[2019] UKFTT 211 (TC)

TC07058

Appeal number: TC/2013/06506

VAT – MTIC – whether there was a grey market in Sony PS3s – soft bundles – whether knew or should have known deals were connected with fraud – credibility of evidence – inferences from absent witnesses – appeal dismissed

FIRST-TIER TRIBUNAL
TAX CHAMBER

EDC DIRECT LIMITED **Appellant**

- and -

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

TRIBUNAL: JUDGE ANNE REDSTON
MRS HELEN MYERSCOUGH

Sitting in public at the Rolls Buildings, Fetter Lane, London from 1 October 2018 to 12 October 2018

Mr William Frain-Bell of Counsel, instructed by the Khan Partnership LLP for the Appellant

Mr Howard Watkinson of Counsel, instructed by the General Counsel and Solicitor to HM Revenue and Customs, for the Respondents

DECISION

Introduction

1. This appeal concerns missing trader intra-community ("MTIC") fraud. The goods in question were not mobile phones, as is often the case, but electronic equipment, particularly Sony PlayStations ("PS3s").

2. HM Revenue & Customs ("HMRC") refused to allow the appellant, EDC Direct Limited ("EDC") to deduct VAT input tax of £426,145.52 incurred on the purchase of the goods, on the grounds that the purchases were connected with MTIC fraud, and EDC knew or should have known that this was the case. It was accepted by both parties that as EDC was run by Mr Chhatwal, it was his knowledge which was relevant; it was also accepted that the burden of proof was on HMRC.

3. HMRC's primary case was that Mr Chhatwal knew the disputed transactions were part of an orchestrated and contrived fraud; their secondary case was that he should have known this was the position.

4. Although Mr Frain-Bell said in his skeleton argument that EDC disputed whether certain Deals were connected to fraud, the position changed during the hearing, so that EDC accepted that each of the 20 Deals in issue were connected with MTIC fraud; Mr Chhatwal also accepted that each was part of an orchestrated and contrived fraud, but denied that he knew, or should have known, this was the case.

5. The Tribunal found that Mr Chhatwal knew that the purchases were connected with MTIC fraud. In the alternative, we found that he should have known this was the position. EDC's appeal is dismissed and HMRC's decision confirmed.

Terminology

6. We have used the accepted terminology in MTIC appeals, namely that:

   (1) a party who exports or "dispatches" goods to a foreign purchaser is known as the "broker";

   (2) a party who buys from the importer of the goods is known as "the acquirer"; and

   (3) intermediate purchasers between the acquirer and the broker are known as "buffers".

7. When we use the term "Deal" we mean the part of the deal chain with which EDC was involved, from supplier to EDC to customer, and not the whole of the chain.

8. At various points we refer to sales to and from the European mainland, which for simplicity we have referred to as "the EU".

9. PS3s are manufactured by Sony, and could be sold either as single stand-alone consoles, or with one or more games/accessories, when it was known as a "bundle". If the PS3 was packaged with the game/accessory in the same box, it was known as a "hard bundle". If the PS3 and the game/accessory were packaged in separate boxes, it

was a "soft bundle". Most of the PS3s at issue in this appeal were said to have been derived from soft bundles which had been split, with the PS3s and the games /accessories being sold separately (a "split soft bundle").

The Deals

10. The Deals were labelled from A to T. HMRC refused to repay all the input VAT for the 20 Deals, other than for part of Deals H, Q and S, where the goods were sourced from more than one company (a split supply chain). HMRC were unable to trace part of each of these split Deals to a fraudulent tax loss within the relevant time limits, and so repaid the related VAT to EDC. HMRC subsequently traced these purchases back to a missing trader.

11. In one of these split chains, the missing trader was BAK Enterprises GmbH ("BAK"); in the other two, it was Winnington Networks Ltd ("WNL"). In addition to those two split Deals, HMRC traced a further 18 of EDC's transactions between February and July 2011 to WNL, but this linkage was also identified too late for HMRC to refuse to repay the related VAT to EDC.

12. HMRC's position is that EDC's participation in these other WNL transactions was a relevant factor when considering whether Mr Chhatwal knew or should have known that the Deals which are under appeal were connected to fraud. At the beginning of the hearing, Mr Frain-Bell reserved EDC's position on this issue, and said he would respond either during the hearing, or in closing submissions, but did not do so. We accept that these other transactions provide relevant evidence.

13. Of the 20 Deals, 18 can be traced directly to fraudulent tax loss occasioned by a defaulting trader ("a basic chain"). In 13 of these Deals, the goods were passed through one or more buffers until they reached EDC, which acted as the broker. In the other five 18 Deals, EDC acted as a buffer, passing the goods to another UK company. The remaining two Deals (Deals B and C) involved contra-trading; the contra-trader was Intekx Ltd. The 18 non-denied WNL transactions were also part of contra-trading schemes. In *CCA Distribution v HMRC* [2015] UKUT 513 (TCC) ("*CCA*") at [4] the UT explained contra-trading as follows:

> "a 'contra-trader'…is a term coined by HMRC to describe a fraudulent trader which (a) acquires goods from a UK trader as a participant in a chain of transactions which includes a defaulting trader (known as the 'dirty chain') and exports them to an EU trader claiming a credit for input tax ('the dirty input tax') on the purchase and (b) in a chain which includes no defaulter (known as the 'clean chain'), imports goods from an EU trader and sells them to another UK trader and then offsets the dirty input tax against the clean output tax he is liable to pay HMRC in respect of the sale to the second UK trader. The purpose of this is to attempt to turn the dirty input tax into clean input tax in the hands of the second UK trader (who himself exports the goods to an EU trader) and to distance the second UK trader from the default in the dirty chain..."

PART 1: THE EVIDENCE

14. This part of the decision summarises the evidence supplied, explains whether we found the witnesses credible and sets out the principles which apply when making inferences about the lack of evidence.

Documentary evidence

15. We were provided with bundles of documents put together by HMRC. These included:

(1) correspondence between the parties, and between the parties and the Tribunal;

(2) various invoices, purchase orders, delivery and collection documents and shipping documentation called CMRs, which stands for "Convention Relative au Contrat de Transport International de Marchandises par la Route";

(3) extracts from Mr Chhatwal's "deal book", which we discuss in more detail at §470ff;

(4) a schedule of EDC's sales for each VAT quarter, from Q3 2007 through to Q4 2012, showing its UK sales, export sales and total sales;

(5) a schedule for the same VAT quarters setting out the percentage of goods purchased from suppliers other than the manufacturer or authorised distributor of those goods (the "grey market");

(6) a schedule giving the sterling/euro foreign exchange ("FX") rate for each VAT quarter for 2007 through to 2012 inclusive, and the same information shown graphically.

16. HMRC also provided the following during the hearing:

(1) a "Deal Overview" schedule which analysed the deal chains for each of the disputed transactions, and included other information about pricing and profits; and

(2) a more detailed schedule which set out the deal chain for each of the transactions, giving the price paid by each person in the chain, the date of each invoice, a description of the goods and (in relation to PS3s) the trade price at which it could be purchased from CentreSoft Ltd ("CentreSoft"), the authorised distributor for Sony products in the UK.

17. No objection was made by Mr Frain-Bell to the handing up of these schedules, or to the various amendments made to them during the hearing; he also referred to the schedules in the course of his submissions. We have therefore taken it that EDC accepted that the figures on the final version of these schedules were correct.

18. On the final day of the hearing, Mr Watkinson handed up copies of correspondence between HMRC and the Khan Partnership LLP, EDC's legal representative, relating to requests for disclosure. These had not been included in the Bundles, but the parties agreed that they had previously been copied to the Tribunals Service.

Witness evidence

19. The Tribunal was provided with witness statements from the HMRC Officers who had investigated the missing traders in the deal chains. By the time of the hearing, EDC had accepted that all the disputed Deals originated with a missing trader, so the evidence of these witnesses was no longer in dispute. The statement of Mr Officer Mark Hughes, the HMRC Officer who visited EDC's offices, was also accepted without challenge.

Approach to witness credibility

20. In *Gestmin v Credit Suisse* [2013] EWHC 3560 (Comm) at [22], Leggat J (as he then was) said:

> "the best approach for a judge to adopt in the trial of a commercial case is, in my view, to place little if any reliance at all on witnesses' recollections of what was said in meetings and conversations, and to base factual findings on inferences drawn from the documentary evidence and known or probable facts."

21. The courts have also referred in number of cases, including *Bailey v Graham* [2012] EWCA Civ 1469, to an article entitled "The Judge as Juror: The Judicial Determination of Factual Issues" in which Bingham J (as he then was) identified the following indicators of where the truth lies: the consistency of the witness's evidence with what is agreed to have occurred, or what is clearly shown by other evidence to have occurred; the internal consistency of his evidence; and the consistency of his evidence with what he has said or deposed on other occasions.

22. Some of the factors relevant to the evaluation of evidence were identified by Lewison J (as he then was) in *Painter v Hutchinson* [2007] EWHC 758 (Ch) when he explained at [3] why he found Mr Hutchison to be an unreliable witness:

> "He was evasive and argumentative. He would launch into tangential speeches when confronted by questions that he could not answer consistently with his case. He attempted to place the most strained readings on the plain words of his pleaded case and his principal witness statement…At times he gave self-contradictory answers within the space of a few minutes of his evidence. New allegations emerged in the course of his cross-examination which had not previously formed part of his pleaded case or his written evidence. It was impossible not to conclude that they had been made up on the spot…[His] case had shifted in important respects either in response to evidence given…or in response to documents that had emerged on disclosure. It changed again and again in the witness box itself. His disclosure of documents has been lamentable and highly selective."

Witnesses called by HMRC

23. Mr Piers Ginn was the HMRC Officer who made the decision under appeal. He provided two witness statements, was cross-examined by Mr Frain-Bell and answered questions from the Tribunal.

24. Mr Damian O'Sullivan, CentreSoft's Finance Director ("FD") since 2009, also provided two witness statements. However, HMRC were informed shortly before the hearing that Mr O'Sullivan was seriously ill, and was not expected to be well enough to return to work in time to give witness evidence at the hearing. The acting FD in Mr O'Sullivan's absence was Mr Michael Sherry, who had been CentreSoft's FD before Mr O'Sullivan's appointment. On 24 September 2018, HMRC made an uncontested application for Mr Sherry's evidence to be accepted, and the Tribunal allowed that application. Mr Sherry largely adopted Mr O'Sullivan's witness statements; he attended the hearing; was cross-examined by Mr Frain-Bell and answered questions from the Tribunal. In this decision, we refer to the evidence in Mr O'Sullivan's witness statements which was adopted by Mr Sherry, as Mr Sherry's evidence.

25. Mr Fergal Gara, the Managing Director of Sony Computer Entertainment UK Limited ("Sony UK") between 2011 and September 2015, provided two witness statements, was cross-examined by Mr Frain-Bell and answered questions from the Tribunal.

26. We found Mr Ginn, Mr Sherry and Mr Gara to be entirely honest and credible witnesses, and Mr Frain-Bell did not suggest the contrary.

Mr Chhatwal's evidence

27. Mr Chhatwal provided two witness statements, was cross-examined by Mr Watkinson and answered questions from the Tribunal. Mr Watkinson submitted that Mr Chhatwal's evidence on the key issues in dispute was not credible, because (a) it was unsupported by documents; (b) he was "continually evasive and won't answer basic questions"; (c) he contradicted himself and (d) he said "what he thinks is going to help him rather than what is true".

28. We agree with Mr Watkinson, and find that Mr Chhatwal was not a credible witness. Our detailed findings are in the main body of this decision, but in summary:

(1) he was evasive in answering straightforward questions, for example as to whether:

(a) he had been given HMRC's Public Notice 726, and whether he had read that Notice, see §102;

(b) he had read a letter from HMRC dated 26 April 2010, see §111-112;

(c) he had received a specific letter from Sony about soft bundles, see §179-180; and

(d) he was aware that there was a higher risk of fraud when purchasing from the grey market when compared to purchasing from the manufacturer or authorised distributor: Mr Watkinson asked him that question over twenty times, see §128;

(2) he changed his evidence without any reasonable explanation or justification. For instance:

(a) faced with the facts about the EU specification of most of the PS3s involved in the Deals, he changed his original evidence about their source, see §525ff;

(b) when asked to substantiate his statement that he would refer to the individual components of the soft bundles to ascertain whether the pricing was credible, he said he had not carried out that exercise, see §222(2);

(c) although he originally said that his deal book recorded his negotiations with suppliers, he then denied this was the case, and even changed the meaning of an acronym used in that book, see §470ff;

(3) when Mr Ginn pointed that Mr Chhatwal's evidence about the due diligence carried out on "Zippy Distribution" ("Zippy"), one of his suppliers, was clearly incorrect, Mr Chhatwal said that his witness statement contained "inexact language" and a "typographical error", which we did not accept, for the reasons explained at §256ff;

(4) despite saying he was unable to access any emails relating to negotiations because of "a technical issue with our server, which resulted in the permanent loss of data", in the course of the hearing he connected to that remote server and recovered emails he believed would support his position, see §490ff;

(5) during his oral evidence he sought to contradict the evidence of Officer Hughes, even though that Officer's witness statement had previously been accepted, see §115;

(6) Mr Chhatwal gave inconsistent evidence about whether manufacturers and authorised distributors sold to internet retailers, see §137;

(7) when in the witness box, Mr Chhatwal elaborated his evidence by adding significant new material, for example in cross-examination he provided, for the first time, evidence about the reasons for Deals A, K and P; and on re-examination he further expanded that evidence in relation to Deals A and K, see §326ff, §390ff and §418ff;

(8) his newly stated reasons for entering into Deal A were directly linked to evidence given earlier in the proceedings by Mr Sherry, see §328ff; and

(9) there were significant gaps in the documents which had been disclosed, see §459ff and §502-514.

29. Mr Chhatwal's evidence therefore shared many of the characteristics which Lewison J had identified in Mr Hutchison, see the extract from *Painter v Hutchinson* above. Mr Chhatwal too was evasive, and "would launch into tangential speeches when confronted by questions that he could not answer consistently with his case". He gave contradictory answers, and added new material which had not formed part of his pleaded case or his witness statements, much of which "had been made up on the spot". His case "shifted in important respects either in response to evidence given…or in response to documents" to which he was taken during the hearing, see for example §328ff, and his document disclosure was deficient, as was that of Mr Hutchison,

30. Where Mr Chhatwal's evidence conflicted with that of other witnesses, we have preferred the evidence of those other witnesses. Where it is unsupported by documentation, we have considered whether it is credible in the context of the available documents and our other findings of fact. That approach is, of course, also consistent with the more general advice given by Leggat J in *Gestmin*, and by Bingham J in the article cited above.

The lack of supporting witness evidence

31. Mr Chhatwal said in his witness statement that he had "a very strong personal relationship with numerous television distributors"; that EDC placed "strong emphasis" on its "relationships with suppliers and customers"; that the "trust and relationships" it had built up with suppliers "was paramount in securing better pricing" and that he had known the owner of Electrocentre Ltd ("Electro") one of his suppliers, for over twenty years before the disputed transactions. He also stated that:

> "In conducting my business, I preferred, where possible to establish long term relationships with counterparties...Trading with a select set of companies ensured that we would get to develop long term relationships arid trust with a handful of companies."

32. EDC's VAT returns were selected for extended verification in 2010 and 2011. In October 2012 and February 2013, Mr Ginn asked EDC to provide further evidence to support its VAT repayment claim and its assertions as to what had happened. On 22 February 2013, the Khan Partnership, EDC's solicitor asked for an extension of time because "EDC may wish to obtain corroborative evidence from its suppliers and customers, some of whom are based overseas".

33. Under cross-examination, Mr Chhatwal accepted that he had been aware for "over five years" of the importance of providing supporting evidence from the individuals with whom the company had carried out the disputed transactions. However, despite his statements about having long-standing relationships with his suppliers and customers, he did not ask any of them to give witness evidence. He gave the following reasons for this:

(1) it had now been five years since EDC had ceased business, and he no longer had any relationship with his suppliers or customers;

(2) he had "no reason" to remain in contact with them after his business ceased; and

(3) he had "lost confidence and no longer wanted to be involved in the business any more" as the result of this investigation.

34. We consider those reasons later in our decision, see §227ff. At this stage we find as a fact, in reliance on the correspondence between HMRC and Mr Chhatwal's solicitors, that he was fully aware, at least by February 2013, that evidence from EDC's suppliers and customers would be relevant to EDC's case. The company did not cease business until June 2013.

Adverse inferences: the law

35. Mr Watkinson asked the Tribunal to draw an adverse inference from EDC's failure to call any witnesses other than Mr Chhatwal. He cited the relevant authorities, namely *Prest v Prest* [2013] 2 AC 415 at [44], and *Wisniewski v Central Manchester Health Authority* [1998] PIQR P324 ("*Wisniewski*").

36. In *Wisniewski* Brooke LJ considered earlier case law, which included *McQueen v Great Western Railway Co* (1875) LR 10 QB 569, in which Cockburn CJ said:

> "If a *prima facie* case is made out, capable of being displaced, and if the party against whom it is established might by calling particular witnesses and producing particular evidence displace that prima facie case, and he omits to adduce that evidence, then the inference fairly arises, as a matter of inference for the jury and not a matter of legal presumption, that the absence of that evidence is to be accounted for by the fact that even if it were adduced it would not displace the *prima facie* case. But that always presupposes that a *prima facie* case has been established; and unless we can see our way clearly to the conclusion that a *prima facie* case has been established, the omission to call witnesses who might have been called on the part of the defendant amounts to nothing."

37. Cockburn J also cited the judgment of Gillard J in *O'Donnell v Reichard* [1975] VR 916, a decision of the Supreme Court of Victoria. Having reviewed the earlier cases, Gillard J said:

> "…the effect of a party failing to call a witness who would be expected to be available to such party to give evidence for such party and who in the circumstances would have a close knowledge of the facts on a particular issue, would be to increase the weight of the proofs given on such issue by the other party and to reduce the value of the proofs on such issue given by the party failing to call the witness."

38. Brooke LJ summarised the position as follows:

> "From this line of authority I derive the following principles in the context of the present case:
>
> (1) In certain circumstances a court may be entitled to draw adverse inferences from the absence or silence of a witness who might be expected to have material evidence to give on an issue in an action.
>
> (2) If a court is willing to draw such inferences, they may go to strengthen the evidence adduced on that issue by the other party or to weaken the evidence, if any, adduced by the party who might reasonably have been expected to call the witness.
>
> (3) There must, however, have been some evidence, however weak, adduced by the former on the matter in question before the court is entitled to draw the desired inference: in other words, there must be a case to answer on that issue.
>
> (4) If the reason for the witness's absence or silence satisfies the court, then no such adverse inference may be drawn. If, on the other hand,

> there is some credible explanation given, even if it is not wholly satisfactory, the potentially detrimental effect of his/her absence or silence may be reduced or nullified."

39. In *CCA* the Upper Tribunal considered the above passage and then said at [66]:

> "This summary does identify some essential requirements before a court or tribunal may draw an adverse inference. Thus: (1) the party seeking the benefit of the inference must have adduced some evidence which shows there is a case for the other party to answer; (2) there must be a reason to expect that material evidence exists; (3) it is open to the party who resists the adverse inference to give a credible explanation, even a not wholly satisfactory explanation, as to why the evidence was not given. Apart from these basic requirements, there is much in the above summary of principle which is left open ended. We refer to the references to the court (or tribunal) being entitled to draw inferences 'in some circumstances' and the court's power to be influenced by an explanation which is not wholly satisfactory. These indicate that there is much about this approach which is not rigid and prescriptive. This reflects the circumstance that it is ultimately for the fact finding tribunal to make what it regards as appropriate findings of fact having regard to all the circumstances of the case including the fact, if this is established, that a party has not called an available witness and has not given a satisfactory explanation for not calling the witness."

40. In the subsequent case of *British Airways PLC v Airways Pension Scheme Trustee Ltd* [2017] EWHC 1191 (Ch) ("*British Airways*") at [141-143], Morgan J summarised the case law and asked the following questions:

> "1. Is there some evidence, however weak, to support the suggested inference or finding on the matter in issue?
>
> 2. Has the Defendant given a reason for the witness's absence from the hearing?
>
> 3. If a reason for the absence is given but it is not wholly satisfactory, is that reason 'some credible explanation' so that the potentially detrimental effect of the absence of the witness is reduced or nullified?
>
> 4. Am I willing to draw an adverse inference in relation to the absent witness?"

41. He added at [146]:

> "even if I eventually conclude that I have not been given a good reason or a credible explanation for the [party] not calling these three witnesses, it does not follow that I will automatically draw [an adverse] inference...In deciding what inferences to draw, I need to take into account not only the fact that [the individuals] were not called, when they could have been, but also other matters such as what I consider to be the most probable finding to make on the basis of all the evidence which I have received."

42. Although the overall conclusions reached by Morgan J were subsequently overturned by the Court of Appeal (see [2018] EWCA Civ 1533), the Court made no criticism of his approach to dealing with adverse inferences.

43. In *HMRC v Sunico* [2013] EWHC 941 (Ch) at [98], Proudman J said that "if the court is to draw adverse inferences, they cannot simply be of a general nature; they must be specific inferences in relation to specific pleaded issues," and the UT in *CCA* endorsed this statement.

Adverse inferences: application

44. Mr Watkinson ended his closing submissions by asking us to infer that the reason Mr Chhatwal failed to call his suppliers and customers to give witness evidence was because they "would have exposed facts unfavourable to it such as that it knew that the transactions were connected with fraud". That was a request for the Tribunal to draw an adverse inference of a general nature. In accordance with the guidance given by the UT set out above, we decline to make that inference.

45. However, Mr Watkinson also submitted that the lack of witness evidence was "particularly acute" in relation to issues such as "bundle splitting", and that:

> "Mr. Chhatwal's entire case on 'the only reasonable explanation' limb of *Kittel* really boils down to what he was told by various people about the three suppliers he used, and what they were doing with PlayStation bundles. There is no contemporaneous document recording anything in support of Mr Chhatwal's evidence. In those circumstances, it is extraordinary that there is no witness from any of his counterparties who can make good Mr Chhatwal's assertions."

46. This is a request for the Tribunal to make a specific adverse inference from EDC's failures to call the third party witnesses who Mr Chhatwal said had told him about bundle-splitting.

47. In the course of our findings of fact, we therefore considered whether to make adverse inferences in relation to EDC's case that there was a commercial market in which soft bundles were routinely split. For the reasons set out at §226ff, we agreed to make that inference. We have also made adverse inferences about the failure to call other witnesses, and the failure to provide certain documents, for the reasons explained at §228ff.

PART 2: THE LAW

48. Article 17 of the Sixth Council Directive of 17th May 1977 is headed "Origin and scope of the right to deduct" and it provides:

> "1. The right to deduct shall arise at the time when the deductible tax becomes chargeable.
>
> 2. In so far as the goods and services are used for the purposes of his taxable transactions, the taxable person shall be entitled to deduct from the tax, which he is liable to pay:

(a) value added tax due or paid within the territory of the country in respect of goods or services supplied or to be supplied to him by another taxable person;….."

49. Articles 167 and 168 of Council Directive 2006/112/EC ("the Principal VAT Directive" or "PVD") provide:

"167. A right of deduction shall arise at the time the deductible tax becomes charged.

168. In so far as the goods and services are used for the purposes of the taxed transactions of a taxable person, the taxable person shall be entitled, in the Member State in which he carries out these transactions, to deduct the following from the VAT, which he is liable to pay:

(a) the VAT due or paid in that member State in respect of supplies to him of goods or services, carried out or to be carried out by another taxable person."

50. Those provisions are incorporated into UK law as Value Added Taxes Act 1994 ("VATA"), ss 24, 25 and 26 as follows:

"**24. Input tax and output tax**

(1) Subject to the following provisions of this section, 'input tax', in relation to a taxable person, means the following tax, that is to say

(a) VAT on the supply to him of any goods or services;

(b) VAT on the acquisition by him from another member State of any goods; and

(c) VAT paid or payable by him on the importation of any goods from a place outside the member States,

Being (in each case) goods or services used or to be used for the purpose of any business carried on or to be carried on by him….

(6) Regulations may provide-

(a) for VAT on the supply of goods or services to a taxable person, VAT on the acquisition of goods by a taxable person from other member States and VAT paid or payable by a taxable person on the importation of goods from places outside the member States to be treated as his input tax only if and to the extent that the charge to VAT is evidenced and quantified by reference to such documents as may be specified in the regulations or the Commissioners may direct either generally or in particular cases or classes of cases;…

25. Payment by reference to accounting periods and credit for input tax against output tax

(1) A taxable person shall–

(a) in respect of supplies made by him, and

(b) in respect of the acquisition by him from other member states of any goods,

> account for and pay VAT by reference to such periods (in this Act referred to as 'prescribed accounting periods') at such time and in such manner as may be determined by or under regulations and regulations may make different provision for different circumstances.
>
> (2) Subject to the provisions of this section, he is entitled at the end of each prescribed accounting period to credit for so much of his input tax as is allowable under section 26, and then to deduct that amount from any output tax that is due from him.
>
> **26. Input tax allowable under section 25**
>
> (1) The amount of input tax for which a taxable person is entitled to credit at the end of any period shall be so much of the input tax for the period (that is input tax on supplies, acquisitions and importations in the period) as is allowable by or under regulations as being attributable to supplies within subsection (2) below."
>
> (2) The supplies within this subsection are the following supplies made or to be made by the taxable person in the course or furtherance of his business–
>
> (a) taxable supplies;
>
> (b) supplies outside the United Kingdom which would be taxable supplies if made in the United Kingdom;…"

51. Thus, if a taxable person has incurred input tax that is properly allowable, he is entitled to set that input tax against his output tax liability. If the input tax credit due to him exceeds the output tax liability, he is entitled to a payment.

52. However, the European Court of Justice ("ECJ"), in *Kittel v Belgium & Belgium v Recolta Recycling* [2006] C-439/04 & C-440/04 ("*Kittel*") held that taxable persons will not be entitled to deduct that input tax if they "knew or should have known" that the purchases on which input tax had been incurred were connected with the fraudulent evasion of VAT. This "*Kittel* test" was expressed as follows, see [55]:

> "…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."

53. In *Kittel* the ECJ also held that it was a matter for the national court to decide whether to refuse entitlement for that reason, see [59] and [61] of the judgment.

54. An allegation that a taxpayer "knew" that the transactions were connected with fraud is not tantamount to an allegation of dishonesty, and there is no requirement for HMRC to plead and particularise an allegation of fraud, see *E-Buyer v HMRC* [2017] EWCA Civ 1416. Mr Watkinson confirmed that HMRC were not alleging that EDC, or its director, Mr Chhatwal, had committed fraud.

55. In the combined cases of *Mobilx v HMRC; Blue Sphere Global v HMRC (No 2)* and *Calltel Telecom v HMRC* [2010] EWCA Civ 517 ("*Mobilx*"), the Court of Appeal

considered the meaning of "should have known". Moses LJ, giving the only judgment with which Chadwick and Carnwarth LJJ both agreed, said at [51] that the phrase meant the same as "knowing or having any means of knowing", and continued at [52]:

> "If a taxpayer has the means at his disposal of knowing that by his purchase he is participating in a transaction connected with fraudulent evasion of VAT he loses his right to deduct, not as a penalty for negligence, but because the objective criteria for the scope of that right are not met. It profits nothing to contend that, in domestic law, complicity in fraud denotes a more culpable state of mind than carelessness, in the light of the principle in *Kittel*. A trader who fails to deploy means of knowledge available to him does not satisfy the objective criteria which must be met before his right to deduct arises."

56. Moses LJ went on to say that the following did not meet the necessary threshold (our emphases):

(1) a trader who should have known that he was *running a risk that* the transaction might be connected with fraud, see [56];

(2) a trader who knows or could have known no more than that *there was a risk* of fraud [55];

(3) a trader who should have known that it was *more likely than not* that it was so connected [60].

57. Instead, it must be shown that the trader should have known that he *was* taking part in a transaction connected to fraud. This includes those who:

(1) should have known from the circumstances which surround their transactions that they were connected to fraudulent evasion [59];

(2) choose to ignore obvious inferences which arise from the facts and circumstances in which they have been trading [61];

(3) should have known that the only reasonable explanation for the transactions was that they were connected with fraud [59]; and/or

(4) have the means of knowledge available and choose not to deploy it [61].

58. At [72] Moses J referred to the first instance decision in *Blue Sphere Global* ["BSG"], in which the VAT Tribunal had said at [227] that it would have been appropriate for BSG's director to have asked the following questions:

> "(1) Why was BSG, a relatively small company with comparatively little history of dealing in mobile phones, approached with offers to buy and sell very substantial quantities of such phones?
>
> (2) How likely in ordinary commercial circumstances would it be for a company in BSG's position to be requested to supply large quantities of particular types of mobile phone and to be able to find without difficulty a supplier able to provide exactly that type and quantity of phone?

> (3) Was Infinity [one of the suppliers to BSG] already making supplies direct to other EC countries? If so, he could have asked why Infinity was not making supplies direct, rather than selling to UK traders who in turn would sell to such other countries.
>
> (4) Why are various people encouraging BSG to become involved in these transactions? What benefit might they be deriving by persuading BSG to do so? Why should they be inviting BSG to join in when they could do so instead and take the profit for themselves?"

59. Moses LJ said at [83] that these were "important questions which may often need to be asked in relation to the issue of the trader's state of knowledge" and went on to endorse the following passages from Clarke J's judgment in *Red 12 v HMRC* [2009] EWHC 2563 (Ch) ("*Red 12*"):

> "[109] Examining individual transactions on their merits does not, however, require them to be regarded in isolation without regard to their attendant circumstances and context. Nor does it require the tribunal to ignore compelling similarities between one transaction and another or preclude the drawing of inferences, where appropriate, from a pattern of transactions of which the individual transaction in question forms part, as to its true nature eg that it is part of a fraudulent scheme. The character of an individual transaction may be discerned from material other than the bare facts of the transaction itself, including circumstantial and 'similar fact' evidence. That is not to alter its character by reference to earlier or later transactions but to discern it.
>
> [110] To look only at the purchase in respect of which input tax was sought to be deducted would be wholly artificial. A sale of 1,000 mobile telephones may be entirely regular, or entirely regular so far as the taxpayer is (or ought to be) aware. If so, the fact that there is fraud somewhere else in the chain cannot disentitle the taxpayer to a return of input tax. The same transaction may be viewed differently if it is the fourth in line of a chain of transactions all of which have identical percentage mark ups, made by a trader who has practically no capital as part of a huge and unexplained turnover with no left over stock, and mirrored by over 40 other similar chains in all of which the taxpayer has participated and in each of which there has been a defaulting trader. A tribunal could legitimately think it unlikely that the fact that all 46 of the transactions in issue can be traced to tax losses to HMRC is a result of innocent coincidence. Similarly, three suspicious involvements may pale into insignificance if the trader has been obviously honest in thousands.
>
> [111] Further in determining what it was that the taxpayer knew or ought to have known the tribunal is entitled to look at the totality of the deals effected by the taxpayer (and their characteristics), and at what the taxpayer did or omitted to do, and what it could have done, together with the surrounding circumstances in respect of all of them."

60. In *E-Buyer* the Chancellor, Sir Geoffrey Vos, giving the leading judgment with which Hallett LJ and the Master of the Rolls both agreed, cited the same passages and then said at [26]:

> "I digress to record that we were told in the course of oral argument that this passage from the *Red 12* case is regarded as a road map for FtT hearings in this kind of case."

61. Mr Frain-Bell said that by this passage the Court of Appeal had "recently acknowledged" that the points made by Clarke J in the cited paragraphs of *Red 12* were an "appropriate guide for FTT hearings in this type of case", and he structured his closing arguments around that "road map".

62. There are two problems with that submission. The first is that the Court of Appeal in *E-Buyer* did not approve the use of *Red 12* paragraphs as a "road map". Instead, the Chancellor recorded a statement made by counsel in the course of the proceedings. He made no other comment about the *Red 12* passage, and in particular, did not go on to approve its use as a "road map".

63. The second is that there is no guarantee that this "road map" will always deliver a tribunal to the right location. Instead, we must focus on the *Kittel* test itself. As Moses J said in *Mobilx,* that test "is simple and should not be over-refined", and tribunals should not be deflected from that question, see [59] and [82].

64. In assessing whether the *Kittel* test is met on the facts of this case, we of course have regard to the guidance given by the higher courts, including that in *Red 12,* and the following further points:

(1) a tribunal should not unduly focus on the question whether a trader has acted with due diligence, because that may "deflect a tribunal from asking the essential question posed in *Kittel*, namely, whether the trader should have known that by his purchase he was taking part in a transaction connected with fraudulent evasion of VAT" see *Mobilx* at [82]).

(2) However, "the exercise of due diligence or the lack of due diligence can potentially be relevant. If the trader has not carried out due diligence in relation to a transaction, that might assist HMRC in showing that the trader knew or should have known that the transaction was connected with fraud. Conversely, if due diligence has been exercised by the trader, that fact might not be conclusive as to whether the trader did not know or should not have known that a transaction was connected with fraud; the due diligence might have been done as window dressing and there might be other evidence which established that the trader knew or should have known that the transaction was connected with fraud", see *CCA* at [52]; and

(3) a tribunal must be careful not to over-compartmentalise the factors, but must consider the totality of the evidence – in other words, the Tribunal must not consider the evidence "in a piecemeal fashion without looking at the evidence as a whole", see the Court of Appeal's decisions in *Davis & Dann Ltd v HMRC* [2016] EWCA Civ 142 ("*Davis & Dann*") at [60] and *CCA* at [46].

PART 3: THE SUBMISSIONS

65. In this part of our decision, we summarise the parties' submissions, which are considered in more detail later in our decision.

