Neutral Citation: [2023] UKFTT 91 (TC)

Case Number: TC08719

**FIRST-TIER TRIBUNAL**
**TAX CHAMBER**

Location: Taylor House,
88 Rosebery Avenue, London

Appeal reference: TC/2018/01455

*PERSONAL LIABILITY NOTICE - penalty issued to sole director of company - company had been assessed to VAT as a result of denial of input tax deduction on Kittel grounds - whether inaccuracies in company's VAT return – whether any such inaccuracies were deliberate, including significance of whether inaccuracy upheld on basis of knew or should have known - whether any deliberate inaccuracies were attributable to Appellant - held company should have known, insufficient to constitute deliberate inaccuracy - appeal allowed*

**Heard on:** 4 May to 11 May 2022
**Judgment date:** 30 January 2023

**Before**

**TRIBUNAL JUDGE JEANETTE ZAMAN**
**TRIBUNAL MEMBER JOHN AGBOOLA**

**Between**

**KULDIP BACHRA**

**Appellant**

**and**

**THE COMMISSIONERS FOR HIS MAJESTY'S REVENUE AND CUSTOMS**

**Respondents**

**Representation:**

For the Appellant: David Bedenham, counsel, instructed by Rainer Hughes

For the Respondents: Howard Watkinson and Ishaani Shrivastava, counsel, instructed by the General Counsel and Solicitor to HM Revenue and Customs

## DECISION

### INTRODUCTION

1. Mrs Bachra has appealed against HMRC's decision of 15 December 2017 to issue her with a personal liability notice ("PLN") pursuant to paragraph 19 of Schedule 24 to the Finance Act 2007 ("FA 2007"). The PLN issued on that date was for £1,177,422.96. HMRC have since withdrawn 43 purchases by OWD from these appeals, and by the time of the hearing took the position that, based on the re-calculated potential lost revenue ("PLR"), the penalty due was £928,551.20.

2. Mrs Bachra had been the sole director of OWD Ltd (trading as Birmingham Cash & Carry) ("OWD"). HMRC had denied OWD the right to deduct input tax which it had claimed in the periods 03/14 to 12/16 on the basis that the input tax was incurred on transactions connected with the fraudulent evasion of VAT and OWD knew or should have known of the same. They issued assessments to OWD of the VAT due and later notified OWD of the assessment of a deliberate inaccuracy penalty. OWD did initially appeal against the assessment, but its liquidator subsequently withdrew that appeal; OWD has not appealed the penalty. HMRC's position was that OWD's deliberate inaccuracies were wholly attributable to Mrs Bachra as the director of OWD, and the PLN was issued on the basis that she is liable to pay 100% of the deliberate inaccuracy penalty issued to OWD.

3. The issues in this appeal (on which HMRC bears the burden of proof) are set out fully below and included Mrs Bachra's challenge to some of the transaction chains, the denial that OWD knew or should have known of the connection to the fraudulent evasion of VAT, the denial that any inaccuracies were deliberate and against any such inaccuracies being attributable to Mrs Bachra.

4. On the basis of our findings of fact and for the reasons set out fully below, we have decided that all of the transactions which are the subject-matter of this appeal were connected with the fraudulent evasion of VAT and that OWD should have known of that connection. However, we concluded that OWD did not know of the connection and, on this basis, the inaccuracy was not deliberate and the conditions were not satisfied for HMRC to be able to issue the PLN to Mrs Bachra. Accordingly, Mrs Bachra's appeal is allowed.

### BACKGROUND FACTS

5. Mrs Bachra was, at all material times, the sole director of OWD which operated a "cash and carry" business in Birmingham. OWD registered for VAT with effect from May 2013, and operated from premises in Rabone Lane from October 2013. Amongst the goods sold by OWD was alcohol, although they did sell soft drinks and some other goods. There were various visits by HMRC officers to OWD, which were attended by Mrs Bachra, representatives from CBS Associates (who were OWD's accountants) and later including representatives from Vincent Curley & Co Ltd (in addition to CBS Associates). These visits, and the correspondence between the parties, are described further in Findings of Fact.

6. On 24 January 2017 HMRC issued OWD with an assessment to VAT for £38,415 on the basis that "you have claimed input tax in connection with purported supplies from Chameleon Trading Services Limited [in periods 12/16 and 06/16]. This has led to a tax loss in the supply chain…It appears you have purchased from a hijacked trader". OWD appealed against the assessment.

7. On 5 June 2017 HMRC notified OWD of its decision to deny OWD the right to deduct input tax of £2,064,130 incurred on 375 purchases (also referred to and numbered as "Deals") made in VAT periods 03/14 to 12/16, and issued OWD with a corresponding assessment. HMRC relied on the *Kittel* principle, stating that the input tax was denied on the basis that it

was incurred in transactions connected with the fraudulent evasion of VAT and OWD knew, or should have known, of the same.

8. On 27 June 2017 HMRC officers attempted to visit the Rabone Lane site because HMRC had been unable to obtain the records for January 2017 onwards and the 03/17 VAT return had not been submitted. The building was in the process of being demolished. The officers were told that the building had been empty when work started in April 2017 and the new building was for Dhamecha, another cash and carry company. Staff at CBS Associates could not say whether any of OWD's records were there. OWD'S VAT registration was cancelled with effect from 1 April 2017 by letter of 29 June 2017.

9. OWD appealed against the *Kittel* decision and the assessment which had been raised in respect thereof.

10. OWD went into liquidation in August 2017 and the appeals by OWD have been withdrawn.

11. On 2 October 2017 HMRC informed OWD that they intended to charge a penalty of £1,177,422.96, and the penalty explanation schedule set out the basis for this as follows:

(1) the PLR was £2,101,541;

(2) the behaviour was deliberate;

(3) disclosure was prompted; and

(4) a reduction of 40% was allowed for quality of disclosure, allowing 10% for telling, 10% for helping and 20% for giving. HMRC did not consider there to be any special circumstances. The penalty percentage applied was thus 56% of the PLR.

12. On 2 November 2017 HMRC notified OWD of an inaccuracy penalty assessment under s97 and Schedule 24 FA 2007 of £1,177,422.96 for the VAT periods 03/14 to 12/16, on the basis that had been set out in the penalty explanation schedule.

13. On 15 December 2017 HMRC issued the PLN to Mrs Bachra for that same amount of £1,177,422.96 on the basis that they believed she personally gained or attempted to gain from the inaccuracy and that she was liable to pay 100% of the penalty imposed on OWD because she was acting as the sole director of OWD during the periods in question.

14. The decision to issue the PLN was upheld on review, and Mrs Bachra gave notice of appeal to the Tribunal on 19 February 2018.

15. The PLR which formed the basis of the issue of the penalty to OWD and the PLN to Mrs Bachra was based on the disallowance of credit for input tax on 375 Deals in the VAT periods 03/14 to 12/16. The amount of the PLN which HMRC are seeking to have upheld in this appeal has changed:

(1) in their re-amended Statement of Case dated 1 May 2020 HMRC said the PLN was for the sum of £977,190.32;

(2) HMRC's skeleton argument dated 12 April 2022 was based on the sum of £926,864; and

(3) in an updated table (set out at [16] below) provided to the Tribunal on 3 May 2022, HMRC further adjusted these amounts, resulting in a total of £928,551.20.

16. These changes are all based on changes to the amount of the PLR - the reduction for disclosure is unchanged. HMRC's position by the time of the hearing was that the adjusted penalty amount is:

| Quarterly VAT period | Adjusted PLR (£) | Adjusted penalty amount (£) |
|---|---|---|
| 03/14 | 133,777 | 74,915 |
| 06/14 | 23,937 | 13,404 |
| 09/14 | 178,612 | 100,022 |
| 12/14 | 156,571 | 87,679 |
| 03/15 | 180,870 | 101,287.20 |
| 06/15 | 235,187 | 131,704 |
| 09/15 | 168,209 | 94,197 |
| 12/15 | 175,575 | 98,322 |
| 03/16 | 151,050 | 84,588 |
| 06/16 | 117,256 | 65,663 |
| 09/16 | 62,859 | 35,200 |
| 12/16 | 74,233 | 41,570 |
| **Totals** | 1,658,136 | 928,551.20 |

**RELEVANT LEGISLATION**

## VAT and right to deduct input tax

17. Articles 167 and 168 of Council Directive 2006/112/EC of 28 November 2006 on the common system of VAT (the "2006 Directive") provide as follows:

> "**Article 167**
>
> A right of deduction shall arise at the time the deductible tax becomes chargeable…
>
> **Article 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…"

18. Article 273 of the 2006 Directive provides that "Member States may impose other obligations which they deem necessary to ensure the correct collection of VAT and to prevent evasion, subject to the requirement of equal treatment as between domestic transactions and transactions carried out between Member States by taxable persons and provided that such obligations do not, in trade between Member States, give rise to formalities connected with the crossing of frontiers".

19. The above provisions are reflected in UK domestic legislation by ss24 to 26 Value Added Tax Act 1994, which provide 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;…
>
> 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…
>
> (2) Subject to the following provisions of this section, "output tax", in relation to a taxable person, means VAT on supplies which he makes…
>
> (6) Regulations may provide -

(a) for VAT on the supply of goods or services to a taxable person… 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 or other information 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…

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…) 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 –
…

(b) supplies outside the United Kingdom which would be taxable supplies if made in the United Kingdom;…"

## Personal liability notices

20. Schedule 24 FA 2007 sets out the circumstances in which HMRC may issue a penalty:

"1 (1) A penalty is payable by a person (P) where -

(a) P gives HMRC a document of a kind listed in the Table below, and

(b) Conditions 1 and 2 are satisfied.

(2) Condition 1 is that the document contains an inaccuracy which amounts to, or leads to -

(a) an understatement of a liability to tax,

(b) a false or inflated statement of a loss ..., or

(c) a false or inflated claim to repayment of tax.

(3) Condition 2 is that the inaccuracy was careless (within the meaning of paragraph 3) or deliberate on P's part.

…"

21. VAT returns are a document listed in the Table to which paragraph 1 refers.

22. Paragraph 19 provides for HMRC to issue a penalty to an officer of a company by which certain penalties are payable:

"19 (1) Where a penalty under paragraph 1 is payable by a company for a deliberate inaccuracy which was attributable to an officer of the company, the officer is liable to pay such portion of the penalty (which may be 100%) as HMRC may specify by written notice to the officer.

(2) Sub-paragraph (1) does not allow HMRC to recover more than 100% of a penalty.

(3) In the application of sub-paragraph (1) to a body corporate other than a limited liability partnership "officer" means -

(a) a director (including a shadow director within the meaning of section 251 of the Companies Act 2006 (c. 46)),

...

(5) Where HMRC have specified a portion of a penalty in a notice given to an officer under sub-paragraph (1) -

(a) paragraph 11 applies to the specified portion as to a penalty,

(b) the officer must pay the specified portion before the end of the period of 30 days beginning with the day on which the notice is given,

(c) paragraph 13(2), (3) and (5) apply as if the notice were an assessment of a penalty,

(d) a further notice may be given in respect of a portion of any additional amount assessed in a supplementary assessment in respect of the penalty under paragraph 13(6),

(e) paragraphs 15(1) and (2), 16 and 17(1) to (3) and (6) apply as if HMRC had decided that a penalty of the amount of the specified portion is payable by the officer, and

(f) paragraph 21 applies as if the officer were liable to a penalty.

…"

**AUTHORITIES ON LOSS OF ENTITLEMENT TO DEDUCT INPUT TAX**

23. The European Court of Justice (the "CJEU"), in its judgment in the joined cases of *Axel Kittel v Belgium and Belgium v Recolta Recycling SPRL* (C-439/04 and C-440/04) [2008] STC 1537, confirmed that taxable persons who "knew or should have known" that the supplies in which input tax was incurred were connected with the fraudulent evasion of VAT would not be entitled to claim a credit in respect of that VAT input tax in the manner described above:

"44. The Court drew the conclusion, at paragraph 51 of *Optigen*, that transactions which are not themselves vitiated by VAT fraud constitute supplies of goods effected by a taxable person acting as such and an economic activity within the meaning of Article 2(1), Article 4 and Article 5(1) of the Sixth Directive where they fulfil the objective criteria on which the definitions of those terms are based, regardless of the intention of a trader other than the taxable person concerned involved in the same chain of supply and/or the possible fraudulent nature of another transaction in the chain, prior or subsequent to the transaction carried out by that taxable person, of which that taxable person had no knowledge and no means of knowledge.

45. The Court observed that the right to deduct input VAT of a taxable person who carries out such transactions likewise cannot be affected by the fact that, in the chain of supply of which those transactions form part, another prior or subsequent transaction is vitiated by VAT fraud, without that taxable person knowing or having any means of knowing (*Optigen*, paragraph 52).

46. The same conclusion applies where such transactions, without that taxable person knowing or having any means of knowing, are carried out in connection with fraud committed by the seller.

…

51 … traders who take every precaution which could reasonably be required of them to ensure that their transactions are not connected with fraud, be it the fraudulent evasion of VAT or other fraud, must be able to rely on the legality of those transactions without the risk of losing the right to deduct the input VAT.

52. It follows that, where a recipient of a supply of goods is a taxable person who did not and could not know that the transaction concerned was connected with a fraud committed by the seller, Article 17 of the Sixth Directive must be interpreted as meaning that it precludes a rule of national law under which the fact that the contract of sale is void, by reason of a civil law provision which renders that contract incurably void as contrary to public policy for unlawful basis of the contract attributable to the seller, causes that taxable person to lose the right to deduct the VAT he has paid. It is irrelevant in this respect whether the fact that the contract is void is due to fraudulent evasion of VAT or to other fraud.

…

55. Where the tax authorities find that the right to deduct has been exercised fraudulently, they are permitted to claim repayment of the deducted sums retroactively … It is a matter for the national court to refuse to allow the right to deduct where it is established, on the basis of objective evidence, that that right is being relied on for fraudulent ends…

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

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

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

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

60. It follows from the foregoing that the answer to the questions must be that where a recipient of a supply of goods is a taxable person who did not and could not know that the transaction concerned was connected with a fraud committed by the seller, Article 17 of the Sixth Directive must be interpreted as meaning that it precludes a rule of national law under which the fact that the contract of sale is void - by reason of a civil law provision which renders that contract incurably void as contrary to public policy for unlawful basis of the contract attributable to the seller - causes that taxable person to lose the right to deduct the VAT he has paid. It is irrelevant in this respect whether the

fact that the contract is void is due to fraudulent evasion of VAT or to other fraud.

61. By contrast, where it is ascertained, having regard to objective factors, that the supply is to a taxable person who knew or should have known that, by his purchase, he was participating in a transaction connected with fraudulent evasion of VAT, it is for the national court to refuse that taxable person entitlement to the right to deduct."

24. In *Mahagében kft v Nemzeti Adó- és Vámhivatal Dél-dunántúli Regionális Adó Foigazgatósága and Peter David v Nemzeti Adó- és Vámhivatal Dél-dunántúli Regionális Adó Foigazgatósága* (C-80/11 and C-142/11) [2012] STC 1934 the CJEU gave additional guidance:

"53 According to the Court's case-law, traders who take every precaution which could reasonably be required of them to ensure that their transactions are not connected with fraud, be it the fraudulent evasion of VAT or other fraud, must be able to rely on the legality of those transactions without the risk of losing their right to deduct the input VAT (see *Kittel and Recolta Recycling*, paragraph 51).

54 On the other hand, it is not contrary to European Union law to require a trader to take every step which could reasonably be required of him to satisfy himself that the transaction which he is effecting does not result in his participation in tax evasion (see, to that effect, Case C-409/04 *Teleos and Others* [2007] ECR I-7797, paragraphs 65 and 68; *Netto Supermarkt*, paragraph 24; and Case C-499/10 *Vlaamse Oliemaatschappij* [2011] ECR I-0000, paragraph 25).

55 Moreover, in accordance with the first paragraph of Article 273 of Directive 2006/112, Member States may impose obligations, other than those provided for by that directive, if they consider such obligations necessary to ensure the correct levying and collection of VAT and to prevent evasion.

56 However, even though that provision gives the Member States a margin of discretion (see Case C-588/10 *Kraft Foods Polska* [2012] ECR I-0000, paragraph 23), that option may not be relied upon, according to the second paragraph of that article, in order to impose additional invoicing obligations over and above those laid down in Chapter 3, headed 'Invoicing', of Title XI, headed 'Obligations of taxable persons and certain non-taxable persons', of that directive and, in particular, Article 226 thereof.

57 Furthermore, the measures which the Member States may adopt under Article 273 of Directive 2006/112, in order to ensure the correct levying and collection of the tax and to prevent evasion, must not go further than is necessary to attain such objectives. Therefore, they cannot be used in such a way that they would have the effect of systematically undermining the right to deduct VAT and, consequently, the neutrality of VAT, which is a fundamental principle of the common system of VAT (see, to that effect, inter alia, *Gabalfrisa and Others*, paragraph 52; *Halifax and Others*, paragraph 92; Case C-385/09 *Nidera Handelscompagnie* [2010] ECR I-0000, paragraph 49; and *Dankowski*, paragraph 37).

58 As regards the national measures at issue in the case in the main proceedings, it must be noted that the Law on VAT does not prescribe specific obligations, but merely provides, in Paragraph 44(5), that the taxation rights of the taxable person indicated as the purchaser in the invoice may not be called into question, provided that that person has acted with due diligence in respect of the chargeable event, bearing in mind the circumstances under which the goods were supplied or the services performed.

> 59 In those circumstances, it follows from the case-law referred to in paragraphs 53 and 54 of the present judgment that determination of the measures which may, in a particular case, reasonably be required of a taxable person wishing to exercise the right to deduct VAT in order to satisfy himself that his transactions are not connected with fraud committed by a trader at an earlier stage of a transaction depends essentially on the circumstances of that particular case.
>
> 60 It is true that, when there are indications pointing to an infringement or fraud, a reasonable trader could, depending on the circumstances of the case, be obliged to make enquiries about another trader from whom he intends to purchase goods or services in order to ascertain the latter's trustworthiness.
>
> 61 However, the tax authority cannot, as a general rule, require the taxable person wishing to exercise the right to deduct VAT, first, to ensure that the issuer of the invoice relating to the goods and services in respect of which the exercise of that right to deduct is sought has the capacity of a taxable person, that he was in possession of the goods at issue and was in a position to supply them and that he has satisfied his obligations as regards declaration and payment of VAT, in order to be satisfied that there are no irregularities or fraud at the level of the traders operating at an earlier stage of the transaction or, second, to be in possession of documents in that regard.
>
> 62 It is, in principle, for the tax authorities to carry out the necessary inspections of taxable persons in order to detect VAT irregularities and fraud as well as to impose penalties on the taxable person who has committed those irregularities or fraud.
>
> 63 According to the case-law of the Court, Member States are required to check taxable persons' returns, accounts and other relevant documents (see Case C-132/06 *Commission v Italy* [2008] ECR I-5457, paragraph 37, and Case C-188/09 *Profaktor Kulesza, Frankowski, Józwiak, Orlowski* [2010] ECR I-7639, paragraph 21).
>
> 64 To that end, Directive 2006/112 imposes, in particular in Article 242, an obligation on every taxable person to keep accounts in sufficient detail for VAT to be applied and its application checked by the tax authorities. In order to facilitate the performance of that task, Articles 245 and 249 of that directive provide for the right of the competent authorities to access the invoices which the taxable person is obliged to store under Article 244 of that directive.
>
> 65 It follows that, by imposing on taxable persons, in view of the risk that the right to deduct may be refused, the measures listed in paragraph 61 of the present judgment, the tax authority would, contrary to those provisions, be transferring its own investigative tasks to taxable persons."

25. The *Kittel* principle has been clarified by Moses LJ in *Mobilx Ltd (in administration) v HMRC* [2010] EWCA Civ 517 at [30]:

> "…the Court made clear that the reason why fraud vitiates a transaction is not because it makes the transaction unlawful but rather because where a person commits fraud he will not be able to establish that the objective criteria which determine the scope of VAT and the right to deduct have been met."

