Neutral Citation Number: [2023] EWHC 775 (Ch)

Case No: CR-2014-002247;
Appeal ref: CH-2022-000041

IN THE HIGH COURT OF JUSTICE
BUSINESS AND PROPERTY COURTS OF ENGLAND AND WALES
ON APPEAL FROM MS RAQUEL AGNELLO KC sitting as a Deputy Insolvency and Companies Court Judge
INSOLVENCY AND COMPANIES LIST (ChD)
IN THE MATTER OF JD GROUP LIMITED IN LIQUIDATION ("JD GROUP")
AND IN THE MATTER OF THE INSOLVENCY ACT 1986

Royal Courts of Justice, Rolls Building
Fetter Lane, London, EC4A 1NL

Date: 03/04/2023

Before :

SIR ANTHONY MANN (sitting as a judge of the High Court)

- -

Between :

DEEPAK BHATIA	**Appellant**
- and -	
CHRISTOPHER PURKISS (as Liquidator of JD Group Ltd)	**Respondent**

- -
- -

Kevin Pettican (instructed by **Treon Law**) for the **Respondent/Appellant**
Peter Shaw KC (instructed by **Wedlake Bell LLP**) for the **Applicant/Respondent**

Hearing date: 25th-26th January 2023

- -

Approved Judgment

Remote hand-down: This judgment will be handed down remotely by circulation to the parties or their representatives by email and release to The National Archives. The deemed time and date of hand down is 10.30am on 3rd April 2023.

.....

SIR ANTHONY MANN

Sir Anthony Mann :

Introduction

1. This is an appeal from an order of Deputy ICC Judge Agnello made on 3rd February 2022 in which she declared that between March 2006 and May 2006 the appellant Mr Bhatia, a director of JD Group Ltd ("the Company"), was a knowing party to the carrying on of the business of the Company with intent to defraud a creditor by causing the Company to participate in a Missing Trader Intra Community ("MTIC") VAT fraud transaction, and is liable to contribute to the Company's assets, pursuant to Insolvency Act 1986 section 213. She also declared that the participation in the fraud during that period, and the submission of a VAT return for that period claiming VAT input credits, was a fraudulent breach of his duty, pursuant to section 212 of the Act. As a result he was ordered to pay £1,785,892 to the company in respect of the claims and a sum of over £782,000 in respect of interest. Her judgment has the neutral citation number [2022] EWHC 202(Ch).

2. In short, Mr Bhatia appeals the finding of the deputy judge on the overall basis that the judge's assessment of Mr Bhatia's state of mind was flawed in terms of the conclusions drawn from the evidence and because of a failure to consider other evidence properly or at all. Accordingly the dishonesty assessment was flawed. He also appeals the basis on which the damages were calculated.

3. There is also a respondent's notice seeking to uphold the decision, if necessary, on the basis of non-fraudulent breach of duty. If this becomes relevant then there is a limitation point which arises. The judge below did not consider this point on the footing that she had already found against Mr Bhatia and it was not necessary to do so.

4. Mr Kevin Pettican appeared for Mr Bhatia; Mr Peter Shaw KC appeared for the respondent liquidator.

MTIC fraud

5. There was no dispute as to the general nature of MTIC fraud, an activity which has become significant under the current VAT regime and which has become increasingly familiar to the courts. As cited by the judge in this case, it was summarised by the Court of Appeal in *Natwest Markets plc v Bilta (UK) Ltd* [2021] EWCA Civ 680 in the following terms:

> "4. The criminals involved in MTIC fraud exploit the fact that imports and exports of goods between Member States of the EU are VAT-free. Like all successful forms of fraud, the essential mechanics are simple. A trader ("the defaulter") imports goods from State A into State B, and sells them on within the latter State. No VAT would be payable on the goods when imported, but the onward sale (and any sales further down the chain within State B) would attract a liability to VAT until such time as the goods are exported to another Member State (which could be State A or State C). The final link in the chain will be the person who exports the goods, who is often an accomplice of the defaulter. The intervening sales and purchases are known as "buffer transactions".
>
> 5. The initial buyer in the chain in State B will pay the price of the goods plus VAT to the defaulter, or sometimes to a third party nominated by the defaulter (often, ostensibly, the person from whom he purchased the goods). The buyer would then be able to offset the VAT he had paid to the defaulter against any liability which he had to account to the revenue authority in State B for VAT received on the price of the goods he sold on. The exporter at the end of the chain can claim back from the revenue authority in State B the VAT that he has paid to the person from whom he purchased the goods, because the goods have now been exported to another EU State in a zero-rated transaction. Meanwhile, the defaulter would pay the price of the goods to its supplier in State A, syphon off the VAT (or pay it to an associate) and then vanish or, if a company, go into liquidation without accounting to the revenue authority in State B for the VAT."

The transactions in this case and how the present claim arose

6. The transactions which were the subject of this claim were 12 in number, though they were part of a much larger number of apparently similar transactions in which the company was involved over the period between September 2005 to August 2006. They involved the purchase and onward sale of large numbers of mobile phones. In that period the company conducted 530 such transactions. The 12 transactions in this case were conducted in a limited part of that period in April and May 2006, and were all included in the company's VAT return for the period ended 31st May 2006. They were part of chains which HMRC identified as being chains down which the mobile phones passed. In 7 of the chains the company was the exporter of goods which had been imported at the beginning of the chain shortly before the export sale. The goods were passed down the chains (involving a number of entities) and the company exported them. It had paid VAT on its own purchases in these chains but did not need to collect VAT on the export. That ostensibly gave it the right to reclaim the input tax

it had paid to its seller. In 5 of the chains the company was the importer in a chain which ended with an export. In those chains the company did not pay VAT on its purchase but collected VAT when it sold them on into the chain but in the end did account for it properly to HMRC.

7. Details of the chains appear in the judgment below at paragraphs 17 to 29 and it is unnecessary to reproduce that detail at this point. It is sufficient to record that:

(i) In the 7 export chains (ie the chains in which the Company was the exporter) the original importer defaulted in accounting for VAT arising at the beginning of the chain, and the company reclaimed the VAT that it had paid on its purchase on its VAT return for the period.

(ii) In the 5 import chains (in which the company was the importer) the company was stated to be the recipient of VAT on its onward sale, and sought to account for that in the same return.