HMRC's case

66. HMRC's position was that Mr Chhatwal knew that all the Deals were connected to fraud, or in the alternative, he should have known this was the position, because each of the Deals were part of an orchestrated fraud against HMRC. Mr Watkinson said that Mr Chhatwal's knowing participation in those frauds is clear from the evidence before the Tribunal, and the inferences which should be drawn from that evidence. In particular:

(1) much of EDC's case rested on assertions by Mr Chhatwal, but he was not a credible witness and no supplier or customer had been asked to give evidence to support EDC's case;

(2) there was no commercial market for PS3s which had been split from "soft bundles" made up of PS3s and games or accessories, and Mr Chhatwal knew this was the case. He would therefore have known that the prices at which the suppliers offered to sell the PS3s could not be explained other than by reference to a fraudulent transaction chain, and were too good to be true;

(3) he knew that the profit margin on PS3s was tight, and therefore also knew that the margin EDC was making was too good to be true;

(4) the due diligence checks EDC undertook were casual and lax. Either it collected insufficient information to make an informed decision as to the *bona fides* of its customers and suppliers, or about their financial ability legitimately to enter into such high value transactions; or, having collected the information, it simply ignored the obvious conclusions;

(5) the goods in the deal chains were purchased from the grey market, whereas previously EDC purchased almost entirely from authorised dealers and manufacturers. Mr Chhatwal had sought to explain this radical shift to the grey market by reference to FX differences and stock variances, but neither explanation is supported by the independent third-party evidence;

(6) many of the goods traded in the chains were EU specification, meaning that they had been imported into the UK only to be dispatched out of the UK again. This made no commercial sense;

(7) EDC rarely recorded on its invoices whether the PS3s were of UK or EU specification; this was because neither EDC nor its customers had a genuine commercial level of interest in the goods being traded;

(8) most of the deal chains were completed within a few days; the disputed transactions which form part of these deal chains were mostly carried out very quickly, sometimes on a back-to-back basis, and this indicates that the transactions were pre-arranged;

(9) there are significant gaps in the documentation, and Mr Chhatwal's explanations for the absence of these documents are not credible. If EDC was seeking its own trades within an active marketplace, evidence of the systems it used and records of its comparisons between competing suppliers would be capable of being produced;

(10) under its terms and conditions, EDC retained title to the goods it sold until the receipt of full payment. Yet it often allowed its customers to ship the goods into mainland Europe before payment had been received. In the context of high value wholesaling this required a level of unregulated trust that could only have been produced by the parties being knowingly part of a fraudulent scheme where they knew they would be paid come what may as monies were passed down the supply chains;

(11) EDC was not purchasing from authorised distributors or manufacturers and it would therefore ordinarily have been a commercial imperative for EDC to inspect the goods, but EDC has produced no evidence of inspection reports and some of the delivery documents are marked "unchecked". The lack of inspection and record keeping meant that, if goods were returned by the customer, EDC could not even know whether it had supplied the item(s) in question, let alone that the order was complete and the stock in good condition;

(12) there was no commercial reason for the length of the deal chains, which consisted almost entirely of wholesalers;

(13) the same companies appear in many of the deal chains, and 21 of the 28 companies which participated have now been deregistered; this is beyond coincidence;

(14) those orchestrating the fraud had a pool of companies at their disposal that they could bring into play; as soon as one company was deregistered it was replaced by another. The links between the defaulters and the scale of their defaults shows that the fraudulent defaulting traders did not operate in isolation;

(15) some of the suppliers and customers had traded directly between each other in other transactions, so the interposition of EDC made no commercial sense; and

(16) any trader concerned to avoid MTIC carousel fraud would have been astute to record and retain the serial numbers of the goods that it dealt in. This is a clear and controlled way in which a trader could protect itself from dealing in the same stock more than once, which would be an indication that the trader was in a carousel. It has the commercial advantage of providing clear records in the event of dispute or the need for insurance claim, yet EDC did not record the serial numbers of the goods it traded in these transaction chains.

67. Mr Watkinson also said that those who orchestrated these frauds would only succeed if they could reliably ensure that each participant knew from whom to purchase and to whom to sell in each chain. EDC was the broker in many of the chains, and so played a pivotal role. Moreover, given that Mr Chhatwal was very experienced in the wholesale market for electronic goods, any fraudster would be bound to be cautious in using him as an innocent dupe, fearing that Mr Chhatwal's experience would allow him to detect the fraud. Furthermore:

(1) the Deals involved twenty separate transactions, of which 18 took place between February 2011 and May 2011, a period of only four months. EDC was also involved in a further 18 fraudulent transactions in which WNL was the defaulter; these took place between February 2011 and July 2011. It was not

credible that Mr Chhatwal could have been duped so many times, by so many different suppliers and customers, into undertaking the transactions which were part of fraudulent transaction chains, within the same short period;

(2) the scale of EDC's involvement could be seen by considering the VAT position: during periods 02/11 to 05/11, between 67% and 51% of EDC's input VAT arose from MTIC related transactions, being both the Deals and the transactions in which WNL was the defaulter; and

(3) EDC's profits were the highest, or the second highest, of all participants in the deal chains. If EDC was an innocent dupe, the fraudsters would have had no reason to allocate so much of the profit to him.

68. Mr Watkinson also put forward, with markedly less enthusiasm, the alternative submission that if Mr Chhatwal did not know that the Deals were connected to fraud, he should have known, given the facts which the Tribunal should find from the evidence, as set out above.

EDC's case

69. On behalf of EDC, Mr Frain-Bell submitted that:

(1) there was a genuine commercial market in split soft bundles;

(2) Mr Chhatwal had a genuine and reasonable belief that the PS3s he traded had been sourced from split bundles. That explained the low prices and the profit margins;

(3) Mr Chhatwal only knew the suppliers and customers with which he traded, and had carried out sufficient and appropriate due diligence on them; he had no knowledge of the length of the deal chains, or the other participants;

(4) whether the PS3s were of EU or UK specification was of no commercial significance;

(5) recording serial numbers was neither practical nor standard industry practice;

(6) although EDC does not have documentary evidence of Mr Chhatwal's negotiations with the parties, he has provided his phone records, and these show he carried out the negotiations by phone;

(7) it was unreasonable to criticise EDC for not calling suppliers and customers as witnesses, given that EDC ceased trading in 2013 and has had no relationship with the relevant individuals since that date.

70. As already noted, Mr Frain-Bell also relied on the fact that the Deals did not have many of the characteristics commonly seen in other MTICs, and which form the "road map" referred to at §61. These characteristics have been italicised in the subparagraphs below, followed by Mr Frain-Bell's core submission on each point:

(1) *compelling similarities between one transaction and another;* the Deals were all different;

(2) *identical mark-ups on each of the Deals*: EDC's profit varied considerably from Deal to Deal;

(3) *a business with practically no capital*: EDC was a substantial operation with a significant turnover;

(4) *no stock remaining in the hands of the* participants: there were occasions when the stock purchased by EDC was not all disposed of to the customer;

(5) *all the transactions in the period are traced to tax losses*: EDC carried out many deals during these VAT periods which have not been traced to tax losses. Moreover, some of the stock which forms part of a disputed transaction was purchased at the same time and on the same invoice, as other goods which have not been challenged, and some stock was sold along with other goods which again have not been challenged.

71. Although for the reasons explained at §62-63, we do not accept his submission that the Tribunal should follow that "road map", we have of course taken the points above into account in coming to our conclusions.

PART 4: EDC AND ITS MARKETPLACE

72. This part of our decision sets out our findings of fact about the following:

(1) EDC's position generally;

(2) Mr Chhatwal's state of knowledge about the risk of MTIC fraud; and

(3) Sony, CentreSoft and soft bundles.

EDC's position generally

73. The business run by EDC originated as a sole proprietorship, run by Mr Gurcharn Singh Chhatwal, Mr Chhatwal's father. He registered for VAT in 1975 as a retailer of electrical goods, and later incorporated the business as Electrical Discount Centre Limited. In 1997, the business was transferred to a new company, EDC Direct Limited, the Appellant in this appeal. Mr Gurcharn Chhatwal was initially the only shareholder, but in January 2007, he transferred 50% of the shares in EDC to his son**.**

74. Mr Chhatwal started working in the business when he left university in 1991, some 20 years before the transactions in question. He began his first witness statement by saying "I am the Managing Director and a 50% shareholder of EDC". However, he then says at para [31]:

> "Whilst I was involved in Electrical Discount Centre on a day-to-day basis, due to family and cultural reasons, my father was appointed as the Managing Director. I therefore did not have the title of Managing Director or any similar appointment as this would have been disrespectful to my father who had spent the better part of two decades building the business."

75. It was, however, not in dispute that during the relevant period Mr Chhatwal ran all aspects of EDC's business, and was in terms if not in title, its managing director, and was experienced in the trade in which EDC operated.

76. By 1994 EDC had two shops, one in Gravesend and one in Bexleyheath. In 1995 or 1996, Mr Chhatwal began to expand the business by providing insurance replacement goods to customers of the Woolwich. To do this, it set up a call centre to communicate with the customers, and to identify appropriate replacement products for those which had been lost or damaged. When Barclays took over Woolwich in 2000, the business grew dramatically. A number of manufacturers began to supply EDC directly, and it became an authorised distributor for those manufacturers. In 2001, Sony awarded EDC the accolade of being "dealer of the year", and about the same time, EDC started to attract business from other insurance companies.

77. In 2006, Aviva began to underwrite the insurance policies sold by Barclays. Aviva used a model which allowed suppliers to compete on price. EDC had built its business on its expertise in selecting appropriate replacement goods, and the Aviva model undercut its profits. EDC began to move into the wholesale market for audio-visual equipment, selling both to other retailers and to large corporates, such as Amazon and Paddypower. Under its standard terms and conditions, which applied at the time of the disputed transactions, EDC retained title to the goods until payment was received from the customer.

78. In around 2008, EDC began carrying out substantial business with CentreSoft, Sony's authorised distributor in the UK. We make further findings about Sony and CentreSoft at §130ff .

Total sales and the move into the export market

79. EDC's sales in the calendar year 2007 were just over £4m. In 2008 sales grew to £19.2m, and in 2009 they increased further to just under £30m. In 2010 they fell to £26m in 2010, followed by a further fall in 2011 to £18.3m.

80. Until Q3 of 2008 all EDC's sales were made to customers within the UK. In that quarter, EDC made its first export sales. These were £758k, rising to £5m in the following quarter, and between £4.6m and £8.6m in each quarter of 2009. The goods exported were mostly televisions, camcorders, cameras, PlayStations and home cinemas**.** Mr Chhatwal attributed this move into the export market to a combination of three factors:

(1) the decline in EDC's insurance business;

(2) the decline in the UK market following the economic crisis in autumn 2008; and

(3) FX fluctuations.

81. There was no challenge to the first two of those causes, but the FX position was put in issue by HMRC, and our findings are set out in the next following paragraphs.

82. In 2007 £1 was worth around €1.4, but the economic crisis in 2008 caused the euro to strengthen against the pound, almost reaching parity in Q1 2009, before easing somewhat. The company's exports, and the FX rate were as follows:

Sales Quarter	Total sales £k	Exports £k	£/euro
Q2 2008	£4,227	0	1.26
Q3 2008	£6,144	£758	1.26
Q4 2008	£6,973	£5,144	1.12
Q1 2009	£9,776	£8,633	1.10
Q2 2009	£5,177	£4,694	1.14
Q3 2009	£4,832	£3,879	1.15
Q4 2009	£10,148	£8,550	1.11

83. On 4 September 2009 Mr Chhatwal told a HMRC Officer that he was "able to make a small margin due to the exchange rates" when buying stock in the UK and selling it into the EU**.**

84. We accept that the sudden fall in the FX rate at the end of 2008 helped EDC to sell more goods to the EU in the last quarter of 2008 and during the first part 2009, but the benefit of those differences was small, as Mr Chhatwal said at the time.

Whether FX fluctuations were a reason for the disputed transactions

85. Of the 20 disputed transactions, 18 took place in the first two quarters of 2011; of the remaining two transactions, one was in the previous quarter and one was in the following quarter.

86. In Mr Chhatwal's first witness statement he said that "EDC was able to achieve good profits" these transactions, in part because it was "taking advantage of exchange rates". However, that was contradicted by other sources of evidence.

87. The first of these is the sterling/euro exchange rate at the time of the disputed transactions. As the table below shows, there was little fluctuation:

Sales Quarter	Total sales £k	Exports £k	£/euro
Q2 2010	£4,059	£2,952	1.17
Q3 2010	£3,154	£2,047	1.20
Q4 2010	£9,005	£5,985	1.16
Q1 2011	£7,428	£5,881	1.17
Q2 2011	£4,696	£2,203	1.13
Q3 2011	£3,523	£1,096	1.14
Q4 2011	£2,683	£260	1.17

88. The second source of evidence is Officer Hughes' witness statement, which was unchallenged. He visited EDC on 22 June 2010. His Notebook formed the basis for his report of that visit, and he said (emphasis added):

> "At the date of the visit, 22 June 2010, EDC's EU export sales had dropped due to the Euro exchange rate. UK retail sales had increased as a consequence. EDC envisaged their future EU export sales would drop by up to 60% due to the said Euro exchange rate problem."

89. Third, there is Mr Gara's evidence, which was also unchallenged. This is relevant because all but two of the 20 disputed transactions involved goods manufactured by Sony. Mr Gara stated that Sony sought to manage pricing of the same goods across Europe, so that it was fair to all customers. Prices would not be adjusted on a week by week basis, because that would cause too much volatility, but if there was a significant shift in the FX rates, Sony would adjust the pricing so that, for example, the price paid by German customers was in line with that paid by UK customers. In his experience, there were few opportunities for arbitrage based on currency movements.

90. Finally, when Mr Chhatwal met with Officer Hughes on 22 June 2010, he said that (emphasis added) "the exchange rate with the euro has dictated a change in their trading approach and in consequence EDC are making increasing amounts of UK sales". In other words, by June 2010, EDC was no longer benefitting from the small margin on the £/euro exchange rate. And as shown in the table above, in June 2010 the £/euro exchange rate was 1.17, the same as in the first quarter of 2011.

91. Taking into account the minimal FX fluctuations; Officer Hughes' unchallenged evidence; Sony's policy of making adjustments to prevent differential pricing, and Mr Chhatwal's own statement to Officer Hughes in 2010, we find as a fact that currency differences do not provide a reason for EDC's profits on the disputed Deals. Given Mr Chhatwal's knowledge of that export market, we also find that he knew this was the position.

Grey market purchases

92. In Q3 of 2007, EDC purchased 95% of its goods from manufacturers or authorised distributors (the "direct market"), and the other 5% from other sellers (the "grey market" or the "indirect market"). In Q4, purchases from the grey market rose to 15%, but fell back to 10% and 7% in the following two quarters. From Q3 2008 through to Q3 2009, EDC made no grey market purchases. None of the goods purchased from the grey market during this period was exported.

93. In Q4 2009 EDC's grey market purchases rose again to 13%, of which 80% were exported. Grey market purchases in the next four quarters were low, ranging from 0% to 2%, of which 90% were exported.

94. Thus, before 2011 there had only been one quarter in which EDC both (a) purchased from the grey market, and (b) exported those goods, and in that quarter, grey market purchases were only 13% of the total.

95. There was then a sudden change: in Q1 2011 grey market purchases more than tripled from that previous maximum, from 13% to 43%, of which 84% were exported; in Q2 2011, grey market purchases were 42%, of which 30% were exported. Grey market purchases then dropped dramatically. The table below shows the contrast

between 2010 and the first two quarters of 2011, with the pattern reverting back for the final two quarters:

Sales quarter	% direct market	% grey market	% grey market exported
Q1 2010	98%	2%	90%
Q2 2010	98.5%	1.5%	90%
Q3 2010	100%	0%	N/A
Q4 2010	99%	1%	90%
Q1 2011	57%	**43%**	**84%**
Q2 2011	58%	**42%**	**30%**
Q3 2011	92%	8%	8%
Q4 2011	100%	0%	N/A

96. Mr Watkinson submitted that there had been a "radical" change in EDC's trading pattern in Q1 and Q2 of 2011, and we agree.

97. All the goods in the 20 disputed transactions were purchased in the grey market. Of these, 18 took place in the first two quarters of 2011, with one transaction in the previous quarter and one in the following quarter. In other words, there is a clear correlation between the shift in EDC's trading pattern and the transactions linked to fraud.

Contact with HMRC in 2008

98. On 29 August 2008, EDC asked to move onto monthly VAT returns. HMRC refused, because there was insufficient evidence that it had become a repayment trader. On 29 September 2008, EDC's then agent, Bespokes Ltd, appealed that decision on the basis that EDC had "started to export large quantities of goods to other EC countries" and "purchases these goods from UK suppliers". A second request was refused on 25 November 2008, for the same reason: EDC had not shown that it was an established repayment trader on the basis of its past history, and could not show proof of future export transactions.

99. On 26 November 2008, Officer Barry Howard visited EDC's premises to carry out a VAT Audit, and checked the despatch file relating to its exports to Germany. He found "all paperwork in order". On 29 January 2009 Bespokes made a further application for monthly VAT returns, and this was granted with effect from 03/09.

Meeting with HMRC in August 2009

100. On 20 August 2009, two HMRC Officers, Mr Mark Hughes and Ms Jane Humphrey, made an unannounced visit to EDC because one of EDC's customers, AS Trading, had been identified as a missing trader in Denmark. Officer Hughes gave unchallenged witness evidence that he and Officer Humphrey discussed "MTIC fraud

risks and due diligence" with Mr Chhatwal, and issued him with Public Notice 726. That evidence is supported by a contemporaneous note of the meeting.

101. On 4 September 2009, some two weeks after that visit, HMRC Officer Myra Snook called Mr Chhatwal. Her contemporaneous note of that call states that "Mr Chhatwal informed me that he had received a visit from two officers warning him about MTIC trade."

102. During his cross-examination of Mr Chhatwal, Mr Watkinson referred to his meeting with Officers Hughes and Humphrey. First, he asked Mr Chhatwal whether he knew why he had been given Notice 726. Instead of answering that question in a straightforward manner, Mr Chhatwal said that Officer Hughes had approved of EDC's due diligence. Mr Watkinson put the question again, and Mr Chhatwal said that it had been provided in order to inform EDC "that there was MTIC fraud in certain markets". Mr Watkinson asked Mr Chhatwal if he had read that Notice, and again Mr Chhatwal sought to avoid answering the question, saying instead "I was given the notice by Officer Hughes after he had spent a lot of time at our offices". On that question being repeated, Mr Chhatwal said he had read it "briefly". Mr Watkinson handed a copy of the Notice to Mr Chhatwal, and the following exchange took place:

> "Mr Watkinson: Do you recall being given notice 726?
>
> Mr Chhatwal: Can't recall 100 per cent, but probably was.
>
> Mr Watkinson: The heading, 'Joint and several liability for unpaid VAT'. Did you understand, having been given this notice, that if VAT went missing in the supply chain, that HMRC might try to hold your company liable for it?
>
> Mr Chhatwal: Yes
>
> Mr Watkinson: Was that important to you?
>
> Mr Chhatwal: Very
>
> Mr Watkinson: So you must have read this notice?
>
> Mr Chhatwal: I was informed by Officer Hughes.
>
> Mr Watkinson: Did you read the Notice?
>
> Mr Chhatwal: I may have, briefly, but Officer Hughes confirmed everything."

103. Mr Watkinson then read aloud from the following part of the Notice which set out the "specified goods" to which it applied, for supplies made after 1 May 2007:

> "the specified goods are any:
>
> - equipment made or adapted for use as a telephone and any other equipment made or adapted for use in connection with telephones or telecommunication;
> - equipment made or adapted for use as a computer and any other equipment made or adapted for use in connection with computers or computer systems…;

- other electronic equipment made or adapted for use by individuals for the purposes of leisure, amusement or entertainment and any other equipment made or adapted for use in connection with any such electronic equipment.

This final bullet includes items such as digital cameras, camcorders and other portable electronic devices for playing music and games such as iPods, hand-held or portable DVD players, Playstation Portables (PSP's) etc."

104. Mr Watkinson then asked "Mr Chhatwal, you knew that trading in PlayStations and iPods in the grey market carried an increased risk of MTIC fraud, didn't you?" to which Mr Chhatwal replied "None of the products were modified". After Mr Watkinson pointed out that this response did not answer the question, the following exchange occurred:

> "Mr Watkinson: Did you know, at the time of undertaking these transactions, dealing in the grey market in PlayStations and iPods carried an increased risk of MTIC fraud?"
>
> Mr Chhatwal: We dealt with a whole range of products, PlayStations, iPods, televisions and so forth. When Mr Hughes visited me, he knew exactly what we were supplying, where those goods were going.
>
> Mr Watkinson: [repeats question]
>
> Mr Chhatwal: No
>
> Mr Watkinson: So it follows that despite being issued with this notice, you cannot have read it, yes?
>
> Mr Chhatwal: I briefly would have gone through the notice if I'd received it, but I was taking the expert guidance from Mr – Officer Hughes when he visited my premises…"

105. In reliance on (a) the contemporaneous record of Officers Hughes and Humphrey; (b) the unchallenged witness evidence of Officer Hughes; and (c) Mr Chhatwal's own statement as recorded by Officer Snook that he was warned during that visit about MTIC fraud, we find as a fact that Mr Chhatwal was issued with Notice 726 during that first visit. The Notice explained when a business could be held liable where VAT was lost because of MTIC fraud. Given that Mr Chhatwal accepted in cross-examination that this was "very" important to EDC, we also find on the balance of probabilities that Mr Chhatwal read Notice 726 after he received it. Finally, Mr Chhatwal's repeated attempts to avoid giving straightforward answers to Mr Watkinson's questions about that Notice formed part of our assessment of his credibility, see §28(1).

106. Notice 726 also states "HMRC does not expect you to go beyond what is reasonable. But HMRC would expect you to make a judgement on the integrity of your supply chain and the suppliers, customers and goods within it". It goes on to set out a number of "indicators" which may alert a trader to the risk that a deal is connected with an MTIC fraud. These include:

(1) can a brand new business obtain specified goods cheaper than a long established one?

(2) have normal commercial practices been adopted in negotiating prices?

(3) do the quantities of the goods concerned appear credible?

(4) do the goods have UK specifications, yet are to be exported?

107. It also says:

> "A business trading within a market should have a reasonable idea of the market prices for the goods on any given day. If goods are offered at what appears to be a bargain price then you should find out the reason for the low cost, if it's too good to be true, then it probably is."

108. The contemporaneous note of the meeting between the Officers and Mr Chhatwal also records that Mr Chhatwal said that EDC:

(1) trades in home entertainment systems, predominantly televisions, but also made small volume sales of iPods;

(2) was an authorised distributor for Sony, Samsung, Panasonic and other major television manufacturers;

(3) purchased directly from the manufacturer and sells on;

(4) sourced its overseas customers using the internet;

(5) had never received unsolicited approaches from third parties;

(6) employed a firm to carry out credit checks on customers for insurance purposes; and

(7) checked VAT numbers on the Europa website.

109. The note also includes the following passage:

> "explained to trader that AS Trading are currently a missing trader in Denmark. EDC last dealt with AS Trading in April. Paperwork seen. Satisfied with it all…issued PN726, although satisfied the system EDC have in place is adequate."

Letter about verification of MTIC status

110. There were two methods of checking a trader's status for MTIC purposes. One was to use HMRC's "Vision" system, which was operated from their Wigan Office, by reference to the trader's VAT Registration Number ("VRN"). The other was to check the EU's Europa website. Mr Ginn's unchallenged evidence was that the Vision system contained information about the VAT status of all EU traders, and that the data was more up to date that that on the Europa website.

111. On 26 April 2010, HMRC sent EDC a letter about the continuing risk of MTIC fraud, which included the following passage:

> "you may previously have been verifying the VAT status of new or potential Customers/Suppliers with your Local Office or the National

> Advice Service. However, requests for verification of new Customers/Suppliers should now be faxed to Wigan HMRC Office Fax number [xxx]. If you do not have fax facilities please contact [tel no]."

112. Mr Chhatwal accepted that this letter was addressed to EDC, but when asked in cross-examination if he had read it, initially said he "could not remember"; then that he "may not have done if it was a circular and was not anything specific to our company", and finally that he "did not recall" reading the letter. We find as a fact that the letter was received by EDC. As it was not a "circular" but concerned matters which were "specific to" EDC, we further find that Mr Chhatwal read that letter when it was received.

Meeting with HMRC on 22 June 2010 and subsequent VAT returns

113. On 22 June 2010, Officer Hughes made a second visit to EDC, this time accompanied by Officer Palmer. They met with Mr Chhatwal, who said EDC:

> (1) sold home entertainment systems, predominantly televisions, to wholesalers;
>
> (2) sold small volumes of gaming consoles and games. These were purchased from CentreSoft and Gem Distributors and sold to EU customers, which EDC found via the internet, and that EDC checked the VAT numbers of these customers using the Europa site; and
>
> (3) employed a firm to carry out credit checks on customers for due diligence purposes.

114. Officer Hughes's contemporaneous note of that meeting concluded by saying that he was "satisfied the system EDC have in place is adequate". He also examined "a selection of invoices and related paperwork" and was "satisfied all [were] correct", before concluding "this trader is not an MTIC trader". In his witness statement, Officer Hughes added that he recalled looking at EDC's due diligence paperwork and commenting to Mr Chhatwal that "it is some of the best I have seen".

115. In his oral evidence, Mr Chhatwal sought for the first time to challenge HMRC's meeting notes and Officer Hughes' witness statement (which had already been accepted). He said: "in 2010 when Mr Hughes visited me, he was made aware that I was purchasing from the indirect market. I actually gave him the traders' names". We prefer the contemporaneous evidence of Officer Hughes and reject this late challenge.

Meeting with HMRC on 29 November 2010 and extended verifications

116. On 29 November 2010, Officers King and Chanan visited EDC, because one of its customers, Sarl Starfish Enterprises, was a missing trader, and EDC had not verified its VAT status with HMRC's office in Wigan. Mr Chhatwal told them that he bought directly from 14 named companies which he described as "manufacturers and authorised dealers"; these included Sony, Samsung and Electro. He also said that no purchases were made from the EU. He accepted that he did not check the status of Sarl Starfish with Wigan, and said he "cannot remember why he did not use Wigan".

117. The Officers discussed MTIC fraud with Mr Chhatwal, and he "advised that he is well aware of the situation". They issued Mr Chhatwal with another copy of Notice 726, pointing out in particular the due diligence checks, they also told him that HMRC's office in Wigan "should be used in all verifications". Their internal report concluded by noting that there was "the potential for [EDC] to become caught up in MTIC fraud" and they recommended that EDC's next VAT repayment be inhibited pending a detailed examination.

118. On 20 December 2010, HMRC selected EDC's November 2010 VAT return for extended verification, and they did the same with the VAT returns for February 2011 through to June 2011. These HMRC letters:

(1) highlighted the risk of MTIC fraud;

(2) explained HMRC's position on repayment claims in the light of that risk;

(3) sets out the test from *Kittel*: and

(4) reminded traders proactively to take reasonable precautions to ensure that they were not involved in MTIC fraud.

119. As the result of those extended verifications and subsequent enquiries, HMRC issued the decisions now under appeal.

Mr Chhatwal's state of knowledge at the time of the disputed transactions

120. In this part of our decision, we first consider the evidence, and then make further findings about Mr Chhatwal's understanding of the risks of MTIC fraud.

Reliance on statements made by Officer Hughes?

121. Mr Chhatwal said that he had understood from Officer Hughes' comments during his meetings in August 2009 and June 2010 that HMRC had confirmed that EDC was carrying out appropriate due diligence; that this was effective in ensuring that the companies with which it traded were legitimate; and that he had relied on those assurances in relation to the disputed transactions. Mr Frain-Bell asked the Tribunal to find as a fact that this was the position.

122. We decline to make that finding, because it is clear from our detailed examination of the due diligence carried out on the disputed transactions at Part 5, and the Deals at Part 6, that there are very significant differences between (a) the information Mr Chhatwal gave to Officer Hughes in those two meetings, and (b) the facts of the disputed transactions. It is not credible that Mr Chhatwal was unaware of those differences, which we summarise as follows:

(1) in the first meeting with Officer Hughes, Mr Chhatwal said that EDC purchase "directly from the manufacturer", but in all the disputed transactions the goods were bought from another wholesaler;

(2) the goods in all but two of the disputed transactions are games consoles with more than half the deals being for over £100,000; but in his first meeting with Officer Hughes, Mr Chhatwal did not refer to games consoles, and in the second, he said only that EDC sold "small volumes";

(3) Mr Chhatwal told Officer Hughes that he had had never received unsolicited approaches from third parties, but on his own evidence he was approached by BAK's director, see §275; he also followed up an unsolicited approach from A Novo UK Ltd ("Anovo"), see §266. We also found Mr Chhatwal's evidence as to how he made contact with Everyberry Ltd, Zippy, and Anisur Rahman, Unipessoal LDA ("ARU") to be unreliable, see Part 5; and

(4) despite saying during both meetings that EDC employed a firm to carry out credit checks on customers for due diligence purposes, this was not the position, as Mr Chhatwal subsequently accepted. Instead, in August 2008, it obtained an insurance proposal from Euler Hermes ("Euler"), a credit insurance firm, see §295. This was valid for a year, and so was significantly out of date by the time of the disputed transactions. In addition, of the seven customers involved in the disputed transactions, only two – Ewert Phono GmbH ("Ewert") and Redcoon GmbH ("Redcoon") – were considered by Euler.

123. Mr Frain-Bell also asked the Tribunal to find as a fact that from his conversations with Officer Hughes, Mr Chhatwal believed that it was enough to check each of the customers and suppliers involved in the disputed transactions on the Europa website before beginning to trade with them, rather than using Wigan.

124. We accept that in June 2010 Mr Chhatwal told Officer Hughes he was continuing to use Europa, and that Officer Hughes did not say that he should instead use Wigan, despite the April 2010 letter requiring that all verifications be carried out via Wigan. However, the position was made absolutely clear when Officers King and Chanan visited EDC on 29 November 2010: they told Mr Chhatwal to use Wigan for all verifications. That visit predated all of the disputed transactions other than Deal A. We therefore find that, by the time of Deal B, Mr Chhatwal knew that he should check all his suppliers and customers with Wigan.

125. As is clear from our findings of fact at Parts 5 and 6, Mr Chhatwal checked the VAT status of RLR Distribution Ltd ("RLR"), one of his three suppliers, with Wigan before entering into the transactions with that company. He checked the VAT status of ARU, one of his seven customers, with Wigan, after concluding the contract to sell the goods, but before they were shipped. Mr Chhatwal either did not check the VAT status of the other suppliers/customers with Wigan at all, or he did so after the transactions had taken place.

126. Mr Frain-Bell also asked us to find as a fact, in reliance on Mr Chhatwal's statements to Officer Hughes, that he checked each of the suppliers and customers with Europa. Given that (a) Mr Chhatwal also informed the Officers that EDC employed a firm to carry out credit checks on customers, which was untrue, and (b) our overall findings on Mr Chhatwal's credibility, we declined to make this type of general finding unless it was supported by documentation. Instead, we considered the position in relation to each of the suppliers and customers, see Part 5. That showed that there was no documentary evidence that EDC checked the VAT status of any of its suppliers or customers, other than possibly Ewert, on the Europa website before entering into the disputed transactions.

Mr Chhatwal's knowledge of the risk of MTIC in the grey market

127. We have already found the following facts:

(1) On 20 August 2009, Officers Hughes and Humphrey discussed "MTIC fraud risks and due diligence" with Mr Chhatwal, and issued him with Public Notice 726, and he read that Notice, see §105.

(2) Notice 726 sets out a list of high-risk items (see §103), including "electronic equipment made or adapted for use by individuals for the purposes of leisure, amusement or entertainment and any other equipment made or adapted for use in connection with any such electronic equipment"; this includes "portable electronic devices for playing music and games such as iPods".

(3) On 29 November 2010, Officers King and Chanan discussed MTIC fraud risks with Mr Chhatwal, and he "advised that he is well aware of the situation", see §117.

(4) On 20 December 2010, HMRC sent EDC the first of several extended verification letters, which set out the *Kittel* test and reminded the company to take all reasonable precautions, see §118.

128. Mr Watkinson asked Mr Chhatwal whether he knew there was a higher risk of VAT fraud in the grey market, and he replied "That was not my mind-set". When asked whether he thought the grey market in PS3s was affected by MTIC fraud, he initially answered "no". It was only after being asked essentially the same question over twenty times that he finally accepted that, before entering into the disputed transactions, he knew "there was an increased risk of fraud in the grey market in consumer electronics".

129. We find as facts that, by the time of the disputed transactions, Mr Chhatwal had a good knowledge of the risk of MTIC fraud and knew what he should have been doing to avoid it.

Sony, CentreSoft, and soft bundles

130. It was common ground that the PS3s in the disputed transactions were all manufactured by Sony. Although Mr Chhatwal's original position was that they derived from soft bundles bought from CentreSoft, see §525ff, by the time of the hearing, EDC had accepted that this was not the position. Nevertheless, the approach taken by CentreSoft to soft bundles was a relevant part of Mr Chhatwal's evidence. This part of our decision sets out our findings of fact about:

(1) Sony, which manufactured the PS3s involved in most of the disputed transactions;

(2) CentreSoft, the authorised distributor for Sony products in the UK;

(3) the margin on PS3s;

(4) their supply chain;

(5) whether there were PS3 stock shortages or surpluses during the relevant period;

(6) hard and soft bundles generally;

(7) Sony soft bundles and the "Sony Letter", which is explained below;

(8) the monitoring and policing of Sony soft bundles; and

(9) whether a commercial marketplace for split soft bundles existed.

Sony

131. Sony UK is a wholly-owned subsidiary of Sony Computer Entertainment Europe Ltd ("SCEE"); SCEE itself is a wholly-owned subsidiary of Sony Corporation. Mr Gara often referred to both SCEE and Sony Corporation as "Sony", and we adopted the same approach.

132. Sony UK is responsible for the distribution, marketing and sale of PlayStation branded consoles, peripherals, accessories and packaged videogame software in the UK and Ireland. One of the accessories was a "Move Starter Pack" (also known as a "Starter Move Pack" or a "Move Controller"), a camera which tracks a player's physical movements and translates them into the movements of their character on the PS3.

133. During the period of the disputed transactions there were two PS3 models available: a 160GB and a larger 320GB. CentreSoft's wholesale price for a 160GB PS3 was £198.79, and its price for a 320GB model was £226.6.

134. A "slim" version of the PS3 was first introduced in 2009 and an improved "slim" model came on the market in 2012. Mr Sherry's evidence was that the "slim" version came with thinner casing than the standard model, making it more attractive to the user. Mr Chhatwal's evidence, which was challenged by Mr Watkinson, but which was consistent with that given by Mr Sherry, was that the slim model replaced the standard model, so that at the relevant time all newly manufactured PS3s were the slim version first produced in 2009, and we accepted this was the position.

135. Sony UK supplies CentreSoft, its UK authorised distributor, with its products; it also supplies certain major retail chains. Sony UK does not supply smaller businesses, whether wholesalers or retailers.

136. Sony has similar subsidiaries in other EU countries, including Germany and Portugal, and those subsidiaries operate a consistent business model**.** There was a conflict in the evidence as to whether Sony's subsidiaries sold to internet retailers. Mr Chhatwal said that manufacturers such as Sony introduced terms of trade "to eliminate internet sellers". This was robustly rejected by Mr Gara, who said that Sony subsidiaries sell products to both (a) businesses which operate from "bricks and mortar" premises and (b) businesses which sell via the internet, because it "would not make commercial sense" for a Sony subsidiary to operate the "arbitrary restriction" of selling only to those operating from traditional premises and refusing to sell to online retailers.

137. We also note that Mr Chhatwal's own evidence on this issue was inconsistent. In addition to his statement that manufacturers such as Sony introduced terms of trade

"to eliminate internet sellers", he also said that in the year 2000 "manufacturers did not look favourably on internet sales [because] internet retailers were blamed for diluting pricing of manufacturers' products", but that this had changed after 2001. That evidence is easily reconciled with that given by Mr Gara, who was an entirely credible and reliable witness. We find as a fact that, at least since 2001, Sony subsidiaries sold PS3s to internet retailers.

