this appeal, having regard to all the evidence and our conclusion that Mr  
Ramdane, and therefore the Appellant, was blinded to the true nature of the  
transactions, we consider that the Appellant’s state of mind was broadly equivalent to  
negligence and that, having considered all the evidence, we are satisfied that the  
Appellant should have known that its transactions were connected to fraudulent  
evasion of VAT. We are not satisfied, on the basis of our view that it is for HMRC to  
discharge the burden of proof in this respect, that the Appellant’s mind was dishonest,  
and that it knew of that connection.

**Decision**

84. For these reasons, we dismiss this appeal.

5 The Appellant has a right to apply for permission to appeal against this decision pursuant to rule 39 of the Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules 2009. 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.

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**ROGER BERNER**

**TRIBUNAL JUDGE**  
**RELEASE DATE: 28 January 2010**

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