Neutral Citation: [2024] UKFTT 00774 (TC)

Case Number: TC09270

FIRST-TIER TRIBUNAL
TAX CHAMBER

Location: Manchester

Appeal reference: TC/2019/09205
TC/2021/00692

VALUE ADDED TAX – assessments made under s73 VATA – whether to best judgment – yes – whether quantum was shown to be excessive – no –- appeal dismissed

PENALTIES – deliberate penalty – whether conduct was deliberate – yes – appeal dismissed

PERSONAL LIABILITY NOTICE – conduct attributed to director – whether his conduct led to penalty – yes – appeal dismissed

Heard on: 5 – 11 July 2024
Judgment date: 20 August 2024

Before

TRIBUNAL JUDGE AMANDA BROWN KC
SUSAN STOTT

Between

(1) ANCIENT & MODERN JEWELLERS LIMITED
(2) ZACHARY COLES

Appellant

and

THE COMMISSIONERS FOR HIS MAJESTY'S REVENUE AND CUSTOMS

Respondents

Representation:

For the Appellant: Mr Leon Kazakos KC of Counsel instructed by JMW Solicitors LLP

For the Respondents: Ms Joanna Vicary and Ms Charlotte Brown of Counsel, instructed by the General Counsel and Solicitor to HM Revenue and Customs

DECISION

INTRODUCTION

1. This is an appeal against three decisions issued by HM Revenue & Customs (**HMRC**):

(1) Assessments issued to Ancient & Modern Jewellers Ltd (**A&M**) pursuant to section 73 Value Added Tax Act 1994 (**VATA**) for the VAT prescribed accounting periods 08/14 to 08/18 (**Assessments**). The Assessments were originally issued on 4 December 2018 in the sum of £5,474,249 but they were reduced on review to the sum of £5,004,595; the reduced Assessments were notified on 9 December 2019. The Assessments were raised on the basis that HMRC considered that the Appellant had incorrectly accounted for VAT under what is known as the second-hand margin scheme for goods as provided for in section 50A VATA and associated secondary and tertiary legislation.

(2) Penalties issued to A&M pursuant to Schedule 24 Finance Act 2007 (**Sch 24 FA07**) (**Penalties**). The sum assessed in respect of the Penalties is £2,802,573.20 representing 56% of the tax considered to have been lost through the deliberate but not concealed conduct of A&M. The Penalties were notified to A&M on 8 January 2020.

(3) A personal liability notice (**PLN**) was issued pursuant to paragraph 19 Sch 24 FA07 to Mr Zachary Coles (**ZC**) pursuant to which ZC has been made personally liable to pay the Penalties. He was so notified on 6 January 2021.

2. In this judgment A&M and ZC together will be referred to as the **Appellants**.

3. A&M has appealed the Assessments and Penalties. In summary the grounds of appeal are:

(1) As regards the Assessments that they have not been raised in exercise of HMRC's best judgment. Whilst accepting that a best judgment challenge is a high bar A&M contend that the conduct and mindset of HMRC's investigating and assessing officer, Mr Riyaz Patel (**RP**), was so unreasonable that it vitiates the whole assessment. This is despite accepting that in the periods assessed A&M had incorrectly accounted for VAT and that thereby under declarations arose. In the alternative, the Appellant contends that the Assessments are overstated and should be reduced; in this regard (but subject to their best judgment challenge) A&M accepts that there were inaccuracies in the VAT returns because the margin scheme was used to account for VAT on watches purchased by way of intracommunity supply and imports to which the margin scheme is inapplicable.

(2) As regards the Penalties A&M contends that to the extent that amounts are assessable, the errors were not deliberate errors, at best they are innocent mistakes and at worst they are careless.

4. On the basis that it is contended that the errors giving rise to the Penalties were not deliberate ZC contends that the conditions for paragraph 19 Sch 24 FA07 are not met, and the PLN should be set aside.

5. In correspondence prior to the lodging of the appeals the Appellants raised several complaints regarding HMRC's conduct in the investigation and concerning what could be legitimately expected in terms of the remediation of errors in returns considering previous HMRC visits. The parties were agreed that we have no jurisdiction to consider the terms of these complaints or questions of legitimate expectation save to the extent that the conduct was sufficiently egregious that it provided evidence that HMRC had failed to act to their best judgment (as to the relevant test see paragraphs 10 to 12 below).