138. We further find that this was also the position for other manufacturers and authorised distributors of electronic goods. We come to this conclusion on the basis of Mr Chhatwal's evidence about a change of practice in 2001, together with the reasonable inference that if Sony was selling directly to internet retailers, other large manufacturers and their authorised distributors were doing the same.

CentreSoft

139. CentreSoft is a wholesaler of computer games and consoles. It does not actively target foreign markets, so nearly all its revenue is derived from UK sales (including sales to the British offshore territories). It is Sony's UK authorised distributor, and also distributes games produced by other companies. Mr Sherry described its role in relation to Sony as follows:

> "CentreSoft's basic function as an official distributor is to act as the intermediary between Sony and retailers who sell Sony's products to the public. This role is necessary because it is not cost-effective for Sony to deal directly with all the independent retailers who operate single outlets or small chains, and because we 'add value' by offering hardware and software deals. Although independent retailers make up the majority of our customers, we also supply some large retailers such as supermarkets, national chains (e.g. Dixons), and major mail-order firms (e.g. Shop Direct, formerly known as Littlewoods). Some large retailers deal directly with Sony instead of buying from us; it depends on the various commercial factors involved in each case."

140. The majority of CentreSoft's customers are retailers, but it also sells to a small number of "sub-distributors" or intermediate wholesalers, who then sell to retailers. In the period from 2008 through to 2011, EDC purchased goods costing £2.1m from CentreSoft**,** made up as follows:

2008	£807,970
2009	£908,445
2010	£141,988
2011	£271,987
Total	**£2,130,401**

141. During 2008 and 2009, EDC's largest single purchases of an earlier version of the PS3 were for 500 and 670 consoles respectively, with other purchases ranging from single units to 30, 40, 50, 100 or 500 consoles. During the first nine months of 2010, EDC purchased single units, or round numbers of 10 or 50 units, of PS3s. In

September 2010, EDC purchased 150 units, followed by 250 units in October, 100 in November and 20 in December (ignoring occasional returns). In 2011, EDC purchased 1,200 units as a single transaction in January of that year; apart from that purchase, EDC bought only 8 PS3s, of which 6 were returned. Mr Chhatwal's evidence was that the 1,200 units were soft bundles.

Cross-border sales of Sony products

142. Sony allows its authorised distributors to make "passive" sales outside their territories. A passive sale is one made in response to a customer request. Sony does not prohibit "active" sales, where the distributor takes the initiative, because that would breach the EU principle of freedom of movement, but Mr Gara was unaware of any such sales by authorised distributors. When asked about cross-border sales of Sony products by wholesalers who were not authorised distributors, his unchallenged evidence was that although such grey market sales "could and did happen", this was the case only "to some small degree" and was "not an issue of any materiality".

143. Although cross-border sales from the UK to the EU, or vice versa, were not prohibited by Sony, there were two possible difficulties. The first was that UK PS3s came with a manual and packaging in English, and EU PS3s came with a manual and packaging in French, German, Italian and Dutch. However, Mr Gara's oral evidence was that most customers used the instructions provided within the PS3 to set it up and operate it, and it was possible to opt for those instructions to be displayed in a range of languages. We therefore find that the language of the packaging and the manual was not a barrier to cross-border sales.

144. The second possible difficulty was that UK PS3s came packaged with a fitted three-pin plug, and EU consoles came with a fitted two-pin plug. This meant that:

(1) products shipped by Sony to the UK would therefore have UK plugs. If they were exported and sold to an EU retailer, that retailer would need to supply the end-user customer with an adapter which would allow the use of the PS3 in the EU; and

(2) products shipped by Sony to the EU would have EU plugs. If they were exported to the UK and sold to UK retailer, that retailer would need to s his end-user customer with an adapter which would allow the use of the PS3 in the UK.

145. It was not in dispute that Sony never supplied adapters to convert the PS3s from one type of plug to another, and never supplied CentreSoft with EU specification PS3s.

146. In 2013 the UK subsidiary of an internet and phone retailer called Pixmania included the following provision in its general terms and conditions: "some products come with 2-pin plugs, adapters from European to UK plugs are supplied with your order". Having been asked to consider those terms and conditions, Mr Gara said:

> "There's obviously free movement of goods. The expectation is we produced a product that was intended to be most suitable for the UK customer by including the correct plug and ensuring all manuals are in the right language, but there's nothing to stop someone buying a

> product from Amazon Germany and buying the European spec product or Pixmania as may be the case. What Sony would not have authorised at any stage is to put an adaptor into the box because they'd have no control over the safety of that adaptor or if somebody was swapping out power leads that would…potentially risk the customer, definitely risk the reputation and void any guarantee."

The margin on PS3s

147. It was common ground that:

(1) Sony sold 320GB PS3s to CentreSoft for £205.43, and CentreSoft sold them to its own customers for £226.61; and

(2) Sony sold 160GB PS3s to CentreSoft for £184.03, and CentreSoft sold them to its own customers for £198.79.

148. Mr Sherry's unchallenged evidence was that:

> "The market in Sony PlayStations and other games consoles operates on very tight margins. This results from the manufacturing process being sophisticated and expensive, and from manufacturers having a strong incentive to promote wide ownership of the hardware so that they can maximise sales of accessories and software (which are cheaper to produce and thus offer higher margins). In the first half of 2011, the available margin throughout the PS3 supply chain was only 13-14 per cent, and this had to be shared between the official distributor (and any sub-distributor) and the retailer."

149. In answer to a question from the Tribunal, Mr Sherry added that 4-6% of that margin is taken by CentreSoft. Mr Gara estimated that the retailer's margin was between 5-10%; that estimate was based on publically available retail prices, and his knowledge of the price at which Sony sold the goods to the wholesalers, and that estimate was not put in issue by Mr Frain-Bell.

150. Taking the upper end of all those figures, we find as a fact that the maximum margin for wholesalers who sit between the authorised distributor and the retailer is 5%. Given that Mr Chhatwal was very experienced in buying and selling PS3s, we further find that he knew margins were tight, and also knew the maximum margin which wholesalers would obtain in that market.

The PS3 supply chain

151. In reliance on the unchallenged evidence of Mr Gara and Mr Sherry, we find that:

(1) the typical supply chain for PS3s involved Sony, the authorised distributor, and a retailer;

(2) when Sony directly supplied a small number of major retailers, the supply chain involved two companies, Sony and the retailer;

(3) CentreSoft sold mostly to independent retailers, and the supply chain then involved three companies, Sony, CentreSoft and the retailer;

(4) CentreSoft made a small number of sales to intermediate wholesalers such as EDC; Mr Sherry's estimate, which Mr Frain-Bell accepted, was that there were less than ten such intermediate wholesalers. The supply chain then consisted of four companies; and

(5) it therefore follows that the normal PS3s supply chain between Sony and the customer consisted of two, three or four companies.

152. Mr Chhatwal told Officers Hughes and Palmer on 22 June 2010 that EDC sold overseas to internet retailers (our emphasis)**,** so there was a four-stage supply chain (Sony, CentreSoft, EDC and the retailer); the length of that chain was therefore consistent with our findings above.

153. However, in his evidence for this appeal Mr Chhatwal said EDC also normally sold to EU wholesalers, and therefore participated in a five stage supply chain. Taking into account our findings about the normal supply chain; the tight profit margins in that supply chain; the evidence of Mr Sherry and Mr Gara and Mr Chhatwal's own statements to Officers Hughes and Palmer, we find that EDC normally sold PS3s to retailers and not other wholesalers.

154. Mr Gara and Mr Sherry were asked whether they had ever encountered a PS3 supply chain involving three or more intermediate wholesalers – in other words, a six-stage supply chain: Sony, the authorised distributor, the three wholesalers and the retailer. Neither had ever seen such a chain. Mr Sherry did not believe it would be economically viable because of the tight margins, and Mr Gara said it was "difficult to see how it would be commercially advantageous to do so". We agree. Again, given Mr Chhatwal's familiarity with the PS3 market place, we find that Mr Chhatwal knew this was the position.

Sony stock allocations

155. The next following paragraphs make findings about Sony's allocations of stock to its various authorised distributors and other direct customers. Mr Chhatwal's evidence was:

> "it is well known in the electronics trade that the UK receives a larger than proportionate stock allocation from the manufacturers compared with other European countries."

156. Mr Gara responded by saying:

> "That was definitely not the case in respect of Playstation. In fact, Playstation 3 was far stronger in Continental Europe than it was in the UK, where Xbox 360 has done significantly better during that period."

157. Faced with this conflict of evidence, we prefer that given by Mr Gara, both because it is more specific, and also because we have found him to be a reliable witness. We find as a fact that the UK did not receive a larger than proportionate allocation of PS3s compared to other EU countries.

Stock surpluses or shortages?

158. Mr Gara also gave unchallenged evidence that:

(1) Sony's stock levels are "are based on an analysis of the demand from CentreSoft and our direct retailer customers", with the aim of matching supply to demand as closely as possible;

(2) Sony was not aware of any economically significant shortages of PS3s during the period from July 2010 to July 2011; and

(3) it was "not Sony practice to sell Playstation 3 at discounted prices to dispose of surplus stock". He added that Sony sometimes discounted prices to stimulate the market, for instance around Christmas, but that this discounting was "never" to deal with stock surpluses.

159. Mr Sherry's evidence, which was also unchallenged, was that:

(1) CentreSoft managed its stock levels by matching them to pre-orders from its customer base, with a small excess to deal with urgent orders. As a result, stock surpluses occurred only on "limited occasions", when CentreSoft would ask Sony for assistance. This usually took the form of an advertising campaign to boost sales, or the provision of discounted accessories or software which CentreSoft could package with the consoles. On the rare occasions when there had been a surplus, CentreSoft had never reacted by dumping surplus stock on unofficial wholesalers; and

(2) the only time that PlayStations were in short supply was at launch, and when asked specifically to confirm whether there was a shortage during the first five months of 2011, he denied it.

160. We find as a fact, in reliance on this evidence, that during the period of the disputed transactions, CentreSoft had no shortage of PS3s in stock, and it would therefore have been possible for EDC (and the other UK companies in its supply chains) to purchase from CentreSoft the PS3s required to satisfy customer orders.

Hard and soft bundles generally

161. It was common ground that consoles were frequently sold with one or more computer games, and/or with one or more accessories. When the game or accessory was packaged together with the console in the same box, it was known as a "hard bundle". When the console was packaged in one box, and the game/accessory in another box, it was known as a soft bundle. A soft bundle could be made up of more than one discounted game and/or accessory.

162. A hard bundle was a single item, with a single bar code. Each part of a soft bundle had its own bar code. Soft bundles were more flexible and quicker to set up than hard bundles and so used more frequently. In both hard and soft bundles, the game/accessory was included with the console on a free of charge or heavily discounted basis.

163. It was common ground that there was a difference between the following types of soft bundle:

(1) those where Sony decided which free or heavily discounted game/accessory was to be provided with the console ("a Sony soft bundle");

(2) those where CentreSoft decided what free or discounted game/accessory would be provided with the console ("a CentreSoft soft bundle").

164. Mr Chhatwal exhibited several emails from CentreSoft which referred to soft bundles. Many of the games in those soft bundles were described as "platinum". As Mr Ginn said, platinum games were "older games that have been out for some time". Although a platinum game would still have some retail value, this would be reduced compared to newer games. Many of the soft bundles were made up of older games which had a lower retail price if sold separately than newer games.

Sony soft bundles and the Sony Letter

165. Mr Sherry's witness evidence was that:

> "Soft bundles are put together by Sony: they determine the contents and they issue [CentreSoft] with a buy price. A typical example would be a free piece of software for every PS3 purchased. CentreSoft would receive the PS3 and the software together; it would then sell them on to its customers, who in turn would sell them to the end-users."

166. Both Mr Gara and Mr Sherry gave consistent evidence that the purpose of packaging the PS3 with a game or accessory was to make the offering more attractive to the end consumer. As Mr Sherry said, this arrangement also benefited Sony and CentreSoft, because more PS3s were sold.

167. Mr Gara's evidence was that the authorised distributors and the small number of large retailers with which it dealt directly, were barred by the terms and conditions under which the Sony soft bundles were supplied ("the Sony T&C"), from splitting the soft bundles and selling the consoles and games separately. He said:

> "As soft bundles are intended to benefit the consumer, [Sony UK] supplies them subject to terms and conditions that do not allow them to be broken up by the retailer or official distributor if the retailer wants the benefit of the discounted combined trade price for the products which [Sony UK] is supplying as a soft bundle."

168. Clause 1.1 of the Sony T&C stated that the terms applied to "Goods", which were defined to include "all sales and/or supplies of goods and/or services " by Sony UK to "any purchaser or potential purchaser". Clause 2.2 included the condition that "no bundling or compilation of Goods…is permitted without separate authorisation".

169. In addition to the Sony T&C, Sony UK also wrote to its authorised distributors and the small number of large retailers with which it dealt directly, setting out the "Soft Bundling Conditions of Supply" ("the Sony Letter"). As CentreSoft was Sony UK's authorised retailer in the UK, it received a copy of the Sony Letter, which opens by saying:

> "From time to time, [Sony UK] may offer you, the Retailer the opportunity to supply (soft bundle) certain software titles (to be

> determined by [Sony UK]) free of charge to consumers purchasing a new PlayStation ("a Soft Bundle Offer")

170. Mr Gara accepted that CentreSoft was "the Retailer" referred to in that opening paragraph. Mr Frain-Bell invited him also to agree that the term "consumer" referred to a company such as EDC, which purchased from CentreSoft and might either sell the Soft Bundles via its retail shop, or on-sell them to another wholesaler or retailer; if that were correct, it would follow that the prohibition on splitting a soft bundle did not apply to EDC, because it was a "consumer". Mr Gara said that the term "consumer" in the Letter meant the end customer, not an intermediate purchaser such as EDC**.**

171. Although the meaning of the Sony Letter is a question of law, it is one which must be understood by reference to "the matrix of fact", see Lord Wilberforce in *Reardon Smith Line v Hansen-Tangen* [1976] 1 W.L.R. 989 as endorsed in *Investors Compensation Scheme Ltd v West Bromwich Building Society* [1998] 1 All ER 98 at p 114 *per* Lord Hoffman. We therefore decided it was simpler to deal with the meaning of the Sony Letter in this part of our decision, which otherwise makes only findings of fact.

172. Lord Hoffman's guidance in that same case requires that we ascertain "the meaning which the document would convey to a reasonable person having all the background knowledge which would reasonably have been available to the parties in the situation in which they were at the time of the contract". In carrying out that exercise, we considered the second paragraph of the Sony Letter, which reads:

> "Where [Sony UK] makes a Soft Bundle Offer, the offer is made for the consumer benefit, to ensure the consumer receives a new, unopened, free of charge, game title, nominated by [Sony UK], without cost or profit (other than indirectly through increased sales) to the Retailer. The offer is made on the basis that the consumer received and does not swap, exchange, or otherwise return that game title…"

173. The reasonable person would understand "the consumer benefit" in that paragraph as a reference to the advantage gained by the individual consumer who purchases a Sony soft bundle: he would acquire both the console and the new "unopened" game for the price of the console alone, but on condition that the game is non-returnable.

174. The Sony Letter also requires the Retailer to sell the Soft Bundle to the consumer at a retail price no higher than the price at which the console would have been sold on a stand-alone basis. That condition would make little sense if "the consumer" was an intermediary such as EDC, who would never purchase at the retail price.

175. Taking the above factors into account, we therefore find that "the consumer" in the Sony Letter is the end-customer.

176. The Sony Letter also said that the Soft Bundle Offer provided that:

(1) Sony UK nominated the games which were part of a Soft Bundle Offer; these formed the "Software Pool" for that particular Soft Bundle Offer;

(2) a consumer who purchased an item of hardware (a "Bundle Customer") must be informed by the Retailer that he is entitled to choose one game only (unless otherwise agreed in writing by Sony UK) from the Software Pool, and that game was provided free to the consumer;

(3) the Retailer was prohibited from increasing the overall price of the Soft Bundle, i.e., prohibited from charging for the added game; and

(4) the Retailer was free to provide other free games to Bundle Customers, but these "Optional Units" did not form part of the Soft Bundle Offer, and were provided at the Retailer's own cost.

177. The Sony Letter also set out the financial arrangements for a Sony soft bundle. The game which formed part of a soft bundle was purchased from Sony by the authorised distributor, here CentreSoft, at the normal wholesale price. CentreSoft was required to provide monthly sales reports, setting out the number of Soft Bundles purchased by consumers, together with evidence that consumers had received both the hardware and a "free, new, unopened copy of their chosen title from the Software Pool". On receipt of those sales reports and related evidence, Sony UK gave CentreSoft a "retrospective credit" against the purchase cost of games which had formed part of those Soft Bundles. Sony UK had the right to audit CentreSoft's records, in order to check that the Soft Bundle Offers were provided in accordance with the specified conditions.

178. In other words, once CentreSoft could demonstrate to Sony that one of the identified soft bundle games had been provided to the same consumer as had purchased the PS3, the purchase price CentreSoft had paid for the game was reversed. As a result, the cost of providing the game was borne by Sony UK, and the game was free to CentreSoft. If CentreSoft had instead split the Sony soft bundle, selling the game separately from the PS3, it would not receive the retrospective credit, and so would bear the cost of the game.

179. Mr Sherry's evidence was that CentreSoft sent a copy of the Sony Letter to all its customers, including EDC. However, Mr Chhatwal's witness statement said "I do not recall receiving a copy" of the Sony Letter and that he was unaware of there being any obligation not to split Sony soft bundles**.** During cross-examination, Mr Watkinson asked him twice whether Mr Sherry's evidence that CentreSoft sent the Sony Letter to all its customers, including EDC, was untrue. Mr Chhatwal first avoided answering that question; on it being repeated, he said (emphasis added):

> "something as important as that would have probably required their retailers to sign something and return back to them to say they'd received the letter, acknowledged the terms and conditions, and were now going to adhere to it. But when – if you – <u>if I haven't received the letter</u>, I then start receiving offers which doesn't say anything about splitting bundles. If I then purchase products from them, a soft bundle from them, and receive nothing on the invoice, or anything from Jane Revell [of CentreSoft's sales staff], then I assume that I can do what I

> wish with this soft bundle…CentreSoft were not policing the soft bundle deals…they were supposed to be monitoring soft bundles…"

180. We note that (a) Mr Chhatwal did not say he had not received the Sony Letter, but instead says what the position would be "if" he hadn't received it; (b) Mr Chhatwal's awareness that CentreSoft were supposed to be policing the Sony soft bundles only makes sense if he also knew that Sony did not intend the bundles to be split, and (c) Mr Sherry and Mr Gara, unlike Mr Chhatwal, were wholly credible witnesses. We therefore prefer their evidence to that of Mr Chhatwal, and find as facts that EDC received a copy of the Sony Letter, and Mr Chhatwal knew that Sony required that Sony soft bundles were not to be split.

181. The next issue is whether, despite Sony's interdiction, CentreSoft permitted or encouraged the splitting of soft bundles. The evidence was conflicting. Mr Sherry stated that "on multiple occasions, the sales team at CentreSoft will have reiterated" that its customers were required to offer consumers the benefit of the free games provided as part of a Sony soft bundle. Mr Gara gave consistent evidence, saying that across the industry everybody knew that Sony soft bundles were not to be split. Mr Chhatwal's evidence on this point developed during the hearing:

(1) in his first witness statement, he said that "CentreSoft were not prepared to split bundles";

(2) under cross-examination, he initially confirmed that evidence, saying that "on many occasions" he phoned Ms Revell, who worked in CentreSoft's sales department, and asked if she would split the bundle and sell the PS3s at a cheaper price, and Ms Revell said "I can't split the bundle";

(3) however, he then went on to say – for the first time – that CentreSoft's approach was that *EDC* could do what it wanted with the bundle once purchased.

(4) In re-examination Mr Chhatwal further elaborated his evidence, saying:

> "Jane Revell continuously encouraged us to split bundles to try and make more money. She realised that consoles were being sold cheaper in the marketplace, and she would tell me: look buy some peripheral items that we've got at a discount, so you can then make a profit which will then lower the price of the console. And it wasn't just her. It was several members of the telesales staff."

182. The evidence in Mr Chhatwal's first witness statement is consistent with that given by Mr Sherry: CentreSoft staff were not allowed to split bundles. We find that to be a fact. We reject Mr Chhatwal's elaboration and expansion of his witness evidence, as set out (3) and (4) above. Had that been the position, he would have included that evidence in his witness statements. We therefore find that CentreSoft staff refused to split Sony soft bundles, and did not encourage EDC to split the bundles after purchase.

Monitoring and policing Sony soft bundles

183. CentreSoft originally applied Sony's retrospective credit system, referred to at §177, to the wholesalers and retailers which were its own customers, so that it required them to pay the full price for the PS3s and the games. When provided with proof that the end-customer had purchased the entire soft bundle, CentreSoft reimbursed the cost of the game to the retailer. However, Mr Sherry said:

> "As this system had obvious cash-flow disadvantages for the retailer, CentreSoft started to offer the discount to the retailer up-front in relation to some soft bundles. In other words, Sony sold the bundle items to CentreSoft at the full price [i.e., the wholesale price of the PS3 and the game] and we sold them onward to the retailer at the discounted price [i.e., the wholesale price of the PS3 only]. After selling the bundle items together as a single unit at the discounted price to the end-user the retailer would report the sale to CentreSoft and we would then request and receive the credit from Sony [and so recover the price paid by CentreSoft to Sony for the game]. CentreSoft and the retailer were still legally required to sell the bundle onwards as a single unit. This system has gradually become much more common than retrospective crediting of the discount to the retailer, but both systems were operating alongside each other in late 2010 and the first half of 2011."

184. Mr Gara was taken to this passage during his oral evidence, and said he had been unaware that CentreSoft were not operating a retrospective credit policy with its own customers. He added that CentreSoft was nevertheless still required to have evidence that the bundles had not been split; if it was unable to produce that evidence to Sony's satisfaction, CentreSoft would have to bear the cost of the game or accessory, instead of receiving the retrospective credit from Sony.

185. Four methods were used to try and ensure that a Sony soft bundle was not split by a retailer or intermediate wholesaler.

(1) as explained above, if Sony knew that the bundle had been split so that the end consumer received only the console without the free game, CentreSoft would have to bear the cost of that free game and would be unable to recover it from Sony;

(2) CentreSoft required its customers to provide Electronic Point of Sale ("EPOS") data. Because the console and the game each had their own bar code, this EPOS data would show whether the same customer had purchased the PS3 and the game at the same time. However, Mr Sherry said that when CentreSoft moved away from retrospective credits, it also stopped requiring the provision of EPOS data, and would instead apply "a sort of common-sense test";

(3) monitoring of retailers via a field force called "Team Playstation", a joint venture between CentreSoft and Sony. The field force carried out spot checks on retailers to see if consumers were enjoying the bundle at the right price, and it provided reports to both Sony and CentreSoft**.** A retailer who was found not to be operating the Sony soft bundle policy would no longer be offered Sony soft bundles; and

(4) the operation of the market place. Mr Sherry's unchallenged evidence was that:

(a) the larger independent retailers with which CentreSoft dealt, complied with the soft bundle rules; and

(b) UK consumers "obviously knew what deals were out there" and so a retailer or intermediate wholesaler who purchased a soft bundle, and then split it, would be "taking a risk, definitely" that the consumer would not purchase the PS3s as a stand-alone item, when they knew that Sony was offering a free game bundled with the PS3.

186. However, Mr Sherry also accepted, under cross-examination, that it was difficult for Sony and CentreSoft to police whether a wholesaler or retailer was splitting bundles. We agree, especially after CentreSoft stopped collecting the EPOS data. There remained a risk that bundle-splitting would be identified by the field force, resulting in access to future Sony soft bundles being lost, and there was also a risk that consumers would not purchase the PS3 without the game. However, it would be possible for a person to decide to run those risks and split a Sony soft bundle.

CentreSoft soft bundles

187. As noted above, CentreSoft was also free to make up its own soft bundle deals, using both Sony games/accessories and games/accessories from other manufacturers. Where this happened, the cost of any such games/accessories was borne by CentreSoft, not by Sony.

188. CentreSoft's customers were not sent any written document (equivalent to the Sony Letter) which required them to sell the free/discounted games together with the console. However, we have already found as a fact that Mr Chhatwal was told by CentreSoft staff that EDC could not split soft bundles; this included both CentreSoft soft bundles and Sony soft bundles. The rationale for this policy was that the purpose of constructing a soft bundle was to increase sales of PS3s, and splitting off the free/discounted game/accessory would undermine the purpose of the bundle, see §166.

189. However, there was no retrospective credit system and no collection of EPOS data, and as reports from the field force went to both Sony and CentreSoft, we have inferred that its focus was Sony soft bundles, not CentreSoft soft bundles. We therefore find that CentreSoft's only method of ensuring that the bundle was passed to the consumer was its reliance on the operation of the market place i.e., consumers' knowledge of the bundles available, and the pricing of those bundles.

Other EU authorised distributors

190. Sony supplied soft bundles to authorised distributors in other parts of the EU, and used the same control mechanisms. Mr Gara described it as "a very consistent business model across…the whole EU". However, there was no evidence that those distributors had relaxed the retrospective credit system. In the absence of any such evidence, and noting Mr Gara's surprise that CentreSoft had diverged from Sony's requirements, we find on the balance of probabilities that other EU distributors

continued to follow the requirements in Sony's T&C and the Sony Letter. As a result, it would be more difficult to split a Sony soft bundle offered by an EU distributor than it would be to split one offered by CentreSoft, because EU retailers would need to provide sufficient proof that both parts of the soft bundle had been sold to the same consumer, in order to trigger the retrospective credit.

191. However, just as CentreSoft was free to make up their own soft bundles, so to were the EU authorised distributors. We had no evidence as to how their soft bundle system worked. We infer that, as in the UK, it would be possible for soft bundles put together by EU authorised distributors to be split, subject again to market pressures.

Was there a market for split bundles?

192. Part of EDC's case was that:

(1) intermediate wholesalers purchased substantial volumes of soft bundles from one or more authorised distributor(s) and/or from the few large retailers supplied directly by Sony;

(2) those intermediate wholesalers split the bundles;

(3) the PS3s were sold separately from the games/accessories with which they had originally been bundled, to different wholesalers or retailers;

(4) a significant market existed in splitting and selling on these split bundle products;

(5) the profit on the games/accessories allowed the intermediate wholesalers to reduce the price of the PS3s below that at which they were available from the authorised distributor(s).

193. HMRC's position was that EDC had provided no reliable evidence:

(1) that a commercial market in split bundles existed at all; and/or

(2) if a commercial market did exist, how big it was, and how the goods were priced.

194. We next consider the evidence, and then make findings of fact on whether there was a commercial grey market in which soft bundles were broken up, with the PS3s and the games/accessories being sold separately to different wholesalers.

The Equanet email

195. EDC relied on an email from a company called Equanet, the wholesale arm of Dixons, which was dated 3 February 2011. In the email, Mr Brunt of Equanet's sales department said:

> "I have been offered the following stock of Sony PS3 320GB on offer. Have 500+ stock but will go fast. Price at £224.98."

196. The price of £224.98 was £1.63 below CentreSoft's wholesale price of £226.61. Mr Chhatwal said the only reason why Equanet would have been able to sell the PS3 for less than CentreSoft's price was that it had purchased a soft bundle, split off the

"free" game from the PS3, made a profit on the game, and in the light of that profit, reduced the price of the PS3s to £224.98**.**

197. However, Mr Sherry's evidence provided an alternative, and in our view more credible, explanation, which we accepted:

(1) although CentreSoft *sold* PS3s for £226.61, it had *purchased* them from Sony UK at £205.43;

(2) Dixons was one of the large retailers supplied directly by Sony UK (see §139), so would have been able to purchase PS3s for around the same price, and certainly for less than the £224.98 in the Equanet email;

(3) Equanet obtained occasional surplus stock from Dixons, and could therefore have acquired that stock for less than the £224.98 at which it was offering to sell this limited number of PS3s.

198. In other words, the PS3s being offered by Equanet were surplus Dixons stock being offered at above cost price but slightly below CentreSoft's normal trade price of £226.61. The Equanet email therefore does not demonstrate the existence of a commercial market in split bundles.

The Pixmania screenprint

199. The second piece of documentary evidence relied on by EDC was a screenprint of an internet offer from Pixmania, offering to sell a 320GB PS3 console for £245 including VAT, together with a game called Pro-Evolution Soccer ("PES") 2012. Mr Gara said that PES games were manufactured by a third party for Sony and sold together with a console as a hard bundle; this was accepted by Mr Frain-Bell and Mr Chhatwal in the course of the hearing. It was common ground that new versions of PES came out each year, as the members of the real-life football teams changed.

200. EDC's position was that the PS3 in the Equanet email must have been part of a split soft bundle, because £245 was "considerably lower" than the 2010-11 retail price for a 320GB PS3, which was £271.93 (£226.61 + 20% VAT). We did not accept this, for the following reasons:

(1) as Mr Frain-Bell accepted in the course of the hearing, the Pixmania offer was for a hard bundle, in other words, a single box which contained both the PS3 and the PES2012 game. Thus, for EDC's submission to be correct, the PS3 would have to have been split from a soft bundle, and then repackaged in a single box with the PES2012 game, to make the hard bundle on offer here. Not only did EDC not put forward any evidence to that effect, it was not credible that Pixmania would seek to create its own hard bundle, given that the market was familiar with the hard bundle manufactured for Sony;

(2) although the Pixmania screenprint was not dated, other material from Pixmania exhibited by Mr Chhatwal was downloaded on 27 March 2013, and Mr Chhatwal confirmed that the Pixmania screenprint was taken when he was preparing his witness statement (which was signed on 28 November 2014);

(3) Mr Gara's unchallenged evidence was that the price of PS3 fell over time, beginning at around £350 and ending at around £99. The price of a PS3 would therefore have been lower in 2013 (and in 2014) than in 2010-11;

(4) Mr Chhatwal said that PES2012 came out during 2012, and was replaced during 2013. He accepted that PES2012 would have had "a limited shelf-life" by March 2013. We find that it was a platinum game by that date, and would have been of even less value by November 2014; and

(5) careful examination of the Pixmania screenprint showed that the offer was marked as "clearance".

201. We find that the Pixmania screenprint is an advert for a hard bundle made up of a console and a platinum game packaged together, which was being sold cheaply to clear Pixmania's stocks of that hard bundle. It does not provide evidence that a commercial market in split bundles existed.

The examples

202. In their letter of 28 March 2013, the Khan Partnership put forward two examples of how a business could make money by purchasing a soft bundle, and selling the parts separately. The first example is based on the sale of a PS3 160GB plus the following games/accessories:

Non-console bundle elements	**Buys**	**Sells (worst case)**	**RRP (excl VAT)**	**Sells 80% RRP**
Sniper Ghost Warrior	£16.00	£18	£24.99	£19.99
Shift 2 Unleashed	£20.25	£23	£33.33	£26.66
Lego Star Wars III Clone Wars	£19.00	£23	£33.33	£26.66
Tiger Woods	£20.25	£25	£37.49	£29.99
Yakusa 4	£19.65	£23	£33.33	£26.66
PS3 Wireless Keypad	£9.15	£12	£20.83	£16.66
TOTALS	£104.30	£124		£146.63
MARGIN		£19.70		£42.33

203. The information in the example was derived as follows:

(1) the list of games and accessories, and the prices in the "buys" column were taken from an email dated 12 May 2011 sent by Ms Revell of CentreSoft to EDC. This was around the end of the period during which the disputed transactions took place. The email contained a soft bundle offer made up of a Sony 160GB console, plus the games and accessories in the example, at the prices there set out;

(2) the Recommended Retail Price ("RRP") figures were taken from an email sent by Mr Chhatwal to the Khan Partnership on 11 March 2013, in which the

RRP was given including VAT. The example has netted those figures down at 17.5% instead of the correct 20%, so the figures in the example are too high;

(3) Mr Chhatwal said at the hearing that:

(a) the RRP figures were derived from "from my knowledge and from my memory" as at 11 March 2013, when he sent the email to the Khan Partnership; and

(b) the same was true of the "worst case" figures;

(4) the 80% of RRP columns are calculated; the 80% was Mr Chhatwal's own estimate of a possible price at which the component parts of a bundle might be sold.

204. Although Mr Chhatwal did not identify the basis for the second example, it seems to the Tribunal to have been based on an email received from Ms Revell on 16 June 2011, after the last of the disputed transactions. In the email she offered to sell EDC a soft bundle made up of a PS3 320GB console, with a free Move Starter Pack and a free "Move Heroes" game; two further games and a wireless keypad at a discounted price. The "buys" column totalled £43.15; the "worst case" column totalled £92.99 with a margin of £49.84, and the "80% of RRP" column totalled £103.31 with a margin of £60.16.

205. EDC's case was that if a trader accepted one of these soft bundles, and split off the games, he could make a profit of at least the amounts shown in the "worst case" columns, and that it was more likely that he would make the profit shown in the "80% of RRP" columns. The availability of those profits would allow the consoles to be sold at a discounted price.

206. We find as follows:

(1) the profit margins in the examples lack any sort of independent support. We note in particular that:

(a) the RRP prices are derived from Mr Chhatwal's memory, some two years after the disputed transactions took place, and we have found his evidence to lack credibility;

(b) in transposing those RRP figures from Mr Chhatwal's email to the examples, the VAT was wrongly calculated, so those RRP figures are in any event overstated for that reason;

(c) although we have no specific information on whether any of the games were "platinum" games, we have made the general finding, based on other CentreSoft emails, that many of the games included in soft bundle offers were platinum games, so had a lower retail value;

(2) the second soft bundle offer was made after the end of the relevant period, and the first was made at the end of that period; so there is no necessary inference that similar bundles were on offer throughout the relevant period; and

(3) the examples were based on soft bundles offered by CentreSoft, but that company did not supply any of the consoles in these transaction chains (see

§130); the Tribunal had no evidence about the bundles on offer from EU distributors, so we had not basis on which to find that similar bundles, at similar prices, were available from those distributors; and

(4) even if the "RRP" and "buy" figures were in fact correct (and we make no finding to that effect), so that a profit could be made by splitting bundles and selling the games and accessories separately from the PS3s, it does not follow that bundle-splitting actually happened. In other words, these theoretical examples do not provide evidence of a commercial marketplace in which bundles were routinely split, with the consoles being sold separately from the games.

Deal chains B, O and S1

207. Three of the deal chains – B, O and S1 – began with an identified soft bundle, which was split part way through the chain, before the consoles were purchased by EDC.

208. Deals O and S1 had the same defaulter, JK Distribution Ltd ("JKD"). They also had the same number and type of goods, and the same companies participated in the deal chain, which was as set out below:

Company	**purchase price**	**sale price**	**profit**
JKD	unknown	£204.47	unknown
General Online Services	£204.47	£204.97	£0.50
Northwell UK Ltd	£204.97	£205.47	£0.50
CBR Consultancy Ltd	£204.47	£206.50	£2.03
Electro	£206.50	£204.50	£(2.00)

209. In both Deals, JKD sold 1,000 soft bundles made up of (a) PS3 320GB consoles, and (b) a game called Killzone 3, to the next company in the chain, and passed the bundle down the chain until it reached Electro, which sold the consoles (without the game) to EDC. The consoles in Deal O were EU specification, and we find on the balance of probabilities that the consoles in Deal S1 were also EU specification, given the otherwise identical nature of the two Deals.