26. Considering further the extent of knowledge, Moses LJ stated:

> "55. If HMRC was right and it was sufficient to show that the trader should have known that he was running a risk that his purchase was connected with fraud, the principle of legal certainty would, in my view, be infringed. A trader who knows or could have known no more than that there was a risk of fraud

will find it difficult to gauge the extent of the risk; nor will he be able to foresee whether the circumstances are such that it will be asserted against him that the risk of fraud was so great that he should not have entered into the transaction. In short, he will not be in a position to know before he enters into the transaction that, if he does so, he will not be entitled to deduct input VAT. The principle of legal certainty will be infringed.

56. It must be remembered that the approach of the court in *Kittel* was to enlarge the category of participants. A trader who should have known that he was running the risk that by his purchase he might be taking part in a transaction connected with fraudulent evasion of VAT, cannot be regarded as a participant in that fraud. The highest it could be put is that he was running the risk that he might be a participant. That is not the approach of the Court in *Kittel*, nor is it the language it used. In those circumstances, I am of the view that it must be established that the trader knew or should have known that by his purchase he was taking part in such a transaction, as the Chancellor concluded in his judgment in *BSG*: -

"The relevant knowledge is that BSG ought to have known by its purchases it was participating in transactions which were connected with a fraudulent evasion of VAT; that such transactions might be so connected is not enough." (§ 52)

57. HMRC object that the principle should not be restricted to those cases where a trader has deliberately refrained from asking questions lest his suspicions should be confirmed. This has been described as a category of case which is so close to actual knowledge that the person is treated as having received the information which he deliberately sought to avoid (see Lord Scott in *Manifest Shipping Co Limited v Uni-Polaris Insurance Co Limited and Others* [2001] UKHL 1 and *White v White* [2001] 1 WLR 481 paragraphs 16 and 17, 486 E-G). HMRC seeks to rely upon the views of Lewison J in *Livewire and Olympia* [2009] EWHC 15 (Ch) (§ 85) and Burton J in *R (Just Fabulous) v HMRC* [2008] STC 2123 (§ 45) that:

"The principle of legal certainty must be trumped by the 'objective recognised and encouraged by the Sixth Directive'."

58. As I have endeavoured to emphasise, the essence of the approach of the court in *Kittel* was to provide a means of depriving those who participate in a transaction connected with fraudulent evasion of VAT by extending the category of participants and, thus, of those whose transactions do not meet the objective criteria which determine the scope of the right to deduct. The court preserved the principle of legal certainty; it did not trump it.

59. The test in *Kittel* is simple and should not be over-refined. It embraces not only those who know of the connection but those who "should have known". Thus it includes those who should have known from the circumstances which surround their transactions that they were connected to fraudulent evasion. If a trader should have known that the only reasonable explanation for the transaction in which he was involved was that it was connected with fraud and if it turns out that the transaction was connected with fraudulent evasion of VAT then he should have known of that fact. He may properly be regarded as a participant for the reasons explained in *Kittel*.

60. The true principle to be derived from *Kittel* does not extend to circumstances in which a taxable person should have known that by his purchase it was more likely than not that his transaction was connected with fraudulent evasion. But a trader may be regarded as a participant where he should have known that the only reasonable explanation for the circumstances

in which his purchase took place was that it was a transaction connected with such fraudulent evasion."

27. On questions of proof, Moses LJ stated:

> "81. HMRC raised in writing the question as to where the burden of proof lies. It is plain that if HMRC wishes to assert that a trader's state of knowledge was such that his purchase is outwith the scope of the right to deduct it must prove that assertion. No sensible argument was advanced to the contrary.
>
> 82. But that is far from saying that the surrounding circumstances cannot establish sufficient knowledge to treat the trader as a participant. As I indicated in relation to the BSG appeal, Tribunals should not unduly focus on the question whether a trader has acted with due diligence. Even if a trader has asked appropriate questions, he is not entitled to ignore the circumstances in which his transactions take place if the only reasonable explanation for them is that his transactions have been or will be connected to fraud. The danger in focussing on the question of due diligence is that it 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. The circumstances may well establish that he was."

28. At [83] Moses LJ stated that he could do no better than repeat the words of Christopher Clarke J in *Red12 v HMRC* [2009] EWHC 2563 (Ch):

> "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 e.g. that it is part of a fraudulent scheme. The character of an individual transaction may be discerned from material other than the bare facts of the transaction itself, including circumstantial and "similar fact" evidence. That is not to alter its character by reference to earlier or later transactions but to discern it.
>
> 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."

29. In *Fonecomp Limited v HMRC* [2015] EWCA Civ 39 it was submitted that the words "should have known" (per Moses LJ in *Mobilx* ) meant "has any means of knowing" (at [51]) and that the Appellant could not have found out about the fraud even if it made inquiries because the fraud did not relate to the chain of transactions with which it was concerned. Arden LJ in the Court of Appeal (with whom McFarlane and Burnett LJJ agreed) said, at [51]:

> "However, in my judgment, the holding of Moses LJ does not mean that the trader has to have the means of knowing how the fraud that actually took place occurred. He has simply to know, or have the means of knowing, that fraud has occurred, or will occur, at some point in some transaction to which his transaction is connected. The participant does not need to know how the fraud was carried out in order to have this knowledge. This is apparent from [56] and [61] of *Kittel* cited above. Paragraph 61 of *Kittel* formulates the requirement of knowledge as knowledge on the part of the trader that "by his purchase he was participating in a transaction connected with fraudulent evasion of VAT". It follows that the trader does not need to know the specific details of the fraud."

30. In *Davis and Dann Ltd v HMRC* [2016] STC 126, the Court of Appeal approached the "should have known" test on the basis of Moses LJ's statement in *Mobilx* that it required that "the only reasonable explanation" for the transactions must have been connection to fraud. It was common ground in that case that what HMRC needed to show was that the only reasonable explanation for the transactions was that they were connected to a VAT fraud (at [4], citing *Mobilx* at [59]).

31. In *AC (Wholesale) Limited v HMRC* [2017] UKUT 191 (TCC) the Upper Tribunal concluded that the "only reasonable explanation" formulation was simply one way of showing that a person should have known that the transaction was connected to fraud:

> "29…Moses LJ was clear that the test in *Kittel* was a simple one that should not be over refined. It is, to us, inconceivable that Moses LJ's example of an application of part of that test, the 'no other reasonable explanation', would lead to the test becoming more complicated and more difficult to apply in practice. That, in our view, would be the consequence of applying the interpretation urged upon us by Mr Brown. In effect, HMRC would be required to devote time and resources to considering what possible reasonable explanations, other than a connection with fraud, might be put forward by an appellant and then adduce evidence and argument to counter them even where the appellant has not sought to rely on such explanations. That would be an unreasonable and unjustified evidential burden on HMRC. Accordingly, we do not consider that HMRC are required to eliminate all possible reasonable explanations other than fraud before the FTT is entitled to conclude that the appellant should have known that the transactions were connected to fraud.
>
> 30. Of course, we accept (as, we understand, does HMRC) that where the appellant asserts that there is an explanation (or several explanations) for the circumstances of a transaction other than a connection with fraud then it may be necessary for HMRC to show that the only reasonable explanation was fraud. As is clear from *Davis & Dann*, the FTT's task in such a case is to have regard to all the circumstances, both individually and cumulatively, and then decide whether HMRC have proved that the appellant should have known of the connection with fraud. In assessing the overall picture, the FTT may consider whether the only reasonable conclusion was that the purchases were connected with fraud. Whether the circumstances of the transactions can reasonably be regarded as having an explanation other than a connection with fraud or the existence of such a connection is the only reasonable explanation is a question of fact and evaluation that must be decided on the evidence in

> the particular case. It does not make the elimination of all possible explanations the test which remains, simply, did the person claiming the right to deduct input tax know that, by his purchase, he was participating in a transaction connected with fraudulent evasion of VAT or should he have known of such a connection."

32. The case law also indicates that it is necessary to guard against over-compartmentalisation of relevant factors, and to stand back and consider the totality of the evidence (*Davis and Dann*, and *CCA Distribution v HMRC* [2017] EWCA Civ 1899).

**ISSUES**

33. HMRC bears the burden of proof in respect of all of the issues in this appeal, namely:

(1) whether there were inaccuracies in OWD's VAT returns - this requires HMRC to establish that OWD was not entitled to the input tax claimed, ie that the *Kittel* test is satisfied in relation to the relevant purchases. This in turn requires the following to be determined:

(a) was there a fraudulent evasion of VAT;

(b) if so, were OWD's purchases on which input tax have been denied connected with that fraudulent evasion; and

(c) if so, did OWD know or should it have known that its purchases were connected with that fraudulent evasion of VAT. HMRC's position was that both of these alternative limbs were met;

(2) whether such inaccuracies were deliberate - HMRC's position was that once it is established that there were inaccuracies in OWD's VAT returns on the basis of *Kittel*, such inaccuracies were deliberate for this purpose, irrespective of whether we base our conclusion on OWD knowing or that it should have known of the connection to the fraudulent evasion of VAT. Mr Bedenham (whilst submitting that the test in *Kittel* was not satisfied in any event) submitted that a conclusion that OWD should have known was not and could not be deliberate conduct.

(3) whether such deliberate inaccuracies were attributable to Mrs Bachra - in this context, Mr Bedenham submitted that even if constructive knowledge (based on a conclusion that OWD should have known) is sufficient to satisfy the deliberate test on the part of OWD, in the absence of actual knowledge on the part of Mrs Bachra, the inaccuracies cannot properly be attributed to her; and

(4) whether the penalty and PLN were correctly calculated.

34. As stated above, the burden of proof is on HMRC in respect of all these issues, the relevant standard of proof being the balance of probabilities. In *HMRC v Citibank NA, E Buyer UK Limited* [2017] EWCA 1416 (Civ) the Court of Appeal held that satisfying the burden of proof in respect of the allegation that a taxpayer knew or should have known that its transactions were connected with the fraudulent evasion of VAT does not require HMRC to prove that the taxpayer (or those acting on its behalf) was dishonest or fraudulent. HMRC has not pleaded dishonesty or fraud in respect of either OWD or Mrs Bachra. However, where HMRC seeks to allege that a person has fraudulently defaulted on a VAT liability (which is a necessary part of the *Kittel* principle), that does amount to an allegation of fraud or dishonesty made against a non-party.

35. The penalty issued to OWD and the PLN issued to Mrs Bachra were based on HMRC's denial of credit for input tax on 375 Deals. HMRC have subsequently withdrawn their case in respect of 43 of these Deals for various reasons – for some it was because they had pleaded the

wrong defaulter in the Statement of Case and accepted it was too late to amend fairly; others because they could not prove the deals traced to fraudulent tax losses; one because the supply was not of alcoholic goods and some because HMRC accepted they could not prove that the alleged defaulting trader had not declared the deals (due to absence of business records). HMRC did not accept that any of the withdrawn deals, save for that involving non-alcoholic goods, were untainted by a connection with fraud, but they were not pursued for the purposes of this appeal. (The deal packs, and the Deal numbers referred to in this Decision, retained their original numbering.)

36. Mrs Bachra's appeal against the PLN must be allowed to the extent that the penalty issued to OWD related to the denial of credit for input tax on those 43 Deals. We consider the status of the PLN and HMRC's change of position in relation to the amount at issue further in the context of the Discussion on the calculation of the PLN below (at [269] to [276]).

37. Of the remaining 332 Deals, Mrs Bachra accepted that HMRC have established a connection with the fraudulent evasion of VAT in many of these deals, but did challenge some denials on the basis that HMRC have not proved the transaction chains. (Mrs Bachra had initially also challenged whether HMRC had established that there was a fraudulent default in respect of some of the alleged defaulters, and this challenge was maintained in Mr Bedenham's skeleton argument, but after the conclusion of the oral evidence at the hearing Mr Bedenham confirmed that it was now accepted by Mrs Bachra that all of the businesses said to be the defaulting trader in specified deals were fraudulent defaulters.) We consider this challenge to the transaction chains in the Discussion on whether there were inaccuracies in OWD's returns (at [150] to [168]).

**EVIDENCE AND WITNESSES**

38. The hearing bundles were extensive, and we heard evidence from two witnesses, Mrs Bachra and Officer Joanne Jones of HMRC, both of whom were cross-examined on their evidence.

39. The documentary evidence included:

(1) visit reports prepared by HMRC - the accuracy of these was largely unchallenged by Mrs Bachra. Mrs Bachra did state, for example, that she could not recall saying she was worried about giving the wrong answer (a statement that was recorded in one of the reports), but she had not kept any notes of those meetings herself and we were not shown any notes that may have been taken by, eg, CBS Associates or Vincent Curley & Co. The reports did describe matters such as where there had been strong disagreements between, eg, Officer Kim Deakin and Mr Curley. We concluded that HMRC's visit reports were broadly accurate as a record of the discussions which had taken place at the visits. We did note that those reports included at the end a section on "Conclusions/credibility" and this is not a record of the meeting but a record of the HMRC officers' conclusions and opinions, and there were occasional opinions expressed in the body of the report to, eg, reluctance on the part of Mrs Bachra. We treat these opinions as such, and note that these sections were mainly referred to by Mr Bedenham when criticising HMRC's approach to OWD and Mrs Bachra;

(2) transaction documents in relation to the deals;

(3) due diligence information which had been compiled and provided to HMRC by OWD; and

(4) correspondence between HMRC and OWD, including arranging meetings, warnings of MTIC fraud, information notices and tax loss letters.

40. OWD is in liquidation and the records of OWD are in the possession of the liquidator, not Mrs Bachra. Neither party had requested a copy of the records from the liquidator.

41. Mrs Bachra had provided two witness statements. In responding to the matters relied upon by HMRC in their Statement of Case, Mrs Bachra emphasised that she did not have OWD's records, she was now responsible for looking after her husband (who had been taken seriously ill in 2017), the visits by HMRC were several years ago and she had not been experienced in running a business and dealing with suppliers. As to Mrs Bachra's evidence:

(1) Mrs Bachra was able to specify that she had visited the premises of a handful of the suppliers in question (eg SS Traders Ltd ("SS Traders") and Wentworth Drinks Ltd ("Wentworth")).

(2) She did assert that for every purchase there would have been a full set of documents (including purchase orders) and that due diligence was always done on suppliers by CBS Associates (in addition to the reports produced by The Due Diligence Exchange ("DDE")). The documentary evidence does not support this – some of the deal packs were incomplete, and given that this information was being provided to HMRC contemporaneously, the subsequent liquidation of OWD can have no bearing on the absence of the remaining documents. This is also the case for the due diligence; as set out below, we have found that DDE were not always instructed to carry out due diligence; and whilst we have concluded that CBS Associates did basic identity checks and VAT number verification, we do not accept they did any more than this.

(3) For the most part Mrs Bachra's evidence was vague – notably the lack of explanation as to discussions on pricing and what she had done when considering the risks of trading with particular suppliers. There were many instances where Mrs Bachra said she could not remember.

42. We did not find Mrs Bachra's evidence to be helpful; and there were areas where her evidence was contradicted by contemporaneous documentary evidence, as noted above. We have generally sought to corroborate Mrs Bachra's evidence by reference to documentary evidence or visit reports when making our findings of fact and reaching conclusions as we were not satisfied that her evidence was reliable. That is not, however, a conclusion that Mrs Bachra's evidence was untruthful (and we note that HMRC had not pleaded dishonesty).

43. Officer Jones had been employed by HMRC since February 1987 and in her current role (which she has been in since July 2012) she examines the compliance of businesses operating in the alcohol trade and investigates alcohol supply chains. Officer Jones had provided four witness statements in relation to OWD. The VAT assessment issued to OWD had been issued by Officer Kim Deakin (who had visited OWD during the VAT periods in issue), who has since left the team. Officer Jones had issued the penalty to OWD in November 2017 and the PLN to Mrs Bachra in December 2017 but had not visited OWD whilst the company was trading.

44. We found Officer Jones to be an honest and credible witness. Officer Jones was not, however, able to add anything to the information contained in HMRC's visit reports as she had not been present at any of those visits.

45. Officer Jones had also provided witness statements in respect of some of the other traders in the transaction chains, namely ALT Supplies Ltd ("ALT"), Neat Trading Ltd ("Neat") and Yewhall Ltd ("Yewhall") (each of which were accepted to be fraudulent defaulters) and Bestbuys Supplies Ltd ("Bestbuys") (a buffer trader). Officer Jones' evidence as to matters of fact in those witness statements was not challenged.

46. There were witness statements from a multitude of HMRC officers setting out HMRC's position in relation to each of the fraudulent defaulters and buffer traders. Mr Bedenham did

not require those witnesses to attend the hearing to be cross-examined on their evidence and their evidence of fact in those statements was not challenged.

47. We have taken account of all of the evidence and submissions when making our findings of fact and reaching our decision, but have not found it necessary to refer to all of the evidence and submissions in this Decision.

**FINDINGS OF FACT**

48. We set out here our findings of fact, which mainly relate to the background to the establishment of OWD, the visits by HMRC officers to OWD (each of which was attended by Mrs Bachra) and the due diligence conducted by OWD in respect of its suppliers. We make additional findings of fact in the Discussion.

### Mrs Bachra and establishment of OWD

49. Mrs Bachra had owned and rented out a number of off-licences. In around 2003, having rented out or sold these retail businesses, she was employed at Eastenders Cash & Carry ("Eastenders") as a cashier. Eastenders was owned by Kulwant Hare (Mrs Bachra's brother) and Alexander Wilson. She was promoted to the role of warehouse manager of the warehouse in Birmingham, and held that role for nine years. This role did not involve her dealing with suppliers.

50. In around 2013 Eastenders shut down this Birmingham business. OWD bought the stock held by Eastenders in its warehouse in Rabone Lane and then operated from those premises itself.

51. OWD had been incorporated on 17 May 2013. The application form to register for VAT was received by HMRC on 20 May 2013 and stated that its business activities were the sale of confectionery, soft drinks, tobacco, sweets, crisp, milk and bread, butter, etc. This application was submitted by Hoang Van Dinh, OWD's first director. The effective date of VAT registration was 27 May 2013. Mrs Bachra was appointed as director of OWD on 3 June 2013 and was the sole director throughout VAT periods 03/14 to 12/16 and until OWD went into liquidation in 2017.

52. In October 2013 OWD informed HMRC that its principal place of business had changed to Rabone Lane, Smethwick, Birmingham - OWD operated from these premises throughout the VAT periods in issue.

53. OWD operated a cash and carry business, supplying retailers (including clubs, pubs and restaurants) and traders with various products including alcohol. Sales of alcohol accounted for 65 to 70% of its turnover, and this was the mainstay of its business. OWD also sold, eg, soft drinks, confectionary, toiletries, cleaning products and electronic cigarettes.

### Supplies of alcohol to OWD

54. OWD purchased alcoholic goods from a number of different suppliers. Mrs Bachra, and thus OWD, was approached by these suppliers attending the warehouse in Rabone Lane and offering to supply various goods.

55. Mrs Bachra explained that OWD did want to buy from sources closer to the manufacturer, but its size meant that it was usually not possible to buy direct in this manner. Jeff Street, who was appointed as manager during the VAT periods in issue, did focus on this and OWD did join a buyers' group to try to improve its purchasing power.

56. There are 332 purchases by OWD in respect of which HMRC has denied credit for input tax. The fact that these supplies took place, the dates, supplier and value were agreed between the parties. The final deal to which this appeal relates, Deal 375, took place on 9 December 2016.

**Contact between OWD and HMRC**

57. We describe here the visits by HMRC to OWD and some of the correspondence between them.

58. We had the visit reports from HMRC and, as set out above, concluded that they were broadly accurate as a record of the discussions which had taken place. Mr Bedenham did challenge the fairness of the observations which were made by HMRC in those reports (usually presented under the heading "Conclusions/credibility") and we address those to the extent required in the Discussion.

***23 October 2013***

59. On 23 October 2013 Officers Brian Nolan and Stephen Dunckley made an unannounced visit to OWD's premises and they met with Mrs Bachra. The visit report records:

(1) Mrs Bachra had purchased the business from Eastenders because it was closing down and she had been an employee of the company, mainly on the cash desk. There was no association with Eastenders - she purchased stock from them and some employees stayed when she took over.