(iii) The judge below found that those chains were each part of an MTIC fraud (see paragraph 32 of her judgment), and that finding is not challenged on this appeal.

8. At the end of the relevant month the company filed a VAT return. There were a lot of transactions included within that return but for present purposes it is necessary to note (as found by the judge) that two of the elements were:

(a) £2,117, 762 as reclaimed input tax on the transactions in which the company was the exporter; and

(b) £1,243,200 declared as output tax on the import transactions in which the company was the importer (free of tax) and sold to another UK company and was paid output tax. That would normally give rise to an offset of the one sum against the other, leaving a net claim in favour of the Company. However, after an investigation HMRC disallowed the offset of the £2,117,762 on the basis that the Company knew or had the means of knowing that the transactions were connected to MTIC fraud, and HMRC had suffered loss. The effect of this disallowance was that the Company was left with a net liability for VAT of £1,246,736 which comprised primarily the output tax on the 5 import transactions.

9. The Company appealed that determination and in that connection served what the judge described as extensive evidence, on some of whose content (or absence of content) she relied to a certain extent in her own determination. The appeal was allowed to drag on until it was struck out on 22nd March 2012. That helps to explain part of the highly undesirable delay in this matter.

10. On 21st March 2014 HMRC issued an assessment for a misdeclaration penalty in the sum of £285,897 pursuant to section 63 of the VAT Act 1994 in respect of the

misdeclaration in the May 2006 VAT return. There was no appeal by the Company in respect of that assessment and HMRC's claim in the liquidation is in the sum of £1,286,470.78 and the £285,897 penalty. The large sum largely reflects the VAT liability in respect of that May 2006 assessment.

11. The present proceedings were issued on 7th May 2020. The liquidator[1] claims the sum of £457,975 plus the penalty sum under section 213 of the Act (fraudulent trading), or alternatively the sum of £2,117,762 less profits on the transaction, but adding the penalty sum, in relation to the statutory misfeasance (section 212) claim.

The judge's findings

12. Having considered the liquidator's evidence, the documents and having heard from Mr Bhatia in person, the judge found that he had actual knowledge of the MTIC fraud in this case and found him liable accordingly. Her judgment considers the 12 chains on which the HMRC assessments were based and (as I have said) found them to be the constituents of an MTIC fraud. She then set out the relevant tests for dishonesty arising out of the cases (to which I will come) and there is no challenge to her identification of those authorities and the tests, though there is a challenge as to how she applied them. Having recorded the parties' submissions she then considered detail of the evidence going to the point. She came to the conclusion that Mr Bhatia, as a director of the Company, had actual knowledge of the MTIC fraud. She drew her overall conclusions in paragraphs 88 and 89 of her judgment, and since Mr Pettican relied heavily on what he said was the poverty of paragraph 88 it is necessary to set it out (with paragraph 89) in full:

> "88. I am satisfied that the Respondent had actual knowledge of the MTIC fraud. He was aware and knew the following:-
> (1) He had read the material and in particular the Notice and was fully aware of the warnings and what constituted MTIC fraud and the types of checks which a company needed to carry out so as not to be liable;
>
> (2) The level of awareness and knowledge of the Respondent was extremely high by virtue of the written documentation and the information provided in meeting with HMRC;
>
> (3) There was in reality no due diligence carried out before the Respondent caused the Company to enter into high value transactions with unknown parties. It is clear, in my judgment, that the Respondent was well aware of this and yet tried to

[1] During the course of the proceedings Mr Purkiss succeeded Ms Hall as liquidator and was substituted as a party.

pretend that due diligence was carried out. This is because he knew that a failure to carry out due diligence or to check the integrity of the chains would create a liability of the Company to HMRC;

(4) The trade arrangements were uncommercial in that:

(i) There is no evidence of any terms and conditions between the parties;

(ii) The complete lack of due diligence being carried out by the Company prior to entering into transactions for substantial sums.

(iii) Enabling goods to pass to a party who had not yet paid for the goods with no credible explanation relating to the risk to the Company.

(iv) The deliberate lack of any knowledge relating to the import and the export parties to the chains.

(v) The lack of credibility that in some way there was no need to obtain references or carry out due diligence on the one hand and then the reliance by the Respondent on the so called, 'on going' due diligence which occurred after the transaction in general had been carried out;

(vi) The apparent lack of insurance in respect of the goods although, as I will deal with at the end of the judgment, there is an attempt by the Respondent to add to the evidence he gave before me.

(vii) The fixed mark ups and complete lack of evidence as to any negotiation of price with a complete lack of any written record or communication over price, delivery dates, specification, risk or insurance. The Respondent's explanations here are, in my judgment, wholly unconvincing as I have set out above.

(viii) The back to back nature of the majority of these large transactions.

(ix) The re circulation of some of the phone units.

89. Based on these factors, in my judgment, the Respondent was aware that these transactions formed part of MTIC fraud. I reject accordingly his evidence that he was unaware of the MTIC fraud and I also reject his evidence that he honestly believed that these were commercial transactions and that there was he believed no link to MTIC fraud. Such a stance is not

> credible in the light of my findings on the evidence set out above. In my judgment, as is clear from the authorities that I have referred to above, it is not necessary for me to be satisfied that the Respondent was aware of the identity of the other parties in the chain. In this case, the way in which the Company conducted its business, the lack of checks, the release of goods and the other matters set out above, establish that the Respondent was aware of this being a fraudulent enterprise. The Respondent deliberately elected not to carry out proper due diligence and other steps suggested by HMRC. This, in my judgment, was precisely because he was aware that the chains were part of a MTIC fraud. Accordingly, in my judgment, the Respondent knew that the Company was participating in a MTIC fraud. It is clear that such participation is dishonest under the objective standards applicable. The transactions were not genuine commercial transactions but were created and carried out exactly as described above in relation in the extracts from the various cases. Accordingly, in my judgment, the Respondent is liable pursuant to section 213 of the Insolvency Act 1986 in dishonestly causing the Company's participation in the MTIC fraud. Bearing in mind the findings I have made, there is no need for me to deal with blind eye knowledge."