210. We find that those Deals provide no evidence that there was a genuine market in split soft bundles, for the following reasons:

(1) Officer McCullough gave unchallenged evidence about JKD. The company's only director was a Mr Katumba. On 14 April 2011, shortly before these Deals took place, Mr Katumba was awarded income support on the basis that he was unemployed and unable to work; he had previously been on incapacity benefit. JK was registered as operating from Mr Katumba's home address, a residential house divided into flats. Two HMRC officers visited him at that address, and identified that the rooms in the flat were sublet. The officers found Mr Katumba to be "confused" and "often incomprehensible".

(2) Sony UK sold soft bundles to CentreSoft, its authorised UK distributor, for £205.43. Other EU authorised distributors sold soft bundles for similar prices, because Sony sought to manage pricing of the same goods across Europe, so they were in line, see §89.

(3) JKD sold the bundles to General Online Services for £204.47, less than the price charged by Sony to its authorised distributors. It is not remotely credible that JK, a company set up by Mr Katumba and operating from a single room in a residential flat, could purchase these bundles for a price lower than that charged by Sony to its authorised distributors.

(4) It is EDC's case that wholesalers purchased soft bundles from authorised distributors and split them to sell the console and the game separately, and so make a profit. But JK did not do that. Instead, it sold the entire bundle for a profit of only 50p, to the next company in the chain. That company on sold it for the same tiny profit, and the third company made only £2.03. That is inconsistent with EDC's own case as to how the supposed commercial market in soft bundle splitting operated.

211. Deal B also began with a split soft bundle. As noted earlier in this decision, this was a contra-trade, in which Intekx Ltd was the contra-trader. The deal chain is set out below:

Company	purchase price	sale price	profit
Recette	unknown	£213.46	unknown
Biznesa Meistars SIA	£213.46	£213.89	£0.43
Intekx Ltd	£213.89	£214.21	£0.32
Refill Ink Centre Ltd	£214.21	£215.38	£1.17
Gemini Technology Ltd	£215.38	£187.50	£(27.88)

212. Recette Ltd ("Recette") sold 3,100 soft bundles made up of (a) PS3 UK specification 320GB consoles and (b) a game called Gran Turismo 5, to the next company in the chain, and so on, until it reached Gemini Technology Ltd ("Gemini"). Gemini sold 500 PS3s to a company called Impact Technologies Ltd for £187.50, £27.88 less than the price at which it purchased the bundle.

213. We find that Deal B also does not provide evidence that there is a genuine market in split soft bundles, because:

(1) Recette cannot have purchased the soft bundle from CentreSoft, as it was prepared to sell the bundle for £213.46, which is £13.15 less than it would have had to pay CentreSoft to purchase the bundle. That the bundle did not originate from CentreSoft was also confirmed by the unchallenged evidence of HMRC's investigating officers. By the time of the hearing, EDC had accepted this was the case.

(2) Recette cannot have purchased the bundles from an authorised distributor overseas, because the consoles were UK specification.

(3) Recette cannot have purchased the bundles from Sony UK, because it does not supply smaller wholesalers, see §135.

(4) Sony UK does directly supply certain major retail chains in the UK, such as Dixons. However, Recette did not purchase the bundles from a large UK retailer because:

(a) there is no evidence that the few large retailers supplied directly by Sony UK were selling those bundles to wholesalers, let alone that they were doing so for less than CentreSoft's wholesale price;

(b) the only relevant evidence is Equanet's email discussed at §195 above, which shows that it had just over 500 consoles (not bundles) for £224.98, i.e., £1.63 below CentreSoft's price of £226.61. Equanet therefore offered to sell this limited number of consoles for £11.52 more than the price at which Recette sold the bundle.

(5) Furthermore, as stated above in relation to Deals O and S1, it is EDC's case that wholesalers purchased soft bundles to split them and make a profit from selling the console and the game separately. Like JK, Recette did not do that. Instead, it sold the entire bundle for a profit of only 43p to the next company in the chain, Biznesa Meistars SIA, which is registered in Latvia. That company on-sold it for an even smaller profit of 32p, and the third company made only £1.17. This is not consistent with EDC's own case about how the supposed commercial market in soft bundle splitting operated how

214. We therefore find that the bundles in Deals B, O and S1 do not provide reliable evidence that there was a genuine market in splitting soft bundles.

215. Mr Watkinson submitted that the only feasible explanation as to how these and other goods had entered the deal chains was that they had been purchased by the fraudsters and then circulated repeatedly as the component parts of a carousel. However, it is not necessary for us to make specific findings as to how the companies at the top of the deal chains acquired the goods. We make only the limited finding that the goods were purchased in order to enable the fraud.

The prices of the consoles

216. EDC's suppliers sold 160GB consoles for as little as £178 (Deal M) and 320GB consoles for as little as £197 (Deal C). Those prices are 10% and 13% less than CentreSoft's wholesale prices of £198.79 and £226.61 respectively.

217. Mr Watkinson submitted that if, contrary to his submissions, there was a market in splitting and selling soft bundles, it would operate on the basis of undercutting the authorised distributor: there was no commercial reason why the bundle splitter would reduce his profits by selling the consoles so far below that established market price. This was exactly what had happened when Equanet offered to sell the consoles which it sourced from Dixons. We agree with Mr Watkinson that these steep discounts are inconsistent with the existence of a commercial market for split soft bundles.

Witness evidence about EDC's own practice

218. Mr Chhatwal was asked if EDC had ever split a bundle. He said that EDC sometimes had to supply a console as part of its insurance replacement business – i.e., the customer was entitled to a new PS3 under its insurance policy, and if EDC acquired the PS3 with a free game, it would provide the console to the customer, but there was no need to supply the free game as well, because the customer was only entitled to a replacement PS3. The Tribunal then asked:

> "…if there was so much profit in this, could you not have taken these bundles yourself, and then sold the games in one direction, rather than just buying the console and not the game."

219. Mr Chhatwal's response was:

> "I didn't have a market for them. I didn't have contacts in software side to sell huge volumes of peripherals and software. That wasn't my field. My field was to sell consumer electronics."

220. However, in Deal T, the last of the disputed transactions, EDC purchased a soft bundle from Zippy, consisting of EU specification PS3s together with Move Starter Packs. EDC sold the PS3s to Anovo. For the reasons explained at §444ff, we are able to make only very limited findings about what happened to the Move Starter Packs.

221. When making submissions about whether there was a commercial market in splitting soft bundles, neither party referred to EDC's splitting of the Deal T soft bundle, but we nevertheless thought we should not disregard it. However, we find that the split which occurred in Deal T was a one-off transaction and not indicative of a market in split soft bundles because Mr Chhatwal himself said that EDC only split soft bundles in situations where the customer required the PS3 as an insurance replacement, and made no reference to having split the bundle in Deal T.

Witness evidence about market practice

222. The Tribunal also had the following witness evidence about whether there was a market in split soft bundles:

(1) Mr Chhatwal said in his witness statement that he "was aware other retailers were often buying the soft bundles offered by CentreSoft, splitting the bundles and then selling the elements of the bundle at a discounted price"; that "Electro Centre advised me on numerous occasions that it was acquiring and splitting soft bundles"; and that "RLR told us that they were purchasing soft bundles, splitting the bundles, achieving a higher margin on the games and was accordingly able to offer EDC the consoles at a lower price".

(2) He also said "I only purchased stock because it made commercial sense. I would refer to the individual components of the soft bundles to ascertain this". However, when this was put to him in cross-examination**,** he changed his evidence, saying he did not know which games or peripherals had been removed from the soft bundles before the PS3s were sold to EDC.

(3) Mr Sherry was asked in cross-examination whether he knew that wholesalers were splitting soft bundles, and stated categorically that he did not. He was then asked whether CentreSoft turned a blind eye to the practice, and he denied this was the position.

(4) Mr Gara similarly denied that there was any such market, saying that "the custom and practice in the industry was soft bundling worked", and that the whole bundle "went to end consumers".

223. Mr Sherry, an honest and credible witness who has been working for CentreSoft since 1996, had no knowledge of this market, and neither did Mr Gara, who had been Managing Director of Sony UK for four years. Mr Chhatwal himself knew nothing about the make-up of any soft bundles involved in the Deals, and when EDC routinely split bundles, this was not to feed the parts of that bundle into the market place, but because there was no commercial need to supply its insurance customers with the free games/ accessories.

224. We find that none of the witness evidence before the Tribunal supports the existence of a commercial market in which soft bundles were split and the component parts sold separately.

Summary of our assessment of the evidence

225. We here summarise our assessment of the evidence set out above:

(1) Only two pieces of independent documentary evidence were put forward by EDC, one from Equanet and one from Pixmania. There is an entirely credible alternative explanation for the first, and the second does not support EDC's case, for the reasons explained at §200.

(2) The Deals themselves do not provide reliable evidence of a market in split bundles, for the reasons set out at §207ff in relation to Deals B, O and S1, and more generally because prices paid by EDC for its consoles are far below those which would have been charged in such a market, see §217.

(3) The only other evidence in support of such a market was that of Mr Chhatwal himself, whom we have found to lack credibility, see §27ff.

(4) Had there been a market in split soft bundles, we would have expected Mr Sherry and Mr Gara to have been aware of that market.

(5) The only reliable evidence of bundle-splitting arose in cases where EDC obtained a soft bundle, but did not need to supply the insurance claimants with the free game. These were occasional, one-off transactions, insufficient to sustain a market, and entirely different in origin from the profit-driven market postulated by Mr Chhatwal. Moreover, Mr Chhatwal did not say that he then sold those free games to a third party, and we infer he sold them in EDC's retail shops. We accept that there may have been other one-off examples of a bundle being split, such as Deal T, but there was no evidence of an organised, commercial, profit-driven market in split bundles.

Adverse inference from failure to call suppliers and/or customers?

226. The case law on adverse inferences was summarised at §35ff. HMRC invited the Tribunal to make an adverse inference from Mr Chhatwal's failure to call any of his suppliers and customers to support his case that the PS3s were derived from split soft bundles, see §45.

227. In deciding whether or not to make that inference, we have set out in italics the first three questions posed in *British Airways*, followed by our responses. The fourth question is answered at §232 below.

(1) *Is there some evidence, however weak, to support the suggested inference or finding on the matter in issue?* Mr Sherry's evidence is sufficient to support an inference that EDC called no witnesses to give evidence on this issue, because there is no commercial market in split soft bundles.

(2) *Has [the Appellant] given a reason for the witness's absence from the hearing?* As we said at §32, Mr Chhatwal stated that EDC was not calling the suppliers or customers involved in the disputed transactions because:

(a) it had now been five years since EDC had ceased business, and he no longer had any relationship with them;

(b) he had "no reason" to remain in contact with them after his business ceased; and

(c) he had "lost confidence and no longer wanted to be involved in the business any more" as the result of this investigation.

(3) *If a reason for the absence is given but it is not wholly satisfactory, is that reason 'some credible explanation' so that the potentially detrimental effect of the absence of the witness is reduced or nullified?* We find that none of the reasons is credible because:

(a) Mr Chhatwal was fully aware, at least by February 2013, that evidence from EDC's suppliers and customers would be relevant to EDC's case, see §33-34, and the company did not cease business until June 2013;

(b) he had every reason to stay in contact with his suppliers and customers, because HMRC were refusing to repay the VAT which EDC had paid on the transactions EDC had entered into with those parties; and

(c) Mr Chhatwal had the confidence to make and then to pursue EDC's appeal; the witnesses relate to his evidence in that appeal, not to EDC's continuing business.

Adverse inference from failure to provide other evidence?

228. It was common ground that there was a greater profit margin on the sale of games compared to the sale of consoles. Mr Watkinson said, and we agree, that if the market postulated by Mr Chhatwal actually existed, the purchaser of the soft bundle would have to sell the games first, because it was only then that he would know by how much he could reduce the price of the consoles.

229. However, the Tribunal was not provided with a single invoice or other document to support EDC's case that there was a commercial market in the purchase and sale of games which had been split from a soft bundle. In Mr Watkinson's words "there is not a single invoice in any of these 37 files [prepared for the hearing] showing games or other peripherals being sold on out of soft bundles to show that this actually happened"; and the Tribunal was not provided with witness evidence from anyone involved in the purchase and/or sale of the games which had originated from a split soft bundle. EDC also did not provide witness evidence from any person who had purchased or sold the console element of a split bundle, or from any person (other than Mr Chhatwal) who had split a bundle and sold the console and the game(s)/accessory to separate customers.

230. Earlier in this decision we set out three essential preconditions which must be satisfied before a court or tribunal can draw an adverse inference, see *CCA* at [66]:

> "(1) the party seeking the benefit of the inference must have adduced some evidence which shows there is a case for the other party to answer; (2) there must be a reason to expect that material evidence exists; (3) it is open to the party who resists the adverse inference to give a credible explanation, even a not wholly satisfactory explanation, as to why the evidence was not given."

231. These are essentially similar to the tests in *British Airways,* which were based on the same underlying case law, but formulated in relation to witness evidence only. Applying the *CCA* requirements to the evidential gaps summarised above:

(1) neither Mr Sherry nor Mr Gara had any knowledge of a commercial market in which Sony soft bundles were split with the separate parts sold separately. Yet the existence of that market was a fundamental part of Mr Chhatwal's explanation for the disputed transactions, so EDC clearly have a case to answer;

(2) if, as Mr Chhatwal said, there was a commercial market in split bundles, it must have involved numerous buyers and sellers, who could have evidenced its existence; this includes those who bought and sold the games which had been split off from the consoles and sold separately. In other words, if there was such a market, material evidence would exist; and

(3) Mr Chhatwal gave no explanation as to why he did not put forward any such person as a witness, or why he did not provide any documents which showed the games being bought or sold.

Drawing the inferences

232. The fourth and final question posed by *British Airways* was whether the Tribunal was "willing to draw an adverse inference in relation to these absent witnesses?" We are willing to draw the inference that the reason why (a) EDC failed to call any customer or supplier to give evidence on this issue; (b) did not call any other witness who had bought or sold any part of a split bundle; and (c) did not provide any documents relating to any sales or purchases of games derived from a split bundle, was because no commercial market in split bundles existed.

233. We have not come to that conclusion automatically, simply because the witnesses were not called, or the documents not provided, but have taken into account "other matters such as what [we] consider to be the most probable finding to make on the basis of all the evidence", in accordance with Morgan J's guidance at [146], see §41. In our judgment, making that inference is consistent with the other evidence considered above.

Conclusion: no commercial market in split bundles

234. We therefore find as a fact, having considered all the evidence and made adverse inferences from the lack of certain evidence, that there was no commercial market in which soft bundles were split, with the consoles and games/accessories sold separately. We consider at §548ff whether Mr Chhatwal knew this was the position.

PART 5: THE SUPPLIERS AND CUSTOMERS

235. In this part of our decision we make findings about the suppliers and customers involved in the disputed transactions, and about EDC's due diligence on each. Some of these findings are taken from our detailed analysis at Part 6 of this decision.

236. In assessing whether Mr Chhatwal knew, or should have known, that any of the suppliers or customers were not reliable trading partners, our starting point is that Mr Chhatwal had a good knowledge of the risk of MTIC fraud, and knew what he should have been doing to avoid it, see our findings of fact at §126. For the reasons set out below, we decided that:

(1) Mr Chhatwal knew some of the suppliers and customers were not reliable trading partners.

(2) he knew or should have known that others were not reliable trading partners, and

(3) in relation to one of his suppliers, and two of his customers, it was not possible for him to infer, merely from their involvement in the disputed transactions, that they were connected to fraud.

237. However, these conclusions are only part of the picture. In order to decide whether all the disputed transactions were connected to fraud, we must consider the totality of the evidence, see *Davis & Dann* at [60] and *CCA* at [46].

The suppliers

238. Three suppliers were involved in the disputed transactions, Electro, RLR and Zippy. Electro was the supplier in eight Deals (A, E, F, G, H, N, O and R). RLR was the supplier in six (B, C, I, J, Q and S) and Zippy was the supplier in the remaining six (D, K, L, M, P and T).

Electro

239. Electro was an independent retailer trading from a shop on Soho Road in the Handsworth area of Birmingham. It was an authorised dealer for well-known companies such as Samsung, CentreSoft, Hotpoint and Bosch. It had a credit limit of

£30,000 with CentreSoft, and in the three years from 2009 to 2011 had purchased goods of £1.6m from that company.

240. Electro was owned by Mr Munir Ahmad, whom Mr Chhatwal had known for over twenty years before the disputed transactions. In 2012, so after the disputed transactions, Electro took fifth place in the "internet retailer" category of the annual "retailer of the year" awards, having been nominated by its customers. Electro went into administration on 19 July 2013 and the administrator, Deloitte LLP, told HMRC that they considered Electro's VAT returns to be inaccurate.

241. In the period before the disputed transactions, Electro's supplies to EDC were as follows:

(1) in the last three months of 2009, Electro sold EDC £1m of consoles. Most were Nintendo, but sales also included 1,178 120GB PS3s at a total cost of £227,569; of these, 953 were sold on two consecutive days, 5 and 6 October 2009; a further 200 consoles were sold in a single deal on 11 November 2009 for £40,800. Electro also sold EDC other goods worth £405,188 in total; and

(2) in the first three months of 2010, Electro sold EDC consoles worth £188,664, of which only 150 were PS3s; it also sold EDC other goods worth £40,467.

242. EDC checked Electro's VRN with Europa on 28 July 2011, after the last of the disputed transactions. It also received an undated letter of introduction; Mr Chhatwal could not remember when this had been provided.

243. Mr Frain-Bell submitted that, given the companies' previous trading relationship, Electro's status as an authorised distributor for CentreSoft, and its good reputation, which remained intact until long after the disputed transactions had been concluded, there was no basis for EDC to think that Electro was not a reliable trading partner.

244. Mr Watkinson relied on the difference between (a) the volume and value of consoles being supplied by Electro in the disputed transactions, and (b) those it had previously sold to EDC. For example, Deal H alone involved consoles which cost £419,375, plus VAT of £83,875. Mr Watkinson said that:

(1) this single invoice exceeded the value of EDC's entire trade with Electro in 2010;

(2) Electro could not have funded such a huge deal, because no lender would have given credit on this scale to Mr Ahmad. Electro was, he said, not another Amazon, but a business run from a shop in Birmingham;

(3) Mr Chhatwal did not ask how Electro was able to fund the volume of deals, had he done so, it would have been obvious it was not commercially possible; and

(4) one of the questions in Notice 726 is whether the supplier is providing a credible amount of stock, and that is not the case here.

245. Mr Watkinson is right that the volume of consoles involved in the Deals was significantly greater than in previous transactions, both on an individual deal basis and in total. However, EDC had made large purchases from Electro before the disputed transactions: it had bought 953 consoles over two days in 2009, which was not very different from the 1,000 consoles in Deal H.

246. As Mr Frain-Bell said, Electro was both a well-known company, and an authorised distributor for CentreSoft, and these were both relevant factors. We decided that it was not possible to infer, simply from the increased volumes of consoles being supplied by Electro, that Mr Chhatwal knew or should have known that it was not a reliable trading partner.

RLR

247. RLR was a small company which begun operating around a year before it entered into the disputed transactions with EDC. EDC verified RLR's VAT registration with HMRC on 2 July 2010. RLR was owned by Mr Pavan Uchil, who had previously been a bank manager. Mr Chhatwal's father had met Mr Uchil in 2009 or early 2010 and Mr Uchil had visited EDC's warehouse. In an undated letter of introduction exhibited by Mr Chhatwal, RLR describes itself as "recently established in January 2010" as a "wholesaler and retailer of a variety of electronic goods for all major platforms".

248. In his witness statement, Mr Chhatwal stated that:

> "I considered RLR to be a secondary channel by which to source goods…I would first exhaust all direct channels of sourcing goods (from the manufacturers themselves) before relying on secondary channels."

249. He also said he had relied on "word of mouth" recommendations to establish that RLR was a reliable trading partner, but did not provide any information about who had provided those references. He carried out no financial due diligence on RLR.

250. In oral evidence, Mr Chhatwal said he had spoken to Mr Uchil about his background in the trade, but when asked by Mr Watkinson whether he knew that Mr Uchil had only recently been a bank manager, and so had no relevant background in wholesaling electronic goods, Mr Chhatwal avoided replying, saying only "I met him at trade shows".

251. Mr Watkinson also asked him why RLR, which had "only been established for a year by a man with no experience in the industry" could have got better prices for PS3s than Mr Chhatwal, who had been in the electronics business for 20 years. Mr Chhatwal's response was that Mr Uchil "may have had relationships with suppliers, such as Electro Centre or those elsewhere in the country where stock allocation was higher, which allowed him to access better deals than EDC".

252. We considered the volume of stock EDC purchased from RLR, compared to that purchased from CentreSoft, Sony's authorised distributor. In 2008 and 2009,

EDC's largest single purchases from CentreSoft of an earlier version of the PS3 were for 500 and 670 consoles respectively, see §141; other purchases ranged from single units to 30, 40, 50, 100 or 500 consoles, and that in 2010 its largest purchase was for 250 units. Although EDC bought 1,200 soft bundles from CentreSoft in 2011, that was very unusual. Against that background, the volumes purchased from RLR are significant: 500 consoles in Deal B and a further 115 ten days later in Deal C; 300 consoles in Deal I and 1,000 more just over a week later in Deal J, with 496 and 800 being supplied in Deals Q and S.

253. We find that EDC had no reasonable basis for believing that RLR was a reliable trading partner, and that Mr Chhatwal knew or should have known that this was the case, because:

(1) he should have asked himself why RLR "a brand new business" could obtain the consoles more cheaply than EDC, a long-established business, and the answer to that question would have identified the significant risk that the consoles did not have a legitimate source;

(2) his response to Mr Watkinson's similar question was speculative: he said "Mr Uchil *may have had* relationships with suppliers…which allowed him to access better deals than EDC". Either he had not asked that question previously, but should have done, or he knew that giving a true answer would not assist him;

(3) his response was also not credible: there were no uneven stock allocations, see §155, and given Mr Chhatwal's experience in the industry, he knew this was the case;

(4) Mr Chhatwal therefore had no good reason for believing RLR could have had legitimate access to such significantly better prices than EDC;

(5) CentreSoft had sufficient stock to supply EDC with PS3s during the relevant period, see §160, and EDC therefore did not "exhaust all direct channels of sourcing goods" before entering into the disputed transactions with RLR, as Mr Chhatwal said was the position; and

(6) Notice 726 identifies, as an MTIC indicator, situations where "a brand new business obtain[s] specified goods cheaper than a long established one", see §106. The volume of consoles purchased from RLR exceeded that bought from CentreSoft, the authorised distributor, and Mr Chhatwal knew or should have known that those stock volumes were not credible, given RLR's small size and lack of established trading history.

Zippy

254. Zippy was a sole trader business operated by Mr Mathew Anness. Mr Anness had previously been the director of a company called Clogs Limited, which went into creditors' voluntary liquidation; he was subsequently disqualified from being a director for six years, from 3 September 2002**.**

255. On 20 September 2005, Mr Anness registered for VAT under the trading name Zippy Distribution; its business activity was stated to be "computer software sales". In Mr Chhatwal's first witness statement he said:

> "I found Mr Matthew Anness, the Director of Zippy Distribution, to be knowledgeable…I had looked at Zippy Distribution on Companies House, however I did not see any evidence of his disqualification."

256. After receiving Mr Ginn's first witness statement, which pointed out that Mr Anness was operating as a sole trader and not as the director of a company called Zippy Distribution, Mr Chhatwal changed his evidence. In his second witness statement he said that calling Mr Anness a "director" of Zippy Distribution was "inexact language", and he had meant to write "I had looked at Mr Anness on Companies House" instead of "I had looked at Zippy Distribution on Companies House". He said that the wording in the first witness statement was simply a "typographic error". Mr Watkinson challenged this in cross-examination**,** saying:

> "This is just made up, isn't it, Mr Chhatwal? You didn't look at anything on Companies House about Zippy or Mr Anness did you?"

257. Mr Chhatwal said he did "verify Mr Anness" but when asked if this was on Companies House, he said only "whatever verification we did, we did check him out".

258. Attached as an exhibit to Mr Ginn's second witness statement were details from Companies House website for a company called "Zippy Distribution Ltd" which was dissolved on 27 November 2007.

259. Taking all the above into account, including Mr Chhatwal's refusal to give a direct answer to Mr Watkinson's question, we find as facts that:

(1) Mr Chhatwal did not check Zippy's status on Companies House, because had he done so, he would have seen that the only company called Zippy Distribution had been dissolved in 2007, years before EDC began trading with Mr Anness.

(2) Mr Chhatwal's amended position, that he knew Zippy was not a company but had nevertheless checked Mr Anness on the Companies House website, is also untrue. Companies House does not hold information about sole traders, so Mr Chhatwal would have had no reason to access that site to check Mr Anness.

260. Mr Chhatwal provided the following evidence in support of EDC's position that it had carried out appropriate due diligence on Zippy:

(1) an undated and unaddressed letter of introduction, which states that Zippy "has been trading in a broad range of IT and consumer related products for many years";

(2) a VAT certificate stating that Zippy's trade was <u>retailing</u> computers, peripherals and software (emphasis added);

(3) website screenshots, in which Zippy stated that it had been "retailing online for over 5 years" and that it was "a reseller of TVs by Samsung and LG Electronics";

(4) a VRN validation with Europa carried out on 28 July 2011 and a validation with HMRC on 26 August 2011, both after the disputed transactions;

(5) Zippy's bank account details; and

(6) an undated application by EDC for £100,000 of credit with Zippy.

261. Mr Chhatwal accepted under cross-examination that he did not carry out any financial checks on Zippy**.** He said this was because he had been introduced to Zippy by sales representatives from LG, a South Korean company, and they told him LG supplied goods to Zippy, and that it was a wholesaler. Mr Chhatwal said he had made "other enquiries", and from the responses understood that Zippy supplied many well-known people and companies in the industry, including Mr Richer of Richer Sounds; he said he also knew that Zippy "sat within LG's wholesale distribution channel rather than the independent retail distribution channel".

262. We find that EDC had no reasonable basis for believing that Zippy was a reliable trading partner, and that Mr Chhatwal knew this was the case, because:

(1) Mr Chhatwal's statements about having checked Companies House were untrue;

(2) his the due diligence was inadequate, consisting of a VRN check after the transactions took place, and other documents/screenshots which did not support the existence of a wholesale business;

(3) when applying for its VAT certificate, Zippy described itself as an online retailer, and there is no reference in its website to it operating in the wholesale marketplace, yet Mr Chhatwal entered into six wholesale Deals with Zippy for PS3s, TVs and iPods, see Part 6;

(4) EDC did not provide any third party witness evidence or other documents to support Mr Chhatwal's statements about having relied on (unnamed) LG sales representatives and unspecified "well-known people" in relation to Zippy's credentials, or its status as a distributor, and we find that this is because no such recommendations were made;

(5) Mr Chhatwal did not ask himself whether Zippy was providing a credible amount of stock, see Notice 726 referred to above;

(6) Mr Chhatwal had no good reason for believing that Zippy, a sole trader with no wholesale experience, could have had access to significantly better prices than EDC; and

(7) EDC carried out no financial due diligence on Zippy, yet entered into six Deals, two of which were for around £100,000, see the summary at §558.

The customers

263. The following seven companies were the customers for all but one of the Deals. We were unable to make a finding as to the customer(s) in Deal K, see §395.

Anovo

264. In Deals N, O, R and T, Anovo was the customer. It was a well-established company which provided after-sales repair and support for high tech products to companies. including Samsung and Vodafone.

265. On 14 February 2011, Mr David Cato of Anovo emailed Ms Nina Kahlon at Samsung, heading his email "trading relationship" and saying:

> "Anovo is a global electronics company and the division I am working within is trading most new and referbished [sic] IT commodities, major brand accessories and peripherals, consumer electronic and gaming hardware/software…I am hoping you can direct our email to the trading team focusing on volume trades in televisions and other commodities."

266. Mr Robert Andrews of Samsung forwarded that email to Mr Chhatwal, saying "another little lead 4 u". Mr Chhatwal made contact with Mr Cato, and said in his witness statement:

> "Having myself worked in insurance, and knowing the stringent checks that are carried out on repair companies, I was satisfied; that if large companies such as Samsung and Nokia were instructing Anovo to repair goods that they must be a good, reputable company."

267. Mr Chhatwal also said that he was told by Mr Cato that Anovo had recently become established in the UK, with the aim of expanding its retail business in Europe; that its main purchasing department for that European retail business was in the UK, and that it wanted to buy televisions and home cinema equipment in the UK to export to Europe. Mr Chhatwal gave the following explanation as to why he had decided to trade with Anovo:

> "Given the discussions I had with Mr Cato regarding the nature of Anovo UK's business and due to the fact that the introduction had originally been made by Samsung, EDC was satisfied that Anovo UK was a legitimate customer."

268. EDC held the following documents about Anovo:

(1) an undated, unaddressed and unsigned letter of introduction from Mr Kevin Coleman, Anovo's CEO, which said that the company carried out repair work and had a "trading and recycling" division;

(2) a copy of Anovo's VAT certificate, which gave its trade classification as "repair computers and peripheral equipment";

(3) undated web pages about Anovo, which stated that the company delivered "customised after-sales solutions to market leading technology companies" and

"partners with operators, manufacturers and retailers to provide a full range of logistical and regeneration services". There is no reference to a trade in PS3s;

(4) a VRN application dated 3 August 2011, after all the disputed transactions had taken place. When Mr Watkinson asked Mr Chhatwal why the VRN check was so late, he replied "I'm not sure"; and

(5) a credit application form issued by EDC, completed on 7 April 2011. We noted that:

(a) under "trade reference" the words "Samsung UK" have been inserted, but no contact name is given. Mr Watkinson asked Mr Chhatwal if he had followed up the reference. He initially said "we must have", and then that he didn't know where the documents were; and

(b) against the line which asks "amount of credit required" is written "nil". Mr Watkinson asked Mr Chhatwal if this was "a joke", given that the stated purpose of the form was to apply for credit. Mr Chhatwal said that Anovo had asked for credit of £1m; that EDC then "researched Anovo", but did not carry out any credit checks, and refused the credit.

269. We find that EDC had no reasonable basis for believing Anovo to be a reliable customer in the PS3 market place, and that Mr Chhatwal knew or should have known this was the case, because:

(1) Samsung simply forwarded to Mr Chhatwal an unsolicited email from Anovo; it provided no assurance as to that company's status or reliability in the context of a trade in PS3s, as Mr Chhatwal accepted in cross-examination;

(2) since (a) there was no Samsung contact name on the credit reference form; (b) Mr Chhatwal knew that Samsung had not endorsed Anovo, and (c) there is no documentary evidence of any follow up with Samsung, we find as a fact that EDC did not take up that trade reference;

(3) the central message of the documents held by EDC was that Anovo's trade was repair and servicing; it is only Mr Cato's mis-spelled email which talks about "trading…gaming consoles";

(4) EDC made no financial checks on Anovo, despite that company both (a) asking for credit of £1m, and (b) completing a credit application asking for credit of £nil; and

(5) EDC did not check Anovo's VRN until long after the Deals had been carried out, and Mr Chhatwal could not explain the reason for the delay.

ARU

270. ARU was the customer in Deals G and H. It was a small company. In his witness statement Mr Chhatwal said he had met Mr Anisur Rahman, the company's sole shareholder and director, around 3-4 months before Deal G, and Mr Rahman had told him ARU regularly traded with the German and Spanish markets, and was interested in buying PS3s and televisions from EDC. That evidence was challenged by HMRC; Mr Watkinson invited us to reject it as unsupported by Mr Rahman or any other evidence.

271. We agree. We noted that when Mr Chhatwal was asked in cross-examination whether he had provided ARU with any documents before beginning to negotiate Deal G, he said "Basically we discussed things on the phone, who we were. He had heard of us". If, as Mr Chhatwal stated was the case in his witness statement, he had already met Mr Rahman some months previously, they would not have discussed "who we were" on the phone, and Mr Chhatwal would not have said "he had heard of us", but rather that they had met previously. There is no documentary evidence to support Mr Chhatwal's statement that he had met Mr Rahman, and there is no reference to that meeting in their email exchanges. We find as a fact that Mr Chhatwal had not met Mr Rahman before deciding to do business with ARU.

272. EDC did not seek to verify ARU's VAT status until after it accepted the first order, see §364 below. EDC exhibited the following:

(1) two documents in Portuguese, a language Mr Chhatwal could not understand**;**

(2) a translated document from the General Directorate of Taxes in Lisbon issued on 24 March 2010, which states that ARU was registered in Portugal but was not tax resident there, and which classified ARU's "main activity" as "CAE 46382 – Trading activity CIRS" and its secondary activity as "retail of equipment". Mr Chhatwal told Mr Watkinson that CAE 46382 meant "trading in commodities";

(3) an undated, unaddressed letter of introduction from Mr Rahman which says that ARU "is an established company which specialises in importing and exporting goods such as electronic goods" and was "based in Lisbon, Portugal";

(4) ARU's contact details and banking information;

(5) a letter from Barclays confirming the company's bank account number; and

(6) an undated copy of Mr Rahman's passport stating that he is a British citizen born in Bangladesh.

273. Mr Chhatwal accepted that EDC had not carried out any financial due diligence on ARU. Mr Watkinson asked Mr Chhatwal whether he had enquired how a company which had been VAT registered for less than a year had the financial wherewithal to carry out a trade for over £170,000 (Deal G), and Mr Chhatwal admitted that he had not asked himself that question**.** We note that Deal G was followed a few days later by Deal H for £236,582, see Part 6.

274. We find that EDC's due diligence was inadequate and that Mr Chhatwal knew ARU was not a reliable trading partner, because:

(1) it was a small company based overseas with which EDC had never previously done business, and about which it had little information;

(2) the information he did possess stated that ARU's trade was commodity trading and retailing, not wholesaling computers; and

(3) he did not make any enquiries as to how ARU had been able to fund the substantial purchases, and carried out no other financial due diligence.

BAK

275. BAK was the customer in Deals F and Q. Mr Chhatwal's evidence was that its director, Mr Sekhon, approached him in 2010 at a trade fair in Berlin, and told him that BAK:

(1) was interested in trading with EDC;

(2) supplied German supermarkets with televisions and electronic goods;

(3) did not trade in "a large quantity of gaming consoles but this was an avenue they were looking at expanding".

276. Mr Chhatwal said he knew BAK was "not a large company, run by 2 or 3 individuals only" but that he had checked its website, which confirmed what Mr Sekhon had told him. No pages from the website were exhibited.

277. Under cross-examination Mr Chhatwal said he had checked BAK's VAT certificate on the Europa website, but had not printed off any documentation to support his statement that this had happened. He did not check BAK's VAT status with HMRC until July 2011, over three months after Deal F, the first of the two Deals.