(2) OWD had paid £180,000 to £200,000 for the stock. Initially Mrs Bachra said that she had paid most of this money on an "as and when" or "drip feed" basis. Later she said that £100,000 had been financed from the sale of a property.

(3) Mrs Bachra said that she made all the decisions about what stock was purchased and at what price, she varied her suppliers, she shopped around for the best deals and tried to get credit from her suppliers.

(4) Mrs Bachra said that when stock was delivered it was checked either by her or an employee, and that delivery notes were sometimes reconciled to purchase orders or passed to OWD's accountant.

(5) Mrs Bachra said that OWD tried to carry out due diligence on suppliers but she let her accountant do it.

(6) The Officers explained the "How to Spot Missing Trader Fraud" leaflet to Mrs Bachra and issued Notice 726 to her.

60. The Conclusion/Credibility section of the report records that either Mrs Bachra never got over her nervousness from the unannounced visit, or she in fact knows little about the business. Getting answers was like "drawing teeth" and this section concludes "I am concerned that in fact Mrs Bachra is in fact "a front" and in reality others control what goes on but I have no evidence to substantiate this."

***13 November 2013***

61. Officers Nolan and Dunckley then visited Deepak Kabra of CBS Associates on 13 November 2013.

62. The visit report includes:

(1) Mr Kabra explained that they are the accountants for OWD but had also become involved in the day-to-day book-keeping; an employee uplifts the business records twice a week.

(2) Stock at the start of the business was valued at the invoice cost from Eastenders to OWD, which was established at £159,841. No physical stock check had been carried out by an independent stock taker, and there were no stock sheets. Payment had been made on a "drip feed", as and when, basis.

(3) There was a general conversation on due diligence and the need to refresh due diligence on established suppliers. "How to Spot Missing Trader Fraud" and Notice 726 were issued.

***27 March 2014***

63. Officers Simon Japes and Dave McMaster visited OWD, and met with Mrs Bachra and Mr Kabra.

64. The visit report records:

(1) Due diligence was undertaken in respect of new suppliers in the form of obtaining a VAT certificate, certificate of incorporation, copy passport and copy utility bill. The accountant does a Europa check on each supplier at the end of each quarter.

(2) They discussed the use of HMRC's Wigan verification unit.

(3) Unsolicited offers of stock had been received but none had been retained.

(4) The officers saw the suppliers' file for January to March 2014. The due diligence pack was not available in respect of the major supplier ALT. The report notes that this was subsequently requested from the accountant.

(5) Other suppliers include manufacturers, eg Budweiser, or companies known to the officers. Other traders were noted and checked against HMRC's Vision, eg Asiana and South East Beers. Due diligence packs included those for Brookfield Drinks and others.

65. The report includes a note that the trader is potentially high risk and twice-yearly visits would be worthwhile.

66. HMRC then sent the following letters:

(1) On 28 March 2014 HMRC issued an MTIC fraud advice letter to OWD which set out examples of indicators of MTIC fraud which should be taken into account when conducting "know your client" checks and how to verify VAT numbers with HMRC in Wigan.

(2) When confirming the details for a visit that had been arranged for 21 July 2015, HMRC wrote on 26 June 2015 warning that HMRC were concerned that the business could be at risk of involvement in supply chains that are connected with fraud.

(3) This was repeated in a letter of 14 July 2015 when the visit was confirmed as re-arranged for 5 August 2015.

67. On 15 July 2015 HMRC issued a Schedule 36 notice to OWD for business records for the VAT periods 06/13 to 06/15, as well as specified records for transactions that had taken place since 1 July 2015, to be provided by 5 August 2015. This notice had not been complied with in full by 14 September 2015, as records for transactions since 1 July 2015 had not been provided.

***5 August 2015***

68. This was a long meeting (over 4 hours), and those attending included Officers Julie Cawley and Kim Deakin from HMRC, as well as Mike Tilt of HMRC, a data handling specialist, Mrs Bachra, Mr Kabra and Nigel Ferrington of Vincent Curley & Co.

69. The visit report includes a list of suppliers to OWD; they include One Way Wholesale, Marchis, Beccha Brands, Ace Drinks and Millennium Wholesale.

70. The first part of the visit report is Officer Tilt's interim report. Officer Tilt had attended to interrogate the computerised record systems namely STL (for the tills) and VT (for the

accounts). That report describes the processes used for customers, stock control and payments from the till, and includes the following:

(1) Risk assessment – Both the owner and the accountants deliberately tried to disguise the location of the server used for the tills. Day passes appear to be issued without any control and this contravenes the requirements of a VAT invoice. This problem appears endemic in the cash and carry industry. The scale of cash payments for the purchase of goods for resale at over 50% is staggering.

(2) Summary – This appears to be a case of deliberate fraudulent activity and I am of the opinion that the accountants are heavily involved. I fear that a lot of the purchases and sales will not be recorded or be highly manipulated by the accountants.

71. The report on the remainder of the visit includes:

(1) Officer Cawley explained the risks of alcohol fraud, reminded OWD of the MTIC awareness letter and Notice 726 that OWD had previously received, and Officer Deakin gave them another copy of both Notice 726, asking them to read the due diligence section carefully, and the leaflet on "How to Spot Missing Trader Fraud".

(2) Mrs Bachra explained that OWD had bought the business as a going concern from Eastenders, and that she had bought the stock from them for between £100,000 to £200,000 with her own money. She had taken over the rental agreement for the premises, and the licence for the STL software (for the tills) that was being used by Eastenders. There was no paperwork for the transfer of business or contract for the purchase of stock, just an invoice from Eastenders to OWD.

(3) Officer Cawley asked whether there were associated businesses. Mrs Bachra "was reluctant but then admitted that Ken Hare from Eastenders was actually her brother's company and so was Hare Wines Harrow and her new supplier Hare wines". Officer Deakin "got the impression" that Mrs Bachra appeared a little reluctant to discuss her involvement in any of the business discussed.

(4) OWD does not prepare management accounts. Mrs Bachra could not explain in detail how she manages cash flow, but Mr Kabra said he monitors the situation monthly. Mrs Bachra confirmed that there was currently around £600,000 of stock. Mrs Bachra wasn't sure if the company was insured to keep cash.

(5) OWD does not have a book keeper, but Mr Kabra sends in his assistant once a week who uplifts all sales and purchase information. Mrs Bachra confirmed that she writes on invoices when she has paid suppliers. OWD does not maintain a cash ledger. They do not give credit to customers.

(6) Mrs Bachra had owned and run two grocery stores and off-licences in London previously.

(7) Her husband ran two cash and carries but had nothing to do with OWD. He was ill and too sick to work. Office Deakin said that Mr Bachra had been seen and spoken to by another officer on an earlier visit. (There is also a note in the report that Officer Deakin recognised Mr Bachra, who was on the premises "and clearly working" whilst they were there.)

(8) OWD holds stock on site; it buys in for retail customers, and not specific back-to-back transactions. The shop floor was full although a full inspection did not take place.

(9) There are 10 staff, including Mr Street and Mrs Bachra's daughter. Mr Street had been employed recently to find new suppliers and promote the business for them.

(10) On due diligence:

(a) Mrs Bachra said that she does not do any due diligence on her customers. She asks DDE to do due diligence (on suppliers), and provided they state they have passed all the vetting tests then she will enter into supplies with them. Officer Deakin explained the dangers of this, and illustrated by reference to the report for Simon Lloyd Ltd ("Simon Lloyd") - DDE said they were still waiting for references and financial reports but OWD had traded anyway. Mrs Bachra said she had refused suppliers, but did not name them.

(b) Mr Kabra confirmed that he did CreditSafe checks and checks the Europa site for VAT numbers, but did not check with the Wigan unit.

(c) Mrs Bachra said she used to do her own due diligence, but this involved copies of passports, etc. Officer Deakin said this only confirms the person or company exists.

(d) Mr Ferrington got cross and said HMRC should tell traders exactly what they should get. Officer Deakin's response was that this was a common-sense decision, HMRC would not give a prescribed list and traders are always going to be responsible for the decision they make and should check any due diligence received to glean exactly what checks have been done and how that fits with Notice 726.

(e) Mrs Bachra keeps the DDE reports. She "does not use" the due diligence, she just trades with new suppliers if Mr Curley says all checks have been made and are satisfactory. Officer Deakin said that she could not rely on this as the decision and consequences are down to her.

(11) Mrs Bachra confirmed that they had received a tax loss letter for Bestbuys. That supplier had been replaced by Simon Lloyd.

72. The Conclusion/Credibility section records that the data handling interim report has significant concerns, and the interview highlighted concerns as to the legitimacy of supply chains, origin of funds for set-up of the business, controls over who is buying stock, quality of due diligence, control of cash and who is the guiding mind behind the running of the company.

73. After the meeting, Officer Cawley wrote to OWD arranging for Officer Deakin to visit OWD on 24 August 2015 (as had been agreed with Mr Kabra) to collect the requested paper records, and arranging a return visit to complete their questions regarding trading activities on 14 September 2015.

74. That meeting in September did not take place as Vincent Curley & Co were not available on that date.

***6 October 2015***

75. Officers Cawley, Deakin and Tilt visited OWD on 6 October 2015. They met with Mrs Bachra, Mr Kabra and Vincent Curley.

76. The visit report lists suppliers to OWD including Millennium Wholesale, Budweiser Budvar UK Ltd, Dassani Off Licence and Corinthian Brands Ltd. The visit report includes:

(1) They discussed (with Mr Curley) tax loss letters that had been issued to OWD. The officers referred OWD to Notice 726 and to Notice 196.

(2) Officer Deakin said she had looked at the sales listing and found missing transactions which may be cancellations or voids – on one day there were 21. Officer Deakin said she had noticed a pattern in that they tended to be at the end of the day. Mrs

Bachra said that customers may bring back alcohol or may get to check-out, not have enough money and get a credit note.

(3) Officer Deakin asked for the current supplier list - this remained outstanding from the Schedule 36 notice. Officer Cawley asked to see a list of transactions on a monthly basis, and a sample of purchase invoices - the top five in value.

77. The meeting was somewhat fractious, in particular between Officer Cawley and Mr Curley. There were various exchanges about the timing of information being provided, and what exactly was being requested.

78. There was then a discussion about specific suppliers. We list all discussed below, but have not summarised the discussion for each:

(1) Hare Wines – Mrs Bachra said that she didn't know if the goods were duty paid; Mr Curley then said the business only buys duty paid goods. She had visited the premises herself.

(2) TJ Drinks Ltd ("TJ Drinks") - They supply soft drinks, not wine or beer. Their contact was Troy. Mrs Bachra said TJ Drinks had popped into the cash and carry and offered 30 day credit terms. Due diligence was undertaken by CBS Associates and DDE. She did not place an order straightaway. Payment was by bank transfer.

(3) Wentworth - The contact was Dwight, he came to OWD's premises but she visited them in Barking. Another supplier had recommended Wentworth some time ago (but she couldn't remember who). Mr Kabra said they did a VAT check, obtained a company incorporation certificate, CreditSafe check and proof of ID. Officer Cawley handed a tax loss letter to OWD in respect of supplies from Wentworth. That letter also named SS Traders.

(4) Southern Drinks Deliveries Ltd ("SDDL") - The supplier, Mike, came to OWD, saying he had heard of them from the trade. Mike was based in Wales. They supplied wine and beer, and OWD paid by bank transfer.

(5) Southern Drinks Wholesale Ltd, trading as Palace Drinks ("SDWL") - Mrs Bachra had found out about them from recommendation. They are based in East Sussex. Paul from SDWL came to see OWD.

(6) Master Resources Ltd ("Master Resources") - They are based in Coventry and are run by Mohammed. OWD had not bought anything from them for a while.

(7) Allan Desmond Ltd ("Allan Desmond") - Mrs Bachra could not remember this supplier as it was an old supplier.

(8) Token Cash and Carry - Mrs Bachra said they had not traded them with a while.

(9) SS Traders - Mrs Bachra said this supplier was based in Hertfordshire. They had not bought anything for a while because the supplier had not been into the cash and carry and hadn't had contact.

(10) Destined Trading Ltd ("Destined") - Mrs Bachra said this supplier was based in the East; she couldn't remember the products.

(11) ALT - She could not remember.

(12) Gujarr Ltd ("Gujarr") - Mrs Bachra could not remember the details about this supplier.

79. In the context of discussing Allan Desmond, Officer Cawley noted that OWD seemed to have a high turnover of suppliers and asked whether customers expect the same stock when

they regularly come to the cash and carry. Mrs Bachra said that they, OWD, had to take what stock was coming.

80. HMRC also asked for records – purchase ledgers for the suppliers discussed, a price list from the cash and carry and records for July to September 2015 in respect of Ace Wines, Millennium Wholesale, Hare Wines, Budweiser, One Way Wholesale, SS Traders and others. They also asked about new suppliers in the last three weeks; Mrs Bachra didn't want to commit herself, and Mr Curley said they would be in the business records. There was a discussion over timing of provision of the records.

81. The Conclusion/Credibility section records:

(1) It appeared that Mrs Bachra was reliant on suppliers turning up to offer goods rather than having regular suppliers with regular orders. There was a high turnover of suppliers. The due diligence as described is minimal.

(2) There is a concern regarding delaying tactics by Mrs Bachra and her advisers in getting records to HMRC.

(3) There has been a serious delay in accessing the data on a server.

***2 February 2016***

82. Officers Cawley and Deakin returned to OWD, meeting with Mrs Bachra, Mr Curley and Mr Kabra (and others).

83. The visit report includes:

(1) There was a discussion about what Officer Deakin referred to as missing sales invoices, noting that there might be a reasonable explanation but OWD needed to provide information as to missing transactions.

(2) Officer Deakin questioned why Mrs Bachra did not know who she was renting the premises from. Officer Deakin said to Mrs Bachra that she appeared not to be running the cash and carry and asked if someone else was running it. Mrs Bachra said no - Officer Deakin found this surprising as in the three interviews she had had, Mrs Bachra seemed vague, could not remember things and always looked to the agent when being asked questions. She should have the requisite knowledge of her own business.

(3) Officer Deakin gave everyone a copy of Notice 196 regarding due diligence, and Officer Cawley gave Mr Curley copies of tax loss letters he had requested (for Bestbuys).

(4) Officer Deakin asked for the purchase invoices that had been requested. They were not available at the meeting, and there was a discussion as to timing of provision of this information which concluded with Officer Deakin saying she would issue a Schedule 36 notice.

(5) There was a discussion about particular sales invoices.

(6) Officer Deakin asked if there were recent new suppliers since December 2015, and Mrs Bachra identified Chameleon Trading Ltd ("Chameleon") and Just Beer Ltd ("Just Beer"). She later added Gempost Ltd ("Gempost"). Mrs Bachra said that for Just Beer, DDE had been instructed to do due diligence, and they did their own; for Gempost they had done the normal due diligence but not yet the enhanced due diligence. Mr Curley said that they were reviewing the due diligence. Officer Deakin said the due diligence doesn't go far enough (commenting on due diligence that only shows that the director exists). She later reiterated that there was not sufficient due diligence currently.

84. In Conclusion/Credibility it was recorded by HMRC that there remain unanswered questions over the ownership of the premises and missing sales transactions. The due diligence is not of an acceptable level, and overall the officers' level of concern remains high.

85. From the report it appears that there had been disagreements between Officer Deakin and Mr Curley in the context of the discussion about whether there were missing invoices. This continued in the context of a discussion about an invoice for rent. Officer Deakin was frustrated by Mr Curley answering on behalf of the trader without reference to her; Mrs Bachra and Mr Curley stepped out of the room for a few minutes at one point. Officer Deakin said Mr Curley was obstructive in the context of her requests for records.

86. On 10 February 2016 HMRC wrote to OWD saying that they would issue best judgment assessments for tax due on missing sales transactions and sales credit notes, issue an assessment to deny input tax on rent from invoices (where those issuing the invoices were not VAT registered), and issue an assessment to correct anomalies on input tax credits claimed in 12/14 and 03/15. The following assessments were issued:

(1) notice of VAT assessment on 12 February 2016 for £319,653 assessing output tax on missing sales transactions and sales credit notes; and

(2) notice of VAT assessment on 3 March 2016 for £128,804, disallowing input tax credits claimed on rents and correcting purchase credits claimed. This was reduced by £8,029 on review.

87. HMRC issued Schedule 36 notices on 15 March 2016 and 12 April 2016 for specified purchase invoices from SDDL, Gempost, Just Beers and STL (no further details specified), sales invoices to Exeter Wine Company and due diligence records in respect of Just Beer, Gempost, Chameleon and Best Drinks Cash and Carry ("Best Drinks"); and for purchase and sales ledgers, and the five highest value purchase invoices, for each of February and March 2016.

88. On 18 April 2016 Officer Cawley wrote to OWD saying she had now had the opportunity to review the due diligence provided in respect of the four new suppliers, Best Drinks, Chameleon, Just Beer and Gempost, setting out specific comments and concerns, concluding in her opinion that the due diligence reports did not meet the requirements set out in Excise Notice 2002.

89. On 23 May 2016 HMRC issued a VAT assessment for £10,255 in respect of the property invoices for 03/16.

90. Another Schedule 36 notice was issued on 20 June 2016.

91. Officer Cawley began trying to arrange the next visit to OWD with Mr Curley on 12 May 2016. Meetings were twice arranged but later cancelled by Mr Curley. The next visit did not take place until 27 July 2016.

***27 July 2016***

92. Officers Cawley, Deakin and Paul Marriott visited OWD and met with Mrs Bachra, Mr Curley, Mr Kabra and another on 27 July 2016.

93. The visit report includes:

(1) Suppliers in the VAT period 06/16 included Just Beer, Thames Wines Ltd ("Thames Wines"), Gempost, Top Spirits Ltd and Millennium Wholesale.

(2) Mr Curley handed over customer listings and responses to Officer Cawley's letter of 18 April 2016.

(3) Mrs Bachra said there were no new suppliers in July, nor were there any new suppliers that had introduced themselves to them.

(4) There was a discussion about missing transaction numbers on recent sales listings. Mr Curley said the transactions were cancelled ones and he had confirmed this with STL; and this was an ongoing situation. Officer Deakin referred to Mrs Bachra having previously said she now kept a copy of all voids, no sales and cancellations and was surprised that Mrs Bachra was now saying she did not, particularly as Officer Deakin had already assessed for this previously. Mrs Bachra said that when the transactions were cancelled or voided, nothing is produced by the till.

(5) Officer Deakin asked about Chameleon – the supplier said that they had never dealt with OWD despite OWD having invoices from them; she was fact-finding about what had happened. Mrs Bachra said DDE had done checks, and Mr Curley referred to the letter he had handed over which dealt with Chameleon. Mr Singh had left due diligence with Mrs Bachra, DDE had visited their premises; whereas the director of Chameleon (Aspal Singh Kaisi) said he had not met Mrs Bachra or the employee of DDE named as having visited them. Officer Deakin said the trader's VAT number may have been hijacked. Mrs Bachra explained that Mr Singh had visited the warehouse to introduce himself, and that she had placed orders with someone else, John, who came on his behalf on later dates. She didn't always order from him when they came around, and hadn't seen the delivery driver, nor was there CCTV footage of them.

(6) Officer Deakin reminded Mr Kabra again to use HMRC's VAT check hotline, saying that she had been telling him for months to use this but that it was only a suggestion.

94. In Conclusion/Credibility the officers said "It is a concern that OWD's level of due diligence did not highlight problems with Chameleon. KB's explanations are not convincing…KB still buys from people who are described as passing trade and makes an initial order on the slimmest of due diligence…".

95. HMRC issued further Schedule 36 notices on 30 August 2016.

***4 November 2016***

96. The final visit by HMRC to OWD during the periods under appeal was on 4 November 2016. Officers Cawley and Marriott attended as well as Mrs Bachra, Mr Kabra and Mr Barring of Vincent Curley & Co.

97. The visit report includes:

(1) Millennium would be the new supplier of beer. Thames Wines had supplied wine in September.

(2) The due diligence for Thames Wines was being enhanced as it was over a year old. The contact at Thames Wines, Manjeet Sahota, had initially approached Mrs Bachra.

(3) Officer Cawley said she wanted to review other due diligence. Some files were handed over; and Mr Barring asked her to put her other requests in writing.