13. The nature of those findings is in the main self-explanatory. However, one matter requires explanation. Paragraph 88(1) refers to "the Notice". This is a reference to HMRC Notice 726, which is a notice which explains to the recipient how he/she might be made liable for VAT for being involved in an MTIC fraud. It sets out the sort of things which are regarded as reasonable measures to avoid being held to have known or had reasonable grounds to suspect that VAT on goods in a chain would go unpaid. The Notice was given to Mr Bhatia very early on in his trading in mobile phones and it pointed out various matters of which the judge held that Mr Bhatia was aware, such as establishing the integrity of the supplier and the supply chain, insurance for the goods, the commercial viability of any increase in price in the goods and verification of VAT status. She also held that he was made aware of the risks of trading in mobile phones from meetings that he had when he was visited by HMRC from time to time. It was his failure to carry out some of the suggested measures that was relied on by the judge in support of her conclusion as to his knowledge of what he was doing.

14. On the way to those findings the judge made some detailed findings about the evidence, from time to time observing that she did not accept Mr Bhatia's evidence on various points; she did not find him credible in those respects. They can be adequately summarised as follows:

> (a) In paragraphs 14-32 she considered the 12 chains of deals in which the Company participated which were relied on by the liquidator in this case as being

MTIC fraud chains. There is no appeal from the findings that they were MTIC fraud chains.

(b) At paragraphs 33-47 she considered the legal principles applicable to the finding of fraud. There is no material dispute or complaint about the principles she set out there.

(c) At paragraphs 51 - 87 she considered the evidence on actual knowledge. The detailed findings here resulted in the conclusions in paragraphs 88 and 89 set out above. She considered:

(i) The 726 notice and Mr Bhatia's knowledge of it, and the various meetings that he had with HMRC officers.

(ii) A consideration of the due diligence procedures carried out by the Company in relation to its seller in some of the export transactions, coming to the conclusion that there were not any "robust procedures" or there was no proper due diligence in existence at all (paragraph 61).

(iii) The circumstances of the late obtaining of VAT numbers of various companies and the release of goods before they were paid for.

(iv) The absence of any evidence of pre-contract communications between the Company and its trading counterparties.

(v) The absence of proper due diligence in relation to other contractual counterparties. Mr Bhatia's evidence was said to "lack credibility". She found that not carrying out due diligence was deliberate because any such due diligence would have revealed a lack of integrity in the supply chains and an open awareness of MTIC fraud (paragraph 77).

(vi) The creation of files to give the false impression that due diligence inquiries had been carried out.

(vii) Other aspects which demonstrated that the transactions were not commercial - the lack of terms and conditions, the absence of evidence of negotiations, the uniformity of markups, the post-dating of an inspection report and more instances of the premature release of goods before payment.

15. These were findings that under-pinned her conclusions in paras 87 and 88. As a result of these findings Deputy ICCJ Agnello found Mr Bhatia to be guilty of fraudulent trading and fraudulent breach of duty. She made certain findings in relation to quantum to which I will come.

16. The deputy judge also said something in her refusal of permission to appeal which is relied on by Mr Pettican in this case. Her written reasons for refusing permission

included the words: "This was not a collusion case". These were words relied on by Mr Pettican in this appeal in relation to what was and was not considered by her.

The statutory provisions and the relevant law as to the dishonesty test

17. Section 213 of the Act provides as follows:

> "213(1) If in the course of the winding up of a company it appears that any business of the company has been carried on with intent to defraud creditors of the company or creditors of any other person, or for any fraudulent purpose, the following has effect.
>
> (2) The court, on the application of the liquidator may declare that any persons who were knowingly parties to the carrying on of the business in the manner above-mentioned are to be liable to make such contributions (if any) to the company's assets as the court thinks proper."

18. Section 212 provides:

> "212 (1) This section applies if in the course of the winding up of a company it appears that a person who—
>
> (a) is or has been an officer of the company,....has misapplied or retained, or become accountable for, any money or other property of the company, or been guilty of any misfeasance or breach of any fiduciary or other duty in relation to the company.
>
> (3) The court may, on the application of the official receiver or the liquidator, or of any creditor or contributory, examine into the conduct of the person falling within subsection (1) and compel him—
>
> (a) to repay, restore or account for the money or property or any part of it, with interest at such rate as the court thinks just, or
> (b) to contribute such sum to the company's assets by way of compensation in respect of the misfeasance or breach of fiduciary or other duty as the court thinks just.

19. It was common ground that the test for the relevant state of mind for determining dishonesty is set out in *Ivey v Genting Casinos* [2018] AC 391:

> "When dishonesty is in question the fact-finding tribunal must first ascertain (subjectively) the actual state of the individual's knowledge or belief as to the facts. The reasonableness or otherwise of his belief is a matter of evidence (often in practice determinative) going to whether he held the belief, but it is not an additional requirement that his belief must be reasonable; the question is whether it is genuinely held. When once his actual state of mind as to knowledge or belief as to facts is established, the question whether his conduct was honest or dishonest is to be determined by the fact-finder by applying the (objective) standards of ordinary decent people. There is no requirement that the defendant must appreciate that what he has done is, by those standards, dishonest".

20. It is unnecessary to set out much more authority than that. The judge below expressed herself as following that guidance (with some elaboration from the authorities which I do not need to set out), and the thrust of this appeal is that the judge did not carry out the correct exercise required by that authority.

21. The parties before me seemed to be in agreement that the decision of the judge was an evaluative one depending on an inference to be drawn from primary facts, and as such it could only be interfered with if the decision:

> " … was wrong by reason of some identifiable flaw in the judge's treatment of the question to be decided, such as a gap in logic, a lack of consistency, or a failure to take into account some material factor, which undermines the cogency of the conclusion." (*Re Sprintroom Ltd* [2019] WECA Civ 932)

For my part I am not sure that the finding in relation to Mr Bhatia's state of mind was quite of that quality but I am content to apply that test. In doing so I bear in mind that the process for the judge was not one of the remorseless application of logic to established primary facts. It depended to a significant extent on whether she believed some of what Mr Bhatia was saying in his evidence in the witness box. That, as always, is an important consideration in appeals on facts.

The basis of the appeal

22. The basis of this appeal can be summarised as follows:

(a) The judge failed to make any findings as to Mr Bhatia's state of knowledge or belief in relation to the MTIC fraud. She failed to find what he actually knew about the fraud. This means that the first limb of the *Ivey* test has not been fufilled.