278. Mr Ginn's unchallenged evidence was that:

(1) BAK operated in the environmental sector, trading and selling cleaning and filter systems in the field of waste disposal, and provided related advice and services in the environmental sector;

(2) BAK had never filed a VAT return, was involved in MTIC transaction chains and traded carbon credits;

(3) the German VAT authorities carried out investigations into BAK in November 2011, and found that:

(a) it had not operated from its registered address since 27 January 2011 (so before any of the Deals between BAK and EDC took place);

(b) the company could not be located after that date; and

(c) it was deregistered with effect from June 2011; and

(4) Mr Sekhon has pleaded guilty to extensive involvement in VAT fraud.

279. In cross-examination Mr Chhatwal agreed that BAK was "a thoroughly fraudulent enterprise" but said he did not realise this at the time, as "there was nothing untoward".

280. We do not agree. We do not accept Mr Chhatwal's evidence that he checked BAK's website, because he has provided no supporting evidence, and because BAK was not trading in electronic goods at all. We find that Mr Chhatwal had no reliable information that BAK was a legitimate trader in games consoles. We also find that

EDC did not check BAK's VAT number before beginning to trade, because there is no paperwork to that effect, and because EDC carried out no other due diligence on BAK.

281. We agree with Mr Ginn that "EDC's behaviour is not that of a legitimate company trying to protect itself from potential fraud within these trade sectors"; that EDC's due diligence was inadequate; that EDC had no reasonable basis for believing that BAK was a reliable trading partner; and that Mr Chhatwal knew this was the case.

Everyberry

282. Everyberry was the customer in Deal A; it sold the goods to Office Depot International Ltd ("Office Depot"), part of a large international group also known as Viking). Mr Chhatwal's evidence was that he was provided with Everyberry's details by Samsung, and added that:

> "The background to Samsung's referral was that Everyberry, a supplier to Viking (one of the UK's leading office suppliers), had written to Samsung on behalf of Viking to request Samsung to supply televisions. However, Samsung would not supply directly to Everyberry/Viking because neither had a retail front. Samsung's representative passed on Everyberry's name to EDC because we had an established retail front."

283. Under cross-examination he said:

> "We worked in partnership with Everyberry. The whole point of the partnership was I was recommended by Samsung to liaise with Everyberry, because they had direct links with the Office Depot CEO. Everyberry was a supplier to Office Depot supplying Chinese lanterns, paper stationery, and the CEO had expressed a desire to increase the turnover at Office Depot, and one of the ways they could see that happening is by introducing high value items like consumer electronics, and that's why they showed an interest in selling Samsung products…But because they didn't have a bricks and mortar presence, Samsung were not prepared to deal with them."

284. Mr Watkinson challenged all of that evidence, and said it was entirely uncorroborated. We agree: Mr Chhatwal has provided no third party evidence to support his statement that Samsung's policy was not to deal with suppliers who had no retail presence, and we have already found as a fact that large manufacturers such as Samsung did supply internet retailers such as Office Depot, see §138.

285. Mr Chhatwal also asserted that Samsung knew that EDC and Everyberry were acting as conduits to Office Depot, an online retailer. However, in our view it was not plausible that Samsung would knowingly undermine its own policy, and this was a further reason why we decided his evidence on this point was not credible.

286. We also find, on the balance of probabilities, that it is unlikely that the CEO of Office Depot would have asked its supplier of Chinese lanterns and paper stationery

to locate and source high value consumer electronics, and that Mr Chhatwal, an experienced trader in those goods, knew this was the position.

287. EDC relied on three items of documentation to demonstrate its due diligence. The first was a letter of introduction from Everyberry, which read:

> "I am writing to you to introduce our company to seek business partnership for promoting electrical and electronic goods in the UK."

288. The bottom of the page contained were the following messages (wording as in original):

> "Everyberry Ltd is a new supply channel for innovative and strongly branded products…for some products we can guarantee prominent sales and promotion positions in catalogues, online stores and in-store displays. For buyers, our direct relationships with the manufacturers help us to ensure a consistent supply of the latest and most sought after products. These products will attract customers, offer up- and cross sale opportunities, drive turnover and add glamour to your product portfolio…I would be glad to see your product offers for our promotions."

289. The eccentric use of English reinforces our conclusion that Everyberry would not be selected as an intermediary by large international businesses such as Samsung or Office Depot. Furthermore, as the letter is dated 25 April 2012, over two years after Deal A, and over nine months after the last of the disputed transactions, it cannot evidence EDC's due diligence in relation to Deal A.

290. The other two documents on which EDC relied on were a certificate of incorporation on change of name dated 20 March 2008, and a VAT certificate stating that Everyberry's trade classification was "agents sale of a variety of goods", effective from 1 July 2008.

291. Mr Ginn's unchallenged evidence was that EDC did not verify Everyberry's VRN with Wigan or with HMRC's National Advice Centre. Mr Chhatwal did not provide evidence that he checked it with the Europa system. We find as a fact that EDC did not check Everyberry's VRN at any point.

292. Having assessed the evidence we find that EDC's due diligence was manifestly inadequate; that Mr Chhatwal had no reasonable basis for believing that Everyberry was a reliable trading partner, and that he knew this was the case.

Ewert

293. Ewert was (and remains) a large internet retailer based in Germany. Mr Chhatwal said he had met Ewert's founders at a conference in 2008; had established that it was a long-established family business, and had subsequently often spoken to the founders on Skype. This evidence was not challenged and we accept it.

294. Mr Chhatwal provided two documents relating to EDC's due diligence on Ewert. The first is a print-out from the Europa website dated 9 October 2008, which

states that the VAT number entered was valid. However, the page does not name the company to which it refers, and neither does it give an address: those entries are blank. It is therefore confirmation that the VAT number checked was valid, but does not demonstrate that it was Ewert's number. The second document is entirely in German, a language which Mr Chhatwal accepted he could not understand.

295. Before the disputed Deals, EDC carried out a number of other sales to Ewert, which have not been challenged by HMRC. And, as already noted earlier in this decision, in August 2008 EDC obtained an insurance proposal from Euler, a credit insurance firm, which was valid for a year. Euler was prepared to insure sales to Ewert of up to £100,000 a year. Mr Watkinson pointed out that this was no longer valid at the date of the disputed transactions, and submitted that EDC therefore had no information entitling it to conclude that Ewert had the financial wherewithal to enter into substantial transactions with EDC.

296. We considered the detailed facts set out at Part 6. Deal B on its own was for £92,500. During February and March 2011, EDC conducted four further Deals in which Ewert was the customer; and there was a further sale (Deal H1), which HMRC identified as being traced to WNL too late to deny the VAT. The Deals in which Ewert was the customer totalled £730,850.

297. Mr Chhatwal sought to explain the large volume of these sales by saying that Ewert was one of a number of online retailers which "had large warehouses but no physical retail presence, and therefore did not have accounts directly with the manufacturers or were in regions with insufficient stock allocation". We reject those explanations because we have already found as facts that (a) Sony supplied internet retailers, and (b) stock shortages were rare, and limited to a product's immediate post-launch period.

298. One of the questions in Notice 726 is whether "the quantities of goods involved appear credible". Within a period of just over six weeks – between 9 February 2011 (Deal B) and 21 March (Deal J) – EDC engaged in trades with Ewert of over seven times the annual credit limit advised by Euler, without making any credit checks.

299. We find that EDC's formal due diligence was lacking, and that the reasons given by Mr Chhatwal to justify the high volume of sales were factually incorrect. However, Ewert was a large reputable company selling consumer electronics, with which EDC had previously traded. We decided that it is not possible to infer, simply from the high values involved in the disputed transactions, that Mr Chhatwal knew or should have known that those Deals were connected to fraud.

Redcoon

300. Redcoon was established in 2003, and was one of the largest internet retailers for electronic goods in Europe. In August 2008, Euler offered to insure sales to Redcoon of up to £350,000. Mr Chhatwal's evidence was that in 2008 he met Mr Andreas Oerter, Redcoon's Managing Director, and Mr Michael Hasentab, who was in charge of Product Management for Brown Goods, and had "maintained a very close relationship with them".

301. Mr Watkinson pointed out that:

(1) neither Mr Oerter nor Mr Hasentab were called as witnesses;

(2) Mr Chhatwal's exhibits include a letter of introduction from Redcoon dated 1 August 2011, after the disputed transactions had taken place; and

(3) EDC validated Redcoon's VAT number on 21 July 2011 with Europa, and with Wigan on 31 August 2011, again after all the disputed transactions**.**

302. However, Redcoon was (and is) a very large international business to which EDC was also making significant sales of other goods. For example, in Deal D the total invoice value was £250,126, of which only £78,800 related to the PS3s traced to a fraudulent transaction chain, see §349**.** We find that it was reasonable for EDC to consider Redcoon to be a reliable trading partner.

XXL

303. XXL was a German company. EDC's position was that it had carried out adequate checks, but these consisted only of the following:

(1) Mr Chhatwal's evidence that he met the company's owners at a conference in Germany in 2008;

(2) a copy of a presentation given by XXL, which says that the company was founded in November 2007 and is "a wholesaler and exporter for consumer electronic [sic]" which carries out import/export; and

(3) some documents in German, which Mr Chhatwal was unable to understand

304. EDC first verified XXL's VAT status with Wigan on 22 August 2011, after all the disputed transactions. It carried out no financial due diligence on the company.

305. Mr Chhatwal knew from Notice 726 and from his meetings with the Officers, that PS3s could be used in MTIC fraud and that he should "make a judgement on the integrity of [his] supply chain and the suppliers, customers and goods within it", see §106. Yet the only evidence Mr Chhatwal had (and could understand) was the copy of a presentation provided by XXL itself. He had no independent evidence whatsoever.

306. We find that EDC's due diligence was inadequate; that Mr Chhatwal had no reasonable basis for believing that XXL was a reliable trading partner, and that he knew or should have known this was the case.

Overall conclusions on suppliers and customers

307. We have therefore found as facts that, in a market which Mr Chhatwal knew to be vitiated by MTIC fraud:

(1) he also knew Zippy, Aru, BAK and Everyberry were not reliable trading partners; and

(2) he knew or should have known that RLR, Anovo and XXL were not reliable trading partners; but

(3) Electro, Ewert or Redcoon were all large companies with which EDC had carried out other legitimate business, and their involvement in the disputed transactions was not, of itself, an indicator of fraud.

308. As set out at the beginning of this Part, those findings are only part of the picture. In order to decide whether Mr Chhatwal knew or should have known that each of the disputed transactions were connected to fraud, we must consider the totality of the evidence, see *Davis & Dann* at [60] and *CCA* at [46].

PART 6: EACH TRANSACTION

309. This part of our decision sets out our findings about each of the disputed transactions. Because both parties accepted that all the Deals were linked to fraud, we have not made findings about the parts of the deal chain which preceded EDC's the acquisition of the goods, unless one or more of those earlier transactions were relied on by one of the parties in relation to an issue which was disputed.

310. But before we made our findings, we first had to decide whether to take Mr Chhatwal's mobile phone records into account as part of the evidence.

The mobile phone records

311. Mr Chhatwal exhibited his mobile phone records, together with a schedule ("the Phone Schedule") which matched the numbers on those records to the names of individuals who worked for the three suppliers and for four of the seven customers. Mr Chhatwal had also annotated the mobile phone records to show which calls had been made to the named individuals.

312. Early in the proceedings, Mr Watkinson advised Mr Frain-Bell that he would be asking Mr Chhatwal, by reference to other documents in the Bundle, to show that the phone numbers had been correctly identified as belonging to particular suppliers and customers. However, Mr Chhatwal did not provide any documentary support for the Phone Schedule, either as part of evidence-in-chief or under cross-examination. Mr Watkinson therefore decided not to cross-examine Mr Chhatwal about his mobile phone records.

313. During re-examination, Mr Frain-Bell guided Mr Chhatwal to certain documents within the Bundle, which provided independent support for four of the numbers on the Phone Schedule. In closing submissions, Mr Frain-Bell asked the Tribunal to accept *all* the numbers on the Phone Schedule as having been correctly identified, and not simply the four numbers which had now been independently supported**,** because the sampling exercise he had carried out with Mr Chhatwal showed that the Schedule was reliable.

314. Mr Watkinson responded by asking the Tribunal to ignore the mobile phone records, because he had made several requests for the evidence linking the names and numbers on the Schedule to documentary support within the Bundle. This had only

been provided during re-examination, and this was too late in the proceedings for him to cross-examine Mr Chhatwal about the records.

315. We considered whether it was in the interests of justice to take the mobile phone records into account, and if so, whether we should accept all the records annotated by Mr Chhatwal, or only those for which independent support had been provided during re-examination. We took into account, in particular, the following:

(1) Mr Watkinson had put EDC on notice at an early stage that he would be challenging the mobile phone records, and that if Mr Chhatwal did not provide support for the numbers on the Phone Schedule, he would not cross-examine him on the detail. As a result, there would be some unfairness to HMRC if we took the phone records into account;

(2) however, the Phone Schedule and the mobile phone records had been included in the Bundle, so were not new evidence; all that was new was the provision of documentary support for the Phone Schedule, namely proof that Mr Chhatwal had correctly identified some of the numbers on the records;

(3) Mr Watkinson made submissions in closing on the phone records, including by reference to numbers other than the four which had been specifically validated by Mr Frain-Bell and Mr Chhatwal, so he had not ignored that evidence; and

(4) part of EDC's case was that there had been telephone contact between Mr Chhatwal and the parties, so refusing to take the records into account would weaken EDC's position.

316. We decided that it was in the interests of justice to take the phone records into account. However, we disregarded any call which lasted for five seconds or less, on the basis that no substantive information can have been transmitted; we have also only considered those records which have been identified by Mr Chhatwal as having been made to one of his suppliers or customers; we have not sought to match the numbers ourselves.

Deal A

317. In Deal A, EDC was a buffer. Electro supplied it with 400 soft bundles consisting of UK specification PS3s together with Move Starter Packs (see §132). EDC sold the soft bundles to Everyberry in two batches, one of 100 and one of 300, and Everyberry on-sold to Office Depot.

The transaction

318. On 1 November 2010, Mr Chhatwal called Everyberry and spoke for over 10 minutes**.** There were four further calls on 2 November 2010, totalling almost 20 minutes. On 3 November 2010 Mr Chhatwal called Dipesh, who worked at Electro, four times, for a total of around 10 minutes, and had one very short call with Everyberry.

319. On 4 November 2010:

(1) Mr Chhatwal spoke to Everyberry for around a minute, and to Electro for almost 6 minutes;

(2) Electro issued a pro-forma invoice to EDC for 400 soft bundles, made up of 320GB PS3s and Move Starter Packs at £240 each. This was more than CentreSoft's price of £226.61 for the same soft bundle. The total was therefore £96,000, plus VAT of £16,800. The pro-forma invoice states "this is not a VAT invoice", and the "customer order number" has been left blank. A box at the bottom states "please send delivery details anddeposit [sic] payment of £10k today along with the TV's payment thanks." The document has been manually annotated to say "Pd dep £10,000";

(3) a further document was issued to EDC, headed "invoice", but this document is not on Electro's normal invoice stationery and makes no reference to that company, but only to "Dipesh". It does not refer to the deposit. Despite EDC stating that it was a VAT invoice, that is clearly not the case.

320. On 10 November 2010, Electro issued a delivery note which said that there would be a "Drop Off" at EDC. However, the text of the delivery note refers only to "Move starter pac x 400pcs"; it does not refer to the PS3s.

321. On 26 November 2010, EDC invoiced Everyberry for 300 Move Starter Packs at £0.00 and 300 320GB PS3s for £255 each. The total was £76,500 excluding VAT, and £89,889 when VAT at 17.5% was included. No documentation evidenced the delivery of the bundles to Everyberry or to Office Depot.

322. On 9 December 2010, EDC issued Everyberry with a second invoice for the remaining 100 soft bundles**,** together with 200 Samsung televisions. The bundles cost £29,963 including VAT, and the total invoice value, including the televisions and a delivery charge, was £86,539.25.

323. On 10 December 2010, delivery manifests for 100 Move Starter Packs and100 PS3s were stamped by Office Depot as received unchecked.

324. Meanwhile, on 12 November 2010, Everyberry had paid EDC two amounts of £150,000 and £12,656.05**;** EDC say the first of these amounts was in settlement of both invoices. However, the payment was made was two weeks before Everyberry received EDC's invoices, or any other documentation relating to the Deal, and the amount does not match the invoices.

325. The documentation is incomplete in the following respects:

(1) there are no purchase orders from Everyberry to EDC, or from EDC to Electro;

(2) none of the documents state that the consoles are UK specification;

(3) the pro-forma invoice from Electro does not contain an order number;

(4) there is no VAT invoice from Electro;

(5) Electro's delivery note refers only to the Move Starter Packs, not the PS3s; and

(6) there is no delivery record of the first 300 bundles being received by Everyberry or by Office Depot.

The reasons for the Deal

326. In his witness statement, Mr Chhatwal said that EDC's sales of PS3s were part of a promotional offer for Office Depot customers, and that although EDC received payment from Everyberry, the consoles were all delivered to Office Depot's premises. There was no further information. In particular, Mr Chhatwal did not refer in his witness statement to the fact that EDC paid a premium for the goods; he did not provide any explanation for that premium; and he did not refer to the Move Starter Packs in the context of Deal A.

327. Until the hearing, the only references in his witness statements to Move Starter Packs were in other contexts:

(1) In support of his evidence that CentreSoft regularly offered soft bundles to customers, he exhibited:

(a) an email from CentreSoft to EDC dated 18 November 2010, stating that delivery of EDC's order of 1,000 Move Starter Packs had been delayed because CentreSoft had no more stock, and would not have any for the rest of 2010; and

(b) an invoice from CentreSoft for 1,200 soft bundles made up of PS3s and Move Starter Packs. He stated that EDC "sold some of the consoles and starter move packs to Redcoon at a profit". The related invoice to Redcoon was dated 14 December 2010.

(2) In support of his evidence that "sometimes soft bundles were not constituted of low-value items and on occasions included high demand goods", with the Move Controller being an example of a high-value item, he exhibited a short article dated 25 November 2010 on a gaming website called slashgear.com, which said that "Sony has warned of worldwide stock shortages of the Move controller for PS3".

328. Mr Sherry gave oral evidence on the Friday of the first week of the hearing, and was taken to the email of 18 November 2010. He confirmed that CentreSoft had no stock on that date. On the following Monday, Mr Chhatwal took the witness stand. Under cross-examination he expanded his witness evidence about Deal A, saying that he had committed to provide Office Depot with both PS3s and Move Starter Packs, and that it was the difficulty in obtaining the latter which had driven him to the indirect market. He said:

> "I tried and tried to get stock from CentreSoft. This Playstation move bundle became an extremely popular product. It was out of stock for at least three to four months. There was no chance of getting it from the direct market and I went to the third market, the indirect market to purchase this stock, and I paid a premium for it."

329. On re-examination he further developed his evidence:

> "They [CentreSoft] had issued a soft bundle called the Sony PS3 320 with the Move Starter Pack. When I - again, this is something I'd committed to the Office Depot catalogue as a deal for their customers, and when I went to purchase or try to purchase these products from CentreSoft directly, I was told that there was no more stock coming in for this product. There was no due date. No estimated time of arrival. So again, out of desperation I went to the indirect market…[I was] forced because we had a commitment to our customer, to go to the indirect market. I then ended up paying a premium for that product."

330. Mr Frain-Bell invited us to accept Mr Chhatwal's evidence. Mr Watkinson submitted that:

(1) Mr Chhatwal had elaborated his evidence by linking Deal A with the shortage of Move Starter Packs;

(2) there was no documentary proof that EDC tried to buy the Move Starter Pack soft bundle from any source other than Electro;

(3) if, as Mr Chhatwal said, the Move Starter Pack was "out of stock for at least three to four months" it was "remarkably fortuitous that Electro could supply it at the drop of a hat";

(4) there was no witness or documentary evidence (such as a copy of the Office Depot catalogue, or emails/letters, to support Mr Chhatwal's new evidence that:

(a) Office Depot had included the soft bundles in its catalogue; and/or

(b) EDC had committed to supply Office Depot those soft bundles; and

(5) EDC did not invoice the first 300 of the Move Starter Packs to Everyberry until 26 November 2010, with the final 100 being invoiced on 9 December 2010. EDC had therefore held the goods in stock for three to four weeks, so the claimed urgency did not exist.

331. We agree with Mr Watkinson, for the reasons he gives. We add the following further points:

(1) if the reason for this Deal had been CentreSoft's inability to supply soft bundles including those Move Starter Packs, it is not credible that Mr Chhatwal only remembered that this was the case when he began to give oral evidence;

(2) although Mr Chhatwal exhibited some emails between him and CentreSoft as part of his evidence, he provided none to support his statement that he "tried and tried" to get the soft bundles from CentreSoft before he turned to the indirect market; and

(3) on 14 December 2010, only four days after the 100 Move Starter Packs in the Deal A soft bundle were delivered to Office Depot, EDC supplied Redcoon with identical soft bundles made up of PS3s and Move Starter Packs, and those bundles had been obtained from CentreSoft, see §141.

Deal B

332. Deal B was a contra-trade. EDC purchased 500 UK specification PS3 consoles from RLR and sold them to Ewert.

The transaction

333. There is no evidence of any communication between Ewert and EDC in the period leading up to 7 February 2011. On that day, Mr Chhatwal held five mobile phone conversations with RLR, totalling 7 minutes, and sent a purchase order to RLR for 500 PS3 320GB consoles, each costing £190.50; this was 16% below CentreSoft's wholesale price of £226.61. The total value of the purchase order was £95,250, excluding VAT.

334. On 8 February 2011, RLR issued EDC with a VAT invoice for 500 320GB PS3s with a total value £95,250 excluding VAT, plus delivery charges of £90. On the following day, 9 February 2011:

(1) there were 12 mobile phone calls from Mr Chhatwal to RLR, the longest of which lasted for two minutes, and nine lasted for less than a minute;

(2) RLR issued a delivery note for 500 320G PS3 consoles to be delivered to EDC; and

(3) EDC issued an invoice to Ewert for 500 PS3 consoles at £196.50, a mark-up of 3.1%.

335. On 10 February 2011:

(1) there were 9 further mobile phone calls from Mr Chhatwal to RLR, all of which lasted less than a minute;

(2) EDC paid £114,700 (including delivery) for the goods; and

(3) EDC signed RLR's delivery note evidencing that the goods had been delivered to its premises**.**

336. On 12 February 2011 Ewert's carrier signed a collection slip; a CMR showed that they left the UK that day.

337. On 15 February 2011, Ewert paid EDC for the goods.

338. We note in particular that:

(1) Ewert did not send a purchase order to EDC, and the first evidence of contact between Ewert and EDC was when the carrier collected the consoles from EDC's premises; and

(2) none of the documentation stated that the goods were UK specification, despite the fact that they were being exported to Germany.

Deal C

339. Deal C was also a contra-trade. EDC purchased 115 UK specification 160GB PS3 consoles from RLR and sold them to Redcoon.

340. In the two week period running up to 17 February 2011, there was no documented contact between EDC and Redcoon.

341. On 17 February 2011 a call lasting 24 seconds took place between Mr Chhatwal and RLR. EDC issued RLR with a purchase order for 115 PS3 160GB consoles, each costing £177. This was £21.79 (11%) less than CentreSoft's wholesale price. The total value of the order was £20,355, excluding VAT**.** Typed on the purchase order are the words "must be deliver tomorrow" [sic].

342. All of the following took place on the following day, 18 February 2011:

(1) RLR issued EDC with a VAT invoice for 115 160GB PS3 consoles;

(2) EDC issued an invoice to Redcoon for 115 160GB PS3 consoles at £186, a mark-up of 5.1%;

(3) EDC issued a delivery note to Redcoon for 115 160GB PS3 consoles;

(4) the goods were collected from EDC, along with other goods, by a driver from Redcoon's freight company; the driver signed the collection slip, which identified the consoles; and

(5) EDC paid RLR for the goods.

343. On 25 February 2011 Redcoon paid EDC for the goods.

344. We note in particular that :

(1) there was no purchase order from Redcoon to EDC, and no other evidence of contact between EDC and Redcoon, until EDC issued it with a delivery note; and

(2) none of the documentation stated that the goods were UK specification, despite the fact that they were being exported to Germany.

Deal D

345. EDC was the broker in Deal D. It purchased 500 EU specification PS3 consoles from Zippy, and sold 400 to Redcoon and 100 to XXL. None of the documents in this Deal refer to the specification of the goods.

346. In the two week period running up to 15 February 2011, there was no documented contact between EDC and either of its customers, Redcoon and XXL.

347. On 15 February 2011, EDC sent Zippy a purchase order for 500 160GB consoles at £185 each. Mr Chhatwal's mobile phone records do not show any contact between EDC and Zippy on any date shortly before, or in the days following, the sale to EDC.

348. On 16 February 2011, Zippy invoiced EDC for 500 160GB PS3 consoles for £185 each. This was 18% less than CentreSoft's price of £226.61. The total value of the sale was £92,500 excluding VAT; when VAT was added, the overall cost was £111,000**.**

349. On 17 February 2011, EDC invoiced Redcoon for 400 PS3s at £197 per console, so EDC's mark-up was £12 per unit, or 6.5%. The consoles were included within an invoice for other goods, which were not challenged by HMRC. The total invoice value was £250,126, of which £78,800 related to the PS3s. The consoles were collected by Redcoon's carrier on 18 February 2011.

350. The other 100 PS3s were sold to XXL. A delivery note, but not an invoice, has been provided for this sale. The delivery note is dated 15 February 2011 and there is also a collection document dated 17 February 2011 which was signed on 23 February 2011.

351. Mr Frain-Bell submitted at the end of the hearing that this part of Deal D had never been questioned by HMRC. However, that is incorrect. Although the sale to XXL was omitted from the schedules provided by HMRC, this was because there was no invoice, not because this part of the Deal had been accepted by HMRC. As Mr Watkinson said, they have refused to repay the VAT relating to all 500 units, i.e., those sold to XXL as well as those sold to Redcoon**.**

Deal E

352. EDC was the broker in Deal E. It purchased 1,000 EU specification 160GB PS3s from Electro and sold them to Ewert. None of the documents in this Deal refer to the specification of the goods.

353. There is no evidence of Ewert contacting EDC before EDC purchased the goods. On 7 March 2011 Mr Chhatwal called Electro; the call lasted 6m 44 seconds. On 8 March 2011, Electro invoiced EDC for 1,000 PS3s at a price of £188.50; this is 5% below CentreSoft's wholesale price of £198.79. The goods were delivered to EDC on 9 March 2011, as evidenced by Electro's signed delivery note.

354. EDC invoiced Ewert on the same day, 9 March 2011. The goods were collected by Ewert's carrier on 14 March 2011, together with the goods purchased by Ewert in Deals H and I, and shipped the same day, as evidenced by the delivery note and the CMR.

Deal F

355. EDC was the broker in this transaction. It purchased 500 EU specification 160GB PS3s from Electro and sold them to BAK.

356. There is no evidence of any contact between EDC and BAK before EDC purchased the PS3s. There were two calls between EDC and Electro on 23 March 2011, totalling under 4 minutes**.** On 24 March 2011:

(1) there were six calls between EDC and Electro, for a total of around 20 minutes;

(2) Electro sent EDC an invoice for 500 160GB EU specification PS3s at £188 each, which is 5.43% below CentreSoft's wholesale price of £198.79. The total value of the invoice was £94,000 excluding VAT; and

(3) BAK paid EDC £48,500 by Faster Payments; this is the cost of 250 consoles at the price on EDC's invoice issued the following day.

357. On 25 March 2011:

(1) the goods were delivered by Electro to EDC, as evidenced by a signed Electro delivery note**;**

(2) EDC invoiced the 500 consoles to BAK for £194, a profit of 3.2%. The invoice totalled £197,000; EDC's invoice does not refer to the consoles as being EU specification; and

(3) BAK paid a further £47,850 to EDC by Faster Payments; this is slightly more than the cost of a further 246 consoles.

358. On 28 March 2011, an EDC delivery note confirmed that 400 consoles were collected by BAK's carrier**.** There is no CMR for those consoles.

359. There is no EDC delivery note for the balance of the 100 consoles, but the CMR dated 28 March 2011 has been manually annotated with the words "100 pieces left UK 18/4". This was confirmed by a CMR dated 18 April 2011, which included those 100 consoles, together with the goods purchased in Deal Q, see below.

360. On 6 April 2011 BAK paid EDC the £650 balance. Taking into account the other banking evidence referenced above, BAK therefore paid for the consoles before despatch.

Deal G

361. EDC was the broker in this transaction chain. It purchased 897 160GB EU specification PS3 consoles from Electro, and sold them to ARU. There were a number of inconsistencies in the evidence for this Deal. We first make findings about the evidence provided for the transaction, and then set out the inconsistencies.

The transaction

362. On 21 March 2011:

(1) At 12.02, Mr Chhatwal called Electro and spoke for three minutes.

(2) At 15.01, Mr Rahman emailed Mr Chhatwal, thanking him for his offer made by telephone, but saying that "at that price there is no scope for us to proceed. If you are able to improve your price we may be able to take things forward".

(3) At 16.55, Mr Chhatwal spoke to Electro again, for over 12 minutes.

(4) At 17.39, Mr Chhatwal replied to Mr Rahman by email, saying:

> "Stock is already in our warehouse – because this is our first deal – I'm prepared to sell at £189.50. We have no more margin to work with."

363. On 22 March 2011:

(1) Mr Chhatwal called Electro at 10.46am for 19 seconds, and at 11.20 for 1 minute and 43 seconds.

(2) Mr Rahman emailed Mr Chhatwal saying "are you able to offer me 1,000 units at £188. If so, I am in a position to send payment today". The time of that email is not in evidence. At 11.23, Mr Chhatwal replied, saying "£189 is the last price only 900pcs left".

(3) At 11.46 Mr Rahman emailed Mr Chhatwal, saying "please send me your company documents and pro-forma invoice and I raise a PO for you. Once paperwork is in place I will arrange for payment. Please send me your payment instructions also".

(4) ARU issued a purchase order for 900 EU specification 160GB PS3s at £189 each, a total of £170,100.

(5) EDC issued a delivery note to ARU for 900 PS3s. There is no mention of EU specification. The figure of 900 units has been manually amended to "897".

(6) Electro invoiced EDC for 897 PS3s at £185 plus VAT; the invoice refers to EDC having issued a purchase order, but does not state that the consoles are EU specification.

(7) A further call took place between Mr Chhatwal and Electro at 15.29pm for 4 minutes and 21 seconds.

364. On the following day, 23 March 2011:

(1) ARU paid EDC £170,100 for 900 units by CHAPS. EDC's mark-up was 2.1%.

(2) At 8.58am Mr Chhatwal emailed Mr Rahman, saying the money had been received; that EDC would have 9 pallets ready for collection this afternoon; asking for details of the carrier; and saying "we will need a copy of your CMR upon receipt of the goods in Portugal".

(3) At 9.46am Mr Rahman emailed Mr Chhatwal, saying "as per your telephone conversation" the goods would be delivered to a warehouse in France.

(4) EDC called HMRC's Wigan office, and obtained verification of ARU's status; it followed this up with a fax asking HMRC to confirm the position.

(5) Electro delivered the goods to EDC: the delivery note says "PS3 160GB 900pcs EU spec", but in Mr Chhatwal's handwriting the 900 has been crossed out and replaced it with 897; he has signed the bottom of the delivery note.

(6) Despite having been invoiced by Electro for 897 units the day before, EDC invoiced ARU for 900 units of 160GB PS3s at £189, a total price of £170,100. EDC's invoice does not say that the consoles are EU specification;

(7) Mr Chhatwal then emailed Mr Rahman saying "I have just received the stock – but three units are missing (presumed stolen) – my supplier is sorting this out. I will need to credit you for 3 units and arrange a refund – so there are 897 x ps 160gb eu stock now ready for collection".

(8) EDC issued ARU with a credit note for three units; Mr Chhatwal manually amended EDC's invoice to ARU, reducing the number to 897 units.

(9) At 11.16 Mr Rahman responded with the words: "Stolen? That's not very comforting!" and saying he had received the credit note, but adding: "it can prove to be more hassle than it's worth with adjusting paperwork and receiving back such a small amount of funds. If possible, can you hold the credit there for me?"

(10) The goods were collected from EDC. The collection note, signed by Mr Chhatwal, states that 897 units were collected on 9 pallets.

(11) At 13.45 Mr Chhatwal emailed Mr Rahman, saying "we have a truck collecting 9 pallets. Online BMT direct from Dover. They have no CMR and are delivering to Dover only. He has no paperwork".

(12) At 14.45 Mr Rahman emailed Mr Chhatwal, saying that the freight company had collected 10 pallets rather than the 9 pallets expected.

(13) EDC paid Electro in full.

365. We were provided with the following CMRs, all of which state that the goods left EDC on 23 March 2011:

(1) The CMR exhibited to Mr Chhatwal's evidence is entirely handwritten apart from three stamps giving EDC's name and address. The carrier is named as On Line MBT, and a person called LJ Wall has signed the CMR as the representative of that carrier. The date of taking over the goods is 23 March 2011, and they are described as "PS3 160GB x 897 PCs load unchecked". Under this, the words "10 pallets" have been crossed out and replaced by "9 pallets"; Mr Wall has signed that change. The consignee is ARU, at its address in Portugal; the place designated for the delivery of the goods is Prologic in Rungis, near Paris. The total weight is given as 2.500 kg. The box for the "sender's/agent's reference" is blank. There is no stamp showing that the goods have been received.

(2) Two linked CMRs were exhibited to Mr Ginn's second witness statement. These are both entirely typewritten, other than a handwritten annotation on the first which says "5 pal[lets] black wrapped" and on the second "4 pal[lets] black wrapped", and a stamp giving the name of the carrier as Bullit Express. The date of taking over the goods is 23 March 2011; Prologic is both the consignee and the place of delivery, and the total weight (taking both CMRs together) is 4,800kg. The sender's/agent's reference box has been completed, and the CMRs were stamped by Prologic as having arrived on 24 March 2011.

366. On the same day, 24 March 2011, Mr Chhatwal emailed Mr Rahman at 8.09 am, saying "we have managed with some difficulty to contain it to 9 pallets". At 10.46 Mr Rahman emailed again, saying that the lorry had been stopped at Dover because it was overweight and a second lorry was required.

367. Also on 24 March 2011, HMRC responded to EDC's verification request, saying that they were awaiting "further verification" of ARU's status. On 1 April

2011, HMRC informed EDC that ARU had been deregistered in 2007. Although EDC had not charged VAT on the invoice, it accounted for VAT in its March return, and on 6 April 2011 issued a credit note for the original invoice and sent ARU a new invoice charging VAT. On 7 April 2011, HMRC wrote again, confirming that ARU was VAT registered, and on 13 April 2011, EDC reissued the original invoice without VAT.

Inconsistencies

368. We noted the following inconsistencies about the location and number of the goods:

(1) *Inconsistent location of the ordered goods:* Mr Rahman wanted 1,000 consoles, and Mr Chhatwal originally told ARU on 21 March 2011 that "stock is already in our warehouse" and later said EDC had "only 900pcs left". However, the stock was not "already in EDC's warehouse", because the 900 consoles were invoiced to EDC, and delivered to EDC's premises, by Electro the following day.