(4) Mrs Bachra said she was concerned to hear that suppliers such as Gempost were deregistered. Officer Cawley mentioned the VAT check hotline. Mrs Bachra said she relies on outside professional help. Mr Kabra said all due diligence is outsourced with DDE. Mrs Bachra said she would only deal with companies that have been trading for over a year and will visit them herself.

(5) There was a discussion in relation to four missing purchase invoices from Chameleon.

(6) Mrs Bachra said she kept yellow copies of sales invoices but not cancellations, as they are only on a list showing cancellations without the totals.

(7) Mrs Bachra asked about the AWRS application and whether having assessments against the company would affect it. Officer Cawley said the AWRS section (of HMRC) was completely separate and they had to visit OWD themselves; as the assessments were under appeal she was not sure how it would be viewed by AWRS.

98. The Conclusion/Credibility section records that at this time she was still concerned over the rate of turnover of suppliers that shortly after supplying OWD then become deregistered.

99. HMRC issued Schedule 36 notices to OWD on 6 December 2016, 12 January 2017, 2 February 2017, 2 March 2017 and 9 March 2017.

**Notifications of deregistration and Tax loss letters**

100. OWD was sent various notifications of deregistration and tax loss letters.

101. HMRC issued seven letters to OWD notifying it of counterparties that had been deregistered for VAT ("Notices of Deregistration"):

(1) letter dated 18 June 2014 notifying deregistration of ALT with effect from 11 June 2014;

(2) letter dated 9 January 2015 notifying deregistration of Allan Desmond, with effect from 6 January 2015;

(3) letter dated 25 September 2015 notifying deregistration of Simon Lloyd, with effect from 5 June 2015;

(4) letter dated 15 October 2015 notifying deregistration of SS Traders, with effect from 8 October 2015;

(5) letter dated 5 February 2016 notifying deregistration of SDDL, with effect from 2 February 2016;

(6) letter dated 5 February 2016 notifying deregistration of SDWL, with effect from 16 January 2016; and

(7) letter dated 16 March 2016 notifying deregistration of TJ Wickham Ltd ("TJ Wickham"), with effect from 10 March 2016.

102. During the periods 03/14 to 12/16, HMRC issued seven letters to OWD notifying it that transactions through six of its suppliers had traced to tax losses (the "Tax Loss Letters"). Those letters are in standard form, reminding OWD of HMRC's ongoing investigations into MTIC fraud, stating that as a result of their enquiries in respect of the specified VAT period, HMRC now know that a specified number of transactions commenced with a defaulting trader, resulting in a loss to the public revenue. Those letters identify the purchase invoices which have been traced in transaction chains commencing with a VAT loss:

(1) letter dated 30 June 2015 in relation to 13 purchases in 03/15 from Bestbuys for VAT losses of £51,324;

(2) letter dated 21 August 2015 in relation to 16 purchases in 09/14 from Gujarr for VAT losses of £143,486;

(3) letter dated 21 August 2015 in relation to four purchases in 09/14 from Destined for VAT losses of £31,459;

(4) letter dated 27 November 2015 in relation to one purchase in 03/15 from SS Traders for VAT losses of £23,917;

(5) letter dated 8 January 2016 in relation to six purchases in 03/15 and 06/15 from SS Traders for VAT losses of £36,961;

(6) letter dated 8 April 2016 in relation to two purchases in 09/15 from SS Traders for VAT losses of £8,944; and

(7) letter dated 21 October 2016 in relation to 18 purchases in 06/16 and 19/19 from Gempost and Just Beer for VAT losses of £98,547.

103. During this time there was also a "Balance of Probabilities Tax Loss Warning" letter dated 6 October 2015. That letter warns OWD that a significant number of their purchases "appear to be connected to fraud" with the supply chains commencing with a defaulting trader in the UK, and identifying the suppliers in question as Wentworth and SS Traders. That letter says HMRC were continuing their investigations and once the full amount of unpaid VAT has been established HMRC will issue a tax loss letter to OWD scheduling the relevant transactions.

104. OWD did not trade with any supplier after receiving a Tax Loss Letter or a Notice of Deregistration in respect of that supplier.

105. Further Tax Loss Letters were issued after the VAT periods under appeal:

(1) On 1 March 2017 HMRC sent the following letters:

(a) 24 transactions in 06/16 commenced with a defaulting trader, OWD having been supplied by Chameleon, Just Beer and Thames Wines;

(b) 15 transactions in 09/16 commenced with a defaulting trader, OWD having been supplied by Thames Wines and Gempost; and

(c) 13 transactions in 12/16 commenced with a defaulting trader, OWD having been supplied by Thames Wines and N&R Supplies Ltd ("N&R").

(2) On 2 March 2017 HMRC sent the following Tax Loss Letters:

(a) 42 transactions in 06/15 commenced with a defaulting trader, OWD having been supplied by Wentworth Drinks, SS Traders, Simon Lloyd, SDDL and Master Resources;

(b) 51 transactions in 12/15 commenced with a defaulting trader, OWD having been supplied by Global Trade Europe and SDDL;

(c) 15 transactions in 03/16 commenced with a defaulting trader, OWD having been supplied by TJ Wickham;

(d) 16 transactions in 03/16 commenced with a defaulting trader, OWD having been supplied by Gempost and Just Beer; and

(e) 11 transactions in 03/16 commenced with a defaulting trader, OWD having been supplied by SDDL.

**Due diligence conducted by OWD**

106. Mrs Bachra's evidence as to the due diligence conducted by OWD was that before trading with any suppliers, due diligence was always conducted by OWD's accountant (Mr Kabra at CBS Associates) and by DDE (a business run by Mark Curley, Vincent Curley's son). Suppliers would also sometimes leave due diligence information with OWD when they visited

OWD in Rathbone Lane, and Mrs Bachra did visit the premises of some suppliers, including Wentworth and SS Traders.

107. We make detailed findings below in relation to the documentary evidence of this due diligence, based on the papers which were provided by OWD (and its advisers) to HMRC, and then draw some conclusions as to the level of due diligence conducted. We deal with the suppliers alphabetically rather than the order in which they appeared in the Deals.

108. When assessing the due diligence conducted by OWD, we do not place any weight on the fact that OWD subsequently went into liquidation. HMRC were requesting copies of due diligence packs throughout the VAT periods in issue (not only during the visits, but then requiring them by issuing Schedule 36 notices). We have concluded that the information which was provided contemporaneously to HMRC, and which is now in the bundle, is that which OWD had obtained at the time.

109. We consider the content of the various DDE reports in relation to the different suppliers below. We note at the outset that the reports take a fairly standard form:

(1) The cover letter to OWD states that the business has passed the vetting procedures. Some of these cover letters then address whether, eg, references have been provided, or the financial assessment completed.

(2) The first 12 to 15 pages are generic, describing HMRC's recommendations to check VAT numbers, commenting on market prices, proof of duty payment, difficulties of obtaining these documents in the market, terms and conditions of trade, money laundering requirements and sample excise duty forms.

(3) Business-specific information is then contained in a site visit report (which details who conducted the visit, who they met, ID provided) and a Money Laundering Regulations interview report.

(4) Copies of documents that DDE obtained are included.

(5) There is then a "Business Information Form" of about ten pages, a short section on "First Owner Identification Details" and "Business Verification Action Report" describing steps taken by DDE to verify information provided.

(6) Later reports (those provided in 2016) include a section on "FITTED", and HMRC's requirement (which applies to businesses registered under the Alcohol Wholesaler Registration Scheme and is set out in Notice 196) that businesses take a risk-based approach to due diligence. That section (where included in reports) sets out a narrative on the financial health of the company, identity of the business they intend trading with, terms of any contracts, payment and credit agreements, transport details of the movement of goods involved, existence/provenance of goods and the understanding the nature of the transaction itself.

***ALT***

110. The due diligence provided to HMRC was:

(1) a VAT number check (undated);

(2) certificate of incorporation dated 8 October 2013;

(3) acknowledgement of VAT online enrolment;

(4) copy driving licence and passport of Aaron Taylor; and

(5) VIES VAT number check conducted on 17 March 2014.

***Allan Desmond***

111. The only due diligence information provided to HMRC were DDE reports of which there were two different versions, both of which are dated 17 October 2014.

112. One version of this DDE report was sent to OWD with a cover letter dated 20 January 2015, which states that the business has passed the full vetting procedures and notes that the report details the financial information and references available. The report includes:

(1) they had conducted a site visit on 16 October 2014 and seen Mohammed Asif;

(2) copy VAT certificate dated 9 June 2014 with an effective date of 11 December 2013, business activity being wholesale of alcohol;

(3) certificate of incorporation on change of name from Sakhi Medico Legal Ltd to Allan Desmond Ltd on 9 December 2013;

(4) copy passport of Mohammed Asif;

(5) photos of office space and warehouse (which appears empty); and

(6) the director had previously worked in an off-licence and then decided to change to wholesale.

113. The second version of the report was provided to HMRC in 2019. It is also dated 17 October 2014, with a cover letter of that date; but that includes different photos (although the same visit report) and a landlord's reference from 1 December 2014.

***Bestbuys***

114. The DDE report was sent to OWD on 11 March 2015, and states that the business passed their vetting procedures. The report includes:

(1) DDE had visited the supplier on 26 February 2015 and met with its director, Manoj Patel;

(2) they included copies of, eg, certificate of incorporation, VAT registration certificate, passport of director;

(3) Bestbuys was not given credit by its suppliers;

(4) the VAT number was verified on 11 March 2015;

(5) the company was operating under a company voluntary arrangement (explaining that this meant that at some point the company had become insolvent) and its latest accounts were overdue for filing with Companies House; and

(6) DDE had not been able to obtain references.

***Chameleon Trading***

115. The DDE report was sent to OWD on 3 March 2016. That report stated that the business had passed DDE's vetting procedures and includes:

(1) DDE had visited the trader on 12 February 2016 and met with Aspal Singh Kaisi, the director;

(2) the business operates from a serviced office;

(3) the photos show warehouse space, with lots of racking and crates of goods;

(4) Mr Kaisi had previously worked within a cash and carry for family members, and within the retail sector. He gained knowledge and contacts within the wholesale side of

the industry, and his family supported him in establishing his business through their existing businesses and contacts;

(5) the VAT number was verified on 3 March 2016;

(6) a section deals with the FITTED approach to due diligence; and

(7) they had conducted a credit check with CreditSafe, and Chameleon had a credit limit of £500, with an international score described as "low risk".

***Destined Trading***

116. The due diligence provided to HMRC comprised:

(1) certificate of incorporation dated 10 April 2014;

(2) VAT certificate dated 10 June 2014 with an effective date of registration of 10 April 2014 and business activity description of non-specialised wholesale;

(3) VIES VAT check conducted on 1 September 2014; and

(4) copy passport and driving licence of Aaron Taylor.

***Gempost***

117. The DDE report was sent to OWD on 10 February 2016. That report says that the business passed the vetting procedures and includes:

(1) the visited the business and met with the business representative Makhan Jabble on 9 February 2016. They did not meet the director as he is currently signed off due to ill health;

(2) the director's brother operates a business called Just Beer;

(3) the company had been incorporated on 6 May 1998 and was registered as a high value dealer under the Money Laundering Regulations, and its VAT registration was for the trade classification of wholesale alcoholic drinks;

(4) the director is Jagjit Singh Jabble, who has operated Gempost for 17 years;

(5) the VAT number was verified on 10 February 2016; and

(6) there is a section on FITTED, and that section stated that goods supplied will be paid for on a pro-forma basis and OWD will therefore not be extended credit terms.

***Gujarr***

118. The due diligence provided to HMRC comprised:

(1) a pack of due diligence information sent to OWD by Gujarr on 19 August 2014:

(a) certificate of incorporation dated 10 November 2009;

(b) name of director and address details for Gujarr

(c) company letterhead;

(d) copy passport of Qasim Gujar;

(e) utility bill;

(f) VAT certificate issued on 12 June 2014 with an effective date of 1 December 2012, with a business activity of wholesale alcohol beverages; and

(g) form of lease agreement; and

(2) the DDE report which had been sent to OWD on 27 August 2014 and stated that the business had passed vetting procedures but that they could not provide a financial assessment at that time as the references had not been provided. The report then includes:

(a) the business had recently moved premises;

(b) a utility bill was provided as part of the verification of identity or address, in the form of a final demand from Thames Water for £676;

(c) form of lease of premises dated 20 August 2014 for lease of unit 11 at a business park;

(d) photos of office space and what are labelled as business premises showing the inside of a warehouse, but the external photos are numbered for unit 10; and

(e) Qasim Gujar had previously owned restaurants and off-licences and had one year's experience in wholesale.

***Just Beer***

119. The DDE report was sent to OWD on 15 February 2016 and states that the business passed the vetting procedures, and information relating to FITTED due diligence checks has been provided in the report. The report then includes:

(1) DDE had visited Just Beer on 9 February 2016 and met Makhan Jabble;

(2) the company had moved offices within the same building, and trades from an address which is a shared premises. It operates from the same office as Gempost, which is owned by the director's brother;

(3) the company was incorporated on 18 June 1998;

(4) the director has 32 years' experience in the industry, and is well-known in the industry;

(5) goods supplied to OWD are delivered directly by Just Beer's supplier to OWD's warehouse, and Just Beer acts as a broker in this relationship. The supplier (ie Just Beer's supplier) confirmed that they do not approach OWD directly as Just Beer is well-known in the industry and it is more commercially advantageous for them to foster a good working relationship with Just Beer;

(6) the VAT number was verified on 10 February 2016; and

(7) the FITTED information sets out a credit score for the company and refers to the fact that that score is detailed as very low risk, the director was met personally at the trading address and full documentation provided, the trade classification is incorrect for the business and the director was told it was best practice to amend this.

***Master Resources***

120. The due diligence information provided to HMRC comprised:

(1) a due diligence pack which had been sent to OWD on 23 June 2015, we infer from Master Resources, and includes:

(a) a VAT certificate dated 1 June 2015, with an effective date of registration of 13 May 2014 with a business activity of management consultancy, and a principal place of business in Sheffield;

(b) form of lease agreement for premises in Hounslow;

(c) certificate of incorporation dated 28 January 2014; and

(d) copy passport and bank statement for Mohammad Fazal; and

(2) a DDE report which was sent to OWD on 23 June 2015, stating that the business passed vetting procedures but that they could not provide a financial assessment as they were awaiting references. The report includes:

(a) they had visited premises in Hounslow and Coventry on 15 and 16 June 2015;

(b) the director has five years' experience in the wholesale of alcohol, and had previously worked for family-run businesses within the alcohol industry; and

(c) the company's customers and suppliers currently arrange the transportation of goods.

***Simon Lloyd***

121. There was the following due diligence information:

(1) certificate of incorporation on change of name from Simon Local Builders Ltd dated 4 June 2014;

(2) bank details for the company;

(3) copy driving licence and residence permit for the director, Awara Hawez;

(4) licence for office space at a business centre from 26 January 2014 to 31 July 2015;

(5) cover page (only) for a lease of a unit on an industrial estate in Cardiff, dated 5 September 2014; and

(6) a DDE report that was sent to OWD on 23 April 2015, stating that the business had passed the vetting procedures but they could not provide a financial assessment at that time as the references had not been received. That report then included:

(a) a VAT certificate which had been issued on 27 March 2015, with an effective date of 19 March 2014, and showing a business activity of wholesale of alcoholic beverages;

(b) lease dated 19 January 2015 for a unit on an industrial estate in Cardiff;

(c) the director had two years' experience working in an off-licence, and used these contacts to move into wholesale. His occupation was recorded at Companies House as being an architect; and

(d) the VAT registration was checked on 23 April 2015.

***SDDL***

122. The due diligence provided to HMRC comprised:

(1) certificate of incorporation dated 7 January 2015;

(2) VAT certificate dated 18 January 2015, with an effective date of 8 January 2015, business activity of wholesale of alcoholic beverages, with a principal place of business in Peacehaven;

(3) copy driving licence of Michael Butson;

(4) share certificate;

(5) information letter from HMRC addressed to SDDL;

(6) letter confirming registration for online business banking with Lloyds Bank; and

(7) a DDE report which was sent to OWD on 2 September 2015, stating that the business passed vetting but they did not yet have references. The report includes:

(a) the business had recently moved premises;

(b) photos showing warehouse space, with racking and various crates;

(c) the director had previously worked in warehousing and had four years' experience in retail; and

(d) the VAT registration was verified on 2 September 2015.

***SDWL***

123. The due diligence provided to HMRC was:

(1) a VAT certificate dated 11 October 2012, with a business activity of wholesale of alcoholic beverages;

(2) Money Laundering Regulations certificate showing the company is registered as a high value dealer, which had been issued on 23 October 2014;

(3) copy bank statement;

(4) copy of Paul Bingham's passport and driving licence;

(5) certificate of incorporation dated 5 October 2012;

(6) letterhead of Palace Drinks (SDWL traded as Palace Drinks);

(7) utility bill; and

(8) a DDE report sent to OWD on 31 July 2015 which stated that the business had passed the vetting procedures but that they cannot provide the financial assessment as they are awaiting references. That report then includes:

(a) record of a site visit to premises in Shoreham, with photos of a large warehouse area, showing lots of stock and empty racking, the outside of which had signage for Palace Drinks;

(b) the director was previously a manager at Bookers, and had 29 years' experience in the industry; and

(c) they had verified the VAT number on 30 July, and the MLR registration on 5 August 2015.

***SS Traders***

124. OWD provided the following due diligence to HMRC:

(1) copy passport for Che Wai Leung;

(2) certificate of incorporation dated 17 January 2011;

(3) VAT certificate dated 14 October 2014 with an effective date of 15 June 2011 and a business activity of other food service activities;

(4) amended VAT certificate dated 17 March 2015 with a business activity of wholesale alcoholic beverages;

(5) invoice from Regus for office in Watford;

(6) letter of introduction, and sample letterhead as well as bank details;

(7) VAT number validation dated 3 February 2015; and

(8) a DDE report which was sent to OWD on 28 April 2015, stating that the business passed the vetting procedures but they cannot provide the financial assessment at this time as they were awaiting receipt of references. That report includes:

(a) they had visited the premises in Watford on 24 April 2015 and met the director;

(b) an account statement from Regus invoicing the company for May, the date of which is 25 May 2015; and

(c) photos of office space.

125. We also had:

(1) an extract from that report with a signed declaration from the director dated 22 June 2018; and

(2) a further copy of the report which had been provided to HMRC in 2019, with the same date of 28 April 2015, but containing additional enclosures – eg letters from Pernod Ricard and E&J Gallo Winery in relation to requests for proof of duty paid, the amended VAT certificate (the faxed footer for which says it was received on 28 April 2015 (in contrast to the header which says 28 April 2014 but that cannot be correct as the amended certificate was only issued in 2015)), and a Regus account statement dated 24 April 2015 (rather than the version from May 2015).

***Thames Wines***

126. There were three reports from DDE which were sent to OWD on different dates:

(1) a DDE report was sent to OWD on 27 January 2016, stating that the business had passed the vetting procedures, contains a section on the FITTED information checks and includes:

(a) the company was incorporated on 9 December 2014;

(b) they had visited the business on 26 January 2016 at an industrial estate in Slough and met with the director Manjit Sahota;

(c) the business had registered for VAT, but not yet received their VAT certificate, although the registration number had been verified with HMRC;

(d) photos of mainly empty warehouse space;

(e) the director had worked in car sales, then worked in the alcohol industry with a friend, became a director of a cash and carry and then started Thames Wines – he had ten years' experience in the alcohol industry;

(f) the VAT number had been checked on 28 January 2016;

(g) a CreditSafe report was produced on 16 February 2016, and the business was ranked as moderate risk;

(2) a further version was sent on 8 July 2016, and that report also included:

(a) OWD and Thames Wines have agreed verbal terms and conditions and payment is made on a pro forma basis;

(b) a CreditSafe report dated 4 July 2016 states that the company has a £500 credit limit and an international credit score description of moderate risk; and

(3) the third DDE report was dated 28 September 2006, and included:

(a) updated photos of warehouse space;

(b) updated CreditSafe report of 28 September 2016, still showing £500 credit limit.