6. For the reasons set out in detail below we have determined that the appeals should be dismissed. We have concluded on the evidence before us that:

(1) The assessments were raised in exercise of HMRC's best judgment;

(2) A&M have failed to satisfy us on the evidence presented that the assessments are overstated; whilst there are individual supplies within the sample periods on which we may have reached a different conclusion to that reached by HMRC we consider them to have no consequence on the quantum of the assessments as HMRC rounded up the allowable percentage of margin scheme sales, such rounding more than accommodates for the minor adjustments to the sample periods we might otherwise have made;

(3) A&M deliberately rendered inaccurate VAT returns, ZC, as the director of A&M was aware both of how the margin scheme worked and that the terms of the scheme as provided in law and explained in Notice 718 had to be complied with if a supply was to be taxed under the scheme. ZC knew that the compliance conditions of the scheme were not met and nevertheless rendered VAT returns on the basis that virtually all supplies made were properly taxed under the scheme. Therefore both the Penalties and the PLN were justified;

(4) The mitigation given reducing the maximum penalty from 70% to 56% was entirely reasonable.

(5) In view of these conclusions we do not consider it necessary to determine whether A&M were participants in supply chains involving the fraudulent loss of tax and/or whether A&M knew or should have known about such fraudulent tax loss.

7. Whilst we have the power pursuant to section 84(5) VATA to increase assessments made which, in our view, understate the VAT liability of A&M HMRC did not with any vigour, invite us to exercise this power. We have therefore determined to limit our consideration of the amount due from A&M to the amounts assessed by HMRC.

RELEVANT LEGAL PRINCIPLES

8. There was little or no disagreement between the parties as to the legal principles to be applied when determining these appeals and it is appropriate to set them out before considering the evidence.

Best judgment

9. Section 73 VATA provides that where it appears to HMRC that a taxpayer has rendered returns which are incomplete or incorrect they may assess the amount of VAT due from him to the best of their judgment.

10. The exercise of best judgment was described by Woolf J in *Van Boeckel v CEC* [1981] STC 290 as:

> "The very use of the word 'judgement' makes it clear that the commissioners are required to exercise their powers in such a way that they make a value judgement on the material which is before them.
>
> Clearly, they must perform that function honestly and bona fide. It would be a misuse of that power if the commissioners were to decide on a figure that they knew was, or thought was, in excess of the amount which could possibly be payable, and then leave it to the taxpayer to seek, on appeal, to reduce that assessment.
>
> Secondly there must be some material before the commissioners on which they can base their judgement. If there is no material at all it would be impossible to form a judgement as to what tax is due.

> Thirdly it should be recognised, particularly bearing in mind the primary obligation, of the taxpayer to make the return himself, that the commissioners should not be required to do the work of the taxpayer in order to form a conclusion as to the amount of tax which, to the best of their judgement, is due. In the very nature of things frequently the relevant information will be readily available to the taxpayer, but it will be very difficult for the commissioners to obtain that information without carrying out exhaustive investigations. In my view, the use of the words 'best of their judgement' does not envisage the burden being placed upon the commissioners of carrying out exhaustive investigations.
>
> What the words 'best of their judgement' envisage, in my view, is that the commissioners will fairly consider all material before them and, on that material, come to a decision which is one which is reasonable and not arbitrary as to the amount of tax which is due. As long as there is some material on which the commissioners can reasonably act, then they are not required to carry out investigations which may or may not result in further material being placed before them."

11. That statement has been restated and narrated many times. A taxpayer who seeks to bring a challenge to the exercise of best judgment faces a high bar to jump. In *Rahman t/a Khayam Restaurant v CEC* [1998] STC 826, Carnwath J confirmed that an assessment will have been made in exercise of best judgment unless it "has been reached 'dishonestly or vindictively or capriciously'; or is a 'spurious estimate or guess in which all elements of judgment are missing'; or 'is wholly unreasonable'."

12. In *Pegasus Birds Ltd v CEC* [2004] EWCA Civ 1015 the Court of Appeal offered us the following guidance:

> "38(i) The Tribunal should remember that its primary task is to find the correct amount of tax, so far as possible on the material properly available to it, the burden resting on the taxpayer. in all but very exceptional cases, that should be the focus of the hearing, and the Tribunal should not allow it to be diverted into an attack on the Commissioners' exercise of judgement at the time of the assessment."