(2) *Inconsistent number of units delivered to EDC:* On 22 March 2011, Electro invoiced EDC for 897 units, so Mr Chhatwal can only have been expecting delivery of 897 units. However the following day, EDC invoiced ARU for 900 units, and Mr Chhatwal told Mr Rahman that "I have just received the stock – but three units are missing (presumed stolen)". The other three consoles were not "missing" or "stolen", because they had never been included on Electro's invoice in the first place.

(3) *Inconsistent number of pallets:* On 23 March 2011 Mr Chhatwal signed a delivery note saying that there were 9 pallets, but:

(a) on the same day, Mr Rahman emailed to say that the freight company had complained that there were 10 pallets;

(b) the following day Mr Chhatwal told Mr Rahman that he had managed to contain it to 9 pallets, and does not refer to Mr Rahman's email about needing 10 pallets; and

(c) both versions of the CMRs also stated that the goods were on 9 pallets;

(4) *Inconsistent carrier:* Mr Chhatwal told Mr Rahman that the goods had been collected by a company called "Online BMT" which had no CMR; yet a person called Mr Wall signed a CMR on behalf of a company called "On Line MBT";

(5) *Inconsistent CMRs:* there are numerous differences between the CMR signed by Mr Wall and that stamped by Prologic, including the weight of the goods, the carrier, the consignee and the agent's reference. There was no explanation before the Tribunal as to why there were two completely separate CMR documents for the same load.

369. We return to these inconsistencies, and to the Deal G email correspondence more generally, in Part 6 of our decision.

Deal H

370. In Deal H, Electro was the supplier; Ewert and ARU were the customers, and EDC was the broker. The goods were EU specification 160GB consoles, which Electro had purchased from three different companies: 1,000 from WNL; 900 from a company called Veyron Ltd, and a further 1,000 from a company called CBR Consultancy Ltd ("CBR"). As explained at §11 and §13, WNL was a contra-trader, but HMRC did not identify this in time to deny the VAT from the consoles which were traced to WNL.

The transaction

371. On 24 March 2011, Mr Chhatwal told Mr Rahman by email that he had "1,000 xps3 160gb eu coming in next week – will do at the same price" and Mr Rahman responded by saying "lets see what we can do next week".

372. On 28 March 2011, Electro bought the consoles from WNL and Veyron Ltd; it purchased the consoles from CBR in two deals on 29 and 30 March 2011. On the same day, Mr Chhatwal called Electro three times, and spoke for a total of 13 minutes. EDC did not issue a purchase order for the goods.

373. On 29 March 2011, Electro sent EDC an invoice for 1,000 160GB PS3s at £185 each, and 1,250 PS3 160GB consoles at £187.50. The specification is not shown on the invoice. The prices were 6% and 7% below CentreSoft's wholesale price.

374. On 30 March 2011:

(1) Electro delivered the goods to EDC; the delivery note states that they are "PS3 160GB 1000pcs EU SPEC"; and

(2) ARU issued a purchase order to EDC for EU specification 160GB PS3s, with 739 being priced at £189 and 511 at £189.65, a total cost of £236,582.15; and

(3) ARU authorised a bank transfer to EDC for £236,582.15.

375. There is no evidence of any email or phone contact between Mr Chhatwal and Mr Rahman about the pricing or other elements of this Deal, other than the exchange on 24 March 2011 noted at §371 above.

376. On 31 March 2011:

(1) EDC invoiced ARU for 739 consoles at £189 and 511 consoles at £189.50, a total of £236,582. The specification is not shown on the invoice. EDC's profit margin was 1.1%;

(2) the goods were collected by ARU's carrier, as evidenced by a delivery note, and shipped to ARU; and

(3) EDC paid Electro by CHAPS.

377. As noted above, on 1 April 2011 HMRC informed EDC that ARU had been deregistered in 2007. On 6 April 2011 EDC issued ARU with a credit note although

the goods had already been delivered a week earlier. On 7 April 2011, HMRC agreed ARU had a valid VAT number, and on 13 April 2011 EDC reissued the invoice.

378. In relation to the sale to Ewert, EDC issued an invoice on 25 March 2011 for 1,000 consoles at £191 each, a profit margin of 3.2%. The invoice does not state the specification. The consoles were therefore invoiced by EDC to Ewert four days before Electro had invoiced EDC (and also before Electro had itself purchased the goods, see §372 above). The parties confirmed to the Tribunal that these dates were correct. The Tribunal invited Mr Frain-Bell to comment further, but he did not do so. We return to these inconsistent dates at §581.

Deal I

379. In Deal I, EDC was the broker. It purchased 300 EU specification consoles from RLR and sold them to Ewert. The details were as follows:

(1) In the two weeks before 7 March 2011, there was no purchase order or other evidence of contact between EDC and Ewert.

(2) On 7 March 2011:

(a) Mr Chhatwal made three short phone calls to RLR, totalling less than two minutes;

(b) EDC issued a purchase order to RLR, for 300 160GB EU specification PS3s at £188.50 each, a total of £56,550. The purchase price was 5% below CentreSoft's wholesale price; and

(c) EDC invoiced Ewert for 300 160GB slim consoles; the reference number on the invoice is H1/35567. Each console was priced at £192, so EDC's profit margin was 1.9%. EDC's invoice did not give the specification of the consoles.

(3) On 8 March 2011:

(a) RLR invoiced EDC for 297 consoles at £188.50. The invoice did not give the specification; and

(b) Mr Chhatwal called RLR at 14.45 and spoke for 6 minutes.

(4) On 9 March 2011:

(a) an RLR delivery note records that 297 EU specification PS3s had been delivered to EDC;

(b) a Ewert collection note records that 300 PS3s invoiced under reference H1/35567 had been collected by its freight company, Kurt Beier A/S ("Beier"), at the same time as that company collected the 2,000 PS3s sold to Ewert in Deals E and H; and

(c) Mr Chhatwal called RLR eight times for a total of around seven minutes between 8.33 am and 15.47 pm.

(5) On 10 March 2011, RLR issued EDC with an invoice for three consoles at £188.50.

(6) On 14 March 2011, 300 consoles were shipped to Ewert, and are shown on the same CMR as those in Deals E and H.

380. Mr Frain-Bell submitted that, on the evidence, only 297 consoles were delivered by RLR on 9 March 2011, and the remaining three consoles were delivered on or after 10 March 2011. However, it is clear from the Ewert collection document that 300 consoles were waiting for collection at EDC's warehouse on 9 March 2011, and Ewert was also invoiced for that number of consoles. We find as a fact that 300 consoles were delivered by RLR to EDC on 9 March 2011, as otherwise they could not have been collected by Beier on that day. We return to this again at §592.

Deal J

381. In Deal J, EDC was again the broker. It bought 1,000 EU specification 160GB consoles from RLR and sold them to Ewert. Our findings about the transaction are set out below.

382. Ewert did not issue a purchase order to EDC, and there is no record of any conversation between Mr Chhatwal and Ewert before the transaction took place.

383. On 16 March 2011, Mr Chhatwal spoke to RLR for 1.5 minutes. On the same day, RLR invoiced EDC for 899 PS3 consoles at £187.25, around 6% below the CentreSoft wholesale price. The total value of the goods was £168,338, excluding VAT. The invoice does not state that the goods were EU specification.

384. On 17 March RLR issued a delivery note for 899 EU specification 160GB PS3 consoles.

385. On Sunday 20 March 2011, RLR raised a further invoice for 101 PS3 consoles at the same price. The invoice also does not state that the goods were EU specification. There was no phone call between Mr Chhatwal and RLR before this part of the Deal.

386. On 21 March 2011, RLR issued a delivery note for 101 EU specification 160GB PS3 consoles. On the same day, EDC invoiced Ewert for 1,000 consoles at £192, so a total of £192,000 and a profit margin of 2.54%. The invoice does not state that the consoles are EU specification.

387. A delivery note dated 6 April 2011 confirms that 900 consoles were collected by Ewert on that day. The Tribunal was provided with no information about the other 100 consoles.

Deal K

388. EDC was the broker in this short transaction chain. It purchased 90 Samsung televisions from Zippy; Zippy had purchased them from CH Imports Ltd, the defaulter.

389. There were four calls between Mr Chhatwal and Zippy on 7 and 8 April 2011, totalling around ten minutes. On 11 April 2011, Zippy invoiced EDC for 90 Samsung

32 inch HD Ready TVs, each costing £185, so a total price of £16,650 excluding VAT.

390. EDC was an authorised distributor for Samsung, but Mr Chhatwal's witness statement did not explain why he bought these televisions from Zippy rather than from Samsung. Neither did he provide any information about the customer(s) to whom EDC sold the televisions.

391. Under cross-examination, he said that "the only reason I turned to [the grey] market is because the stock was not available from Samsung direct". Mr Watkinson asked "how has Mr Anness got hold of this stock when you, with all your years in the industry can't get hold of", and Mr Chhatwal gave a lengthy but vague reply.

392. He then went on to say that Office Depot had advertised these televisions in its customer magazine; that EDC had agreed to supply them, and that having purchased the televisions from Zippy, EDC had held them in stock before selling them to 90 individual Office Depot customers. During re-examination, he further developed his evidence, saying:

> "I had promised these TVs to Office Depot. They had produced this brochure to sell on to their customers, and the model number was LE32C450. We were then obliged to supply that TV to any of the customers that purchased that product. We didn't know what kind of demand they would get through their sales, so we didn't necessarily stock a lot of sets, but we were ready when the orders were coming in. The time that they started to receive orders, which was around April/May time, this is a time when a lot of models in the industry are discontinued, and it just so happens that TV then moved from LCD to LED. I had no - Samsung had no stock of this set. I had customers waiting from Office Depot. I had to deliver, because I obviously wanted to keep my relationship going with Office Depot in the long-term. I then had no choice but to go to Zippy and purchase this product for a higher price."

393. We note that:

(1) Mr Chhatwal did not include any of the above detail in his witness statement;

(2) no copies of any documents from Office Depot were exhibited; and

(3) there was no documentary or witness evidence:

(a) to support Mr Chhatwal's statements that there had been a change in the models and that Office Depot customers wanted the older model; or

(b) to explain why Samsung was unable to supply the televisions to EDC, its authorised distributor, and how Zippy came to have access to this stock.

394. In short, we do not accept Mr Chhatwal's belated explanations for this Deal. It is not credible that he remembered this information for the first time during the hearing, but had entirely overlooked it when he was writing his lengthy and detailed

witness statements. We find that Mr Chhatwal elaborated his evidence in the witness box to try and improve its plausibility.

395. Because we have not accepted Mr Chhatwal's later evidence, we are also unable to make findings as to the identity of the customer(s) for these televisions.

Deal L

396. This was another short transaction chain in which EDC was again the broker. The same defaulter, CH Imports, sold 400 UK specification 160GB PS3 consoles to Zippy, who on-sold them to EDC; EDC sold 200 of them to XXL. The details are set out below.

397. No purchase order or other evidence of contact between EDC and XXL preceded the transaction.

398. On 11 April 2011:

(1) a telephone call took place between Mr Chhatwal and Zippy; this lasted for less than two minutes;

(2) EDC issued a purchase order to Zippy for 400 PS3 160GB consoles for £170. This was 15% below CentreSoft's wholesale price. The invoice did not refer to the consoles as being UK specification. The total value of the invoice was £68,000, excluding VAT; and

(3) Zippy invoiced EDC for 400 UK specification 160GB PS3 consoles.

399. On 12 April 2011, Mr Chhatwal called Zippy, and spoke for one minute and 10 seconds.

400. On 13 April 2011:

(1) Mr Chhatwal called Zippy again, and spoke for three minutes and 40 seconds;

(2) EDC invoiced XXL for 200 160GB PS3s at a price of £182 per console, a 7% mark up. The invoice did not state that the consoles were UK specification. Also included on the same invoice were 100 batteries for Samsung 3D glasses, for a total price of £3,600; HMRC have not refused to repay the VAT on those batteries; and

(3) EDC issued XXL with a delivery note containing the same information as was on the invoice.

401. On 14 April 2011, the 200 consoles were collected by XXL's freight carrier.

402. On 20 April 2011, XXL paid EDC for the goods, so payment was made after delivery.

403. The Tribunal was provided with no information as to what happened to the other 200 consoles.

Deal M

404. In Deal M EDC, the broker, purchased 400 160GB PS3s from Zippy and sold them to Redcoon.

405. There was no purchase order or other evidence of contact between EDC and Redcoon in the days leading up to 13 April 2011. On that date:

(1) there are four short phone calls totalling around seven minutes between Mr Chhatwal and Zippy; there had also been two calls the previous day for around three minutes.

(2) Mr Chhatwal emailed Mr Chad, who worked for Zippy, and under the heading "new order", specified "400 x PS3 160GB with eu plug @ £173".

(3) Zippy invoiced EDC for 400 160GB UK specification PS3s at £173 per console, 13% below CentreSoft's wholesale price. The total value of the invoice was £69,200, excluding VAT. There is an inconsistency between the UK specification on this invoice, and the EU specification requested by EDC, which we consider at §546.

(4) Zippy issued a delivery note, which does not refer to the specification. It states that the "ship date" to EDC's premises was also 13 April 2011.

406. The delivery note was signed on 14 April 2011, and we find from this that they were delivered to EDC on that date, and not on 13 April 2011 as shown on the delivery note.

407. On 27 April 2011, EDC invoiced Redcoon for many different items, including "400 PS3 160GB slim" for £178 per unit, a mark-up of 3%. The total value of the invoice was £172,139, including the cost of the PS3s, which was £71,200. On the same day, the goods were collected by Redcoon's courier company and shipped. There was no documented call between Mr Chhatwal and Redcoon at any point between 13 April 2011 and the end of that calendar month.

Deal N

408. In Deal N, EDC was a buffer in the transaction chain. It purchased 1,000 160GB PS3s from Electro for £185.25 each, and sold them to Anovo for £229.20, a total of £229,200.

409. There is no evidence of any contact on or before 4 April 2011 between EDC and Anovo about this Deal. On 4 April 2011, Mr Chhatwal made three short calls to Electro, totalling around seven minutes and Electro invoiced EDC for 1,000 160GB PS3s for £185.25 each. This was almost 7% below CentreSoft's wholesale price.

410. On 5 April 2011:

(1) a document headed "Purchase request" was sent to EDC by David Cato of Anovo, for 1,000 160GB EU specification PS3s, each for £191, so a total value of £191,000. However:

(a) the purchase request has no company logo;

(b) in the box for "purchase ref" the figure "0" has been inserted;

(c) in the box for "reason/sales order reference" are the words "Flip deal stock". Mr Watkinson said that this was a reference to a back-to-back deal, which we understand to mean a purchase which would be on-sold immediately, and this was not disputed;

(d) the bottom part of the form has spaces for authorisation by the department manager and the delivery date; both have been left blank.

(2) EDC did not issue a purchase order to Electro;

(3) EDC issued Anovo with a sales invoice. In the box for "customer order number" is typed "David Cato", and the invoice states that it is for 1000 PS3 slim, EU stock. The price of each console was £191, so EDC's profit margin was 3%; and

(4) the consoles were collected by Anovo's transport company; the collection slip refers to them being EU stock.

411. On 6 April 2011, a call took place between Mr Chhatwal and Mr Cato, lasting 6 seconds**.** On 7 April 2011, so after the goods had been shipped, EDC received payment from Anovo.

Deal O

412. Deal O was similar to Deal N in that the consoles were purchased from Electro and sold to Anovo, with EDC being the buffer.

413. The following steps took place on 28 April 2011:

(1) Mr Chhatwal called Anovo at 9.27am and spoke for just over 3 minutes.

(2) Mr Chhatwal immediately called Electro and spoke for 12 minutes.

(3) there was one more call between Mr Chhatwal and Anovo, and between Mr Chhatwal and Electro, that afternoon, each call lasting around a minute.

(4) Electro invoiced EDC for 480 320GB EU specification PS3s at £204.50 each. This is almost 10% below CentreSoft's wholesale price.

(5) The goods were delivered to EDC by Electro. The delivery note says that the goods are 480 EU specification 320GB PS3s at £204.50 each.

(6) EDC invoiced Anovo for 480 320GB slim PS3s at £250.80 per console, a profit margin of 2%; there is no mention of them being EU specification. The total value of the invoice was £120,384 including VAT.

414. The goods were collected by Anovo on 11 May 2011 and paid for on 13 May 2011, so after the goods had been shipped**.**

Deal P

415. In Deal P, EDC was once again the broker. It purchased 420 Apple iPods from Zippy and sold them to Redcoon.

416. There was no call or other communication between Redcoon and EDC before 27 April 2011. On that day:

(1) Zippy issued an invoice for 420 iPods at £83 each, so for a total of £34,860; with VAT added, the invoiced amount was £41,832;

(2) EDC invoiced Redcoon at £88 per iPod, a profit margin of 6%; and

(3) the goods were collected by Redcoon's carrier, along with other items including the PS3s in Deal M.

417. There was no phone or other contact between EDC and Zippy before the transaction took place, but there were two subsequent calls, one at 17.26 and one the following day.

418. Mr Chhatwal's witness statement does not explain why he purchased these goods from Zippy rather than from Apple. When asked that question in cross-examination he said:

> "this was a product that was required - at the time was extremely short in supply from Apple. I think they were restricting it to one customer -- one unit per customer. Now, Redcoon had a huge demand for this product in Germany. It was something they could make good money on because supply was short. In the end we had to pay a premium for this product, but we helped our customer out."

419. Mr Chhatwal was unable to explain why this evidence had not been in his witness statement, or why he had not supplied any exhibits to support his claims that that there was a shortage of iPods at the time, or that there was a huge unmet demand in Germany. Zippy's webpages (see §260(3)) say its business was "retailing online for over 5 years" and that it was "a reseller of TVs by Samsung and LG Electronics"; there is no reference to a trade in iPods. We reject Mr Chhatwal's new oral evidence and find that, like that of Mr Hutchinson in *Painter v Hutchinson* (see §22), these explanations for Deal P had simply been "made up on the spot".

Deal Q

420. EDC was the broker in this Deal. RLR had purchased 100 160GB consoles from Electro ("Deal Q1") and 400 from a company called EP Consultants Ltd ("Deal Q2"); EDC bought 496 of these consoles from RLR and sold them to BAK.

421. HMRC initially denied all the input tax in relation to the transaction, but subsequently amended the calculation to deny only that relating to Deal Q1, because they were not satisfied that Deal Q2 traced back to a fraudulent tax loss. However, HMRC subsequently identified that EP Consultants had purchased the goods from Link West (UK) Ltd, and that company in turn had purchased the goods from BAK. Thus, part of Deal Q was a carousel, with BAK at the beginning and end of the deal chain. However, HMRC did not become aware of this in time to amend its calculation of the VAT repayment denied to EDC, so it has retained the VAT relating to Deal Q2.

The transaction

422. There was no call or other communication between BAK and EDC about Deal Q on or shortly before 7 April 2011. In making this finding, we took into account Mr Frain-Bell's submission that on 5 April 2011 BAK transferred £650 to EDC's bank account as a part-payment for the goods in Deal Q. However Mr Frain-Bell also identified the same payment as being the final instalment for Deal F, and from our analysis of the bank statements we find that the latter is correct.

423. On 7 April 2011:

(1) EDC issued a purchase order to RLR requiring 500 160GB PS3 slim consoles with EU specification, at a price of £186 each, 6% less than CentreSoft's wholesale price;

(2) RLR invoiced EDC for 496 consoles, not the 500 ordered. The total value of the invoice, excluding VAT, was £92,256; and

(3) RLR did not state on the invoice that the consoles were EU specification**.**

424. On the following day, the goods were delivered to EDC. On 14 April 2011, EDC invoiced BAK for 300 consoles at £189.50 each, a profit margin of 2%. The invoice does not say whether they are EU or UK specification. The total value of the invoice was £56,850.

425. The CMR is dated 18 April 2011, and includes the 100 consoles which formed part of Deal F, see §359. It describes the 300 consoles in Deal Q as consisting of 100 "UK plug" and 200 as "UK stock EU plug".

426. The documentation as to whether the goods are EU or UK stock is therefore contradictory, with EDC ordering EU stock from RLR; RLR's and EDC's invoices omitting to mention the specification; and the CMR saying that they were a mixture of UK and EU stock. We return to this at §546.

427. Mr Frain-Bell identified the following three payments from BAK to EDC as relating to Deal Q: on 12 April 2011 for £10,000; on 13 April 2011 for £40,000 and on 18 April 2011 for £10,000. The total is therefore £60,000, more than the invoice, and this was unexplained. However, we accept that payment was made in full on or before the date the goods were shipped.

Deal R

428. EDC was the buffer in this Deal chain. It purchased 1007 PS3s from Electro and sold them to Anovo.

429. There was no purchase order from Anovo. In the week before 10 May 2011 there were five very short calls between EDC and Anovo, each lasting less than a minute.

430. On 10 May 2011:

(1) there were two further calls between EDC and Anovo, both before 10am, and both less than a minute in length;

(2) these were immediately followed by three calls to Electro, the longest of which was for one minute and 19 seconds;

(3) Electro invoiced EDC for 1007 EU specification 320GB PS3s. The price was £210.75, 7% below CentreSoft's wholesale price. The value of the invoice was £212,225.25 plus VAT of £42,445.05, making an overall total of £254,670.30; and

(4) EDC invoiced Anovo for 1007 EU specification PS3s for £216 plus VAT, a profit margin of 2.5%. The invoice total was £261,014.40.

431. On 11 May 2011 the consoles were collected by Anovo's carrier, together with those invoiced in Deal O; they were paid for on 13 May 2011, at the same time as those in Deal O**.**

Deal S

432. The goods in Deal S originated from a split transaction chain.

(1) In the first strand (Deal S1), as already noted earlier in this decision, the defaulter was JK Distribution Ltd ("JKD"), and the goods were 1000 PS3s with a game called Killzone 3. We have already found as a fact that these were EU specification consoles, see §209.

(2) In the second strand (Deal S2), WNL was the contra-trader, and the goods were 480 PS3s 320GB consoles; neither party has been able to provide evidence showing whether they were UK or EU specification.

(3) In the third strand (Deal S3), WNL was again the contra-trader, but the goods were LCD televisions.

433. On 12 May 2011, Electro purchased all the PS3s (without the games), and the televisions, and sold 780 of the PS3s and all the televisions to RLR. RLR sold these to EDC, and EDC sold them to Redcoon. EDC was the broker for all parts of the Deal. HMRC have not denied the VAT relating to Deals S2 and S3, because they traced back to WNL.

The transaction

434. There was no call or other recorded contact between EDC and Redcoon in the period running up to 10 May 2011.

435. On 10 May 2011, EDC issued a purchase order to RLR for 800 320GB PS3s. The purchase order does not state whether EDC was ordering EU or UK specification consoles. EDC paid £198 per console, 12.63% less than CentreSoft's wholesale price. The total value of the goods (excluding VAT) was therefore £158,400.

436. On 11 May 2011:

(1) there were two calls between EDC and RLR, one for 16 seconds and one for one minute, 54 seconds;

(2) EDC invoiced Redcoon for 185 of the PS3s for £203 each, a profit of 2.5%. The invoice does not mention the specification. The invoice included other items, so the total value was £225,666, of which the PS3s made up £37,555; and

(3) Redcoon collected the PS3s, as evidenced by a signed and dated CMR.

437. On 12 May 2011:

(1) as noted above, Electro purchased the PS3s and the televisions from RLR;

(2) EDC issued a purchase order to RLR for 100 LG LCD televisions at a cost of £170;

(3) RLR issued EDC with a single invoice for (a) the televisions at £170, and (b) 780 320GB PS3s at £198. The invoice does not refer to the specification. The total value of the invoice was £171,440, excluding VAT.

438. On 13 May 2011, an RLR delivery note was signed on behalf of EDC saying that 780 PS3s had been delivered on that day to EDC, along with 100 LCD televisions; the delivery note cross-refers to the numbers on the purchase orders referred to above.

439. It is clear from the documentation set out above that Redcoon collected the PS3s from EDC two days before EDC signed the relevant delivery note to say that they had been received from RLR, and a day before (a) RLR had purchased the goods from Electro and (b) Electro had itself purchased the goods. We return to these inconsistencies at §581.

Deal T

440. EDC was a buffer in this deal chain. It purchased 500 soft bundles containing EU specification PS3s together with Move Starter Packs from Zippy and sold the PS3s to Anovo.

The transaction

441. On Friday 27 May Mr Chhatwal called Zippy and spoke for two minutes; this was followed by three short calls (totalling less than five minutes) between Mr Chhatwal and Anovo. EDC did not issue a purchase order.

442. On 3 June 2011:

(1) Zippy issued EDC with an invoice for 500 EU specification 320GB PS3s with Move Starter Packs, for £210 each. This was 7% less than CentreSoft's wholesale price of £226.61 for a soft bundle, and 16% less than the cost of the components purchased separately (the Move Starter Pack wholesaled at £23.66, so the total cost of the components would have been £250.77);

(2) excluding VAT, the overall total cost was £105,000;

(3) Zippy issued EDC with a delivery note for PS3s, using the same information as on the invoice;

(4) the signed delivery note confirms that the goods were received by EDC**;**

(5) EDC invoiced Anovo for 500 320GB slim consoles. Added to the invoice, in bold, are the words "Note: eu stock". Each console was priced at £207, so £3 below the price EDC had paid for the soft bundle, including the Move Starter Pack. The total value of the invoice was £103,500 excluding VAT.

443. On 13 June 2011, Anovo transferred the goods to its customer, Osmosis Ireland Ltd, so EDC must have delivered the goods to Anovo on or before that date. On 14 June 2011 Anovo paid EDC; payment was therefore made after the goods had left EDC.

The Move Starter Packs

444. The Tribunal asked the parties what had happened to the Move Starter Packs. Mr Frain-Bell said that EDC had sold them separately for a profit. Mr Watkinson accepted that the bundle had been split between the PS3s and the Move Starter Packs, but said that neither party had been able to locate the onward sale document for the Move Starter Packs, and Mr Frain-Bell did not disagree.

445. However, after the hearing, the Tribunal noted that Mr Ginn's second witness statement exhibited two invoices from EDC to Redcoon. The first was dated 16 June 2011, and included 300 Move Starter Packs for £19 each**;** the second was dated 29 June 2011, and included a further 335 Move Starter Packs for the same price. Both invoices also contained other items which are unchallenged by HMRC.

446. We considered whether to make findings about these invoices. We noted that:

(1) although Mr Ginn's evidence was unchallenged, Mr Watkinson had explicitly stated that there was no documentary evidence as to what EDC had done with the Move Starter Packs;

(2) Mr Frain-Bell did not refer to, still less rely on, the two Redcoon invoices exhibited by Mr Ginn;

(3) the invoices show that EDC sold 665 Move Starter Packs to Redcoon, but had acquired only 500 from Zippy;

(4) we were not provided with any linkage (such as invoice or reference numbers) allowing us to be confident that the Move Starter Packs on the Redcoon invoices were in part sourced from the Zippy soft bundle;

(5) Mr Sherry's evidence was that CentreSoft's wholesale price for Move Starter Packs in February 2011 was £23.11. The EU wholesale price would have been similar, see our earlier findings at §89. EDC was therefore selling the Move Starter Packs for more than 17% below their wholesale price. We had had no explanation from either party as to why EDC would sell Move Starter Packs at such a steep discount; and

(6) neither party relied on, or referred to, this soft bundle in the context of their submissions on the existence (or otherwise) of a commercial marketplace for the component parts of soft bundles, see §192ff and in particular §221.

447. In view of these uncertainties, we were only able to find as a fact that EDC had split the bundle, we could not make findings as to what had happened to the Move Starter Packs which had formed part of the bundle.

448. However, if each of the Move Starter Packs had in fact been on-sold for the £19 shown on the Redcoon invoices, the Deal was even more remarkable, because EDC's overall profit would have been £16 per bundle (£19 for the Move Starter Pack, less the £3 loss on the sale to Anovo), which is a 7.6% profit margin.

PART 7: THE CIRCUMSTANCES IN COMBINATION

449. As already cited earlier in this decision, the Upper Tribunal gave the following guidance in *CCA* at [93]:

> "When dealing with a case based on circumstantial evidence, a fact finding tribunal has to do two things. First, it must make its findings as to what the circumstances actually were. Secondly, having determined what the circumstances were, it has to determine what inference to draw from all such circumstances taken together. In the first part of this exercise, the tribunal necessarily will look at the alleged circumstances individually; for the second part of this exercise, the tribunal must look at the circumstances in combination."

450. In *Red 12* at [109]-[111], Clarke J said that the Tribunal can consider "compelling similarities between one transaction and another"; draw inferences from a pattern of transactions including those which are in dispute, and look at the totality of the transactions and not simply consider each one taken in isolation, and this approach was endorsed by Moses LJ in *Mobilx,* see the citation at §59.

451. Having considered the suppliers and customers at Part 5, and each the disputed transactions in Part 6, we now draw together the points which arise from the Deals, with more general findings of fact in Part 4.

Customer driven deals?

452. We first considered whether EDC's business was based on selling goods already acquired from suppliers, or on finding goods required by customers. Mr Chhatwal's evidence was that:

> "on certain occasions, manufacturer sales representatives would offer EDC exceptional end-of-line discounts to acquire remaining stock which we would then sell to customers"

453. In reliance on Mr Sherry's evidence, we have already found that CentreSoft did not discount stock to unofficial wholesalers such as EDC, see §159(1). Thus, while this may be the position for other goods, it is not the case for PS3s. In his witness

statement Mr Chhatwal also described EDC's normal position, which he said always applied in the PS3 market:

> "a customer would approach EDC with a specific product requirement which we would source through our connections in the industry…It made business sense to always ensure customers were available to take on the stock, otherwise we would not commit to high volumes, and expose ourselves to risk."

454. He added that (wording as in original):

> "EDC would generally operate a 'buy to order' policy that is to say that I would source goods on the basis of demand…occasionally I would buy an extra units without a customer secured if a deal was exceptionally good in anticipation of orders from Woolwich and Barclays insurance services or for sale in our retail business."

455. And:

> "Once I understood what the customers' needs were, I would generally contact suppliers and make enquiries as to the availability of stock delivery timeframes and price."

456. However, under cross-examination Mr Chhatwal contradicted that consistent evidence, saying that EDC's sales were driven by stock offered by suppliers:

> "I was offered the stock and then I used my business acumen to make an offer to Redcoon and say to them: look I've got stock, this is the price, it's been split from a bundle; are you interested?"

457. We considered the details of the disputed transactions. Although in Deal G, Mr Chhatwal told Mr Rahman, his customer, that he had stock in his warehouse, but this was not true: Mr Chhatwal then ordered the stock from Electro. EDC did not offer to sell existing stock to its customers in any of the other Deals.

458. We find that EDC's normal commercial practice was only to purchase stock for onward sale to other wholesalers, when it already had a customer lined up. It follows that we do not accept Mr Chhatwal's statement at §456, which is inconsistent with his other evidence and with the details of the transactions.

Lack of documentary evidence

459. As is clear from the details of the Deals in Part 6, there are almost no written records of negotiations between EDC and the suppliers/customers involved in the disputed transactions. Mr Chhatwal gave the following reasons for this:

(1) most of the Deals were carried out on the telephone and he kept the details of those negotiations in his head;

(2) Deal G was an exception to this. He had had extensive email with Mr Rahman of ARU because there was no mobile phone reception**,** and the emails between him and Mr Rahman are evidence of genuine negotiation between the parties on price;

(3) although he had a deal book, or day book, this was only used for certain types of transactions which did not include the Deals;

(4) to the extent that documentation of the negotiations had existed, most could not now be accessed; and

(5) his mobile phone records provide evidence of negotiations.

460. We consider each of those reasons in the next following paragraphs.

No written record?

461. Mr Chhatwal's evidence was that EDC "would have had many, many negotiations with our customers" and that "it was a labour intensive process. I would call numerous suppliers for product availability and price quotes". We accept that this was EDC's normal manner of operating.

462. Mr Chhatwal also said that "thousands of transactions were done on the basis of either through Skype or phone calls and so forth" and that once he had a price, he would "phone up my customer and tell him what the price was" but that no part of that negotiation was written down but "maybe it would have been in my head". He said that when agreement was reached, the deal documents formed the record of the transaction and there was no need to retain details of the negotiations.

463. Mr Watkinson invited us to reject that evidence, saying that the Tribunal was being asked to accept that all these details were being held in Mr Chhatwal's "incredible memory" and that:

> "if [EDC] was seeking its own trades within an active marketplace, then evidence of the systems it used and records of its comparison of competing suppliers would be capable of being produced."

464. Mr Frain-Bell asked us to accept Mr Chhatwal's evidence that he was able to remember the details of the negotiations and did not write them down. He drew an analogy with *Synectiv v HMRC* [2018] UKFTT 0092 (TC) (Judge Falk and Mr Robertson), where the appellant's business was also conducted rapidly by phone, and the FTT allowed the appeal, despite finding at [107] that the documentation fell "far short of what a commercial lawyer might expect to see".

465. We agree with HMRC. EDC was seeking the best deal for its customers from "numerous suppliers", and it is simply not believable that Mr Chhatwal could retain the detail of each supplier's prices, quantities, delivery dates, specifications and locations, without writing this down. EDC's position can be distinguished from that of the appellant in *Synectiv,* because:

(1) in that case the FTT was re-hearing an appeal which had been remitted back from the Upper Tribunal following an earlier hearing in 2013. The FTT came to its decision on the basis of a statement of agreed facts, together with the witness statements and transcripts of oral evidence from the original hearing. The lack of oral evidence meant that the FTT was unable to make findings as to how the deals were put together, see [63] of the FTT decision. In contrast, Mr

Chhatwal has given evidence that he carried out a "labour intensive process" which required him to "call numerous suppliers";

(2) the appellant in *Synectiv* supplied HMRC with complete documentation relating to all trades in issue, including purchase orders and purchase and sales invoices and "details regarding the traded goods such as serial numbers, part numbers, batch numbers, product details, quantity, price per unit, what market research it carried out, name of manufacturer, website address, contact name and name of the authorised distributor" (see [103] of the FTT decision and [25] of the agreed statement of facts), as well as third party inspection reports which provided additional information (see [106] of the decision). In contrast, there are significant gaps in EDC's Deal documents, as we discuss further below; and

(3) the FTT in *Synectiv* made its decision, having assessed a multiplicity of different facts, and it is not appropriate to take one or two particular points and seek to rely on them by analogy in a different case.

Deal G

466. As noted above, Mr Chhatwal's evidence was that the emails between Mr Chhatwal and Mr Rahman of ARU were required because there was no mobile phone reception between him and Mr Rahman, and he asked the Tribunal to accept that the emails were evidence of genuine negotiation between the parties on price.

467. However, none of the many emails between Mr Chhatwal and Mr Rahman refer to there being any difficulty making contact by phone. Instead:

(1) on 21 March 2011, Mr Rahman emailed Mr Chhatwal saying "further to the telephone conversation I would like to thank you for your offer", see §362(2); and

(2) on 23 March 2011, Mr Chhatwal called Mr Rahman asking for details of the delivery address, see §364(3).