(b) In order to make the finding necessary for liability, she needed to establish Mr Bhatia's actual state of knowledge or belief in respect of all relevant matters bearing on whether he was dishonestly causing participation in the MTIC fraud. It was not sufficient to focus simply on the liquidator's case on matters supporting a finding of dishonesty. In this connection Mr Pettican drew attention to a number of matters which he said the judge ought to have considered and referred to, but did not, because they required consideration when considering whether Mr Bhatia had the required knowledge of the scheme, because they pointed against it.

(c) The judge was wrong in assessing the damages as she did. I deal with the detail of this below.

The appeal on the actual findings

23. The first part of the appeal is a complaint about the quality of the finding in paragraph 89 of the judgment below. It is said that the decision is flawed because the judge did not address specifically what, if anything, Mr Bhatia knew about the MTIC fraud and how he came to know it. Because she did not address what he knew she did not deal fairly or properly with Mr Bhatia's case (which she records) that he was not aware of the chains involved in the transactions or of any of the other companies involved in the chains.

24. This complaint is misplaced. The judge paraphrased the reasoning of Patten J in *Morris v Bank of India* [2004] EWHC 528 (Ch) in her paragraph 39 when she said:

> "1.1 The Respondent must have known of the fraud, but need not have known every detail all the precise mechanics;
>
> 1.2 Knowledge includes blind eye knowledge – deliberate shutting eyes because of a conscious fear to enquire will confirm suspicion of wrongdoing;
>
> 1.3 And targeted, speculative suspicion will not be sufficient."

That is an accurate enough paraphrase for these purposes. What Patten J actually said was:

> "They did not have to know every detail of the fraud or the precise mechanics of how it would be carried out, but clearly they did have to know, either from their own observation of what was being done or from what they were told, that BCCI was intent on a fraud. Knowledge, for this purpose, means what it says."

25. In *Alpha Sim v CAZ Distribution Services* [2014] EWHC 207 (Ch) Mr David Donaldson QC (sitting as a deputy High Court Judge) said:

> "He may well not have known the identity of the supplier companies from which the payments were diverted, let alone of the employees all of the managers of those companies who were causing them to incur a VAT liability without collecting the corresponding amount from their purchases, or that the law would categorise that conduct as a breach of fiduciary duty. But that degree of knowledge is unnecessary provided he was aware of the general nature of the scheme and its implications in terms of the deliberate non-receipt of money by a prior supplier."

26. In my view the findings of the judge in her paragraph 89 were within those parameters. Having set out a substantial amount of evidence which went to the question in paragraphs 50 to 87, she drew her conclusions in paragraph 88 and came to an overall conclusion in paragraph 89. She did not necessarily have to go farther and identify which specific elements of the scheme he was aware of; she made a clear finding that he was aware of enough. If the materials she relied on were sufficient to justify a finding of knowledge that he was participating in a VAT fraud she did not have to identify which of the details (if any) he was aware of. There is nothing in this criticism as such.

27. There is then the second basis of the appeal. It is said that particular matters in paragraph 88 which found the allegation of knowledge and dishonesty are not matters which are capable of supporting the relevant inference, or they are (or might be) capable of being attributable to negligence but not necessarily to dishonesty. It is said they do not demonstrate knowledge of the fraud. In his skeleton argument Mr Pettican went so far as to say that none of the items listed in paragraph 88 “involve actual knowledge of the MTIC fraud”.

28. The short answer to this part of the appeal is that even if the findings are consistent with negligence, they are also capable of supporting an allegation of dishonesty, particularly when taken cumulatively and with other factors, which is what the judge did. The points made by Mr Pettican were:

(a) The receipt by Mr Bhatia of the Notice 726, and his awareness of the issue of MTIC fraud based on that notice and his meetings with HMRC officers, were matters which do not demonstrate dishonesty or his knowledge of the fraud in this case. Taken by itself this is correct, but as part of the background to the other points made they are significant. He knew the checks to be carried out in order to avoid the liability referred to in the notice, and therefore to avoid suspicion of participation, and there was a finding that he made a pretence of carrying them out in order to do just that.

(b) In relation to the finding that in reality there was no due diligence carried out (paragraph 88(3)), Mr Pettican accepts that this is capable of being a matter going to actual knowledge of the fraud but the inference cannot be safely drawn without findings as to the origins of the business, and the relationship with the Company's usual counterparty (called "TEC" for short) and how the MTIC fraud actually operated. I do not accept this analysis. This factor is part of the multi-factorial assessment which was made, and the judge was not obliged to find absolutely every fact which might be capable of going to the assessment if there were otherwise sufficient facts established. I deal with a particular point about TEC below.

(c) As to the finding that some of the transactions had features that were uncommercial, it was said that it does not follow from this that Mr Bhatia had actual knowledge of the MTIC fraud. That proposition is true so far as it goes but one needs to add the word "necessarily" to make it properly accurate. When that is done the proposition does not advance Mr Pettican's case much. This factor, which the judge found and which is not challenged, takes its place along with the other items which the judge took cumulatively.

(d) The same point falls to be made in respect of the other factors relied on by the judge.

29. It is now necessary to deal with what can probably be seen to be the biggest point in the appeal on liability, which is an averment of an absence of important findings and considerations by the judge. Mr Pettican says that the judge omitted to deal with the following issues which, if she had considered them, might well have had an important bearing on her views of Mr Bhatia's knowledge. Those matters are:

(a) Mr Bhatia had a prior track record in operating a legitimate and successful VAT registered business, which made fraud inherently less likely in the case of his mobile phone business.

(b) The circumstances in which the Company began trading in mobile phones. It

is said these circumstances went to his state of mind as to the existence of VAT fraud and the inference to be drawn from the other factors relied on by the judge.

(c) The Company's relationship with its usual buyer, The Export Company Ltd ("TEC"). TEC is said to have been the Company's "counterparty" in all but 14 of the 530 mobile phone deals undertaken by the Company, and so understanding the relationship with it is crucial, yet no findings are made about this other than a reference to an alleged "agency" which Mr Bhatia at one point said existed as between him and TEC.

(d) The Company's relationship with Interken, the freight forwarders involved in the transactions in the 12 chains in this case. Since this is said to be a reputable firm it is said to be relevant to consider the extent to which Mr Bhatia relied on them because they would know more about the chains than he did.

(e) The nature of the hundreds of other trades conducted by the Company, to which there is the occasional reference but as to which no finding is made and to which no consideration is given.