13. The parties were agreed that no question of public law jurisdiction arose in this appeal by reference to HMRC's alleged conduct in relation to previous visits or through the investigation. If we were satisfied that the process giving rise to the Assessments does not meet the standard expected to meet the *Van Boeckel* and associated case law test the appeal will succeed in full. If not, we are to determine the correct amount of tax due on the evidence.

Margin scheme

14. The second-hand margin scheme is provided for under Articles 311 - 315 Principal VAT Directive (**PVD**) which, consistently with Recital 51 PVD, provides a scheme for the taxation of goods which re-enter a commercial transaction chain and which have already been subject to tax on their full price at the point at which they enter into consumption. So far as relevant to these proceedings, it provides for tax to be charged on the margin achieved by a taxable business where that business has purchased goods from a non-taxable person. The provisions of PVD were bought into domestic law by section 50A VATA, Value Added Tax (Special Provisions) Order 1995 and certain paragraphs of Notice 718 which have force of law. Use of the margin scheme is optional and subject to strict and precise compliance obligations. Where those obligations are not met VAT is required to be accounted for on the full selling price paid to the taxable reseller of the goods.

15. The detailed compliance rules reflecting the primary/secondary law and/or having force of law set out in Notice 718 relevantly require:

(1) The goods must be second hand goods suitable for further use as they are or after repair.

(2) The taxable dealer wishing to sell using the margin scheme must have purchased the goods from someone who was not previously able to deduct the VAT on their purchase either because they are a non-taxable person (relevant in this appeal either a private individual or an unregistered business) or because the prior sale was also under the margin scheme (there being no entitlement to deduct input tax charged under the margin scheme).

(3) The taxable dealer must either obtain a purchase invoice from another taxable dealer showing that the supply was under the margin scheme or, where purchasing from a private individual/unregistered business the prospective margin scheme user must issue a self-billed invoice in a prescribed form.

(4) A stock book must be maintained in which prescribed information must be recorded including date of purchase and sale, purchase price, selling price, names of seller and purchaser, margin and VAT due.

(5) That the margin scheme cannot be used where VAT is shown on the purchase invoice.

(6) The sales invoice on a margin scheme sale must include a declaration that VAT will be accounted for under the margin scheme.

(7) The margin scheme may only be used when buying from a VAT registered business in the EU where there is a reference to Article 313 PVD, reference to the corresponding domestic legislation or another declaration that the goods have been sold under the margin scheme.

Penalties and PLN

16. Section 97 and Sch 24 FA 07 provide for penalties for errors made by taxpayers in rendering, inter alia, VAT returns. To be liable to a penalty the taxpayer must have rendered an inaccurate return and the inaccuracy must have arisen carelessly or deliberately.

17. As confirmed in *HMRC v Tooth* [2021] UKSC 17 at paragraph [43] deliberate behaviour will usually require that the taxpayer know that the return contains an inaccuracy and that the taxpayer must have intended to mislead HMRC by that inaccuracy. However, the Upper Tribunal in *CPR Commercials Ltd v HMRC* [2023] UKUT 61 has extended the meaning of a deliberate act to include "blind eye knowledge" of the inaccuracy. In that latter case the Upper Tribunal held:

> "23. In our view, where a taxpayer suspects that a document contained an inaccuracy but deliberately and without good reason chooses not to confirm the true position before submitting the document to HMRC then the inaccuracy is deliberate on the part of the taxpayer. If it were otherwise then a person who believed there was a high probability that their return contained errors but chose not to investigate would never be subject to a deliberate penalty. However, the suspicion must be more than merely fanciful. Lord Scott of Foscote urged caution in this context in *Manifest Shipping Co Ltd v Uni-Polaris Insurance Co Ltd* [2001] UKHL 1 at [116]:
>
> > "In summary, blind-eye knowledge requires, in my opinion, a suspicion that the relevant facts do exist and a deliberate decision to avoid confirming that they exist. But a warning should be sounded. Suspicion is

> a word that can be used to describe a state-of-mind that may, at one extreme, be no more than a vague feeling of unease and, at the other extreme, reflect a firm belief in the existence of the relevant facts. In my opinion, in order for there to be blind-eye knowledge, the suspicion must be firmly grounded and targeted on specific facts. The deliberate decision must be a decision to avoid obtaining confirmation of facts in whose existence the individual has good reason to believe. To allow blind-eye knowledge to be constituted by a decision not to enquire into an untargeted or speculative suspicion would be to allow negligence, albeit gross, to be the basis of a finding of privity."