468. Furthermore, as set out at §368, the emails are inconsistent in relation to key factual matters: the location of the ordered goods; the number of units delivered to EDC and the number of pallets required for transportation. Given these factual inconsistencies, we do not accept that the emails show that Mr Chhatwal and Mr Rahman were engaged in a genuine negotiation. Instead, we find they were, at least in part, window-dressing. That conclusion is further supported by the existence of conflicting CMRs for the same goods, see §369(5).

469. However, we accept that the emails do provide evidence of the sort of exchanges which happened in the course of EDC's normal business dealings. Mr Chhatwal and Mr Rahman not only discussed pricing and deliveries, but used the emails as the vehicle to transmit documents: a payment confirmation, an EDC pro-forma invoice; an ARU purchase order, and an EDC invoice. We refer to this example of normal business practice again at §502 below.

The deal book

470. Mr Chhatwal also produced a "deal book" which he said covered both wholesale and retail transactions. As already noted at §455, his first witness statement, described how he negotiated deals (emphasis added):

> "Once I understood what the customers' needs were, I would generally contact suppliers and make enquiries as to the availability of stock delivery timeframes and price."

471. He then said:

> "Exhibited at pages 68 to 72 of DCl are an example of my sales orders recorded during such enquiries and the resulting Sales Order Acknowledgements ('SOAs')."

472. The exhibited documents to which he referred were extracts from his deal book, including a column headed "SOA". Mr Chhatwal therefore himself accepted that his deal book was used to record the results of the negotiations between customers and suppliers, and also said that "SOA" meant Sales Order Acknowledgments.

473. Mr Ginn reviewed the deal book, but could find no reference to any of the disputed transactions; he recorded the result of his review in his first witness statement**.** Mr Chhatwal responded by changing his evidence: his second witness statement states that the "purpose of the book was to record sales orders in respect of televisions".

474. In cross-examination, Mr Watkinson pointed out that the deal book also included transactions involving items other than televisions. Mr Chhatwal again changed his evidence, saying that by "televisions" he had meant "generally a lot of brown goods, so the book includes things like televisions, home cinemas, DVD players"; that the book's purpose was to record rebates from suppliers and that SOA meant "sales out allowances" which was a reference to promotional support provided by manufacturers.

475. As is clear from the exhibited pages of the deal book, it contained details of deals on a whole range of items, including washing machines, fridge freezers, cameras, Blu-ray players and iPhones. EDC regularly purchased Blu-ray players from CentreSoft, and iPhones were the goods involved in Deal P. And, as Mr Watkinson pointed out, the book also records a deal with Everyberry for two iPhones at a cost of £1,020. Everyberry was also the customer in Deal A, and Mr Watkinson asked Mr Chhatwal why he had written down "a potential deal with Everyberry for two iPhones, but not for buying 400 PlayStations". Mr Chhatwal responded by saying "It might have been written down somewhere else". Asked to expand, he said:

> "with the indirect market, it could be the case that when I got a price regarding something, I would write that price down on a piece of paper. I would then phone - it would be in my head and I would then phone up my customer and tell them what the price was. There was no permutation involved in the price. It was just a net price."

476. By "a net price" we understand Mr Chhatwal to mean the price without any sort of rebate. We accept that many of the items in the deal book relate to goods on which the supplier has agreed to a rebate, and that Mr Chhatwal wanted to make a note of those rebates. But there are many other deals recorded in the deal book, and it also includes notes of negotiations, such as "Willie has agreed via email [product ref] x 50 pcs @ £50/unit - £2,500 + VAT" and a subsequent note, saying**:**

> "Agreed with Rob
>
> [product ref] x 200pc @ 126.99 – agreed £99 (£31.99pb)
>
> [product ref] x 60pcs @ 145
>
> [product ref] x 50pcs @ 253.22 – agreed £240 (£13.22pb)
>
> [product ref] x 40pcs @ 195 – agreed £180 (£15 pb)"

477. Mr Chhatwal's evidence about the deal book was inconsistent and lacked credibility. We find that it (a) included the type of items which were bought and sold in the disputed transactions, and (b) if Mr Chhatwal had been carrying out his usual "labour intensive process" of calling "numerous suppliers" in order to make the Deals which are in issue, he would have recorded these in the deal book, as he originally said was the position, when he signed his first witness statement.

Unable to access?

478. EDC's November 2010 VAT return was selected for extended verification soon after its submission, and HMRC took the same action following the submission of the VAT returns for February 2011 through to June 2011. EDC was thus aware very soon after each of the disputed transactions, that HMRC were looking carefully at whether they were connected with fraud, and whether to refuse part of all of the related VAT repayment.

479. On 2 October 2012, Mr Ginn issued EDC with a "pre-assessment letter", setting out HMRC's preliminary view. On 7 December 2012, Mr Balson, a solicitor with EDC's then agent, Pinsent Masons LLP, responded, making various factual assertions by way of explaining EDC's position ("the Pinsents Letter"). On 14 February 2013, Mr Ginn asked for evidence and documents to support those assertions, and for any other information held by EDC or Mr Chhatwal which was "of material relevance" to the issues in dispute.

480. On 21 February 2013, Mr Chhatwal informed HMRC that Mr Balson had moved to the Khan Partnership, and that EDC had decided to instruct that firm instead of Pinsents. On 22 February 2013, Mr Balson asked for an extension of time to respond to HMRC's letter, saying:

> "while it may be true that some of this material is easily retrieved, other evidence will take time to collect: for example, EDC may wish to obtain corroborative evidence from its suppliers and customers, some of whom are based overseas."

481. On 28 March 2013 the Khan Partnership replied to Mr Ginn's letter of 14 February 2013**,** attaching very limited supporting documentation. On 30 June 2013, EDC ceased trading.

482. Mr Chhatwal's first witness statement is dated 28 November 2014. It repeats many of the points made in the Pinsents Letter. On 23 December 2014, HMRC again asked for supporting documentation. On 17 February 2015, the Khan Partnership informed HMRC that:

> "The Appellant utilised a software program for the electronic management of its purchases and sales including for wholesale transactions. The Appellant's licence in respect of this program ended in 2012. Since that time it has not renewed its licence to use this software, as it no longer required access to it. As such, the Appellant cannot access this historical information in electronic form."

483. The letter attached extracts from Mr Chhatwal's deal book, along with certain other material, but also stated that much of the documentation requested by HMRC was outside EDC's custody or control. In particular it said:

> "Mr Chhatwal does not have access to all historical emails which were exchanged during the period 1 January 2008 to 3 June 2011. EDC provided only limited documentation about the disputed transactions."

484. HMRC wrote again on 26 February 2015, asking if there was a separate day book for wholesale transactions, and pressing for the reasons why the other documentation could not be provided. On 25 March 2015, the Khan Partnership replied, saying (emphasis added):

> "The Appellant has made further enquiries into the information which has been retained electronically in relation to its transactions and can confirm that it does not have access electronically to purchase and sales listings for each of EDC's wholesale transactions between Q3/2007-Q4/2012, regardless of whether the licence to utilise the relevant software is renewed as the <u>hard drive on which this information was stored is no longer in use and cannot be recovered</u>."

485. The Khan Partnership also said:

> "The Appellant does not have access to all historical emails which were exchanged during the relevant period as full archives of the Appellant's emails have not been retained. There is no further emails [sic] that the Appellant envisages having access to in the future."

486. In his second witness statement Mr Chhatwal said:

> "In respect of the emails sent to my colleagues, I no longer have access to these emails due a technical issue with our server, which resulted in the permanent loss of data stored in these email account."

487. During cross-examination, Mr Chhatwal was asked if he had documentary evidence of EDC's stock offers to potential customers. In his reply, Mr Chhatwal said that EDC regularly deleted emails. The exchange went like this:

> "Mr Watkinson: Mr Chhatwal, there are no stock offer forms that you have sent out in respect of any of these deals?
>
> Mr Chhatwal: No, and you won't find those with all the other thousands of transactions that I did.
>
> Mr Watkinson: But you say in your evidence that you sent them to a distribution list, including existing customers and prospective buyers. Is that just made up?
>
> Mr Chhatwal: No
>
> Mr Watkinson: So why won't we find them any anywhere?
>
> Mr Chhatwal: Because they're probably done by email and we don't have – I was collating this evidence at the time when I was closing my company down.
>
> Mr Watkinson: You are obliged to keep your business records. You didn't destroy all the evidence of these transactions, did you?
>
> Mr Chhatwal: We – no. We – we had lots of emails coming in all the time, and in order to free up our server space, we were told by our IT department to delete lots of emails on a weekly basis. We had a call centre that was operating on an insurance replacement business, and in order to keep that, the speed of everything, we had to delete a lot of emails."

488. EDC had therefore provided the following different reasons as to why it was only able to provide such limited documentary support for Mr Chhatwal's oral evidence:

(1) the information could not be accessed because EDC had not renewed the licence;

(2) the hard drive was "no longer in use and cannot be recovered";

(3) emails could not be recovered because of "a technical issue with our server" which had led to the "permanent loss of data";

(4) Mr Chhatwal was collating the evidence at the time he was closing the company down, and was therefore distracted; and

(5) EDC's IT department required that "lots of emails" be deleted on a weekly basis.

489. However, in the course of the Tribunal hearing Mr Chhatwal was nevertheless able to connect to the remote server which EDC had had five years ago, and recover emails. This surprising event came about as follows.

490. Mr Chhatwal was cross-examined over three days. As already explained at §312, on Mr Chhatwal's first day in the witness box, Mr Watkinson invited him to produce examples "from within the evidence which we have", which would link the

phone numbers specified in his Phone Schedule with third party evidence from EDC's suppliers and customers. On the following day, Mr Chhatwal said:

> "But on a point which was brought up yesterday about: do I have any evidence of deal transactions; in my process of enquiring about mobile phone numbers matching up with the three suppliers that were required, I managed to make contact with our old remote server, and I have now found some emails showing transactions between myself and those suppliers.
>
> We managed to contact – I managed to contact the remote server. I actually have them all on my phone, and they actually show emails between myself and RLR and Electrocentre and Zippy, not all of the transactions, not all the hundreds of calls that were made, but there is evidence that – it is only because I have been asked to now find mobile numbers that correlate to the people that are on the Vodafone itemised billings."

491. Mr Watkinson said:

> "We have asked for this material for years. Mr Chhatwal's witness evidence was, for example, in respect of the emails, they no longer had access to them due to a technical issue with the server which resulted in permanent loss of data."

492. The Tribunal asked Mr Frain-Bell to confirm our understanding of this exchange:

> "Tribunal: Mr Chhatwal's evidence given under oath [was] that he was last night able to make contact with an old remote server, that he had previously said he couldn't.
>
> Mr Frain-Bell: That's correct."

493. The Tribunal subsequently asked Mr Chhatwal how he had managed to access these numbers. He said:

> "What happened was that I was asked to find out some mobile phone numbers and who they belonged to. I typed in those mobile phone numbers into my phone which I hadn't tried for a number of years because there's nothing happening in this – with regards to this case. I typed it in. It came up with a few emails, not a huge range but a few… So from my phone I was connected to the remote server we had five years ago and the emails popped up on the search facility when I typed in a key word search."

494. The Tribunal found Mr Chhatwal's evidence as to why he had not produced supporting documentation for his oral evidence to be unreliable. Not only did the reasons change over time, but the core assertion – that the data was permanently lost – was undermined by his ability to recover emails during the hearing when he thought they would assist his case.

The mobile phone records

495. Mr Chhatwal said that he made contact with his suppliers and customers by phone, and that it was he, and not another EDC employee, who made those contacts. Mr Frain-Bell submitted that Mr Chhatwal's mobile phone records were evidence of the negotiation which occurred in relation to the Deals.

496. Given the customer-driven approach taken by EDC, Mr Chhatwal would have had to speak to the customer and then to the supplier. However, this this happened in only the following three Deals:

(1) Deal A: On 1 November 2010, before EDC ordered the goods, Mr Chhatwal called its customer, Everyberry, and spoke for over 10 minutes**.** There were four further calls on 2 November 2010, totalling almost 20 minutes, and on 4 November Mr Chhatwal spoke to Everyberry for around a minute. There were also calls between Mr Chhatwal and Electro (the supplier) during the same period.

(2) Deal G: the emails between Mr Chhatwal and Mr Rahman refer to calls having taken place (see §362(2) and §364(3)). Although these are not recorded on Mr Chhatwal's mobile phone records, in reliance on the emails, we accepted that these calls took place. There were also two calls between Mr Chhatwal and Electro on 21 March 2011 for a total of 15 minutes, and a further three calls on 22 March 2011, one at 10.46am for 19 seconds; one at 11.20 for 1 minute and 43 seconds and one at the end of the day, for four minutes and 21 seconds.

(3) Deal O: Mr Chhatwal called Anovo, the customer, at 9.27am and spoke for just over 3 minutes; he then immediately called Electro, the supplier and spoke for 12 minutes. There was one more call between Mr Chhatwal and Anovo, and between Mr Chhatwal and Electro, that afternoon, each call lasting around a minute.

497. Taken on their own, the calls between the parties in these three Deals could have been for the purpose of negotiating terms. HMRC's position was summarised by Mr Ginn, who said that:

> "…the content of those calls is unknown. It could have been it was Mr Chhatwal chatting with the other members of the fraudulent transaction chains."

498. In deciding this issue, we took into account the following:

(1) there was evidence of customer contact by phone in only three of the 20 Deals;

(2) Mr Chhatwal's normal method of transacting business was that he "would call numerous suppliers for product availability and price quotes". The mobile phone records do not reflect that process, but are instead calls to the specific business which supplied the goods in question; and

(3) there was no documentary evidence as to what was said during these calls. The only exception was Deal G, where there was a mixture of phone calls and

emails, but we have already found that the emails were at least in part, window-dressing; and

(4) as Mr Ginn said, the existence of phone contact is not itself proof of genuine commercial negotiation; it is also consistent with knowing participation in fraudulent transaction chains

499. We find that there was no reliable evidence that Mr Chhatwal used his mobile phone to carry out genuine commercial negotiation about the terms of the Deals.

500. In coming to that conclusion, we did not overlook the fact that in a normal transaction the customer would make the first contact, so Mr Chhatwal would receive an inbound call, which would not show on his mobile phone records. However, this did not explain the lack of any record of contact with customers before the Deal was concluded, because on receipt of a customer request, EDC's normal process was to try and source the required stock; Mr Chhatwal would then have had to call the customer back in order to put the available stock offer(s) to him, including timing, quantity and price. As Mr Chhatwal himself said, once he had a price, he would "phone up my customer and tell him what the price was". Thus, even though the first call would be inbound to Mr Chhatwal, his phone records would still record a contact with the customer. Yet there is no evidence of any such contact for the vast majority of the Deals.

Conclusions on negotiation

501. We therefore find as facts that when carrying out his normal commercial business, Mr Chhatwal kept a written record of his discussions, but there are no reliable records of any negotiations relating to the disputed transactions. Either (a) the records exist, but Mr Chhatwal has chosen not to provide them, because they do not assist him; or (b) they do not exist, because the Deals were part of a pre-planned sequence of transactions, and no negotiations were necessary.

Documentary evidence of contact with customers at inception of the Deals?

502. We have already found as facts that (a) EDC ordered goods requested by its customers, and (b) as a matter of normal business practice EDC would receive a purchase order from the customer and issue one to the supplier, as in Deal G discussed at §469 above.

503. However, EDC only received customer purchase orders before contacting the supplier in two of the 20 Deals. One was Deal G, which, as we have already found, contained elements of window-dressing; the other was Deal N. As noted at §410, the Deal N purchase order had unusual features: it was not on headed paper, so had no company logo; in the box for "purchase ref" the figure "0" was inserted; and the spaces for authorisation and delivery date were left blank.

504. We have also already found as facts that EDC twice ordered goods before it received purchase orders from the customer. In Deal H, Electro invoiced 1,000 160GB PS3s to EDC the day before ARU issued its purchase order, and in Deal N,

Electro similarly invoiced EDC for 1,000 160GB PS3s the day before EDC received Anovo's purchase order.

505. Taking all the above into account, we find that (a) there was no reliable documentary evidence that the customers ordered the goods, and (b) the fact that EDC ordered the goods in Deals H and N before receiving the purchase orders from its customers indicates that the Deals were pre-planned.

Contacts with suppliers

506. If, as EDC said was the case, it was ordering the goods from the supplier in a transaction which Mr Chhatwal believed to be genuine, there would need to be contact between EDC and the supplier before that supplier invoiced EDC. Mr Chhatwal accepted that he was the person at EDC who would have made contact with the suppliers in the disputed transactions.

507. Documentary evidence that Mr Chhatwal contacted the supplier before the goods were invoiced exists in nine of the Deals. In Deals B, C, D, I, L, Q and S, EDC issued the supplier with a purchase order; in Deal G, EDC's invoice refers to a purchase order although none has been exhibited, and in Deal M, Mr Chhatwal sent an email setting out his order.

508. Mr Chhatwal also called the supplier on or before the day on which the goods were invoiced to EDC in a further ten Deals (A, E, F, H, J, K, N, O, R and T). Mr Frain-Bell asked the Tribunal to find as a fact that, during these calls, EDC was ordering the goods for its customer. Mr Watkinson submitted that there was no evidence as to what was discussed, and that what was really happening was that Mr Chhatwal was discussing how to operate the fraudulent transactions with which he was involved. He pointed out that many of these calls were extremely brief, often for less than a minute, and so were not consistent with any sort of negotiation or discussion, and that none of the other parties had given evidence as to what had been discussed. We agree with Mr Watkinson that there was no reliable evidence as to what was discussed during these calls, and we decided that we could place no weight on the fact that Mr Chhatwal had spoken to the supplier in these Deals.

509. Thus, there are nine Deals where there was evidence of contact with the supplier as to the goods to be ordered. This was less than half the disputed transactions. Moreover, in Deal P, and the second part of Deal J, there was no evidence of any contact whatsoever between EDC and the supplier – neither phone records nor purchase documentation. The first indication that there had been a deal is the invoice from the supplier to EDC.

Other gaps in the paperwork

510. Mr Watkinson said:

> "Most of what Mr Chhatwal has said in his evidence should be capable of being supported by documentation obtained in the course of his business, yet in respect of these transactions, documents supporting his various explanations are conspicuous by their absence."

511. Mr Frain-Bell accepted that "not every piece of paperwork…is available for every single trade" but submitted that "the majority of the trades come with paperwork"**.**

512. In addition to our findings on whether there are orders from the customers to EDC and from EDC to the supplier, we also considered whether there were other gaps. From our detailed analysis of the Deals in Part 6 we agree with Mr Frain-Bell that the majority of Deals come with invoices, because there are invoices between the supplier and EDC, and between EDC and the customer in all but the following:

(1) Deal A, where there is no VAT invoice from the supplier;

(2) part of Deal D, where there is no EDC invoice to the customer; and

(3) Deal K, where there were no EDC customer invoices and we were unable to make findings about who the customers were.

513. However, the Deals formed part of fraudulent transaction chains, in which the purpose was to obtain repayments of VAT. We therefore place little weight on the existence of the invoices, as their absence would allow HMRC to deny the VAT repayment in any event.

514. In most of the Deals there were also delivery/collection notes and/or CMRs, but there were some gaps – for instance, in Deal A the delivery note was only for the Move Starter Packs, not for the PS3s, and in Deal T there was no record of the goods leaving EDC. Mr Watkinson submitted that without a delivery note, it was not possible to check whether the goods which had been delivered were the same as those which had been ordered, and we agree.

Goods supplied only after payment

515. In two transactions, Mr Chhatwal said he had ensured that EDC received payment from the customer before the goods were despatched, and he was acting commercially to protect EDC's position. One of these transactions was Deal F: Mr Chhatwal said that EDC were paid by BAK before the goods were despatched because he was aware that BAK was a small business. The banking and collection documentation for Deal F shows that payment was indeed received before the goods left EDC.

516. The second was Deal G. Mr Chhatwal said in his witness statement:

> "I made the commercial decision that EDC would require payment up front or a deposit in order to trade with Unipessoal as EDC and Unipessoal did not have a previous history of trading and they were ordering a large amount of stock."

517. However, as Mr Watkinson pointed out, this is not correct: it was Mr Rahman who offered to pay in advance, Mr Chhatwal did not require it. Deal G therefore does not provide evidence that Mr Chhatwal was managing the commercial risk of a new customer. Deal F is the only example of EDC requiring payment before delivery.

Goods supplied before payment

518. In contrast, EDC frequently allowed the goods to be delivered to the customer before it had received payment, despite the fact that it retained title to the goods until payment was received under its terms and conditions, see §77. When Mr Watkinson asked Mr Chhatwal to explain why he had allowed the goods to be despatched before payment, he said:

> "Those were customers that I had an excellent trading relationship with… in business, in real business, you look to deal with people, big customers, you try and get their business…we gave goods away before we received payment, and they were to customers that we had a good working relationship with."

519. We accept that this was the case for the Deals with Ewert and Redcoon. However, it was not the position with XXL or Anovo. In Deal L, EDC released goods worth £36,400 to XXL six days before payment was made. Mr Chhatwal said in his witness statement that he "was happy to allow delivery of the goods before payment" because XXL was "low risk" and "a company of significant standing". However, EDC had no reasonable basis for those conclusions, as it did not check XXL's VAT status until after the transactions in question, and never carried out financial due diligence, see §304.

520. EDC released the goods early in all four Anovo Deals, for a total value of £807,754:

(1) Deal N: EDC released goods invoiced at £229,200 two days before receiving payment;

(2) Deal O: EDC released goods invoiced at £120,384 two days before receiving payment;

(3) Deal R: EDC released goods invoiced at £261,014, two days before receiving payment; and

(4) Deal T: EDC released goods invoiced at £103,500, at least a day before receiving payment.

521. Mr Chhatwal said in his witness statement that EDC did not begin dealing with Anovo until three to four months after he received the email from Ms Nina Kahlon at Samsung on 14 February 2011. Deal N took place on 5 April 2011, and was therefore either the first deal between EDC and Anovo, or one of the first. Anovo was therefore not a customer with which EDC already "had an excellent trading relationship" or "good working relationship", despite Mr Chhatwal stating that this was a precondition before EDC allowed credit.

522. Mr Chhatwal said that Anovo was "a reputable company" which he did not believe would pose a financial risk. However, not only had EDC carried out no financial due diligence on that company**,** but Anovo had asked for credit of £1m and been refused, see §268(5)(b). The normal consequence of refusing credit is that payment must be made before delivery, and in EDC's case this was also in accordance with its normal terms and conditions. However, Mr Chhatwal said that

the result of refusing credit to Anovo was that "all trades were paid either on, or within 3-4 days of, delivery". That is not a refusal of credit. Had payment not been received, EDC would have parted with goods to which it still retained title, to a very new customer, contrary to its general terms and conditions.

523. We agree with Mr Watkinson that releasing the goods in these five Deals before payment was not normal commercial behaviour.

The source of the PS3s and their specification

524. The goods in all but two of the Deals were PS3s. The exceptions were Deal K, where the goods were televisions, and in Deal P, where they were iPods. We next consider the origin of the PS3s, and the issue of their EU/UK specification.

Where did the PS3s come from?

525. EDC's original position was that the majority of the PS3s were UK specification – i.e., with a UK three-pin plug and instructions in English. The Khan Partnership letter of 28 March 2013 said:

> "According to EDC's records (in particular, the invoices which indicate whether the stock was EU specification) the majority of the goods sourced from Electrocentre, Zippy Distribution and RLR Distribution were UK and not EU specification. EDC would only supply EU specification stock if it was specifically requested by the customer."

526. Consistently with that letter, Mr Chhatwal said in his witness statement that "CentreSoft essentially created the soft bundle splitting market by offering competitive prices"; that one of his suppliers, Electrocentre "was purchasing large volume of goods from CentreSoft" and that he was:

> "aware other retailers were often buying the soft bundles offered by CentreSoft, splitting the bundles and then selling the elements of the bundle at a discounted price."

527. In relation to the PS3s purchased by EDC, he said by way of example that all the PS3s sold by EDC to Ewert were UK specification. In relation to the suppliers, he said that "Electro Centre advised me on numerous occasions that it was acquiring and splitting soft bundles" and "RLR told us that they were purchasing soft bundles, splitting the bundle, achieving a higher margin on the games and was accordingly able to offer EDC the consoles at a lower price". Mr Chhatwal did not say that his suppliers told him they were purchasing soft bundles from authorised distributors elsewhere in the EU, importing the soft bundles into the UK, and then splitting those bundles.

528. The picture Mr Chhatwal draws in his witness statement is therefore that:

(1) CentreSoft supplied soft bundles containing UK specification consoles and games;

(2) the purchasers of those bundles split them and sold the consoles separately; and

(3) most of the PS3s in the disputed transactions were sold to EDC by the business which had split the bundle.

529. In his oral evidence Mr Chhatwal took the same position, saying that both Zippy and RLR had told him they were buying the bundles from CentreSoft, and splitting them. However, it is clear from our detailed findings at Part 6 that:

(1) in 14 out of the 18 Deals, the consoles were of EU specification,

(2) Sony never supplied EU specification PS3 models to CentreSoft, see §145, so these EU specification models were not purchased from CentreSoft; and

(3) the PS3s sold to Ewert in Deals E, I and J were EU specification; these Deals involved a total of 2,300 PS3s. It was only Deal B, for only 500 PS3s, where the goods were of UK specification. Mr Chhatwal struggled to explain why he did not know that most of the goods shipped to Ewert were EU specification. Under cross-examination he accepted that "the paperwork, it says something very different".

530. The EU consoles originated in the EU, were imported into the UK and were then re-exported by EDC. Mr Watkinson said there was no reasonable commercial explanation for that circularity, and that the following obvious questions arose:

(1) why the stock was imported into the UK at all, rather than being sold to customers in the EU;

(2) why there was:

(a) an apparent glut of stock in the EU, so that the consoles were imported into the UK, but simultaneously

(b) a high level of demand for the same stock, so that EU companies were coming to the UK to buy more consoles;

(3) why the consoles were imported into the UK without any steps being taken to make them suitable for sale here, such as the addition of plugs;

(4) if the consoles were always intended for the EU market, why they were not warehoused there and subsequently sold from there;

(5) why importers incurred the cost of shipment both to and from the UK, with its associated risks of damage or theft; and

(6) why EU wholesalers were seeking EU specification stock in the UK rather than elsewhere in the EU.

531. We agree with Mr Watkinson for the reasons he gives that there is no reasonable commercial explanation for this circular trade. Mr Watkinson also said that these points would have been obvious to Mr Chhatwal, an experienced trader in PS3s, and again we agree.

532. Faced with the facts about the EU specification of most of the PS3s involved in the Deals, Mr Chhatwal again changed his evidence in the witness box, and said:

> "we were told by our immediate supplier that the bundle had been split in another country, the customer had split the - sold the game on and the other peripheral items, just as you could do it with CentreSoft, and then the console was made available at a very low price."

533. Until then, Mr Chhatwal's evidence had been that his suppliers had told him they had purchased and split the soft bundles, not that the bundles had been purchased and split overseas, and then sold to his supplier.

534. We do not accept his new evidence. Instead, we find as a fact that the reasons why Mr Chhatwal was wrong in his witness statement about the origin and specification of most of the PS3 and why he was not bothered by the uncommercially of a circular trade in EU specification goods is because the origin and specification of the consoles were irrelevant to him. We go on to consider whether he had a legitimate basis for his indifference.

What the customers requested?

535. We begin with the Khan Partnership letter, which says "EDC would only supply EU specification stock if it was specifically requested by the customer". However, the customer only requested EU specification stock in Deals H and N. In the other Deals EU stock was supplied, but there is no evidence – such as a purchase order or email – that the customer had requested it.

536. What about the UK specification goods? These were supplied to the customers in Deals A, B, C and L. In Deal A, the customer was a UK company. But in Deals B, C and L the customers were Ewert, Redcoon and XXL, all German companies. There is no evidence of communication between EDC and either Ewert or Redcoon before EDC purchased the goods from its suppliers in those Deals, so there is no record of EDC obtaining their agreement to receiving UK specification consoles. Moreover, in Deals B and C, none of the documentation stated that the goods were UK specification, and in Deal L, neither EDC's invoice to XXL, nor the delivery note, referred to the specification of the goods.

537. We find as a fact that in all but three transactions, the customer did not request the specification of the goods which it received.

Did it matter if the consoles had the wrong specification?

538. Mr Chhatwal said in his witness statement:

> "The only difference between EU and UK specification PlayStation 3 consoles is the AC power plug and hard copy instruction manual language. The plug can and regularly is changed by supplying a clip on plug or a replacement power cable. I understand that well established legitimate companies such as Redcoon and Pixmania regularly supply clip on plugs or a replacement power cable with their products and the practice is widespread throughout the industry as demonstrated by Pixmania's Terms and Conditions...UK specification goods regularly end up with consumers in the EU and vice versa…Whilst EDC did not place snap on plugs or replacement power cables into the boxes, I am

aware that these products are very cheap. They are about £0.05 to manufacturer."

539. We accept that it is possible to use a UK specification PS3 in the EU, and to use an EU specification PS3 in the UK, by having an adapter or similar. But both parties agreed that it was nevertheless necessary to know the specification of the goods, because the buyer may need to add the correct adaptive device when the goods are sold.

What is recorded on the documentation?

540. We considered whether the specification is clear from the documentation which accompanies the Deals. In the following Deals, there are three consistent documents:

(1) in Deal H, Mr Chhatwal's told Mr Rahman that he had EU specification consoles; Electro's delivery note to EDC gives that specification, as does ARU's purchase order, but it is not included on Electro's invoice to EDC. or on EDC's invoice to ARU;

(2) in Deal N, Anovo ordered EU specification goods from EDC using a purchase order. Although Electro's invoice to EDC does not include a specification, EDC's invoice to Anovo states that the goods are EU specification, as does the collection document; and

(3) in Deal T, Zippy's invoice to EDC specifies EU stock, and this is also included on Zippy's delivery note and EDC's invoice to Anovo.

541. Those Deals are, however, very unusual. In almost all other Deals, there are significant gaps:

(1) in Deals A, B, C, D, E and S, none of the documents say whether the goods are of UK or EU specification. This has only been established as the result of HMRC Officers checking other parts of the relevant deal chain;

(2) in Deals F and O the invoices from Electro to EDC state the specification, but there is no reference to it on EDC's invoice to the customer;

(3) in Deal G, the specification is referred to in the customer's purchase order and subsequent email, but not on the invoice from the supplier to EDC, or on the invoice from EDC to the customer;

(4) in Deal I, EDC issued a purchase order to RLR, the supplier, specifying EU consoles, and RLR's delivery note also says that it delivered EU consoles. But that information is not included on RLR's invoice to EDC, or on EDC's invoice to Ewert; and

(5) in Deal J, the only reference to the specification is on RLR's delivery note to EDC, so the information was not transmitted to Ewert, the German customer.

Did Mr Chhatwal and the customer know the specification

542. When cross-examined about these gaps in the documentary evidence, Mr Chhatwal said that the specification was discussed in phone conversations between him and the customer and the supplier. Mr Watkinson asked him if this was "the kind

of thing you would write down" and Mr Chhatwal responded "maybe it would be in my head", and that "sometimes you would, sometimes you wouldn't" put the specification on the invoice. He said that this didn't matter because "the relationship I had with my customers, they knew what product they were getting".

543. In a legitimate trading transaction it is not credible that such an important fact would be omitted from so much of the paperwork, with reliance being placed instead only on conversations. In any event, as we have already found, Mr Chhatwal only contacted customers before the goods were invoiced in Deal G and Deal N.

544. Mr Chhatwal later said that he called EDC's warehouse before the goods in the Deals were delivered and required his staff to check they were of the correct specification. That evidence was not in his witness statement, and it is not credible that he remembered it for the first time during the hearing. Moreover, it is inconsistent with his other evidence, which we accepted, that EDC checked delivered goods only for obvious visual damage, see §605.

545. We therefore find that the gaps in the documentation were not remedied by oral discussions between (a) Mr Chhatwal and the customer, or (b) between him and EDC's warehouse staff.

Inconsistencies

546. In addition to the gaps in the documentation, the documents for two Deals are inconsistent in relation to the specification of the goods.

(1) in Deal M, Mr Chhatwal's email to Zippy states that EU plugs are required, but Zippy's invoice to EDC says that the consoles are UK specification. We noted that two calls took place between Mr Chhatwal and Zippy after the goods were delivered, and considered whether to infer that this difference was discussed and resolved during one or both of those calls. However, we decided not to make that inference, because in a normal commercial transaction the seller would have confirmed that change of specification to its customer, perhaps by including it on the invoice or on the delivery note; and/or calling the customer, but the invoice and delivery note do not refer to the specification, and there is also no documented call between EDC and Redcoon, the customer; and

(2) in Deal Q EDC ordered EU stock from RLR; the invoices issued by RLR and EDC both omit any mention of the specification, and the CMR states that the goods were a mixture of UK and EU stock.

Conclusions on specification

547. It was not disputed that the parties needed to know the specification. We find that the reason why so much of the paperwork does not state whether the goods were UK or EU origin; and why some of the paperwork is inconsistent, is because origin and specification were irrelevant to the Deals into which EDC was entering. Mr Chhatwal's lack of care over this element of the transactions indicates that he knew the specification did not matter, because the deals were pre-arranged.

Whether Mr Chhatwal knew there was no commercial grey market in split soft bundles

548. We have already found as a fact that there was no commercial marketplace in splitting soft bundles (see §234). It was HMRC's case that Mr Chhatwal knew that this was the position. EDC's case was that Mr Chhatwal genuinely believed there was such a market, and that it was the source of the consoles supplied to EDC as part of the Deals.

549. In deciding this point we took into account the following:

(1) Mr Chhatwal was very experienced in the electronic goods market, having worked at EDC for around 20 years before the disputed transactions;

(2) he was unable to provide any documentary or witness evidence for his alleged belief in the existence of a commercial grey market for split soft bundles, and was himself not a credible witness;

(3) Mr Gara said that "the custom and practice in the industry was soft bundling worked" so that the whole bundle "went to end consumers". He also said it was "highly unlikely" Mr Chhatwal could have thought that he could do what he liked with the component parts of a split bundle, and we infer that it was, in his view, highly unlikely that Mr Chhatwal could have thought that there was an entire market in which wholesalers carried out this bundle-splitting;

(4) Mr Chhatwal's original position as set out in his witness statement was that he believed the bundle splitting had been carried out in the UK, by his immediate suppliers. Had this genuinely been Mr Chhatwal's belief, he would have asked his suppliers to explain the position as soon as he was offered EU specification PS3s, but instead he was unaware of the specification until shortly before the hearing;

(5) he said that EDC would first exhaust all direct channels of sourcing goods before relying on secondary channels, and had "tried and tried" to get the PS3s from CentreSoft, but it is clear from our earlier findings that EDC could have obtained all the PS3s it required for the Deals from CentreSoft, because there was no stock shortage (see §160); and

(6) Mr Chhatwal said in his witness statement that he "would refer the individual components of the soft bundles" to work out whether the pricing "made commercial sense" but later admitted this was incorrect; he had never sought to establish which soft bundle(s) had been the supposed origin of the PS3s, and so had never sought to establish whether the pricing was credible.