(f) Inconsistent findings about insurance.

30. I shall take those points in turn.

31. The legitimate business to which reference is made is presumably that of dealing in childrens' clothing and footwear. The existence of a prior legitimate business says little or nothing about the very different business of trading in mobile phones in the sort of transactions that existed in this case. It was no part of the liquidator's case (or the Revenue's case in the Revenue proceedings) that Mr Bhatia was at all times and in all trades a dishonest trader. If the judgment was silent about the quality of previous different trades then that is because it was irrelevant to the question of whether the participation in the 12 trades in question were, on their particular facts, dishonest.

32. So far as the circumstances of his starting the mobile phone trades were concerned, there are indeed few real findings about that, other than the findings about the Notice and the visits by HMRC. However, what was not made plain was what the evidence was that the judge failed to consider, what findings she would or might have made and how it might have made a difference. The judge was considering 12 particular trades, their features and the surrounding features that accompanied them. Her decision might have been informed by past history, but that history would have needed to have been made clear to her and to have been relevant. It is not apparent to me that either of those was the case.

33. So far as the relationship with TEC is concerned, it is said that understanding the nature of the relationship with TEC was obviously critical to understanding the

Company's business and to any assessment of what Mr Bhatia knew about MTIC fraud. The judge should have made findings in the following areas:

(i) TEC was the main customer (purchaser) for mobile phones purchased by the Company.
(ii) TEC was a very substantial enterprise, with a turnover of over £1bn in 2006.
(iii) It is unsurprising that Mr Bhatia would have taken comfort from the fact that the mobile phone business he was involved in also involved such a substantial player.
(iv) Although the visting HMRC officers will have known of the substantial involvement with TEC (and TEC was the counterparty in the very first trade), they never once expressed misgivings about TEC as a counterparty to trades. HMRC has never disallowed any VAT recovery claim by TEC, and that included claims made in the five import transactions in this case in which TEC was the purchaser from the Company. The liquidator suggested in her evidence that she wished to impugn TEC's commercial probity, but (it is said) Mr Bhatia was not cross-examined on that point.

34. It is correct to say that the the deputy judge did not give a lot of detailed consideration to the relationship with TEC, but it is not correct to say that there was no reference to it. There is a significant reference in paragraph 80, in which she deals with the apparent uniformity of markups on transactions and dealings with TEC. She said:

> "80. The Respondent was also asked about the uniformity as to mark up in relation to the units. Regardless as to the price of the relevant unit, the mark ups were the same even when the identical unit was acquired or sold on for a considerable price difference. In the period September to November 2005, in 99 deals, the Company made a profit of 50 pence per unit notwithstanding that the sale price on the phones varied from about £153 to £489. Mr Shaw put to the Respondent that the mark up was contrived on this evidence. The Respondent denied this and asserted that the Company was an agent for TEC and that the Company provided services and the mark up was 50p. This explanation, in my judgment really lacked credibility. The Respondent was also asked about the mark ups which have been extrapolated into a schedule at paragraph 50 of the Applicant's witness statement. In so far as these were commercial transactions for the acquisition and onward sale of phones, it is pretty extraordinary that there would have been uniformity of mark ups despite vast price differentials in the unit prices of the same phones. I do not believe the Respondent when he suggested that some of the units had certain 'extras' with them. In my judgment, coupled with the evidence of lack of negotiations of price and other details of contracts, this forms part of the evidence that the transactions were not genuine commercial transactions."

35. The deals in question will all have been deals in which TEC was the purchaser. The explanation of agency, intended to explain the low and consistent markup, was not advanced by Mr Bhatia in his evidence in chief. It was only advanced in cross-examination when he was challenged on the point. Up until that point in the proceedings there had been no suggestion that the relationship was anything other than a standard buyer/seller relationship without any agency element. I accept that Mr Bhatia was probably using the word loosely and was not using it to describe a strict principal/agent relationship, but nonetheless the type of relationship he was describing in his cross-examination had not been asserted hitherto, either in the present proceedings or on the preceding VAT appeal. In fact his evidence in defence of the claim in this case did not rely on his view of and dealings with TEC as somehow being an indication of honesty - there is simply a one paragraph sentence which describes TEC as a supplier (not a customer) and points out that it must have been subject to the same investigation as the Company. His prior evidence in the VAT appeal does not develop the point either. The judge below was entitled to consider the evidence advanced before her and conclude that she did not believe the explanation given by Mr Bhatia and therefore to conclude that the markup was contrived and the transactions with TEC were not genuine. She was making that assessment on the evidence she was provided with. She cannot be criticised for not considering some background not actively advanced as a form of positive case, especially in the light of her conclusions about the form of trading actually conducted with TEC. And one must not lose sight of the fact that TEC was the purchaser from the Company in the 5 import transactions which she has found to be MTIC fraud, which finding was not appealed. I do not consider that her failure expressly to consider the points raised by Mr Pettican is a good one for the purposes of this appeal.

36. Turning to Interken (the freight forwarders who held the goods which were the subject of the impugned transactions), the judge said this:

> "81. The Respondent was asked about the role of Interken, the freight forwarder in many of the chains I have dealt with above. The Respondent was challenged about whether the role of Interken was effectively orchestrating the chains. This was denied by the Respondent. In my judgment, it is clear that the freight forwarders were more involved and provided with more details than in a commercial trading arrangement. However, there is insufficient evidence for me to be able to consider the precise role of Interken in the relevant chains. In my judgment, I do not have to determine or really consider what role if any was carried out by Interken, because of the existence of the other evidence which I have set out in this judgment."

37. Mr Pettican's point turns out to be similar to his point about TEC. It was suggested to Mr Bhatia in cross-examination that Interken was orchestrating the chains. As recorded by the judge, Mr Bhatia denied that. Mr Pettican submitted that since the orchestration was rejected, Interken falls be to treated as a freight forwarder who saw

nothing wrong with the transactions, and if that was the case then why should Mr Bhatia see anything wrong in them? He said the judge erred in failing to take this into account and thereby deprived Mr Bhatia of a significant point in his favour.