***TJ Drinks***

127. The due diligence provided to HMRC was:

(1) certificate of incorporation dated 24 July 2014 for TJ Soft Drinks Ltd;

(2) copy of Troy Johnson's passport;

(3) unaddressed and undated letter of introduction giving an address as Bridle Way;

(4) letter from Companies House dated 22 July 2017 which required urgent action as it noted that TJ Drinks Ltd's annual return was due for filing (the last date for filing being 21 August 2015);

(5) utility bill addressed to Mr Johnson at Bridle Way but for a different supply address of Flat 10;

(6) VAT certificate dated 8 July 2015 with an effective date of registration of 1 July 2015 for TJ Soft Drinks Ltd and describing business activity as wholesale of fruit and vegetable juices, mineral water and soft drinks;

(7) acknowledgement of enrolment to submit VAT returns online;

(8) confirmation of a change of registered office address;

(9) letter confirming an agreement to let premises to Mr Johnson from 29 July 2015 for use for soft drinks storage;

(10) copy of Mr Johnson's debit card; and

(11) a DDE report dated 3 August 2015 which stated the business passed the vetting procedures but added that DDE cannot provide the financial assessment as they are currently awaiting receipt of references. The report includes:

(a) they had met Mr Johnson at the business premises on the site visit;

(b) the business operates from the director's residential address;

(c) business commenced trading in July 2015;

(d) the director's family have operated businesses in the retail sector for a number of years, and the director gained experience from working in these family businesses. He also has a number of friends who run cash and carry type businesses and this provided him with relevant knowledge and contacts;

(e) the company's suppliers and its customers arrange for the transport of goods;

(f) TJ Drinks approached OWD having researched potential customers on Google; and

(g) one of the attachments is a confirmation of submission of notice of change of name (does not say on face but from TJ Soft Drinks Ltd to TJ Drinks Ltd).

***TJ Wickham***

128. The due diligence provided to HMRC was:

(1) certificate of incorporation dated 7 January 2016;

(2) bank account details;

(3) part of a VAT certificate showing business activity of non-specialised wholesale of food, beverages and tobacco – the section on "important dates" which usually includes date of certificate and effective date of registration is missing;

(4) VIES VAT number validation of 14 January 2016;

(5) share certificate;

(6) copy passport of Tobias Wickham;

(7) lease agreement for a warehouse to start on 15 February 2016; and

(8) a DDE report sent to OWD on 2 March 2016 which stated that the business had passed vetting procedures and the report contains information on the FITTED due diligence checks. The report includes:

(a) director had previously worked in a wholesale business that dealt in tea, coffee and soft drinks. He inherited some money, had noticed a demand for alcohol and decided to establish a wholesale business in the alcohol industry using this money. He had established the company in January of that year;

(b) estimated current annual turnover of £4 million; and

(c) the VAT number was currently registered to the director's home address as he was in the process of locating premises. He was unable to locate the bottom part of the online VAT certificate on the day of the visit, so they were unable to verify the effective date. They had verified the VAT number on 29 February 2016.

***Wentworth***

129. The due diligence provided to HMRC comprised:

(1) bank statement for the company issued on 10 October 2014;

(2) letter of introduction from Dwight Cunningham of Wentworth;

(3) VAT certificate dated 30 April 2014 with an effective date of registration of 1 September 2013, business activity of alcohol wholesaler;

(4) certificate of incorporation dated 9 August 2013;

(5) copy of Mr Cunningham's driving licence and passport;

(6) a DDE report sent to OWD on 10 March 2015, the cover letter to which stated that the business passed the vetting procedures and that DDE cannot provide the financial assessment at this time as they are awaiting receipt of references. The report includes:

(a) report of site visit on 5 March 2015 to a unit on Atcost Road, where they had met with Mr Cunningham;

(b) various copies of ID verification, which included a VAT certificate dated 3 March 2015 stating the business activity as wholesale of fruit and vegetable juices, mineral water and soft drinks;

(c) letter on behalf of landlord asking rent be paid to different company (as the freehold had been sold), making it clear that Wentworth had been using Atcost Road since July 2014;

(d) photos of the premises, including office space, warehouse space (some stock shown, lots of empty racks) and a business sign for Wentworth outside the unit;

(e) Mr Cunningham had been working in various cash and carries in the London area for the last three to four years, before then forming Wentworth;

(f) uses a haulage company for the movement of goods; and

(g) names of referees are given as individuals from Millennium Cash and Carry Ltd and Seabrook Warehousing Ltd.

130. There was a further copy of this report from DDE which was sent to OWD on 28 May 2015; it is substantially same but states that they could not obtain references and noting this is not necessarily negative.

***Conclusions on level of due diligence conducted***

131. The first DDE report which was sent by DDE to OWD was that for Gujarr on 27 August 2014. There was no DDE report for ALT, Destined or N&R Supplies Ltd ("N&R") (a supplier for which no due diligence was provided to HMRC) and we find that DDE had not been instructed by OWD to conduct due diligence for initial suppliers such as ALT and Destined.

132. For some suppliers (eg Allan Desmond, Gempost and Just Beer), the only documentary evidence of due diligence was the DDE report.

133. Mr Kabra and Mrs Bachra informed HMRC during the various visits that CBS Associates would always conduct due diligence on suppliers. The difficulty with accepting this explanation is that there was no documentary evidence of this for some of the suppliers (as above), and no good reason for the failure to have produced such evidence.

134. This can be illustrated by the due diligence produced for Chameleon Trading (where the only evidence produced was the DDE report). The first supply was on 31 March 2016, by which time there had been several visits from HMRC. In the visit of 2 February 2016, Mrs Bachra named Chameleon Trading as a new supplier from whom they had bought in December, and said that due diligence had been done by DDE. She said that the supplier came to OWD's premises and left due diligence. There was no documentary evidence of what had been left, and no documentary evidence of any due diligence having been undertaken by Mr Kabra. The proximity of HMRC's visit to the dates of trading with Chameleon Trading means that if due diligence had been to hand at that time, we would expect OWD to have provided it. The fact that nothing was given to HMRC leads us to infer that there was nothing other than the DDE report.

135. The position is similar in respect of Just Beer - HMRC sent a Schedule 36 notice to OWD on 15 March 2016 requiring production of specified invoices and documents, including due diligence records in respect of Just Beer (which had originally been requested on 19 February 2016). OWD had only started trading with Just Beer in January 2016, and they only provided the DDE report (from February 2016). This is strong evidence that there was no other due diligence which had been done.

136. In any event, based on all of the evidence before us, including the level of due diligence done for ALT and Destined, and Mr Kabra's explanations to HMRC officers during the visits, and recognising that some of the due diligence held by OWD for suppliers was that which had been handed to them by those suppliers, we conclude that where conducted this involved obtaining the certificate of incorporation of the company, verifying the identity of the director (by obtaining a copy passport and/or driving licence) and some check of the VAT number (generally by conducting a VIES check online).

137. We have concluded, on the balance of probabilities, that, with one exception, the only due diligence conducted by or on behalf of OWD is that which was produced by way of documentary evidence. The exception relates to N&R, where the first supply was on 17 November 2016, ie after the last visit by HMRC to OWD whilst trading, and accept that this would explain why no due diligence for this supplier was provided to HMRC.

138. We address in the Discussion the extent to which this information was then read and assessed by OWD.

**Assessments, appeals and liquidation**

139. HMRC issued a notice of VAT assessment to OWD on 24 January 2017 for £38,415 denying input tax which had been claimed for 12/15 and 06/16 on purchases from Chameleon. The director of Chameleon had no knowledge of OWD and HMRC said it appeared OWD had purchased from a hijacked trader. OWD requested a review (by letter from Rainer Hughes on 6 February 2017). The review conclusion letter from HMRC dated 14 March 2017 upheld that assessment.

140. HMRC notified OWD on 5 June 2017 of its decision to refuse entitlement to the right to deduct input tax on the basis of the application of *Kittel*. The VAT assessment for the periods 03/14 to 12/16 totalled £2,064,126. OWD requested a review; the letter is dated 31 March 2017 but that date cannot be correct. In any event, HMRC replied on 22 June 2017 stating that the request had been passed to the review team.

141. Officer Cawley and Paul Marriott made an unannounced visit to OWD at Rabone Lane on 27 June 2017. The building was being demolished. The builders confirmed that they had been on site since April 2017 and they were building a new cash and carry for Dhamecha.

142. On 29 June 2017 HMRC wrote to OWD Ltd at the address of CBS Associates informing them that OWD's VAT registration was cancelled with effect from 1 April 2017.

143. HMRC had also issued notifications of excise duty assessments to OWD in November 2016, January 2017 and February 2017, as well as related penalty assessments.

144. A liquidator was appointed for OWD on 15 August 2017.

145. As set out in Background Facts above, the penalty was issued to OWD c/o Kingsland Business Recovery of £1,177,422.96 on 2 November 2017 and the PLN for the same amount was issued to Mrs Bachra in December 2017.

**DISCUSSION - WHETHER INACCURACIES IN OWD'S VAT RETURN**

146. As set out above, HMRC must establish, on the balance of probabilities, that OWD was not entitled to the input tax claimed, ie that the *Kittel* test is satisfied in relation to the relevant supplies. This requires the following to be determined:

(1) was there a fraudulent evasion of VAT;

(2) if so, were OWD's purchases on which input tax have been denied connected with that fraudulent evasion; and

(3) if so, did OWD know or should it have known that its purchases were connected with that fraudulent evasion of VAT.

147. Mr Bedenham accepted that the various defaults relied upon by HMRC in each of the specified deals were fraudulent. However, he challenged whether HMRC had met their burden of establishing a connection with the fraudulent evasion of VAT in some of the deals.

**Was there a fraudulent evasion of VAT**

148. The tax losses, and the fact that they resulted from the fraudulent evasion of VAT, were agreed. The fraudulent defaulters were:

(1) ALT (Deals 2-37, 68-70) - direct supplier to OWD;

(2) Logical Retail Ltd ("Logical") (Deals 72-73, 75-86, 92-93) - indirect supplier to OWD - Logical supplied to Gujarr, who then supplied to OWD. HMRC also say that Deal 74 traced to Logical;

(3) Destined (Deals 87-91, 94-96) - direct supplier to OWD;

(4) Fahm Marketing Ltd ("Fahm") (Deals 97-110) - indirect supplier to OWD - Fahm supplied to Allan Desmond, who then supplied to OWD. Mrs Bachra did not accept that the chain of transactions is proved to go back to Fahm for Deals 104-109;

(5) Aphrodite Sales Ltd ("Aphrodite") (Deals 111-116) - indirect supplier - Aphrodite supplied to Wentworth who then supplied to OWD;

(6) Beer Bhai Cash & Carry Ltd ("Beer Bhai") (Deals 117-119, 152, 153-157) - indirect supplier - Beer Bhai supplied to Wentworth who then supplied to OWD and also to Meadowhall Cash and Carry who supplied to SS Traders Ltd and then to OWD;

(7) Happy Days (2007) Ltd ("Happy Days") (Deals 120-132, 158-159) - indirect supplier - Happy Days supplied to Simon Lloyd who then supplied to OWD;

(8) Chattel Broker Ltd ("Chattel") (Deals 133-148) - indirect supplier - Chattel supplied to Bestbuys who were the supplier to OWD;

(9) Elliott Chapman Ltd ("Elliott Chapman") (Deals 149-150) - indirect supplier - Elliot Chapman supplied to More 4 Less Cash & Carry Ltd who were the supplier to SS Traders and on to OWD;

(10) Henry Richardson Ltd ("Henry Richardson") (Deals 160-177, 181-192) - indirect supplier - Henry Richardson supplied to Simon Lloyd and Master Resources, both of which were suppliers to OWD;

(11) TJ Drinks (Deals 200-205, 264-271) - direct supplier to OWD;

(12) KT Enterprises Ltd ("KT Enterprises") (Deals 206-211) - indirect supplier - KT Enterprises supplied to Wentworth who were the supplier to OWD. Mrs Bachra did not accept that the chain of transactions is proved to go back to a fraudulent tax loss in Deals 208-211;

(13) SDWL (Deals 212-213, 215-219, and 259-263) - direct and indirect supplier - where SDWL had not supplied OWD directly, it supplied Meadowhall Cash & Carry Ltd which then supplied to SS Traders who made the supply to OWD;

(14) Global Trade Europe Ltd (Deals 214, 220) - direct supplier to OWD;

(15) Phoenix Wholesalers Ltd ("Phoenix") (Deals 283-289, 295-298) - indirect supplier - Phoenix supplied to Gempost and Just Beer, who were the suppliers to OWD;

(16) JJ General Trading Ltd ("JJ") (Deals 290-294) - indirect supplier - JJ supplied to Gempost who supplied OWD;

(17) Yewhall Ltd ("Yewhall") (Deals 299-304; some of Deals 305 to 313) - indirect supplier to OWD - Yewhall supplied TJ Wickham, the supplier to OWD;

(18) Neat Trading Ltd ("Neat") (some of Deals 305-313) - indirect supplier - these deals were all supplies by TJ Wickham to OWD, and Mrs Bachra accepted that the supplies to TJ Wickham were made either by Neat or Yewhall;

(19) Chameleon (Deals 314-328) - direct supplier to OWD;

(20) Newmoby Ltd ("Newmoby") (Deals 329-344, 348-353) - indirect supplier - Newmoby was a supplier to Gempost and Just Beer, both of whom made supplies to OWD;

(21) Trade Networking UK Ltd ("TNL") (Deals 361-362) - indirect supplier - TNL supplied Safina London Ltd, which supplied Thames Wines, the supplier to OWD;

(22) Saracen Sales Ltd ("Saracen") (Deals 363-370) - indirect supplier - Saracen was another supplier to Safina London Ltd in respect of its supplies to Thames Wines which were then supplied to OWD; and

(23) N & R (Deals 371-375) - direct supplier to OWD.

149. Deals 178-180, 193-199, 221-258 and 272-282 are not listed above against any fraudulent defaulter. They were all supplies by SDDL to OWD. HMRC did not allege that SDDL was a fraudulent defaulter, and Mrs Bachra did not accept that these supplies were connected with the fraudulent evasion of VAT.

**Were OWD's purchases connected with that fraudulent evasion**

150. Dealing with deals where Mrs Bachra challenged whether the supplies to OWD were connected with the fraudulent evasion of VAT, Mr Watkinson acknowledged that HMRC had not produced documentary evidence (eg invoices) but were inviting the Tribunal to draw an inference based on all of the evidence available.

***Deal 74 - purchase from Gujarr***

151. There were 17 purchases by OWD from Gujarr (which was not alleged to be a fraudulent defaulter) in August to October 2014 (Deals 72-86 and 92-93). 16 of those have been accepted as tracing back to Logical (a fraudulent defaulter). There is no documentary evidence that the goods in Deal 74, purchased on 21 August 2014 for a gross amount of £36,680.57, also traced back to Logical.

152. The evidence adduced by HMRC in respect of Gujarr (not specific to Deal 74) establishes that:

(1) HMRC denied Gujarr's claims for £8.5 million of input tax under the *Kittel* principle, this being all the input tax it had claimed. The denial letter stated, amongst other things, that all of Gujarr's transactions had been traced back to fraudulent tax losses;

(2) HMRC assessed Gujarr for £1.5 million of output tax on undeclared sales;

(3) Gujarr went missing from its premises in September 2014;

(4) Gujarr was deregistered for VAT with effect from 9 October 2014; and

(5) Gujarr was wound up and put into liquidation on 28 January 2015.

153. We are satisfied on the basis of this evidence that HMRC have established that, on the balance of probabilities, Deal 74 was connected to a fraudulent tax loss.

***Deals 104-109 - purchases from Allan Desmond***

154. Deals 97-110 were all purchases by OWD from Allan Desmond in October to December 2014. Officer Jones has produced documents tracing 8 of the 14 transaction chains (Deals 97-103 and 110) back to Fahm (a fraudulent defaulter). HMRC did not have complete supporting documents for Deals 104-109 (the invoices to OWD for which were dated 18 to 28 November 2014) showing that Allan Desmond had purchased these goods from Fahm.

155. However, on the basis of:

(1) the pattern of the other eight deals with Allan Desmond; and

(2) Mr Mohammad Asif of Allan Desmond said during a visit by HMRC on 28 November 2014 that the only supplier from whom it had actually purchased was Fahm (he had another potential supplier Mac Drinks lined up but had not yet purchased from them and was hoping to do so the following week),

we accept on the balance of probabilities that Deals 104-109 are also connected to fraudulent evasion by Fahm.

***Deals 208-211 - purchases from Wentworth***

156. OWD bought from Wentworth in Deals 206-211 in July to September 2015. Mrs Bachra accepted that the goods in Deals 206-207 had been supplied by KT Enterprises, a fraudulent defaulter, to Wentworth. There was no documentation connecting Deals 208-211 back to KT Enterprises. HMRC invited us to draw an inference.

157. We note that Deals 206 and 207 took place in July and August 2015, whereas the challenged supplies all took place from 3 to 8 September 2015.

158. There had been earlier supplies in 2015 by Wentworth to OWD, which also traced back to fraudulent defaulters – in some Wentworth had bought from Beer Bhai, others from Aphrodite. This was not a case where the direct supplier to OWD only had one supplier.

159. The evidence from HMRC's visits establishes that:

(1) At a visit by HMRC to Wentworth on 5 August 2015, Dwight Cunningham, the director of Wentworth, said he had started trading with KT Enterprises, and there had been about six deals since July 2015. He had started discussions with TJ Drinks as a potential customer.

(2) At a visit by HMRC to TJ Drinks on 14 September 2015, officers met with Troy Johnson, and referred to his two suppliers but the visit report then lists three of them, being KT Enterprises, OWD and SDDL.

(3) At a visit by HMRC to KT Enterprises on 18 September 2015, Kenneth Tokley said he supplied to Wentworth and TJ Drinks, as well as various market traders.

160. There were also invoices from TJ Drinks to Wentworth for several supplies in October to December 2015.

161. HMRC submitted that the only two potential suppliers to Wentworth for these four deals are KT Enterprises and TJ Drinks, both of which were accepted to be fraudulent defaulters.

162. On balance, and taking account of all of the evidence, we accept that the connection to a fraudulent default has been established by HMRC.

***Deals 350-353 - purchases from Gempost***

163. Gempost was a supplier to OWD between January and August 2016. Gempost was not a fraudulent defaulter, but was accepted as having purchased from Newmoby (a fraudulent defaulter) in Deals 329-338 and 348-349 in May, June and July 2016. Deals 350 to 353 were supplies from Gempost to OWD between 1 to 10 August 2016. There was no documentation linking these supplies back to Newmoby, and HMRC relied on the pattern of trade.

164. Gempost were found to be missing during a visit by HMRC on 24 August 2016, and HMRC had not been able to obtain invoices in relation to these four deals. HMRC did adduce evidence that Gempost had made a further 176 purchases from Newmoby between 15 May and 30 July 2016.

165. Based on the pattern of trade and the fact that Gempost had made more purchases from Newmoby, we drew the inference that Deals 350-353 also traced from Gempost back to Newmoby, and were connected with the fraudulent evasion of VAT.

***Deals 178-180, 193-199, 221-258 and 272-282 - purchases from SDDL***

166. These are all purchases by OWD from SDDL. SDDL is said by HMRC to be a buffer trader - they do not allege it was itself a fraudulent defaulter. HMRC submit that the deals

were connected with the fraudulent evasion of VAT, on the basis that all of SDDL's purchases which they have been able to trace have been traced to fraudulent tax losses, and so, on the balance of probabilities, where SDDL supplied OWD those purchases also traced to fraudulent tax losses.

167. The evidence as to SDDL establishes:

(1) It was incorporated with Mr Michael Butson as its sole director, who had no experience of running a business, set up the company funded by £2,000 from his parents in January 2015, and just over a year later had predicted turnover of around £13 million.