550. We therefore find that Mr Chhatwal knew there was no commercial grey market in split soft bundles, and that he also knew that the PS3s supplied in the Deals had not originated from split soft bundles. Instead, he saw the concept of market in which soft bundles were split as a plausible (but untrue) explanation for the pricing of the consoles.

Buying the goods

551. There are two relevant points here: the prices paid by EDC, and the quantities it purchased from two of its suppliers, RLR and Zippy.

The prices

552. In all the 18 Deals involving PS3s, EDC purchased the consoles from its supplier for a price significantly below CentreSoft's wholesale price, as set out below:

Deal	Model	Centre Soft	EDC	Diff £	Diff %	Supplier
B	320	226.61	190.5	36.11	16%	RLR
C	160	198.79	177	21.79	11%	RLR
D	320	226.61	185	41.61	18%	Zippy
E	160	198.79	188.5	10.29	5%	Electro
F	160	198.79	188	10.79	5%	Electro
G	160	198.79	185	13.79	7%	Electro
H1	160	198.79	185	13.79	7%	Electro
H2	160	198.79	187.5	11.29	6%	Electro
H3	160	198.79	187.5	11.29	6%	Electro
I	160	198.79	188.5	10.29	5%	RLR
J	160	198.79	187.25	11.54	6%	RLR
L	160	198.79	170	28.79	14%	Zippy
M	160	198.79	173	25.79	13%	Zippy
N	160	198.79	185.25	13.54	7%	Electro
O	320	226.61	204.5	22.11	10%	Electro
Q	160	198.79	186	12.79	6%	RLR
R	320	226.61	210.75	15.86	7%	Electro
S	320	226.61	198	28.61	13%	RLR
T	320	226.61	210	16.61	7%	Zippy

553. We have already rejected EDC's explanation for the reduced prices at which it purchased the consoles, namely that it was because of the splitting of a soft bundle, and we have found that Mr Chhatwal knew that there was no commercial market in split soft bundles. It follows from those findings that EDC knew that it could not obtain legitimate goods at these low prices. As set out earlier in this decision, Notice 726 warns traders:

> "A business trading within a market should have a reasonable idea of the market prices for the goods on any given day. If goods are offered

> at what appears to be a bargain price then you should find out the reason for the low cost, if it's too good to be true, then it probably is."

554. Mr Watkinson said that the prices offered to EDC were "too good to be true" and we agree.

555. Furthermore, EDC was purchasing goods in ten of the Deals from Zippy and RLR. It is not credible that either company could source these consoles at a better price than EDC, or that Mr Chhatwal believed that this was the position. Zippy was a sole trader business; its marketing makes no reference to operating in the wholesale market at all, but only to retailing electronic goods (see §260). RLR was a small company run by a former bank manager which became VAT registered around six months before the disputed transactions (see §247). In contrast, Mr Chhatwal had many years of experience in the electronic goods market; had been selling PS3s wholesale since around 2006, and EDC had a turnover of between £19m and £30m during the three years before the disputed transactions (see §79). Yet Mr Chhatwal purchased consoles from Zippy in five of the Deals, at prices which were 18%, 14%, 13% and 10% less than CentreSoft's wholesale prices, and from RLR in five of the Deals at 16%, 11%, 5%, 6% and 13% below CentreSoft's wholesale prices.

556. Mr Chhatwal therefore knew (a) that there was no commercial market in split bundles, and (b) that neither Zippy nor RLR could have had access to the goods at much cheaper prices than EDC. We therefore find that he also knew these PS3s were not part of a legitimate transaction chain.

557. The same is true of the other two Deals where Zippy was the supplier:

(1) In Deal K Zippy supplied EDC with televisions, although EDC was an authorised distributor for Samsung, the manufacturer of the televisions in question, and EDC had vastly more experience in the buying and selling of televisions than Zippy. There is no credible basis on which Zippy would be able to source these goods when EDC could not, at a price which EDC could not better.

(2) In Deal P Zippy supplied EDC with iPods. We have already found Mr Chhatwal's oral evidence about this Deal to lack credibility, see §419. EDC had been trading iPods since at least August 2009 (see §108(1)) and it is not credible that Zippy, a sole trader business in the retail market, could source iPods more cheaply than EDC, or that Mr Chhatwal believed this was the case.

The quantities

558. We have also already found as a fact that EDC carried out no financial due diligence on Zippy or RLR. Yet it carried out the following Deals with Zippy (excluding VAT):

(1) Deal D for £92,500;

(2) Deal K for £16,650;

(3) Deal L for £68,000;

(4) Deal M for £69,200;

(5) Deal P for £34,860; and

(6) Deal T for £105,000.

559. In addition, Zippy invoiced EDC for Deal K on 11 April 2011, and invoiced Deals L and M two days later. The total of the three Deals together was £153,850 excluding VAT. EDC did not have any reasonable basis on which to accept that Zippy, a sole trader, with no experience in the wholesale market, was able to purchase goods of this value for resale.

560. EDC carried out the following Deals with RLR (net of VAT and any delivery charges):

(1) Deal B for £95,250;

(2) Deal C for £20,355;

(3) Deal I for £56,550;

(4) Deal J for £168,338;

(5) Deal Q for £92,256; and

(6) Deal S for £171,440.

561. Yet RLR was run by Mr Uchil, a former bank manager with no relevant background in wholesaling electronic goods, and EDC did not have any reliable basis for accepting that RLR was able to purchase goods of this value for resale.

The profits

562. One of the issues in dispute was whether EDC's margins on stand-alone PS3s were also "too good to be true". We have already found as facts that the maximum margin for wholesalers between the authorised distributor and the retailer is 5%, and that Mr Chhatwal knew this was the position, see §150. Where there was more than one wholesaler in the chain, that maximum margin would have to be shared. EDC always purchased from the goods in the disputed transactions from a wholesaler, so there were always two wholesalers involved. Where EDC had sold to a company other than Redcoon or Ewert, both internet retailers, there were three intermediate wholesalers.

563. EDC's profits for the Deals involving stand-alone PS3s were as follows:

Deal	profit	> 5%	>4%	>3%	>2%	<2%	Redcoon/ Ewert?	No. of w/salers
B	**3.1**			✓			✓	2
C	**5.1**	✓					✓	2
D	**6.5**	✓					✓	2
E	**1.9**					✓	✓	2
F	**3.2**			✓				3
G	**2.2**				✓			3

H1	**3.2**			✓			✓	2
H2	**1.1**					✓		3
H3	**0.8**					✓		3
I	**1.9**					✓	✓	2
J	**2.5**				✓		✓	2
L	**7.1**	✓						3
M	**2.9**				✓		✓	2
N	**3.1**			✓				3
O	**2.2**				✓			3
P	**6**	✓					✓	2
Q	**1.9**					✓		3
R	**2.5**				✓			3
S	**2.5**				✓		✓	2
Totals		**4**	**0**	**4**	**6**	**5**		

564. Thus, there were four Deals where EDC made more than 5%. We agree with HMRC that this was "too good to be true". Given that EDC knew that there were (at least) two other wholesalers involved in Deals F and N, namely its own supplier and customer, the profits on those Deals were also too good to be true.

Share of the profits

565. It was not in dispute that EDC made the highest or second highest profit of all the participants in each of the Deals. Mr Watkinson submitted that this was consistent with knowing participation as a broker, because it is the broker which bears the biggest risk of being left out of pocket if HMRC identifies the fraud in time to deny the repayment. In contrast, if Mr Chhatwal had been an innocent dupe, the other participants in the transaction chain would have had no reason to allocate so much of the profit to EDC, but would have kept a greater share. We agree that this fact is consistent with our other findings.

The speed of the Deals

566. Some of the Deals were conducted within one or two days. For instance:

(1) in Deal C, EDC ordered the goods from RLR on 17 February 2011; on the following day RLR invoiced EDC; EDC invoiced Redcoon; RLR delivered the goods to EDC; Redcoon collected the goods from EDC's site and EDC paid for the goods;

(2) in Deal N, all of the following took place on 5 April 2011: the purchase order was received from Anovo, Electro invoiced EDC and supplied the goods, EDC invoiced Anovo and Anovo collected the goods; and

(3) in Deal P, all the following took place on 27 April 2011: Zippy issued an invoice to EDC and delivered the goods; EDC invoiced Redcoon and Redcoon collected the goods from EDC's premises.

567. Other examples were Deals G and R (two days) and Deals D and L (3 days). In other cases, the invoicing occurred over one or two days, but the shipping took longer.

In Deal O all the paperwork and the delivery to EDC were completed on 28 April 2011, but the goods were collected on 11 May. In Deal E, Electro invoiced EDC on 8 March 2011 and EDC invoiced Ewert the following day, but the goods were not shipped until 14 March 2011. In Deal F Electro invoiced EDC on 24 March 2011, and EDC invoiced BAK on 25 March, and the goods were shipped on 28 March and 18 April 2011.

568. All the disputed transactions were part of MTIC deal chains, and HMRC's unchallenged evidence was that most of the other steps in those deal chains were carried out very rapidly. For instance:

(1) in Deal C the goods were passed between six other companies on 16 February 2017, before being invoiced to RLR on 17 February 2011: EDC ordered the goods on that day, and on 18 February 2011 they were (a) delivered and invoiced to EDC and (b) invoiced and delivered to Redcoon.

(2) In Deal E the goods passed through two companies on 7 March 2011 and two more companies, including Electro, on 8 March 2011; Electro invoiced EDC on the same day and EDC invoiced Ewert on 9 March 2011.

569. Mr Watkinson said that the transactions were contrived and pre-arranged, because it was otherwise impossible for each company to have sourced "exactly the quantity and specification of goods required by its customer" with such speed. We agree. We also note that in Deal F, where the goods were passed through three companies before reaching Electro, the first two invoices are dated 24 March 2011 and the third is dated 25 March 2011, the day *after* Electro issued its invoice to EDC.

570. Mr Frain-Bell said that EDC's business was similar to that of a commodity broker, seeking to match demand and supply, and that such deals were commonly on a back-to-back basis. He again sought to rely on *Synectiv*, where the FTT accepted the Appellant's argument that its trade in the grey market for mobile phones was similar to commodity trading, and the Tribunal said:

> "Back to back trading, which reduced the dealer's risks, was not unusual and is a feature of other commodity markets. Mr Chandoo's evidence was that supply and demand of mobile phones, and therefore prices, usually fluctuated daily on the grey market and this meant that transactions were normally documented within a single working day and, out of necessity, carried out on the basis of a rapid exchange of paperwork."

571. Mr Frain-Bell said that this passage "encapsulated what Mr Chhatwal was doing". Mr Watkinson robustly rejected the analogy, saying:

> "This isn't a market like a commodity market. This is not commodity trading. A Playstation or a television is, as the evidence has shown, a life cycle dependent product destined for an end consumer. It is not like wheat or oil. You don't trade futures in PlayStations. And so it doesn't just sit there and accumulate value, it does the opposite."

572. Mr Watkinson said that the PS3 market was instead "information-transparent", where purchasers knew it was possible to purchase PS3s from a wide variety of suppliers, and knew the prices which were being offered by those suppliers, and where even the authorised distributor had to justify its role by taking the distribution task from Sony and adding value by creating further soft bundles.

573. We agree with Mr Watkinson. His submission was consistent with Mr Sherry's unchallenged evidence that UK consumers "obviously knew what deals were available in the market place". It was also confirmed by Mr Chhatwal himself, when he said (emphasis added):

> "…my customer would tell me that the market price for that product was X amount of money. Was I able to – because there was numerous deals going on in the marketplace – source that product at that particular price?"

574. We add the following further points:

(1) as there was no commercial market in split soft bundles, it follows that the separate parts of the bundles cannot have been traded like commodities;

(2) Mr Chhatwal has provided almost no evidence of any contact between EDC and the customers to initiate the Deals; this would have been a necessary part of any commodity broking business. Instead, there are significant gaps and inconsistencies; and

(3) the position was different in *Synectiv,* where the existence of a commercial grey market was not in dispute, and Mr Chandoo supplied HMRC with complete documentation relating to all trades, see [103] of the FTT decision and [25] of the agreed statement of facts.

575. Mr Watkinson submitted that EDC was a willing and active participant in these pre-arranged transaction chains, and that it is "beyond coincidence" that the parties in these Deals were so often able to contact each other, agree on terms and price, issue the paperwork, organise delivery and collection by the customer, on the same day, or within a two day period. We agree.

The length of the deal chains

576. The length of the deal chains was not in dispute. In Deals B and C there were seven companies in the chain before EDC; in the majority of the Deals there were between six and four companies in the chain, and in those involving Zippy there were only two or three (neither party made submissions as to the reason for there being such a short chain in those Deals and we make no findings on that point).

577. Mr Watkinson submitted that the long deal chains were uncommercial and an indicator of fraud**,** and the Tribunal should take this into account when assessing whether Mr Chhatwal knew or should have known that the Deals were connected with fraud. Mr Chhatwal's evidence was that EDC did not know the other companies in the deal chains, but only its own supplier and customer, and thus did not know they

were so long. In reliance on that evidence, Mr Frain-Bell submitted that the length of the deal chains was irrelevant, because Mr Chhatwal did not know that information at the time EDC did the Deals.

578. We have already found as facts that:

(1) EDC's normal business model was to purchase PS3s from CentreSoft and sell them to a retailer (see §153) whether in the UK or overseas, so it was participating in a deal chain with four participants – Sony, CentreSoft, EDC and the retailer;

(2) a supply chain with four participants was commercially viable, but the margins were tight (see §151ff);

(3) Mr Chhatwal knew that a supply chain involving three or more unofficial wholesalers was not commercially viable (see §154);

(4) in all the PS3 Deals, EDC purchased from an unofficial wholesaler. In ten of those Deals, EDC also sold the PS3s to another unofficial wholesaler, so these deal chains involved a minimum of six participants, including three unofficial wholesalers. In the remaining eight Deals, the PS3s were sold to Redcoon or Ewert, who were internet retailers, and that supply chain therefore involved a minimum of five participants (Sony, the authorised distributor, the intermediate wholesaler, EDC and Redcoon/Ewert).

579. It follows from the above that Mr Chhatwal knew that the deal chains involving customers other than Redcoon/Ewert were not commercially viable, because they contained three unofficial wholesalers; he also knew the Redcoon/Ewert deal chains were longer than EDC's normal commercial business model. We do not need to make a finding about whether Mr Chhatwal knew how many other participants there were in the deal chains.

The value of the VAT involved

580. Mr Watkinson submitted that the scale of EDC's involvement could be seen by considering the VAT position: during periods 02/11 to 05/11, between 67% and 51% of EDC's input VAT arose from MTIC related transactions, being both the Deals and the transactions in which WNL was the defaulter. Mr Frain-Bell was less precise, but we understood him to accept that for VAT periods from 02/11 through to 05/11, at least 50% of EDC's input VAT was traced to fraudulent transactions, and we find that to be a fact.

Other inconsistencies

581. We have already identified and discussed a number of inconsistences: about the location and number of the goods in Deal G; about the ordering of goods before receiving the customer orders in Deals H and T, and the inconsistences about the specification of the goods in Deals M and Q. The documentation also contains the following further inconsistencies:

(1) In Deal H1, EDC purchased 1,000 consoles from Electro and sold them to Ewert. EDC issued its invoice to Ewert on 25 March 2011, four days *before* (a) Electro invoiced EDC and (b) Electro itself purchased the goods.

(2) In Deal S the goods were collected from EDC's warehouse on 11 May 2011, as evidenced by the third party carrier, who signed the collection note; this was two days *before* the goods arrived at EDC from RLR, as evidenced by a signed delivery slip, and they were also collected a day before (a) RLR had purchased the goods from Electro and (b) Electro had itself purchased the goods.

582. Mr Watkinson submitted that these inconsistencies are evidence that the transactions were contrived. Mr Frain-Bell said that the specification inconsistencies were unimportant, but did not respond on the other points. We have already decided that the specification needed to be on the documentation, see §543. We agree with Mr Watkinson that those and other inconsistencies summarised above support HMRC's case that the transactions were contrived.

The "road map"

583. As noted earlier in this decision, Mr Frain-Bell drew our attention to the "road map" referred to by Clarke J in *Red 12*. His submissions are summarised below.

No compelling similarities

584. Clarke J said that the Tribunal should not "ignore compelling similarities between one transaction and another". Mr Frain-Bell said that there were no "compelling similarities" here: although many of the Deals were for PS3s, they were entered into for different reasons, and there were also Deals for iPods and televisions.

585. Although there were similarities between some of the Deals – for example, some are on a back-to-back basis, and many are for PS3s, we agree with Mr Frain-Bell that these are not "compelling" similarities. Had there been compelling similarities between the transactions, we would have taken that into account as a possible indication that HMRC should succeed.

586. However, the converse does not follow. In other words, the lack of compelling similarities does not lead to a conclusion that the appellant neither knew nor should have known that the transactions were connected with fraud. In order to answer that question, the Tribunal must consider all the evidence, see *Davis & Dann Ltd* at [60] and *CCA* at [46], cited earlier.

Identical mark-ups and business capital

587. Clarke J also identified (a) identical mark-ups on the transactions and (b) appellants with "practically no capital but a huge unexplained turnover" as being relevant factors. Mr Frain-Bell said that EDC's profit varied considerably from Deal to Deal, and it was a substantial business with a significant turnover.

588. We agree, see our table at §552 which sets out the profits, and our findings of fact about EDC's historic trading levels at §79. But we cannot decide the *Kittel* test based on the absence of those indicia; again, we must look at all relevant factors.

Stock left over

589. Clarke J also highlighted businesses which participated in purchase and sale transactions, and always managed to match the two, so there was never any left-over stock: he said that one of the factors which may indicate that a transaction is linked to fraud is that all the stock purchased from the supplier is sold to the customer, leaving no unsold stock, see [110] of his judgment.

590. Mr Frain-Bell said that this was not the position here, and pointed to the following transactions (his submissions are in italics, followed by the Tribunal's assessment, based on our detailed analysis at Part 6):

(1) Deal D, *where only 400 of the 500 PS3s were sold on to Redcoon*. We do not accept this. The other 100 PS3s were sold to XXL, at or around the same time, and XXL was not only also a customer in Deal L, but had been involved in other MTIC frauds.

(2) Deal K, *where 90 televisions were left over after the transaction and were sold on, as and when 90 individual orders came in.* This Deal consisted only of the 90 televisions, so they were not "left over". There is no reliable evidence as to what happened to these televisions.

(3) Deal L, *where 400 units were purchased. However only 200 were sold on to XXL, so 200 were left over*. The Tribunal accepts that those 200 consoles did not form part of a disputed transaction.

(4) Deal Q, *where 496 consoles were purchased, 300 were sold to BAK and 196 units were left* over. The Tribunal accepts that 196 consoles did not form part of a disputed transaction.

(5) Deal S*, where 780 consoles were purchased, of which 185 were sold to Redcoon, so 595 were left over*. In this Deal, the documents state that 185 consoles were collected by Redcoon before they had been delivered to EDC, so the Tribunal declines to make any finding as to whether there was any left-over stock.

591. It is therefore clear from the above that in Deals L and Q there was some left-over stock. But again, that does not assist us in deciding whether or not Mr Chhatwal knew or should have known that the Deals were connected to fraud. Just because a regular pattern of selling all the stock to a customer may be indicative of fraud, the occasional presence of some left-over stock does not prove the contrary.

592. We did not overlook the fact that in Deals G and I there was some evidence that some part of the stock had gone missing, and so could not be transferred to the customer. However, in Deal G we found as a fact that part of the purpose of the emails was window-dressing, see §468. In Deal I, we preferred the evidence of Ewert's collection document and the CMR (which showed that all the 300 consoles

had been delivered) to that on RLR's invoice and delivery note (which stated that only 297 had been delivered). Thus, there was no missing stock in that Deal.

All transactions in the period not traced to tax loses

593. The final point made by Mr Frain-Bell in the context of the "road map" was that EDC did not satisfy the indicium, identified by Clarke J, that all the transactions in the period are traced to tax losses, and that many of EDC's deals during these VAT periods have not been impugned. In particular, he drew attention to a number of invoices which included both the goods in the disputed transactions, and other goods. For example:

(1) in Deal A, EDC issued an invoice to Everyberry for 100 PS3s and 200 Samsung televisions. HMRC have only blocked the input tax recovery on the former;

(2) in Deals D, M and S, EDC issued invoices to Redcoon for total amounts of £250,126; £172,139 and £225,666, of which less than half (£78,800; £71,200 and £37,555) related to the PS3s traced to a fraudulent transaction chain, and HMRC did not refuse to repay the VAT on the other items; and

(3) in Deal L, EDC issued an invoice to XXL for 100 batteries for 3D glasses and 200 PS3s, but HMRC only blocked the VAT on the latter.

594. Mr Frain-Bell said that in all these deals, EDC carried out the same due diligence and had the same documentation for the other goods as it had for those where HMRC had denied the repayment.

595. Mr Watkinson's response was that in some of these cases it was clear from the information available that the goods had been supplied to EDC by the manufacturer or authorised distributor: for example, in Deals A and L the televisions and 3D glasses had been supplied by Samsung, and there was obviously no fraud in the transaction chain for those goods. In other cases, HMRC had not been able to trace the origin of the goods, and specifically had not traced them to a defaulting trader or a contra-trader. As a result, the VAT on those goods had been repaid to EDC. The fact that the goods in the disputed transactions had been commingled with other goods was irrelevant.

596. In *Red 12* Clarke J put forward two extremes:

> "A tribunal could legitimately think it unlikely that the fact that all 46 of the transactions in issue can be traced to tax losses to HMRC is a result of innocent coincidence. Similarly, three suspicious involvements may pale into insignificance if the trader has been obviously honest in thousands."

597. This is not a case, like some MTICs, where the appellant has *only* engaged in transactions linked to fraud. EDC has purchased from authorised distributors such as Samsung, and sold those goods to its customers, and those transactions have not been challenged by HMRC.

598. But neither is this a case where there are "three suspicious involvements". EDC has accepted that all the goods involved in the Deals have been traced back to tax losses; there are 20 Deals in issue, and a further 18 where the goods trace back to WNL. Most of these transactions occurred in a relatively short period, with 16 taking place in the three month period from February 2011 to April 2011, contemporaneously with the majority of the WNL transactions. And the sums involved are significant: the VAT denied is £426,145.52, and that does not include the WNL deals.

599. It is true that some of the fraud-related goods have been sold on to customers together with other goods which are not traceable back to a fraudster. But it does not follow that Mr Chhatwal neither knew nor should have known that the impugned goods were connected to fraud. There are other possibilities, most obviously that including the MTIC-related goods in an otherwise benign load may make it more difficult for HMRC to identify and stop the fraud. We therefore place no weight on the fact that the goods in some of the disputed transactions were invoiced and sold together with other goods.

Other points

600. We considered all the evidence and the related submissions of both parties, but found that the following points were not of assistance in coming to our decision.

The slim and the standard PS3s

601. As noted earlier in this decision, Sony first introduced a "slim" PS3 in 2009. Some of the documentation refers to the PS3s involved in the disputed transactions as "PS3 slim" and some simply say "PS3". For example, in Deal B the purchase order refers to "500 PS3 slim" consoles, but RLR's invoice describes them simply as "PS3" consoles. Mr Watkinson drew our attention to this and other similar inconsistencies.

602. However, we have already found as a fact (see §134) that the slim model was first produced in 2009 and replaced the earlier standard model, so that at the relevant time all newly manufactured PS3s were the slim version first produced in 2009. Mr Watkinson asked Mr Chhatwal about old stock, and he agreed that it might stay around for a while. However, the disputed transactions took place in 2011, two years after the introduction of the slim model, and that model was itself discontinued in 2012, see §134. While it is true that some documentation refers to the PS3s as slim, and some does not, the chances of any confusion between "slim" and "standard" PS3s by the time of the Deals was negligible, because in 2011 new standard PS3s were not available in the normal market place. Thus, the difference in the wording on the documentation is of no significance.

Checks on goods

603. It was common ground that there was little or no documentary evidence that EDC carried out checks on the goods received from suppliers, and that there were also few if any recorded checks on goods leaving EDC's premises, with some delivery slips stamped "unchecked" by the freight company or the customer, see for example

Deal A. As this was not in dispute, we did not make detailed findings in Part 6 about the checking (or lack of checking) of the goods in each of the Deals.

604. Mr Watkinson invited us to infer from the lack of checks that EDC had no real interest in the goods. He pointed out that EDC was buying from the grey market, not an authorised distributor, and it made commercial sense to check that it had received what it had ordered. Similarly, if EDC did not check the goods received, and they were subsequently returned by the customer, the company's poor record-keeping and lack of inspection documentation mean that it could not even know whether it had supplied the item(s) in question, let alone whether the order sent out was complete and the stock in good condition.

605. Mr Chhatwal's evidence was that warehouse staff would only inspect stock for signs of physical damage, and this would be recorded on the delivery notes. That was consistent with Mr Sherry's evidence, that CentreSoft would not carry out an inspection of goods delivered as a matter of normal commercial practice. It was only exceptionally, if an employee noticed that a load appeared to have been damaged, that an inspection would be carried out**.** We found that EDC's failure to inspect the goods, other than for visible damage, was normal market practice, and so did not assist us in deciding whether or not Mr Chhatwal knew or should have known that the Deals were connected to fraud.

Serial numbers

606. It was also not in dispute that EDC did not record the serial numbers for the PS3s, or for the televisions and iPods in Deals K, P and S3. Mr Watkinson submitted that these numbers are commercially important in the event of dispute or a claim, and retaining the numbers meant that a trader could be sure that the goods were not re-circulating as part of a carousel fraud. EDC's position was that recording serial numbers was neither practical nor standard industry practice, because the stock was mostly palletised and shrink-wrapped.

607. Mr Sherry's evidence was that CentreSoft never recorded the serial numbers of the PS3s which it bought and sold**,** because it would be operationally difficult and not cost-effective. We found that EDC's failure to record serial numbers was normal market practice, and did not assist us in deciding whether or not Mr Chhatwal knew or should have known that the Deals were connected to fraud.

The Tribunal's conclusion

608. The Tribunal has concluded that Mr Chhatwal knew that the disputed transactions were connected to an orchestrated and contrived fraud, and has dismissed EDC's appeal. In coming to that conclusion, we have taken all our findings into account, and in particular the following:

(1) Mr Chhatwal was not a credible witness, see §28ff;

(2) there was no commercial grey market for split soft bundles (see §234) and Mr Chhatwal knew this was the case, see §550;

(3) EDC made a sudden and radical shift into the grey market, which correlated with its participation in the disputed transactions (see §95), and Mr Chhatwal's explanations for this shift, namely FX differences and stock surpluses in the UK compared to the EU, were not consistent with other reliable evidence, see §91 and §155;

(4) FX differences also do not provide an explanation for the profits EDC made on the exports involved in the disputed transactions, and Mr Chhatwal knew this was the position, see §91;

(5) CentreSoft had available stocks of PS3s during the whole of the relevant period (see §160), and Mr Chhatwal's evidence that EDC would first exhaust all direct channels of sourcing goods (from the manufacturers and authorised distributors) before relying on secondary channels was therefore not credible;

(6) EDC would normally have kept records of negotiation, but there are no reliable records for the negotiations which preceded the Deals, see §501. This is either because Mr Chhatwal has chosen not to provide the relevant records, because they do not assist him, or because they do not exist, because the Deals were part of a pre-planned sequence of transactions;

(7) EDC's normal approach to wholesale transactions was that it responded to customer orders (see §458), but in the case of the Deals there was no reliable documentary evidence that customers contacted EDC before EDC contacted the supplier, see §505;

(8) there is documentary evidence that EDC ordered goods from the supplier in less than half the Deals (see §509). In a further ten Deals Mr Chhatwal spoke to the suppliers before the goods were invoiced, but for the reasons explained at §508, we place no reliance on those calls. In Deals P and the second part of Deal J, there was no evidence of *any* contact between Mr Chhatwal and the supplier before the goods were invoiced to EDC, see §405 and §385. The lack of a documentary record of EDC's orders for the majority of the Deals supports HMRC's case that purchase orders were not required, because the transactions were pre-planned;

(9) it was important that the customer knew whether the PS3s were UK or EU origin, see §539, but many of the Deal documents do not include this information, see §540ff; this was because their origin and specification was irrelevant, given EDC's purpose in entering into the Deals;

(10) Mr Chhatwal was wrong in his witness statement about the origin and specification of the PS3s (see §525ff). This was because, although commercially important, these factors were irrelevant given EDC's purpose in entering into the Deals;

(11) in Deals M and Q, the documentation was inconsistent as to the specification, see §546; in Deal G there were numerous inconsistences, including the location and quantity of the goods, see §368; in Deals H and T, customer purchase orders were dated *after* EDC ordered the goods from the supplier, indicating that the Deals were contrived; in Deal S the goods were collected from EDC's warehouse two days *before* a signed delivery slip stated

that they had arrived at EDC; and Deal H1, EDC issued its invoice to its customer four days *before* its supplier had itself purchased the goods, see §581 for a summary. If the Deals had been normal commercial transactions, the documents would reflect the movements of the goods. These inconsistencies are evidence of pre-planned transaction chains in which such documentary mistakes did not matter;

(12) the prices paid for the consoles were far below those available from CentreSoft, Sony's authorised distributor in the UK, and Mr Chhatwal knew he could not obtain legitimate goods at these low prices, see §552ff;

(13) the maximum margin for wholesalers who sit between the authorised distributor and the retailer was 5%, and Mr Chhatwal knew this was the position, see §150. Mr Chhatwal also knew that there was more than one wholesaler between his supplier and his customer, and so this margin would have to be shared. EDC's profit in four of the Deals was more than 5%, and in Deals F and N, where Mr Chhatwal knew there were three intermediate wholesalers, EDC's profit was more than 3%, see §563. These profits were "too good to be true";

(14) it is, as Mr Watkinson submitted, "beyond coincidence" that the parties in many of the Deals were able to contact each other, agree on terms and price, issue the paperwork, organise the delivery and often collection by the customer, on the same day, or within a two day period, see §566ff;

(15) most of the 20 Deals, and most of the further 18 WNL transactions occurred during a relatively short period of around three months (see §11), and so this is not a case where there were a very small number of fraudulent transactions over a long period;

(16) for VAT periods from 02/11 through to 05/11, at least 50% of EDC's input VAT was traced to fraudulent transactions, see §580;

(17) EDC purchased the goods in ten of the Deals from Zippy and RLR, but knew they were not reliable trading partners, see §262 and §253. It had carried no financial checks on either business, see §261 and §249, and so had no reasonable basis for accepting that either was able to fund such significant and frequent purchases, see §558ff;

(18) Mr Chhatwal also knew that five of its customers, ARU, Anovo, BAK, Everyberry and XXL, were not reliable trading partners, see Part 5, yet still entered into ten Deals with them;

(19) the remaining supplier was Electro, and the remaining customers were Redcoon and Ewert. None of the Deals involved both Electro and Redcoon, but Deal E involved Electro and Ewert. Thus, apart from Deal E, at least one of the parties in every Deal was not a reliable trading partner, and Mr Chhatwal knew this was the position. In relation to Deal E, there were the following indicators that Mr Chhatwal knew the Deal was linked to fraud:

(a) he knew the PS3s had not been sourced from a split soft bundle;

(b) there was no documented contact between Ewert and EDC before the transaction, see §353;

(c) the purchase price was too good to be true, see §552;

(d) the documentation did not refer to the specification of the consoles, §352;

(e) the goods were delivered to EDC, invoiced to Ewert, and shipped to Germany on a single day, see §354;

(20) Mr Chhatwal knew that the PS3 deal chains involving customers other than Redcoon/Ewert were not commercially viable and he knew the Redcoon/Ewert deal chains were longer than EDC's normal commercial business model, see §579;

(21) EDC released goods to XXL and Anovo in five of the Deals before payment had been received, and without having carried out any financial due diligence on those companies (see §518ff); that is not normal commercial behaviour, and it is also contrary to EDC's own terms and conditions, see §77;

(22) EDC made the highest or second highest profit of all the participants in each of the Deals, see §565; if Mr Chhatwal had been an innocent dupe, the other participants would have sought to reduce his share of the profits. Instead, the profit share reflected the risk EDC was running; and

(23) it is not credible that Mr Chhatwal could have been duped so many times, by so many different suppliers and customers, into undertaking the transactions which suited the object of the fraud, or that he had unwittingly matched a participant in the fraud to another participant in the fraud in every transaction, across so many suppliers and customers, thus completing the chains of transactions.

609. HMRC put forward, in the alterative, the submission that Mr Chhatwal should have known that the Deals were connected to fraud. Had we not decided that Mr Chhatwal had the relevant knowledge, we would have found that he should have known. As noted at the beginning of this decision, Moses LJ said in *Mobilx* that such a person includes those who:

(1) should have known from the circumstances which surround their transactions that they were connected to fraudulent evasion [59];

(2) choose to ignore obvious inferences which arise from the facts and circumstances in which they have been trading [61];

(3) should have known that the only reasonable explanation for the transactions was that they were connected with fraud [59];

(4) have the means of knowledge available and choose not to deploy it [61].

610. Mr Frain-Bell asked us to find that the bundle splitting provided "an alternative reasonable explanation" for EDC's participation in the Deals. We do not agree. It is not enough for an appellant to put forward a plausible explanation. The Tribunal must make its findings of fact as to whether that explanation is correct, and if not,

whether the appellant reasonably believed it was correct. We have found as facts that there was no commercial market for split bundles; that Mr Chhatwal knew this to be the position, and that the only conclusion which is consistent with the facts set out in this decision and summarised above, is that he knew the Deals were connected to fraud.

611. If, however, we were to be wrong in that conclusion, we find that Mr Chhatwal should have known that the Deals were connected with fraud. Relevant factors include in particular:

(1) the lack of any genuine source for the PS3s (see §234), and that Mr Chhatwal knew this was the case, see §550;

(2) the fact that many of the PS3s were EU specification, had been imported into the UK and were now being supplied to an EU customer. This makes no commercial sense, and Mr Chhatwal knew this was the position; see §530-1 ;

(3) the prices of the PS3s were between 18% and 5% lower than those charged by CentreSoft, the authorised distributor, see §552;

(4) Mr Chhatwal had no reasonable basis for believing that two of EDC's three suppliers and five of its seven customers were reliable trading partners, yet dealt with them, see Part 5; and

(5) two of EDC's three suppliers had no background in the electronics market, but were nevertheless able to access large quantities of stock which was unavailable to EDC, see §555.

Decision and appeal rights

612. For the reasons set out in this decision, EDC's appeal is dismissed.

613. The Tribunal is grateful to Mr Frain-Bell and Mr Watkinson, and to those who assisted them, for their clear and helpful submissions.

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

ANNE REDSTON
TRIBUNAL JUDGE

RELEASE DATE: 28 MARCH 2019