38. I do not accept that analysis. The judge decided that it would not be right on the evidence to make a serious finding about a non-participant. That was doubtless very sensible and correct in the circumstances. However, it does not deprive Mr Bhatia of a point. The finding (or more accurately the absence of a finding) deprives the liquidator of a point, but otherwise it is neutral so far as Mr Bhatia is concerned. It means that a point of orchestration was not proved, but it is not necessary to make a finding about that anyway - see the point made above about what knowledge is sufficient. Paragraph 81 of her judgment demonstrates uncertainty as to the impact of the evidence about Interken ("In my judgment, it is clear that the freight forwarders were more involved and provided with more details than in a commercial trading arrangement") so she was not satisfied about various aspects of the interaction between Interken and those in the chain, and in the light of that she was entitled not to approach Mr Bhatia's case on the footing that Interken's entire satisfaction was something going to whether Mr Bhatia himself was also entitled to be satisfied (if indeed that point was made to her evidentially and in submission). She simply put Interken on one side and was entitled to do so.

39. For the sake of completeness I add that after the conclusion of the trial but before judgment was delivered Mr Bhatia sought to introduce late evidence from Interken which (Mr Pettican tells me) sought to refute any allegations of wrongdoing. The judgment contains an addendum which explains that the judge refused to allow this late evidence in mainly on the footing that it could and should have gone in before, and in any event her position on Interken made no difference to her assessment of Mr Bhatia's evidence and position which was made on the evidence. While complaint seems to be made about this in Mr Pettican's skeleton, her decision on this point is not as such challenged in the Grounds of Appeal so I will say no more about it.

40. There is one further point which it is appropriate to deal with. It is not raised in the Grounds of Appeal, but bearing in mind the seriousness of this case to Mr Bhatia it is right that I should deal with it. In his skeleton argument Mr Pettican claims that the judgment below did not, when correctly viewed, confine itself to the 12 impeached chains but actually amounted to a finding that the whole of the Company's mobile phone trading was an MTIC fraud. He says that the judge considered transactions outside the 12, seemed to have considered that they all involved MTIC fraud and yet made no findings about them in the crucial paragaphs 88 and 89.

41. I am not wholly sure whether this is a complaint that the judge did consider other transactions or that she did not. However, whatever it is it is misplaced. It is plain that the judge considered and makes findings about the 12 transactions. In the course of that she considered limited evidence about the other transactions, but that was

perfectly permissible and did not indicate that she had extended her findings or ultimate consideration beyond the 12.

42. In paragraph 88(4)(viii) she makes a finding about the commerciality of the transactions in the 12 chains. On its face it is a finding about the 12, but Mr Pettican says that a cross-reference to paragraph 80 demonstrates that it is a finding about other transactions. Paragraph 80 is a paragraph dealing with the uniformity of markups and records the cross-examination of Mr Bhatia around the fact that in the deals done in the period September to November 2005 there was a standard markup of 50p per phone on sales, whatever the value of the phones or the contract. It was put to Mr Bhatia that this markup was contrived. The explanation was that he was in effect an agent for TEC. The judge found that this lacked credibility, and that was a finding she was entitled to make. She also commented adversely on the uniformity of the markup in other transactions, not confined to the 12, and disbelieved an explanation for that given by Mr Bhatia. She then found:

> "In my judgment, coupled with the evidence of lack of negotiations on price and other details of contracts, this forms part of the evidence that the transactions were not genuine commercial transactions."

43. The "transactions" that she was referring to are probably both the 12 chains, (because the judgment until then makes it plain that it is considering the 12) and the large number of other transactions or chains to which she has just referred. There is nothing wrong with the judge's approach in this respect, and it is not clear to me whether Mr Pettican was saying there was. In any event, paragraph 88(4)(viii) would seem to be a finding confined to the 12 chains, but even if it is not then again I cannot see what is wrong with that. Her decision in relation to Mr Bhatia's knowledge was legitimately informed by certain aspects of the background. I cannot see that there is anything in this point of Mr Pettican.

44. The same applies to a similar point made by Mr Pettican in relation to the judge's reliance on two other transactions (outside the 12) which were said to demonstrate the re-circulation of phones - see paragraph 88(4)(ix). This was a reference to two chains involving Oman Trading LLC. Mr Pettican complains that the judge did not analyse those chains or make any finding that they involved MTIC fraud.

45. Again, I am not sure what the substance of the complaint is, but in any event the use of this material by the judge does not somehow impeach her findings about Mr Bhatia's honesty. She judged him to have given untruthful evidence when cross-examined on the point, and concluded that his account was "yet a further incidence of the Respondent seeking to deny evidence undermining his defence" (paragraph 86). That was an approach to credibility that she was entitled to take.

46. It is also appropriate to deal with one further point raised by Mr Pettican even though, again, it did not appear in his Grounds of Appeal. He relied on the fact that, when she refused permission to appeal, the deputy judge gave as one of the reasons for refusing permission to appeal on the new Interken evidence point that it would have made no difference what the knowledge of Interken was. She added: "This is not a collusion case."

47. Mr Pettican submitted that that conclusion (if that is what it was) was inconsistent with Mr Bhatia having knowledge that his trades were part of an MTIC fraud. The main judgment does not find collusion either (despite the liquidator's case that it existed, at least as between TEC and the Company). If there really was no collusion then how, asks Mr Pettican rhetorically, can there be anything other than innocent trading?

48. I do not consider that this point assists him. The first reference to "collusion" in the PTA form is in paragraph (2) where the judge finds there was no real prospect of success on an appeal on the basis that the factors she relied on ought to have been differently weighted. She says:

> "The Appellant relies upon (1) no evidence of collusion before me, (2) a failure to take into that the respondent received no personal benefit for the fraud. [sic] the prospects of defeating findings of fact because (1) it was no part of the case that collusion needed to be established ..."

49. The main reference to "collusion" relied on is in her paragraph (4) which deals with a possible appeal in relation to her refusal to admit new evidence. In this paragraph she makes observations as to whether or not the existence of valid insurance was going to alter her findings. The full context of what she said is:

> "It was not a determinative factor. In relation to Interken, it also would have made no difference what was Interken's knowledge or its position because again that was not part of the case. This was not a collusion case."

50. What the judge seems to be saying is that the case before her did not depend on a finding that identified collusion actually took place. In other words, it was not a case in which the liquidator applicant was necessarily setting up something akin to a conspiracy. There may have been an attempt to demonstrate some collusion, but on the facts as found the actual degree, mechanics and participation in any collusion were not established, and it does not really feature in her judgment. She apparently regarded the case as being one in which the establishment of some particular collusion

was not a necessary feature. That was a justifiable view. The authorities on what has to be demonstrated in order to demonstrate the necessary dishonest intent (see above) demonstrate that that is the case.