(2) All of SDDL's purchases that have been traced have been traced to fraudulent tax losses. Its suppliers were:

(a) Renown Wholesale Ltd - these purchases traced back to Beers R Us Ltd, which did not submit any VAT returns and the evidence supports the conclusion that it had used a false address as its principal place of business;

(b) Wentworth - these purchases traced to Beer Bhai and KT Enterprises, both accepted fraudulent defaulters;

(c) Beer Bhai, an accepted fraudulent defaulter;

(d) Dream Drinks Ltd - this company did not submit any VAT returns, and failed to declare transactions in electronic goods;

(e) TJ Drinks, an accepted fraudulent defaulter;

(f) Garden City Sale Ltd - its supplier was KT Enterprises, an accepted fraudulent defaulter;

(g) Yewhall, an accepted fraudulent defaulter; and

(h) Meadowhall Wholesale Ltd - its suppliers were Beer Bhai and SDWL, both fraudulent defaulters.

(3) SDDL was deregistered with effect from 2 February 2016.

168. On the basis of the evidence, we accept that OWD's purchases from SDDL also traced to fraudulent tax losses.

**Did OWD know or should it have known that its purchases were so connected**

169. We have set out above the principles which have developed in relation to whether a taxable person knew or should have known that its transactions were connected with the fraudulent evasion of VAT. Both parties proceeded on the basis that it is the knowledge and actions of Mrs Bachra that are relevant when considering what OWD knew or should have known; we agree that this is the correct approach as she was the sole director of OWD and her evidence was that she was the person making the decisions.

170. For HMRC, Mr Watkinson submitted:

(1) HMRC's position was that there was evidence of contrivance, an orchestrated scheme to defraud HMRC. Mr Watkinson submitted that HMRC did not need to prove there was such a scheme; but if there was such a scheme this goes to the state of knowledge of OWD. The fact of such a scheme can give rise to the inference that OWD knew its role therein.

(2) Indicia of such a scheme were said to be the scale of the tax losses, pattern of the replacement of defaulting traders, links between several of the companies in the transaction chains, pattern of dealing (where suppliers always had what customers

wanted, a supplier would deliver to middleman's customer yet they were not cut out of the supply chain), use of basic transaction documentation, pricing with an apparently fixed range of mark-ups, and the parties were riddled with indicia of contrived trading (incorrect trade classifications, directors with minimal experience, traders not having storage facilities, provision of credit by businesses lacking apparent means).

(3) HMRC's primary case was that Mrs Bachra actually knew that the transactions were connected with fraud; alternatively, she should have known as they permitted of no other reasonable explanation.

(4) HMRC relied upon the same factors for both of these submissions:

(a) awareness of the risk of VAT fraud, the need for due diligence and that OWD's own transactions had been traced to fraudulent tax losses;

(b) Mrs Bachra's personal links to revenue fraudsters;

(c) repeated connection with fraud;

(d) lack of commerciality;

(e) OWD's failure to provide information to HMRC; and

(f) the due diligence was nothing more than window dressing, an exercise in collecting paper to show to HMRC, sometimes after OWD had started to trade, containing obvious indicia that suppliers were not commercially credible yet no serious thought can have been given to the legitimacy of the suppliers.

171. Mr Bedenham submitted that Mrs Bachra had had the opportunity to run a cash and carry business in Birmingham in 2013, had taken that up and, not having had the experience of such a role, had taken the sensible steps of seeking external help from accountants and subsequently a tax adviser and using a professional due diligence company. Some of the transactions undertaken were subsequently found to have been connected with fraud; but her suppliers were vetted by professionals and nothing about these purchases stood out compared to the remainder of the business. The goods bought were then sold in the cash and carry.

172. Furthermore, Mr Bedenham emphasised that HMRC's own case relied upon the same factors for knowledge and should have known, ie HMRC accepted that these factors are consistent with its position that OWD should have known of the connection to fraud and even if we find that the matters relied upon are made out this does not require a conclusion that OWD knew of the connection.

173. The outcome of this appeal need not necessarily be binary – just as we could find that HMRC had met their burden in respect of some but not all of the connections to fraudulent evasion, we could also conclude that, based on the facts as we have found them, OWD knew or should have known as from a particular date.

174. We have assessed the various factors on which the parties relied in the light of all of the evidence before us and set out our conclusions below.

***Scale of the tax losses***

175. HMRC have established a connection to the fraudulent evasion of VAT for 332 supplies to OWD over a three year period. HMRC have produced a deal overview which records, for each VAT period, the percentage of input tax traced to the fraudulent evasion of VAT. This shows the following:

| **VAT period** | **% input tax traced to fraud** | **VAT period** | **% input tax traced to fraud** |
|---|---|---|---|
| 03/14 | 42 | 09/15 | 52 |

| | | | |
|---|---|---|---|
| 06/14 | 8 | 12/15 | 50 |
| 09/14 | 66 | 03/16 | 69 |
| 12/14 | 53 | 06/16 | 44 |
| 03/15 | 72 | 09/16 | 31 |
| 06/15 | 70 | 12/16 | 28 |

176. The overall percentage (based on the total net purchases) was that 48% of input tax claimed traced to fraud. On the basis of our findings of fact and conclusions as to the connections, we accept this as accurate.

177. Whilst the sale of alcohol was the majority of OWD's business, this was nevertheless only 65 to 70%. Of the non-alcohol sales, there was no evidence as to the proportion of zero-rated or standard-rated products.

178. This is a significant number of transactions, and a substantial proportion of the input tax claimed. The connections have been found to be established through a number of suppliers, several of whom were themselves the fraudulent defaulters (eg ALT, Destined and TJ Drinks), but others were buffers (eg Gujarr and Wentworth), such that the fraudulent default had occurred further down the chain.

***Pattern of replacement of defaulting traders***

179. Mr Watkinson submitted that the general pattern was that when one defaulter was deregistered a new one was brought in to replace it, and questioned why so many companies that were connected to fraud were attracted to OWD.

180. Mrs Bachra's evidence was that she was unlucky, and gave evidence that OWD had traded with some suppliers for longer periods of time. She referred in this context to SDDL and Millennium. SDDL were a supplier from April 2015 to January 2016. However, there was minimal evidence as to the transactions with Millennium – all we have is the fact that they were named as a current supplier in some of the visit reports.

181. We acknowledge the underlying facts in relation to both the scale of the tax losses, and this pattern (which we do find existed) of the replacement of defaulting traders. These factors, viewed in isolation, are not probative; it is possible that OWD was targeted by those connected with fraud as it became known that insufficient questions were being asked by OWD. We do take them into account when reaching our conclusions.

***Knowledge of risk of fraud and warnings given to OWD***

182. Mr Watkinson drew attention to the warnings given to OWD about the general risk of VAT fraud in the alcohol industry, the notifications in relation to OWD's own suppliers and the lack of any meaningful reaction thereto. In this regard, he submitted:

(1) OWD was warned of the risk of fraud in the industry, and told that its own transactions had been traced to fraud, on numerous occasions.

(2) Mrs Bachra accepted that she knew of the risk of fraud, had read Notice 726, had read "How to Spot Missing Trader Fraud", and knew of the need to check counterparties.

(3) At the visit on 5 August 2015 she was given these notices again and told not to blindly rely on due diligence reports.

(4) OWD received seven Notices of Deregistration and Mrs Bachra acknowledged that she was concerned.

(5) OWD received eight Tax Loss Letters (including for this purpose the Balance of Probabilities Tax Loss Warning) in relation to transactions involving six of their suppliers.

183. HMRC had provided Mrs Bachra with the notice on "How to Spot Missing Trader Fraud" at the initial unannounced visit on 23 October 2013 and took her through the notice. They also issued Notice 726 at that meeting. This was before any of the transactions in this appeal.

184. We remind ourselves of the content of these notices.

185. The notice "How to Spot Missing Trader Fraud" is short and clear, and sets out the warning:

> "Be suspicious if your business or those you are dealing with show any of the following characteristics.
>
> • Newly established or recently incorporated companies with no financial or trading history.
>
> • Contacts have a poor knowledge of the market and products.
>
> • Unsolicited approaches from organisations offering an easy profit on high-value/volume deals for no apparent risk.
>
> …
>
> • Entities trading from residential or short-term lease accommodation and serviced offices.
>
> *This list is not exhaustive – use your common sense and be suspicious.*"

186. It goes on to set out that if a trader does not conduct "intelligent risk assessment" including KYC or ignoring adverse indicators a trader risks involvement in fraud.

187. Notice 726 sets out at section 6 on "Dealing with other businesses – How to ensure the integrity of your supply chain" examples of indicators that could alert a trader to the risk that VAT would go unpaid, and include:

> "1) Legitimacy of customers or suppliers. For example:
>
> • what is your customer's/supplier's history in the trade?
>
> …
>
> • does your supplier offer deals that carry no commercial risk for you – eg, no requirement to pay for goods until payment received from customer?
>
> …
>
> • are they high value deals offered with no formal contractual arrangements?
>
> • are they high value deals offered by a newly established supplier with minimal trading history, low credit rating etc?
>
> • can a brand new business obtain specified goods cheaper than a long established one?
>
> • has HMRC specifically notified you that previous deals involving your supplier had been traced to a VAT loss and/or had involved carousel movements of goods?"

188. That same section then says on checks:

> "6.2 Checks carried out by existing businesses
>
> The following are examples of specific checks carried out by businesses that took part in the consultation exercise in 2003 when these rules were introduced. These may also help you to decide what checks you should carry out, but this list is not exhaustive and you should decide what checks you need to carry out before dealing with a supplier or customer:

> • obtain copies of Certificates of Incorporation and VAT registration certificates
>
> • verify VAT registration details with HMRC
>
> • obtain signed letters of introduction on headed paper
>
> • obtain some form of written and signed trade references
>
> • obtain credit checks or other background checks from an independent third party
>
> • insist on personal contact with a senior officer of the prospective supplier, making an initial visit to their premises whenever possible
>
> • obtain the prospective supplier's bank details, to check whether:
>
> (a) payments would be made to a third party; and
>
> (b) that in the case of an import, the supplier and their bank shared the same country of residence.
>
> • check details provided against other sources, e.g. website, letterheads, BT landline records
>
> Paperwork in addition to invoices may be received in relation to the supplies you purchase and sell. This documentation should be kept to support your view of a transaction's legitimacy. The following are examples of additional paperwork that some businesses retain:
>
> • purchase orders
>
> • pro-forma invoices
>
> • delivery notes
>
> • CMRs (Convention Merchandises Routiers) or airway bills
>
> • allocation notification
>
> • inspection reports
>
> Again this is not an exhaustive list, but does show some of the more common subsidiary documentation."

189. Mrs Bachra confirmed that she read these notices. Whilst Notice 726 is stated to apply to supplies of specified goods, the list of which does not include alcohol, Mrs Bachra confirmed she understood that it was relevant because it was handed to her by HMRC. She accepted that she knew of the risk of alcohol fraud in cash and carries before the periods in issue.

190. This awareness of the risks can only have been reinforced by subsequent communications from HMRC:

(1) On 28 March 2014 HMRC sent a generic MTIC fraud advice letter. Some of the factors mentioned in that letter relate to particular industries (eg metals). However, looked at overall this letter is a clear warning, giving as examples newly established or recently incorporated companies, and entities trading from short-term lease accommodation.

(2) HMRC's letter of 26 June 2015 was specific to OWD. It started with confirming the date of HMRC's next visit, and then set out the cost of alcohol fraud, stating that HMRC "are concerned that your business could be at risk of involvement in supply chains that are connected with fraud". They repeated this concern in their letter of 14 July 2015 when they confirmed the meeting was re-arranged.

191. The risks of alcohol fraud were also discussed in detail during the visits from HMRC on 15 August 2015 and 6 October 2015. Furthermore, by 6 October 2015, OWD had received three Notices of Deregistration (the first of which was from 18 June 2014) and three Tax Loss Letters. During that meeting Officer Cawley explained that Tax Loss Letters were an amber light to the trader, which meant that Mrs Bachra may want to make further checks on transactions. In the ensuing discussion with Mr Curley, Officer Deakin pointed out that if she constantly saw tax loss letters in a trader's file then an inference could be drawn that there was a problem with the due diligence checks.

192. There were then further Notices of Deregistration and Tax Loss Letters sent to OWD during the relevant periods.

193. We have no doubt that OWD was aware of the risk of VAT fraud in the alcohol industry throughout the VAT periods in issue, including warning signs to look out for, and was later being told by HMRC that OWD's own transactions were connected to fraud.

***Lack of commerciality - in how OWD began and was run, and absence of commercial transaction documents***

194. Mr Watkinson submitted that the purchase of the business from Eastenders was apparently based on Mrs Bachra's optimism that she could succeed where Eastenders had failed, the business of OWD was not run in a commercial manner (eg with no electronic stock control, management accounts or cash ledger) and that the deals were characterised by a lack of complete commercial documentation.

195. Mrs Bachra was appointed as a director of OWD on 3 June 2013. OWD then acquired the business from Eastenders, the specific date of which is not known but in any event took place by October 2013 (as OWD then registered its own principal place of business at Rabone Lane, which had been the premises previously used by Eastenders).

196. That business transfer was documented simply by an invoice for the stock; and we find that there was no independent stock take (despite Mrs Bachra's statements to the contrary to HMRC during some of the visits), no clear explanation as to the financing of the purchase, and Mrs Bachra was initially not forthcoming in disclosing the connection (through her brother) with Eastenders.

197. Conflicting and vague information was given to HMRC by OWD and CBS Associates about the purchase price for the stock and as to the source of funding:

(1) On 23 October 2013 Mrs Bachra said that the price was £180,00 to £200,000. She also said that a stock take was done independently. The money had been paid as and when; later saying £100,000 had been financed from the sale of a house.

(2) When HMRC visited the accountants on 13 November 2013, Mr Kabra said that stock at the start was valued at the invoice cost from Eastenders to OWD, established as £159,841. No physical stock check had been carried out.

(3) On 5 August 2015 Mrs Bachra told HMRC that OWD had bought the stock for between £100,000 and £200,000, with her personal money. This had been paid to Eastenders, by bank transfer. In that visit, it was also said that OWD owes £350,000 to Mrs Bachra. She had invested £120,000 to £125,000 from the sale of a property and borrowed £240,000 by re-mortgaging another property she owned.

(4) In her second witness statement dated 29 November 2019 Mrs Bachra set out that she took a loan when she purchased the business. The transaction in June 2015 was for approximately £240,000, and she put in the sum of £95,000 from her personal account.

198. We find this lack of clarity troubling; this is information which Mrs Bachra should have known. She controlled OWD, and had provided at least some of the money herself. Mrs Bachra explained in evidence, responding to a challenge that it was not commercially normal not to have an independent stock take, that she was dealing with her brother. That is a fair response – but it is an explanation she gives now, not one that she gave to the officers when they were asking about documentation.

199. There were three other cash and carries within one mile of OWD, including one next door. We infer that it was a competitive market, but Mrs Bachra said this helped bring people in. When asked how she thought that she could succeed with OWD when Eastenders had closed down, Mrs Bachra's evidence was that she thought she could make a go of it, she wanted to get good suppliers, and open accounts with those nearer the manufacturers. The premises were in a good location, and there were lots of potential customers in the area.

200. Mr Watkinson submitted that OWD was not run in a commercial manner; whereas Mrs Bachra said she was running the business, trying to get help, and engaged Mr Street to seek to get better access to suppliers closer to the manufacturers.

201. We find that:

(1) there was no electronic stock control, and stock takes were not done regularly. Instead, goods were ordered once relevant sections of shelves were empty;

(2) there was no cash ledger. A high percentage of sales (85-90%) were in cash and large amounts of cash were kept to pay suppliers, in circumstances where Mrs Bachra did not know whether such cash was covered by OWD's insurance;

(3) transactions were missing from the VAT ledgers. This had been raised by HMRC on various occasions (and had resulted in HMRC issuing assessments for transactions) and whilst Mrs Bachra's position was that there were no missing transactions but instead these were cancelled transactions on the tills, there was no evidence of processes having been changed to seek to avoid this (albeit that the number of such transactions did reduce);

(4) there were no management accounts or cash flow forecasts. Mrs Bachra was not able to provide a convincing explanation of how she managed cash flow, referring only to her own sheets (which were not produced to HMRC or in evidence) showing what was coming in each day;

(5) Mrs Bachra didn't know current duty rates; and

(6) Mrs Bachra gave contradictory information to HMRC as to whether the price lists were inclusive or exclusive of VAT, a confusion which is difficult to understand given that these were OWD's own price lists, her evidence was that she was in control and this (unlike the duty rates) is very basic information which we would expect her to have known.

202. There were two themes in relation to the transactions with suppliers which are of potential concern:

(1) Provision of credit - Mrs Bachra sought to obtain goods on credit wherever possible. Such an approach is not notable on its own; the difficulty is that OWD, a relatively new business where there was no evidence before us of its creditworthiness, was given credit, for tens of thousands of pounds (and occasionally for over £100,000) by suppliers which (according to the due diligence information, which OWD had) had minimal means of their own. OWD was given large credit by, eg Wentworth (£95,000), TJ Drinks (£150,000) and Thames Wines (£260,000); and

(2) Delivery to OWD by supplier's supplier – In the context of seeking trade references, DDE routinely makes the point that there is a commercial difficulty (if not impossibility) of obtaining information in relation to the identity of the suppliers to a trader's own supplier, on the grounds that parties are not going to disclose such information voluntarily as they, the middleman, would then be at risk of being cut out from the transaction chain. Yet Gempost, a direct supplier to OWD, did not have its own warehouse, and goods were delivered to OWD by Gempost's suppliers; such suppliers would, on this logic, have been in a position to cut Gempost out of the chain and negotiate directly with OWD. This did not happen. Mrs Bachra explained that Gempost had been in the industry for a long time and was a very strong supplier, with lots of connections, and she didn't think anyone would want to go behind their back.

203. In terms of the transaction documents, Mr Watkinson drew attention to:

(1) many of the invoices from suppliers contained a retention of title clause, ie OWD was receiving these goods on credit, selling them in the warehouse at a time when they didn't own them - effectively ignoring the terms on which they were purchased;

(2) there were contradictions between OWD and certain suppliers as to whether credit was provided; and

(3) some documents were missing from deal packs, eg purchase orders, remittances, invoices, delivery notes.

204. Mrs Bachra's evidence was that there would always be a purchase order, a delivery note (sometimes this might have been marked on the invoice) and remittance records as well as an invoice. This way she would know what had been delivered; and it would be obvious whether or not payment had been made. Mrs Bachra said that all supplies (ie including those from suppliers which have not been challenged such as Millennium) were deal with in the same way.

205. It is quite clear that there was incomplete documentation for many of the deals, eg:

(1) ALT Supplies - no purchase orders were provided. Mrs Bachra said that there would have been a purchase order, either faxed or emailed, or sometimes drawn up in the presence of the supplier and he would have taken it with him;

(2) Gujarr - there was an invoice from Gujarr to OWD for Deal 72, but no delivery note, remittance note, or purchase order. For other Gujarr deals, there were some purchase orders;

(3) Destined - for Deal 87 there was only an invoice;

(4) Allan Desmond - for Deal 97, there was an invoice, delivery note and payment acknowledgement, but no purchase order. The deal packs show that Allan Desmond claimed to retain title until payment had been made in full; and

(5) Wentworth - there were very few purchase orders. For Deal 111, the invoice was annotated with ticks and notes recording dates and amounts of three payments made by "TT" to a Barclays account, with a delivery note, and some payment confirmations (although the first stated that the payment had been delayed by the bank and was scheduled for a later date, rather than that it had been made). Wentworth claimed to retain title until payment had been made in full, and credit was provided.

206. We do not accept that there would always have been complete documentation for each deal - the documentation provided contradicts this, and this cannot be explained by reference to OWD's subsequent liquidation as this is information that was being requested by HMRC whilst the company was trading. We also find that OWD paid minimal, if any, attention to the

details of these documents – no thought was given to the retention of title clause in situations where goods were sold to OWD on credit, and some of the documents kept as evidence of remittance simply showed that a payment transfer had been requested by OWD, not that it had subsequently been made.

207. However, we note that:

(1) HMRC did not challenge the fact that the goods were actually supplied to OWD and then sold in the cash and carry; some of the matters on which HMRC seeks to rely would be of greater significance if the VAT fraud was alleged to involve the carousel of goods, or non-existent goods. That was not the case here; and

(2) whilst Officer Jones had referred to Officer Deakin's conclusions in relation to well-established suppliers such as Millennium and that there was a "full audit trail" of transactions, which was said to include delivery notes, bank payments, order forms and annotations to show receipt of the goods, we had no documentary evidence of those deal packs and Officer Jones confirmed that she had not reviewed them herself. Mrs Bachra's evidence was that OWD dealt with everyone in the same way. We could not test this by reference to any documentary evidence in relation to OWD's transactions with other (non-challenged) suppliers.