> 24. Although the concepts of blind-eye knowledge and recklessness as to the truth or falsity of a statement may intersect, they are clearly not identical. As we have already stated, HMRC did not ask us to consider whether an inaccuracy is deliberate where a taxpayer is reckless as to whether the document contains any errors. In the absence of any argument on the point from HMRC, and because it is not necessary for the purposes of this decision, we do not consider whether recklessness is a sufficient basis for determining that an inaccuracy is deliberate further in this decision, and make no comment either way."

18. Where a penalty arises for deliberate conduct which was not concealed but disclosure of the inaccuracy was prompted by HMRC the penalty range is 35-70% of the potential lost revenue (i.e. the assessable/assessed tax). HMRC, or the Tribunal on appeal, can mitigate from the highest end of the range to the lowest end where the taxpayer co-operates with HMRC with reductions given for telling, helping and giving.

19. Sch 24 FA 07 (paragraph 19) provides that an officer of the company may be notified that they are personally liable for the company penalty where the penalty is a deliberate penalty and the deliberate inaccuracy is attributable to the officer of the company, HMRC may only recover the penalty from either the company or the officer to whom the PLN has been issued.

MTIC case law

20. We were referred to the body of case law pursuant to which it may be determined that a party in a supply chain may become liable for VAT fraudulently lost in the supply chain above or below the assessed party. In essence liability to tax will fall on a non-fraudulent party where fraudulent loss has been established and the assessed party knew or should have known of the fraud. Traders acting in good faith, taking every step which could be reasonably expected to be taken to satisfy themselves that the transaction to which they are party does not contribute to the relevant fraud, will not be liable to assessment.

21. Assessments are usually raised under these principles in supply chain fraud by way of refusal of input tax recovery on purchases of goods or services in respect of which there has been a demonstrated tax loss somewhere in the supply chain. However, in accordance with the judgment of the Court of Justice of the European Union in *UAB Litdana v Valstybinė mokesčių inspekcija prie Lietuvos Respublikos finansų ministerijos* (C-624/15) at paragraph [48] the principles are similarly appropriate where tax is lost through the fraudulent use of the margin scheme.

22. Of importance in all these cases is that the primary responsibility for preventing fraud rests with the tax authorities. Whilst taxpayers are required to do what might be reasonably expected to prevent themselves being caught up in a fraudulent supply chain the tax authorities cannot expect taxpayers to do more than is reasonable in the circumstances and

otherwise to act in good faith. Taxpayers who have taken the necessary precautionary steps are entitled to rely on documentation received at face value.

23. We do not set out further detail of the approach we would have to follow and the matters on which we would need to be satisfied as provided for in this line of cases because, in the end, as indicated above, the principles were not relevant to our determination of these appeals.

EVIDENCE

24. The documentary evidence made available to us was extensive. We had three bundles of documents exceeding 15,000 pages together with 8 very large spreadsheets.

25. Witness statements were provided by ZC, Mr Aaron Hunter-Cooke (**AHC**) (A&M's accountant) Mrs Elizabeth Penny (**EP**) (A&M's bookkeeper at the relevant time) Mr Andrew Clinton Payne (**AP**) (expert appointed by the Appellants) and Mr Riyaz Patel (**RP**) (HMRC's investigating and assessing officer). All witnesses gave sworn oral testimony and were subject to cross examination and re-examination.

26. Given the volume of evidence made available to us this judgment is, necessarily, only a summary. We have carefully considered all documents from the bundle to which we were specifically referred by the parties or to which we have referred to below. In doing so we are satisfied that we have acted in accordance with the overriding objective and cognisant of the guidance provided by the Upper Tribunal in *Adelekun v HMRC* [2020] UKUT 244 (TCC) in which it was stated:

> "... It cannot be assumed that just because a document appears in a hearing bundle that the tribunal panel will take account of it; if a party wants the tribunal to consider a document then the party should specifically refer the tribunal to it in the course of the hearing (see *Swift & others v Fred Olsen Cruise Lines* [2016] EWCA Civ 785 at [15]). This is not least to give the tribunal adequate opportunity to consider and evaluate the document in the light of the reliance a party seeks to place on it, but also to give the other party the opportunity to make their representations on the document. That is particularly so where, as here, there were several hearing bundles before the FTT relating to the various previous proceedings and the one containing the relevant additional documents was voluminous comprising 434 pages."