51. Accordingly, this point does not assist Mr Pettican on this appeal.

52. Last there is the question of inconsistent findings as to insurance. At paragraph 88(4)(vi) the judge relies on the lack of insurance in respect of goods as being an aspect of the uncommercial nature of the trade arrangements. Mr Pettican points to paragraph 84 as being inconsistent with that:

> "84. When asked by Mr Shaw about the failure to produce the insurance policy and certificate, the Respondent replied that this did not mean that insurance was not in place. There was no evidence of the payment of any premium. The Respondent then asserted that he was not responsible for obtaining the relevant documentation and that HMRC had written to Interken. He asserted that the insurance was obtained by Interken for the Company. As I will deal with at the end of this judgment, after the trial had concluded and I had reserved judgment, the Respondent sought to place further evidence relating to insurance before me. However, the issue of whether there was insurance in place is simply one of many factors relied upon by the Liquidator in support of its case that these were not commercial transactions. There is no evidence that the Company paid any premium for the alleged insurance. In those circumstances, it is difficult to accept, even if it was Interken who arranged the insurance, that there was valid insurance when there was no evidence that the premium was paid. I should add that the issue of whether or not there was valid insurance was not treated by me as a determinative factor in relation to whether the Respondent knew that the transactions were part of the MTIC fraud. <u>In light of the other available evidence which I have set out in this judgment, the issue of insurance, as whether there was or was not valid insurance in place, has made no difference to my assessment of the Respondent and his knowledge</u>." (my emphasis to show the alleged inconsistency).

53. He also points to paragraph 99 as being inconsistent with the finding in paragraph 88. In that paragraph the judge is considering quantum, and in that context takes into account, against Mr Bhatia, the fact that an insurance premium had been paid:

> "99 … Although there is an issue relating to insurance, for the calculation of the net profits, the Liquidator is prepared to accept an insurance charge be included which reduces the profits. The Respondent's case is that there was insurance in place and the Liquidator maintained that there was no insurance. As I have set out below, I have not found it necessary to determine this issue due to the overwhelming evidence which I have set out. As the Respondent's case is that there was in some way insurance, this reduction of the insurance expenses from the gross profits, seems in my judgment to be correct."

54. The judge returned to this point in her added paragraphs dealing with the application to admit fresh evidence. That evidence included evidence relating to a Certificate of Insurance whose validity had apparently been challenged by the liquidator. In that context judge said:

> "102. ..... The issue of lack of valid insurance was one of the factors relied upon by the Liquidator as to why the deals were not commercial transactions. It is important to note that it was not the only factor relied upon. As will be noted above, I considered and determined many other factors relied upon by the Liquidator. In my judgment, as I have noted above, the existence or otherwise of valid insurance was not and is not determinative of the findings I have made above. There is, as I have set out, overwhelming evidence in support of the Liquidator's case."

55. There is indeed a degree of confusion in this. Paragraph 88 seems to indicate clearly that the absence of insurance was something that the judge did take into account in considering the commerciality of the transactions, which went to the state of Mr Bhatia's knowledge. The other paragraphs referred to seem to muddy the waters on that somewhat, and treating insurance as being in place for the purpose of assessing quantum does indeed seem to be quite contrary to what seems to be held in paragraph 88. However, I do not think it necessary to resolve the confusion and to ascertain exactly what the judge was saying, because I do not think that the confusion gives rise to any basis for an appeal. Either the judge thought that there was no insurance, which told against Mr Bhatia, or she was not particularly satisfied that there was insurance but in any event she thought there was enough evidence for the liquidator to succeed anyway. Either way, the apparent, or possible, inconsistency does not assist Mr Bhatia. Insurance was not a key factor for the judge.

Disposition of the appeal on liability

56. It follows from the foregoing that the appeal on liability fails and falls to be dismissed. At the end of the day the appeal seeks to overturn an evaluative decision of the judge reached on the basis of unappealed (and unappealable) findings of primary fact, and Mr Bhatia has not brought himself within any of the established mechanisms for succeeding in such a challenge.

57. Like the judge below, I consider that that makes it unnecessary to consider the alternative claim of non-dishonest breach of director's duty and the limitation point that accompanies it.

The appeal on quantum - the findings of the judge

58. The judge having found that Mr Bhatia was liable under section 213 and for fraudulent breach of duty under section 212, she then turned to the question of quantum. She found that the quantum recoverable under each of those heads was different, and acceded to the invitation of the liquidator to award the higher sum, namely that which she found due under section 212.

59. First she made findings about the sum which should be ordered to be paid under section 213. She held that the basis of this claim is "the loss suffered by HMRC" (paragraph 92), though at paragraph 97 she starts by considering "the claims which HMRC has against the company" (see below), which is not necessarily the same thing. This seems to have been calculated as made up of the following three elements:

(i) The output tax on the 5 import transactions (the tax that the company did not pay because it was relying on setting off the reclaimed tax on the 7 export sales). This sum (not identified in this part of the judgment, but is to be inferred) is £1,246,736.17.

(ii) A deduction from that sum of £799,312.50. This is the sum which the Revenue disallowed as a VAT reclaim from a company lower down in one of the chains (First Talk Mobile Ltd) when that company exported the phones which had been imported by the Company. This was said to generate the net sum of £457,897. Mr Shaw accepts that there is a slight miscalculation here. The net figure ought to be £443,887.50.

(iii) Adding in the mis-declaration penalty of £285,897.

60. This seems to have been the basis on which the Revenue calculated its loss. Having considered authority (*Morphitis v Bernasconi* [2003] EWCA Civ 289) she said:

""

> "In my judgment, the correct approach in this case is to consider the claims which HMRC has against the company".

She rejected submissions made on behalf of Mr Bhatia that the loss should be assessed on the basis that the transactions had not occurred and accepted the submission that the calculation should be on the basis that the transactions were legitimate transactions and VAT claims. The penalty was a debt owed by the company and not, for the purposes of section 213, a "punishment".