208. There was no documentary evidence of any negotiation of price, or discussions with suppliers in relation to availability of requested stock.

***Delays in providing information to HMRC***

209. Mr Watkinson submitted that OWD had repeatedly failed to provide full information to HMRC when requested, this occurred throughout the VAT periods in issue, and the fact that the visit reports reveal that there was antagonism or conflict between Mr Curley and the HMRC officers does not exculpate Mrs Bachra. This submission was particularly relevant to HMRC's submissions on actual knowledge.

210. HMRC's first substantive visit to OWD during the periods in issue was on 27 March 2014. Some information was requested and we have no evidence that this was not provided promptly.

211. HMRC did issue several Schedule 36 notices to OWD in order to obtain books and records. The first was issued on 15 July 2015; however, on the facts that notice does not support a conclusion that OWD had failed to provide information when requested to HMRC:

(1) HMRC's letter of 26 June 2015, arranging a visit for 21 July 2015, enclosed a list of records HMRC would need to see (and they related to the time from start of the business to the end of the most recent VAT return period). That letter also said that HMRC would need to have the computerised records at least two weeks before the visit.

(2) HMRC then issued the information notice requiring production of the records on 15 July 2016. That does not fit, as the request to see records which had been made in June was for those records to be available for the visit, which was being arranged for 21 July 2015, ie the week after the information notice. It cannot be said that OWD was "late" providing these records at this time.

212. The meeting did not take place until 5 August 2015. The records which had been requested (by the letter in June 2015) had not all been provided at that meeting. HMRC were still chasing for the deal log on 14 September 2015.

213. However, the visit reports from 6 October 2015 and 2 February 2016 record several instances where HMRC were requesting information (whether ledgers or due diligence records) in respect of new suppliers or recent transactions and Mr Curley challenged HMRC's

entitlement to request such records, or refused to commit to timely production of the records (on one occasion saying they would be provided when they got around to it). He was OWD's agent, and although the reports do support a conclusion that Mrs Bachra had sought to smooth some matters over, the reality is that there were still significant delays in producing documents requested by HMRC. Schedule 36 notices were issued on 15 March 2016 and 12 April 2016 for purchase and sales invoices, due diligence packs and ledgers, and further notices were issued on 20 June 2016, 30 August 2016 and 6 December 2016.

214. One striking aspect of the visit reports is the interim report from Officer Tilt, the data handling specialist, on 5 August 2015, where during his first visit to OWD he concluded that OWD had deliberately tried to disguise the location of the server used for the tills. The location of this server became an issue in subsequent visits as well (including in October 2015 and February 2016). The striking aspect is the apparent speed with which Officer Tilt reached such a strident conclusion during that one meeting. On the basis of the facts before us, we are not satisfied that OWD had tried to disguise the location of the server - Mrs Bachra gave permission for Officer Tilt to contact STL to ask about the server, and we conclude that Mrs Bachra did not know where it was or how the system operated at that time.

215. The visit reports also indicate that HMRC were concerned about the failure to provide information relating to "missing transactions":

(1) At the visit on 6 October 2015, it was noted that Officer Tilt had not been given access to the information in respect of the computerised till system, STL, ahead of the meeting. Officer Deakin explained that she had looked at the sales listing in the records and had found missing transactions which may be cancelations or voids; Officer Tilt asked for the back-up of the STL system which should show the reason for the missing invoices.

(2) At the visit on 2 February 2016, it was clear that Officer Deakin had still not received access to the STL information, and there was no information as to the missing sales from the records.

(3) On 12 February 2016 HMRC gave notice of assessments, with total VAT due of £319,653, for what HMRC said were missing sales transactions and related missing output tax not declared for the periods 09/13 to 06/15. The schedule lists more than 6,000 missing sales transactions and a number of missing credit notes.

216. Mrs Bachra denied that there were off-record stock sales. Her explanation was that the tills were being used to get a value for an item, or do a stock check; and that these void/cancelled transactions don't generate an invoice. This comes up as a line in the records. There was nothing, she said, to show – nothing more could be printed off. This was explained by Mrs Bachra in the visit on 4 November 2016 (and confirmed in evidence).

217. We find that there were significant delays in providing the information which had been requested to HMRC, in circumstances where the information should have been readily to hand; this included delays in providing the due diligence which had been conducted on particular suppliers, and transaction records for stated periods. We were not satisfied that OWD concealed the location of the server for the tills.

***Due diligence***

218. Mr Watkinson submitted that OWD was repeatedly advised of the need to carry out due diligence and that OWD's due diligence was inadequate. In his submission, OWD's due diligence was nothing more than window dressing, an exercise in collecting paper to show to HMRC, eg some due diligence was only obtained after OWD had started to trade with the relevant company and therefore can have had no impact on the decision to trade with it. There

were obvious indicia that OWD's suppliers were not commercially credible, and posed a serious risk of fraud, that OWD could, and should, have ascertained. Mr Watkinson submitted that no serious thought can have been given to the legitimacy of OWD's suppliers.

219. We have set out in detail in the Findings of Fact (at [106] to [137]) the due diligence which was conducted by OWD in relation to its suppliers.

220. Mrs Bachra's evidence was "risk was always considered" when dealing with new suppliers, she relied heavily on her accountant and Mr Curley (which we take to mean the reports commissioned from DDE) but acknowledged that "passing" the due diligence (referring to the DDE reports) went a long way towards helping her make up her mind.

221. We have carefully considered the contents of all of the due diligence information which was actually obtained by OWD in respect of its suppliers. There were a multitude of warning signs that should have merited further enquiries, or a decision not to trade, and these are apparent on even a quick review.

222. By way of examples:

(1) ALT - The due diligence did no more than confirm the existence of the company (which had only been incorporated three months before the first deal with OWD) and its VAT registration (which stated its business activity as wholesaling motor vehicles). The only dated VAT check was conducted on 17 March 2014 - OWD had traded with ALT on 34 occasions by then. The business was being run from the director's residential address in Colchester at the time of its first transactions with OWD.

(2) Bestbuys - The company was in CVA, and was not given credit by its own supplier.

(3) Destined Trading - This company was incorporated on 10 April 2014, its VAT certificate was dated 10 June 2014 and its first transaction with OWD was on 1 July 2014. The director whose identity was verified (we infer by CBS Associates) was Aaron Taylor (albeit that he had not been appointed as director until August 2014) - Mr Taylor had been the director of ALT, in respect of which OWD had been sent a Notice of Deregistration on 18 June 2014.

(4) Gujarr - The business had recently moved and had signed a lease for its new premises just a few days before the date of the report (which was after the first supplies), the utility bill provided by way of verification was a final demand for £676, particularly noteworthy as the cover letter from DDE had drawn attention to the fact that no financial assessment was provided (as references were awaited) and so this was one of the only pieces of data relevant to creditworthiness. The photos include a photo of a warehouse at unit 10, but the form of lease (which had been provided separately by Gujarr on 19 August and was included within the DDE report) shows that they were leasing unit 11. The director was the only employee; he lived in Hounslow but the warehouse was in Bolton.

(5) Master Resources - In twelve days, between 16 June and 28 June 2015, this company made supplies to OWD totalling £430,000, on credit. There was no due diligence until 23 June 2015, and the due diligence pack supplied on that date included a VAT certificate dated 1 June 2015 (albeit with an effective date of 13 May 2014), with a business activity of management consultancy.

(6) Simon Lloyd – OWD was buying from this company in 2015, and it had changed its name from Simon Local Builders Ltd in June 2014.

(7) TJ Drinks – The company had only been registered for VAT for one month before the first deal with OWD and was late filing its annual return. It had rented premises for

the storage of soft drinks (rather than alcohol), and at the time of the site visit by DDE it was based from the director's home. One of the attachments to the DDE report is a confirmation of submission of notice of change of name, but this information is not included in the body of the report to explain the difference in names used in the supporting documentation.

223. Mrs Bachra said that she had noticed the change of name of Simon Lloyd (although she had not queried it); this was one of the only examples of her evidence being that she had even noticed something at the time the information was provided (as when she was taken to what HMRC said were warning signs in the documentation in relation to other suppliers her position was generally that she had done the due diligence, and she could see now, ie in preparing for or at the hearing, that there were warning signs).

224. There were several occasions where OWD had started trading with a new supplier before any substantive due diligence had been conducted:

(1) Bestbuys - the supplies were made from 23 January to 5 March 2013; the only due diligence was the DDE report, dated 11 March 2015.

(2) Gempost - the DDE report was sent to OWD on 10 February 2016, by which time there had been seven supplies to OWD, the first of which was invoiced on 14 January 2016.

(3) Gujarr - the first invoice is dated 15 August 2014, and a pack of basic due diligence was sent to OWD by Gujarr on 19 August 2014. This is just a few days after the first transaction but means that OWD had traded with a new supplier in two transactions without having any due diligence, and those transactions had a value of over £100,000. The DDE report was not sent to OWD until 27 August 2014.

(4) Master Resources - a due diligence pack was sent to OWD on 23 June 2015, after the first five transactions. The DDE report was also sent to OWD on that same date.

(5) SDDL - the first deal was on 24 April 2015, yet the DDE report was not sent to OWD until 2 September 2015.

(6) SS Traders - the first transaction with OWD was on 30 March 2015, but the DDE report was not provided to OWD until 28 April 2015, after the first five deals.

(7) TJ Wickham - the DDE report was not sent to OWD until after they had ceased trading with them.

225. We have already described the format of the DDE reports. They give the appearance of being substantive documents. They state that the relevant business has passed the vetting procedures on the cover page. We have referred to some of the specific contents of the reports in our Findings of Fact. We add the following:

(1) Later reports (eg Gempost in February 2016, Chameleon Trading in March 2016) include a section on FITTED, the due diligence condition (which was not applicable to OWD at that time) which requires businesses to take a risk-based approach to due diligence checks and makes all checks bespoke to the trading relationship. The narrative in that section of the DDE report largely uses information already set out elsewhere to populate the headings. Yet the section on FITTED also raises questions, eg for Chameleon Trading:

(a) The report says the company has now been trading for over seven years and has built a reserve of working capital – yet it is apparent from a print-out from Companies House that the company was incorporated on 24 February 2014, and

the VAT certificate shows it was registered for VAT with effect from 1 April 2014. This does not sit with the company having been trading for seven years by 2016.

(b) The company's landlord was contacted and confirmed that the business pays their bills on time therefore demonstrating credit worthiness – the invoice from the landlord for the office shows rent for March 2016 of £325. If this was the landlord in question, this amount can hardly provide reassurance given the size of supplies being made. If it was a landlord for the warehouse, there is no evidence of that reference, or the amount of rent.

(2) There are also various oddities in relation to the dates of the DDE reports:

(a) Allan Desmond - OWD was sent reports on 17 October 2014 and 20 January 2015. The first contains a reference that is dated 1 December 2014, and the photos of the warehouse are different in the two reports (with no mention of a second site visit having been made - which would have been an obvious explanation for the differences). Mrs Bachra confirmed that she had not noticed that the photos were different.

(b) SDWL - the DDE report was provided to OWD on 31 July 2015 (which was before OWD first traded with SDWL), yet that report states that DDE had verified the registration under the Money Laundering Regulations on 5 August 2015.

(c) SS Traders - the DDE report was sent to OWD on 28 April 2015, and that report as printed includes an account statement from Regus dated 25 May 2015.

(d) TJ Drinks - the DDE report was sent to OWD on 3 August 2015, but the declaration signed by the director is dated 29 August 2015.

(3) We did not have any examples of businesses not having passed DDE's vetting procedures. We did not have the benefit of any evidence from DDE and have no evidence as to what facts would result in a business not passing. We infer that a failure to verify the existence of the company (eg absence of evidence of incorporation), or inability to verify a VAT number, would result in the business not passing vetting procedures, but do not know the extent to which matters we have flagged as warning signs could become the basis for failing vetting.

226. Mrs Bachra was warned by HMRC not only of the importance of conducting due diligence on suppliers, but on the need to consider its contents. The notices which she was given drew attention to the warning signs. At the visit of 2 February 2016, having discussed due diligence in relation to various new suppliers (including Just Beer and Gempost), Officer Deakin was clear throughout that her view was that the due diligence didn't go far enough, and reiterated that there was not sufficient due diligence currently. Officer Cawley's subsequent letter in April 2016 set out various specific concerns in relation to particular suppliers.

227. Instead, the documentary evidence, which Mrs Bachra had at the time of entering into many of the supplies (albeit not always before the first few supplies with a new supplier), shows that the suppliers with whom OWD was dealing bore some of the characteristics about which HMRC were warning, or which should have raised concern:

(1) Several suppliers had initial registrations for VAT in business activities that had nothing to do with alcohol wholesaling, eg, ALT- tyre wholesaling, Destined Trading - sales consultancy, Chameleon Trading - retail sale of beverages, Allan Desmond - medical reports, Wentworth - soft drinks wholesaler, Simon Lloyd - builder, Master Resources - management consultancy, and SS Traders - other food service activities;

(2) Directors who appeared to have no experience in the wholesale alcohol trade - Aaron Taylor of ALT, Mohammed Asif of Allan Desmond, Qasim Gujar of Gujarr, and Awara Hawez of Simon Lloyd;

(3) Newly incorporated or VAT-registered companies - SDDL was incorporated on 7 January 2015 and its first deal with OWD was on 24 April 2015, TJ Wickham was incorporated in January 2016 and traded with OWD the following month, TJ Drinks was registered for VAT with effect from 1 July 2015 and started trading with OWD on 16 August 2015;

(4) Traders were based at residential premises or serviced office addresses with no storage facilities - eg ALT (which did not store goods at a warehouse), SS Traders operated from a serviced office of Regus and TJ Drinks was operating from the director's residential address;

(5) Traders providing goods on credit with minimal creditworthiness themselves -

(a) Bestbuys was in CVA, was not given credit by its own suppliers (understandable given its previous insolvency) and yet provided goods on credit to OWD;

(b) Gempost - the section on FITTED says that Gempost has said it is not extending credit to OWD; yet Mrs Bachra said they did. The first four deals were invoiced from 14 January to 2 February 2016, at which point Gempost had given OWD credit of £104,000;

(c) SDWL - the DDE report stated that they could not provide a financial assessment, and DDE later reported that they had not been able to obtain references. There was no evidence as to the financial position of the company; whilst Mrs Bachra said that the accountant did credit checks, there was no CreditSafe report;

(d) Just Beer - OWD was given credit of £83,000 in the first four transactions (in January 2016), at a time before OWD had received the DDE report;

(e) Thames Wines - Credit reports in the various DDE reports showed this company had a £500 credit limit; yet Deal 362, on the same date as one of the reports, was for a value of £72,000, and OWD was given credit for that supply;

(f) TJ Drinks was a new business, yet in Deals 200-203 in August 2015 OWD were supplied goods of £150,000 on 30-day credit; and

(g) Wentworth - Wentworth gave credit of £95,000 to OWD at a time when OWD had no financial information to explain how they were able to do this.

228. Additional factors relied upon by HMRC in this context included:

(1) directors who have been disqualified for lengthy periods;

(2) traders with sudden and commercially inexplicable increases in turnover;

(3) traders going missing from their premises;

(4) traders refusing to produce their records, failing to comply with Schedule 36 information notices, failing to meet with HMRC when asked to and lying to HMRC about their trade;

(5) traders failing to carry out due diligence despite notification of tax losses; and

(6) traders being subject to excise duty assessments.

229. The hearing bundles include witness statements (and supporting exhibits) from HMRC officers in relation to each of the fraudulent defaulters and some of the buffer traders which set out the evidence in support of these and other contentions, eg:

(1) N&R - N&R had had two previous directors since its incorporation on 18 February 2015, each of whom was a director of previously failed companies;

(2) Thames Wines - this business had a seizure of admittedly diverted alcohol from outside its warehouse, and a seizure of stock and cash prior to OWD trading with it; and

(3) TJ Wickham - when HMRC visited TJ Wickham on 17 February 2016, Mr Wickham said there were two suppliers for their wholesale business, Yewhall Ltd and Neat Trading Ltd. Mr Wickham said Neat were recommended to him by OWD, a customer of his. Mr Wickham did not specify a name for whom at OWD. Mrs Bachra said she never came across Neat herself.

230. We would expect that the facts in relation to N&R could have been discovered by OWD (or by DDE on its behalf) with further investigation. However, there were some matters, eg the seizures, which could not reasonably have been expected to have been discovered by OWD. We place no weight on such matters when assessing OWD's knowledge or what it should have known.

*Conclusions on due diligence*

231. We have carefully considered the evidence in relation to the due diligence conducted by OWD:

(1) The due diligence was littered with warning signs, both viewed in isolation and when looking at the similarities between the types of suppliers being used. There were various examples where Mrs Bachra accepted when giving evidence that the due diligence was not good enough, or that there were warning signs in the documents. She had these documents at the time, and should have realised this then.

(2) There was no evidence of any critical thought having been given as to whether or not to trade with a particular supplier. Mrs Bachra did not consider how these suppliers, many of them newly established, with inexperienced directors and minimal apparent resources of their own, could provide credit to OWD, or obtain a better price from their own suppliers than OWD could obtain elsewhere.

(3) These failures could be explained either by Mrs Bachra having simply failed to read the paperwork provided (in particular the content of the DDE reports) or having taken a decision that the content was irrelevant (once they had "passed" vetting) and she would trade with them anyway.

(4) Her evidence was that the DDE reports went a long way to helping her make up her mind to trade with a supplier – we find that once DDE said a business had passed the vetting procedures, this was sufficient. Mrs Bachra paid no attention to what DDE might have meant by "passing" vetting; and was content to trade with new suppliers even if no substantive due diligence had yet been received.

232. The above addresses the evidence which is available in respect of the suppliers which are involved in the transactions with which this appeal is concerned. There are matters on which we did not have evidence:

(1) Mrs Bachra said she had rejected suppliers; but her evidence in this regard was vague. There was no detail either as to the identity of these suppliers or the reasons for rejection. In the context of setting out an example of what she understood to be a red

flag transaction to be avoided, she referred to suppliers turning up with goods in the back of a van. We infer that these are the suppliers she was rejecting.

(2) We have referred in the context of considering the commerciality of OWD's business to the lack of information in relation to OWD's transactions with non-challenged suppliers. That is also apparent here. We do not have any evidence as to the due diligence which was conducted by OWD on such suppliers – not only do we not therefore have a comparator as to the level of due diligence, but we are not able to assess the extent to which reports such as those compiled by DDE on those suppliers would also, on their face, contain potential warning signs.

***Credibility of Mrs Bachra***

233. HMRC challenged Mrs Bachra's credibility, both as a witness and as to whether she had been the person in control of OWD, drawing attention to what they submitted was the possible role of Mrs Bachra's family members. Mr Watkinson's submissions included that the vagueness and contradictions of Mrs Bachra's evidence supported an inference that she knew of the connection with fraud. HMRC's Statement of Case had expressly referred to the previous involvement of Mrs Bachra's family in excise duty fraud, and this was also relied upon in Mr Watkinson's written submissions.

234. We have addressed Mrs Bachra's evidence at [41] to [42] above, concluding that her evidence was not helpful, but not reaching a conclusion that it was untruthful.

235. As regards Mrs Bachra's family:

(1) The directors of the Eastenders companies included Kulwant Hare, Mrs Bachra's brother. Mr Hare and two of his brothers were convicted of conspiracy to cheat the revenue by alcohol diversion fraud in 1995 and imprisoned.

(2) Mrs Bachra's husband, Rajinderpal Singh Bachra, was a director of two companies (Sunshine Goods Ltd and Sunshine Leicester Ltd) both of which were compulsorily de-registered for VAT and owed more than £1.3 million to HMRC. The Sunshine companies traded in fraudulent supply chains. Mr Bachra was convicted of the fraudulent evasion of duty in 1997 and imprisoned. Mr Bachra had also worked for Eastenders.

236. The accuracy of this information was not challenged by Mr Bedenham; he did challenge its relevance, submitting that HMRC had pursued Mrs Bachra because of these family relationships.

237. Mrs Bacha's position has been throughout that she was running the business of OWD - she made all the decisions about which goods are purchased and at what price. She has said that her husband and her children sometimes helped at the cash and carry.

238. It is apparent from HMRC's visit reports that HMRC had concerns about OWD because of Mrs Bachra's family relationships, and were questioning whether Mrs Bachra had control of OWD or whether it was being run by others (particularly her husband). This can be seen from:

(1) The Conclusion/Credibility section of the visit report from 23 October 2013, which records that either Mrs Bachra never got over her nervousness from the unannounced visit, or she in fact knows little about the business. Getting answers was like "drawing teeth". "I am concerned that in fact Mrs Bachra is in fact "a front" and in reality others control what goes on but I have no evidence to substantiate this."

(2) Officer Deakin refers in the report of 5 August 2015 to recognising Mr Bachra who was present at OWD that day and "clearly working". There are several references in that report to Mrs Bachra not knowing details of her business - eg when first asked about the

split between alcohol and zero rated goods; knowledge about what to sell goods for; current duty rates. The Conclusion/Credibility section of the report identifies HMRC's concern as to who is the guiding mind behind the running of the company.

(3) At the visit on 2 February 2016 Officer Deakin questioned why Mrs Bachra did not know who she was renting the premises from. Officer Deakin said to Mrs Bachra that she appeared not to be running the cash and carry and asked if someone else was running it. Mrs Bachra said no - Officer Deakin found this surprising as in the three interviews she had had, Mrs Bachra seemed vague, could not remember things and always looked to the agent when being asked questions.

239. On the basis of the evidence, we find as follows:

(1) OWD bought the business from Eastenders, which was part-owned by her brother. The family relationship likely influenced the lack of commercial documentation and the absence of an independent stock take.

(2) Mrs Bachra had not readily volunteered this information to HMRC - at the visit of 23 October 2013, Mrs Bachra said only that she had bought the business from Eastenders, she had been an employee there, and there was no association with Eastenders. She did confirm her brother's involvement with Eastenders in the meeting in August 2015.

(3) There was no evidence of any involvement of Mrs Bachra's brothers in OWD after that acquisition.

(4) Mr Bachra was sometimes present at OWD, and Mrs Bachra's evidence in her witness statement was that there were occasions that he dealt directly with traders.

(5) Whilst Mrs Bachra's evidence was vague (and this cannot be explained by reference only to the passage of time, or her lack of access to the original books and records, as her explanations to HMRC during the visits was often vague, and sometimes contradictory), we are not satisfied that this means that someone else, ie Mr Bachra, was in fact running the business.

**Conclusions on knew or should have known**

240. There are 332 Deals in issue before us. In some the fraudulent defaulter was a direct supplier to OWD (eg ALT, Destined, TJ Drinks), in others indirect (eg Gujarr, SS Traders, Wentworth). We are mindful throughout that HMRC need to establish that, on the balance of probabilities, OWD knew or should have known that its transactions were connected to fraudulent tax losses, in accordance with the guidance set out in the authorities; and that this needs to be satisfied in respect of each denial of input tax credit.

241. Taking account of all of the evidence before us, we have no doubt that OWD should have known that all of the transactions which are the subject of this appeal were connected with the fraudulent evasion of VAT.

242. We rely in particular on:

(1) Mrs Bachra's knowledge of the risk of VAT fraud in the alcohol industry throughout the VAT periods in issue.

(2) Despite being aware of the warning signs to look out for, and later being told that some of OWD's own transactions were connected to fraud, OWD:

(a) failed to ensure that full due diligence was conducted before starting to trade with some new suppliers,

(b) did not recognise that the due diligence which was conducted included various of the warning signs which had been pointed out by HMRC, and

(c) did not give critical thought to this information, eg, how the suppliers could provide significant amounts of credit to OWD, or obtain a better price than OWD could obtain elsewhere.

(3) This is exacerbated in later periods by the pattern of new suppliers introducing themselves to OWD at its premises in circumstances where those new suppliers seemed on paper to bear some of these same warning signs as those in respect of which OWD were receiving Notices of Deregistration and/or Tax Loss Letters.

243. This conclusion is sufficient to establish that there was an inaccuracy in OWD's VAT returns. Mr Bedenham's submission was that such a conclusion is not sufficient in the context of an appeal against a PLN, as he submitted that this did not constitute deliberate conduct as required by paragraph 19. We have considered those submissions below in relation to the requirements of paragraph 19 and at this stage address whether HMRC have established, on the balance of probabilities, that OWD knew that its transactions were connected with the fraudulent evasion of VAT.

244. We note at the outset that HMRC relied on the same factors for establishing both alternative limbs of the *Kittel* principle, ie their own case recognised that the factors they were relying upon to establish knowledge of OWD, even if established, could be explained by a conclusion that OWD should have known of the connection.

245. Some of the facts as we have found them do provide some support for the conclusion that OWD, through Mrs Bachra, knew of the connection to the fraudulent evasion of VAT:

(1) the number of transactions which were connected to the fraudulent evasion of VAT, and the proportion of input tax claimed by OWD to which they relate;

(2) the simplicity of the deal chains, which meant that in many instances OWD were dealing directly with the fraudulent defaulter, or the indirect connection involved just one buffer (which is more significant for the transactions with Gempost as the fraudulent defaulter, ie Gempost's supplier, was delivering the goods to OWD);

(3) the pattern of replacement of defaulting traders with those with similar characteristics – which, when taken together with [(1)] and [(2)] above, are part of what HMRC were relying upon as indicative of orchestration;

(4) the contradictory answers Mrs Bachra gave to HMRC during visits on matters which she would (irrespective of her experience or otherwise of owning a business) be expected to be able to answer, in particular in relation to the acquisition of the business from Eastenders, eg whether there was an independent stock take and the purchase price;

(5) the significant delays in providing information which had been requested to HMRC, in circumstances where the information should have been readily to hand; and

(6) failing to ensure that full due diligence had been conducted before commencing trading and then failing to pay detailed attention to the contents of the DDE reports, and to consider whether they were credible suppliers.

246. Notwithstanding the range of the matters identified above, we nevertheless considered that the question of whether OWD knew of the connection to the fraudulent evasion of VAT to be finely balanced. We considered all of the evidence to which we were taken, and sought to consider the transactions undertaken by OWD in the light of all the evidence available to us

and concluded that there were two particular difficulties when seeking to assess whether HMRC have met their burden of proof:

(1) Whilst we found Mrs Bachra's evidence to be vague and not helpful, we were not persuaded that she was untruthful.

(2) We had minimal evidence in relation to the transactions undertaken by OWD that were not the subject of a denial of input tax credit. We do not refer here to the 43 withdrawn deals, but instead to the transactions with other suppliers, eg Corbelli Wines. We were not overly troubled by the absence of deal packs in respect of these transactions (which it appears were at the very least seen by HMRC during its monitoring of OWD as Officer Deakin had found there was what she termed a full audit trail for these transactions), although evidence as to how OWD had started to trade with them would potentially have been relevant. We have made lengthy findings of fact in relation to the due diligence actually conducted by OWD on the suppliers in the transactions which are the subject of this appeal, emphasising the warning signs which are revealed and yet were not noticed by OWD and thus were not taken into account when deciding whether or not to trade. In contrast, we had no documentary evidence in relation to the due diligence which was conducted on these other suppliers – we would have found it helpful to see what could be seen or inferred from, eg, their VAT certificates, site visits and discussions with their directors.

247. Mr Watkinson acknowledged that the evidence on which HMRC relied was circumstantial; there were no smoking guns. That is not surprising, but of itself it does not necessarily mean that HMRC will be unable to meet their burden.

248. Viewing all of the evidence before us, and considering the absence of evidence in relation to non-challenged suppliers, we were ultimately not satisfied that HMRC have established, on the balance of probabilities, that OWD knew of the connection to the fraudulent evasion of VAT.

**DISCUSSION – WHETHER CONDITIONS FOR ISSUE OF PLN SATISFIED**

249. Paragraph 19 provides for HMRC to issue a penalty to an officer of a company by which certain penalties are payable. Paragraph 19(1) provides:

> "19(1) Where a penalty under paragraph 1 is payable by a company for a deliberate inaccuracy which was attributable to an officer of the company, the officer is liable to pay such portion of the penalty (which may be 100%) as HMRC may specify by written notice to the officer."

250. HMRC issued an inaccuracy penalty on 2 November 2017 to OWD. The penalty amount was £1,177,422.96 for the VAT periods 03/14 to 12/16, and this was imposed on the basis that the behaviour was deliberate. The PLN was issued to Mrs Bachra on 15 December 2017 for the whole of that amount.

251. HMRC bear the burden of proving that the inaccuracies in OWD's returns were deliberate, that the deliberate inaccuracies were attributable to Mrs Bachra and that the penalty is correctly calculated. We take these issues in turn.

**Whether inaccuracies were deliberate**

252. Mr Watkinson submitted that if we were satisfied that OWD's returns were inaccurate, the inaccuracies should be found to be deliberate irrespective of which limb of the *Kittel* test we find is satisfied.

253. Mr Bedenham accepted that if we found that OWD knew that the transactions were connected with the fraudulent evasion of VAT then this would constitute a deliberate

inaccuracy for this purpose. Mr Bedenham submitted that a finding that OWD should have known for the purposes of the *Kittel* test is not a finding of actual knowledge or actual intention and cannot constitute deliberate conduct.

254. In the light of our conclusion above, that OWD did not know but should have known of this connection, we need to reach a conclusion on Mr Watkinson's submissions that a finding that OWD should have known of the connection is sufficient to constitute a deliberate inaccuracy for the purposes of paragraph 19.

255. Mr Watkinson's submissions included:

(1) Inaccuracies within paragraph 1 of Schedule 24 can be careless or deliberate, but deliberate encompasses both concealed and non-concealed acts. There could be said to be a sliding scale of types of behaviour.

(2) In *Auxilium Project Management v HMRC* [2016] UKFTT 249 (TC) at [63], the Tribunal provided the following explanation of a deliberate inaccuracy which has been widely followed and approved:

> "a deliberate inaccuracy occurs when a taxpayer knowingly provides HMRC with a document that contains an error with the intention that HMRC should rely upon it as an accurate document".

(3) "Deliberate" also includes adopting a Nelsonian approach where a person has deliberately refrained from making enquiries about, or closed their eyes to, the correct position (eg *Clynes v HMRC* [2016] UKFTT 369 (TC) at [82, 86], *Cannon v HMRC* [2017] UKFTT 859 (TC) at [21]). *Clynes* also concerned the imposition of a PLN under paragraph 19 in respect of inaccuracies in a company's VAT returns, but those inaccuracies related to a failure to declare all cash invoiced by the business and accounting for VAT on the basis that the conditions for the flat rate scheme applied when on the facts the business was ineligible for that scheme (as its turnover exceeded the threshold). At [82] the Tribunal referred to deliberate as meaning that a person must to some extent have acted consciously, and said at [86]:

> "86. However, we consider that the term "deliberate inaccuracy on a person's part" can extend beyond this. Our view is that, depending on the precise circumstances, an inaccuracy may also be held to be deliberate where it is found that the person consciously or intentionally chose not to find out the correct position, in particular, where the circumstances are such that the person knew that he should do so. A person cannot simply escape liability by claiming complete ignorance where the person clearly knew that he should have taken steps to ascertain the position. We view the case where a person makes such a conscious choice not to take such steps with the result that an inaccuracy occurs, as no less of a "deliberate inaccuracy" on that person's part than making the inaccuracy with full knowledge of the inaccuracy."

(4) This encompasses the "only reasonable explanation" test in the second limb of *Kittel*. Approaching the issue by reference to the limbs of *Kittel* was how the Tribunal tackled a similar case in *Bell & Hovers v HMRC* [2017] UKFTT 272 (TC).

(5) The Supreme Court's decision in *HMRC v Tooth* [2021] UKSC 17 (concerning the meaning of "deliberate inaccuracy" in s118 Taxes Management Act 1970) can be read across to the statutory wording in this case and the Supreme Court's approach at [45] - [47] supports that in *Auxilium* above. At [47] the Supreme Court said:

> "[47] It may be convenient to encapsulate this conclusion by stating that, for there to be a deliberate inaccuracy in a document within the meaning of section 118(7) there will have to be demonstrated an intention to mislead the

> Revenue on the part of the taxpayer as to the truth of the relevant statement or, perhaps, (although it need not be decided on this appeal) recklessness as to whether it would do so."

256. We do not agree with Mr Watkinson's submission that an inaccuracy which is based on a finding that OWD should have known of a connection to the fraudulent evasion of VAT constitutes a deliberate inaccuracy. We gratefully adopt the explanation of a deliberate inaccuracy set out in *Auxilium*. As the Tribunal in *Auxilium* went on to explain, the question of whether there is a deliberate inaccuracy is a subjective test; it is not whether a reasonable taxpayer might have made the same error or even whether this taxpayer failed to take all reasonable steps to ensure that the return was accurate. It is a question of the knowledge and intention of the particular taxpayer at the time.

257. Neither *Clynes* nor *Cannon* were concerned with the question whether the "should have known" limb of the *Kittel* test equates to deliberate for the purposes of the legislation on penalties. We do not find them helpful in reaching a conclusion on this point. In *Tooth*, the Supreme Court questioned whether recklessness could constitute deliberate conduct but then said that the issue need not be determined in that appeal. This does not therefore provide us with further guidance on this matter.

258. Instead, we have focused carefully on the entirety of the judgement of Moses LJ in *Mobilx* to remind ourselves of what is captured by the "should have known" limb of the *Kittel* test. Moses LJ set out who is to be treated as participating in the fraud (with the consequence that they would lose their entitlement to input tax), and setting the boundaries around what it is that should have been known to be treated as such a participant. The language used in that context does include reference to choice and intention, eg in [61] the reference to a person who has the means of knowledge available and chooses not to deploy it, or chooses to ignore obvious inferences from the fact and circumstances; and at [64] "If it is established that a trader should have known that by his purchase there was no reasonable explanation for the circumstances in which the transaction was undertaken other than that it was connected with fraud then such a trader was directly and knowingly involved in fraudulent evasion of VAT".

259. However, this language is concerned with the entitlement to input tax, ie whether there was an inaccuracy at all, and describing the persons (who have met the know or should have known threshold) as being directly and knowingly involved in the fraudulent evasion of VAT for that purpose. We do not accept that this reasoning requires us to conclude that the inaccuracy was deliberate.

260. Mr Watkinson submitted that the description by Moses LJ of what is caught by "should have known" goes beyond carelessness. We agree that the description is such that someone who is found to meet this threshold will almost inevitably be found to have been careless; but the ease with which that conclusion can be reached does not mean that they should be treated as having knowingly provided HMRC with a document that contains an error with the intention that HMRC should rely upon it as an accurate document. Our conclusion was that OWD should have known that this was the case; but that is not actual knowledge.

261. We have concluded that the inaccuracy in OWD's returns was not deliberate.

262. That conclusion means that Mrs Bachra's appeal is allowed (as paragraph 19 only allows a penalty to be attributed to an officer of the company where the penalty was payable by the company for a deliberate inaccuracy). As we heard full argument on the remaining issues we address them below.

**Whether deliberate inaccuracies were attributable to Mrs Bachra**

263. Paragraph 19 allows HMRC to issue a PLN where a penalty is payable by a company "for a deliberate inaccuracy which was attributable to an officer of the company".

264. HMRC's position was that Mrs Bachra was the sole director of OWD, her evidence was that she was running the company, meeting suppliers, placing orders, and that no-one else was dictating what she should do, and that therefore any deliberate inaccuracy of OWD was and could only be attributable to her.

265. Mrs Bachra's position was that only if she had actual knowledge that OWD's VAT returns contained an inaccuracy could it be properly said that any deliberate inaccuracy by OWD was attributable to her.

266. If we had concluded that OWD had actual knowledge of the connection with the fraudulent evasion of VAT, that would have constituted a deliberate inaccuracy and we would accept Mr Watkinson's submissions that such inaccuracy must be attributed to Mrs Bachra, as she was responsible for the actions of OWD.

267. If we had concluded that "should have known" was sufficient to constitute a deliberate inaccuracy on the part of OWD, such that paragraph 19 was capable of being satisfied, we would also have decided that the inaccuracy was then attributable to Mrs Bachra for the same reason - there was no-one else, and the failings of OWD, as well as the actions of OWD, could only be attributed to Mrs Bachra.

268. We would, therefore, have concluded that HMRC had satisfied their burden on this issue.

**Calculation of penalties and PLN**

269. HMRC must establish that the PLN was correctly calculated. We address in this context the calculation of the PLN, the withdrawal by HMRC of some of the deals, and what were said to be the subsequent re-calculations of the PLN.

270. We note at the outset that HMRC issued the PLN to Mrs Bachra in December 2017 and there was no evidence or submission that an amended PLN has since been issued to her.

271. The PLN issued by HMRC to Mrs Bachra and which is the subject-matter of this appeal was issued for the amount of £1,177,422.96, this being the amount of the penalty which had been issued to OWD. The PLR figure which formed the basis of that penalty was made up of the £38,415 and the £2,064,130 assessments which had been issued to OWD. The changes to the amount of the PLN which HMRC have sought to have upheld in this appeal are:

(1) in their re-amended Statement of Case dated 1 May 2020 HMRC said the PLN was for the sum of £977,190.32;

(2) HMRC's skeleton argument dated 12 April 2022 was based on the sum of £926,864; and

(3) in the table (set out in the Background Facts) provided to the Tribunal on 3 May 2022, HMRC further adjusted these amounts, resulting in a total of £928,551.20.

272. Mr Bedenham submitted that Mrs Bachra's appeal must be allowed in respect of the difference between the amount of the PLN as initially issued in December 2017 and the amount now claimed as due by HMRC as HMRC have withdrawn their case in respect of that amount. We agree.

273. The changes made by HMRC to what they say is the amount of the PLN are all based on changes to the amount of the PLR - the reduction for disclosure is unchanged (and neither party submitted that any different reduction for quality of disclosure should be substituted). In the

absence of submissions on this matter, we accept and would apply the reduction which has already been applied by HMRC, 40%.

274. With one exception, the amounts (of PLR and correspondingly the PLN) set out in the table provided by HMRC on 3 May 2022 for each VAT period are equal to or less than the amount assessed by way or penalty to OWD and thus in the PLN. The exception is for the period 06/15, where the penalty table accompanying the penalty explanation letter set out PLR of £230,985 and a penalty (to be issued to OWD) of £129,351.60. HMRC now seek a penalty of £131,704 for this period, based on PLR of £235,187, and seek to impose this by way of amendment or re-calculation of the PLN.

275. We did not receive submissions from the parties as to whether HMRC should be able, in the context of seeking a decision to uphold the PLN in a lower amount than that which had been issued to Mrs Bachra, to increase the amount of the penalty and resulting PLN for one of the VAT periods (albeit with decreases elsewhere more than offsetting this increase). On the basis that we have already decided to allow Mrs Bachra's appeal and this question does not need to be determined by us, we considered it was not in accordance with the overriding objective to seek submissions from the parties on this specific question (being mindful that this would result in increased costs for the parties). Our preliminary view, reached without the benefit of any submissions, is that it is not open to HMRC to seek to impose an increased amount by way of penalty (or PLN) for any particular VAT period in circumstances where they have not re-issued the penalty (or PLN) accordingly, as this is not only necessary for the issuance of the penalty of that (higher) amount but also is required as a matter of fairness to enable the taxpayer to know the case they need to answer.

276. We would therefore decide, if we had not allowed the appeal on other grounds, that the PLN should be calculated at the amounts set out in the table at [16], with the exception that the PLN for 06/15 should be reduced to £129,35160.

**DISPOSITION**

277. Mrs Bachra's appeal is allowed.

**RIGHT TO APPLY FOR PERMISSION TO APPEAL**

278. 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.

**JEANETTE ZAMAN**
**TRIBUNAL JUDGE**

**Release date: 30th JANUARY 2023**