61. Turning to the claim under section 212, she calculated the claim differently. She looked at the other 7 transactions in which the company was the exporter and in respect of which it paid VAT which it could not then recover because the reclaim was disallowed by HMRC. She started with the irrecoverable VAT paid. That was the sum of £2,117,762. This was a loss to the company. From that she deducted the profits made on those deals (£615,767), and added back in the misdeclaration penalty. That generated a net loss of £1,785,892. Since that sum was greater than the loss she held to be recoverable under section 213, that was the sum she ordered to be paid by Mr Bhatia.

The arguments on the appeal and their resolution

62. The arguments on the appeal were within a fairly narrow compass.

63. The case seems to have been presented to the judge below as one in which the liquidator had two alternative claims and the Revenue was entitled to elect for the one which gave them the greater remedy. It does not seem (at least from the judgment) that that analysis was particularly disputed by Mr Bhati. Arguments were presented to try to knock each of them down. Before me Mr Shaw, at the end of his submissions, accepted that the two remedies (section 212 and section 213) might be cumulative and not alternatives, but he was content to confine himself to their being alternatives, and he elected for the one which gave him the most money (on the judge's analysis that was obviously the section 212 remedy).

64. I will deal first with the remedy for breach of director's duty under section 212. Mr Pettican criticises the judgment below as not addressing his case at the hearing, a case which he reproduced before me. He submits that the judge should have assessed damages on the basis of the difference between the actual position of the Company and the position it would have been in but for the breach of duty. What he identifies as the breach of duty is crucial to his submissions. He fastens upon a couple of

remarks in the judgment which he says amount to a finding that the whole of the Company's mobile phone business was illegitimate. He submits that the correct comparison is between the actual position of the company and the position it would have been in but for Mr Bhatia's breach of duty, ie had it decided not to enter into the mobile phone business at all. If the company had not embarked on that business it would not have had the £2.1m odd to lose in the 7 export transactions.

65. It is true that in one sentence the deputy judge does seem to say that the whole of the mobile business was illegitimate. Her paragraph 99 considers the computation of loss under section 212 and computes it in the manner set out above. Having done so she went on to consider whether she should confine her award to the lesser sum which she calculated as due under section 213 and considered that she need not do so. She went on:

> "99 …. In my judgment, providing I am satisfied that the sums claimed are the loss suffered, then I can award the higher of the two alternatives. The Company operated a babywear business for many years. It was a business which appeared to be well operated. <u>The Respondent then decided that the Company was going to embark on what he knew was a risky and illegitimate business because it was a business the purpose of which was to defraud HMRC.</u> That caused a loss to the Company. In those circumstances I will order that the Respondent is liable to pay the sum of £2,117,762, less the profits and including the misdeclaration penalty for the reason I have set out above …" (my emphasis)

66. The emphasised sentence is a curious one in the circumstances of this case. The judgment makes it plain that the case turns on the 12 transactions said (and found) to be an MTIC fraud. There was no attempt to demonstrate that the whole of the business, in the sense of every other mobile phone transaction, was also part of a fraud, though there were one or two aspects of the evidence and cross-examination which relied on features of one or two other transactions. It was certainly the case that the whole business was risky - hence the 726 notice on which HMRC placed such reliance; but as I understand it it was not part of the case that the whole business was fraudulent and the judgment does not contain the sort of specific findings that would be necessary in order to support such a finding.

67. Accordingly, I do not consider that this single sentence amounts to a finding on which Mr Pettican can rely for his purposes. I do not think that it means what it appears to say, even though it is not clear what the judge actually meant. That takes away the foundation of his submission. In any event, I consider that the approach is wrong in principle. For the purposes of the misfeasance claim each transaction which was entered into which was done as part of a fraudulent scheme was a separate breach of

duty, They are each capable of supporting a separate damages claim, and can be aggregated, as here, to see what damages have accrued in a particular period. Unless the defendant somehow seeks to say that it is artificial to do that because the transactions were part of a much bigger fraud which has yielded some overall profit, so loss was not caused by these individual transactions (an argument which would be very difficult to run in any event), then it is appropriate to take the fraudulent and wrongful transactions in this case and to see what damages flow from them. Of course, the defendant in this case is not alleging some wider fraud which protects him from the consequences of the narrower one, so the point does not arise.

68. That being the case, the approach of the deputy judge to assessing damages under section 212 was correct, save for one limited matter that is conceded. Mr Pettican accepted that if his point, based on a wider fraud, was unsustainable then the approach of the deputy judge was correct.

69. The one point that requires adjustment is the treatment of insurance in the calculation. In her judgment on liability the judge found that one of the uncommercial aspects of the transactions in question was the absence of insurance. When it came to assessing the damages, and in assessing the profits to be set off against the incurred VAT liability, she took into account an amount for insurance premiums (thereby reducing the profits and increasing the net claim). There is an obvious inconsistency here, as Mr Shaw accepted, and it is not appropriate to bring an insurance premium into account. It is not immediately apparent to me what the adjustment in the final sum should be (the judge does not identify it in her paragraph 99) but the parties doubtless know what it is and can agree the figure.

70. Mr Pettican also challenged the recovery of the penalty under this head, but the basis of this challenge was again his misplaced invocation of the overall trading since it started as being an activity which generated some sort of net profit to the company. Since that approach does not avail him, his dispute on the addition of the misdeclaration penalty fails. He rightly accepted that otherwise the penalty was a loss which Mr Bhatia had inflicted on the company (assuming, of course, misfeasance in the first place).

71. As I understood it, Mr Pettican did not challenge the ability the liquidator to claim the greater of the two assessments. Since on the basis of the findings of the judge, the section 212 misfeasance claims gave a greater claim than the claim under section 213, it is unnecessary to consider her findings under this latter head, and Mr Pettican's attempts to impeach them, and I shall not lengthen this judgment unnecessarily by doing so. I will, however, add that the question of whether the section 213 claim is an alternative claim or a separately sustainable claim is something which may require attention in another case, as may the technique of quantification. For my part I am not satisfied that they are necessarily alternatives. However, I do not propose to embark

on a consideration of these points in this case where, as a result of the attitude of the liquidator, the point does not arise and has not been argued or analysed.

Disposition

72. It follows from the above that this appeal falls to be dismissed, save that the final sum falls to be adjusted downwards slightly to reflect the erroneous inclusion of the cost of the non-existent insurance referred to above.