27. We have not excluded from our consideration any document to which we were referred unless so indicated in our consideration of the evidence. However, we do not refer to every document, rather we refer to those on which we rely to have formed our view and, as necessary, deal with all conflicts of evidence which we needed to resolve in order to reach our conclusion.

28. In the sections concerning the evidence of the individual witnesses we set out the salient points of evidence, as appropriate by reference to and with relevant quotations from exhibited documents. As the hearing before us lasted 4.5 days our recitation of the oral evidence is also a summary.

Burden of proof

29. As indicated above we have not found it necessary to consider, or conclude, whether within the supply chains in which A&M participated there is an established fraudulent tax loss or that A&M knew or should have known of any loss were that loss to have arisen fraudulently. Had we considered it necessary to do so the burden would have been on HMRC to establish the relevant facts justifying such a conclusion.

30. However, HMRC bore the burden of establishing that the amounts of tax determined to be payable were not correctly declared by A&M in consequence of the deliberate conduct of ZC.

31. It was for A&M to satisfy us, on the balance of probabilities, that the Assessments were either not made to HMRC's best judgment or, in the alternative, that they were excessive and that we should have reduced the quantum.

Documentary evidence

32. The documentary evidence provided to us, and on which our decision depends, broadly fell into the following categories:

(1) The exhibits to ZC's statement comprising principally emails showing travel itineraries, information or copy invoices for the purchase of watches and emails with HMRC.

(2) The exhibits to RP's first and second statements. These were extensive. The principal documents to which we needed to have regard were: historic visit reports and associated correspondence, Standard Committee on Administrative Co-Operation (**SCAC**) request reports and associated correspondence with the tax authorities of various EU Member States, enquiry/investigation correspondence and related documents disclosed, extracts of A&Ms business records including sample purchase and sales invoices for periods 11/17, 02/18 and 05/18, information extracted from the VAT International Exchange System (**VIES**), various company searches; A&M's annual accounts, RP's analysis and assessment schedules/calculations.

(3) ACP's expert report and accompanying analysis together with all available purchase and sales invoices for period 11/15 together with associated documentation.

(4) Full copy of A&M's margin scheme stock book record for assessment periods.

RP's evidence

33. It is appropriate to start with a summary of RP's evidence as it provides a narrative to the investigation and an explanation of the Assessments and Penalties. Included within this summary is the evidence relating to RP and HMRC's concerns that A&M was a participant that knew or should have known that there was a fraudulent tax loss in certain of the supply chains. However, and as set out below because we have upheld the assessments for other reasons our findings of fact in this regard are limited.

34. In the main we found RP to be a credible witness. There were, however, matters and issues on which RP was reluctant to accept obvious propositions put to him by Mr Kazakos. We were therefore unable to accept all RP's evidence; where we do not accept his evidence, we say so in our findings of fact.

35. RP is a Higher Officer and has been employed by HMRC since 2005. Since 2012 he has been part of the Specialist Investigations Office renamed Fraud Investigations Service. His focus is on supply chain fraud and the team to which he is allocated is the missing trader intra-community fraud (**MTIC**) team.

Evidence relating to the A&M's business generally

36. RP narrates the registration history and business activities of A&M by refence to the relevant registration documents: A&M was first registered for VAT with effect from 1 September 2007. A&M's predominant business activity is of a watch dealer with almost de minimis involvement in the retail sale of other jewellery and watch/jewellery repairs. It operates from retail premises open by appointment only and through a website iconicwatches.co.uk. The business has storage facilities separate to the retail premises and it

is those storage facilities which are its registered place of business. The business is registered for PAYE with 6 employees. The business was previously carried on by the Coles family but not through a limited company. None of this evidence was controversial.

Visits to A&M prior to the enquiry resulting in the Assessments

37. HMRC's contact with A&M is set out in RP's statement and the associated visit reports are annexed to the statement. The history of the relationship was considered important by RP in his assessment of A&M's conduct when raising the Penalties and issuing the PLN. As regards the visits made to the Appellant prior to RP's involvement we were provided with the following evidence:

(1) Visit report for a full VAT audit undertaken by Officers Wilmot and Lee on 05/12/11 and 14/03/12 at which annual accounts, the second-hand stock book, and purchase invoices were inspected. No officer of the company was available at the visit, but AHC represented the business. A range of potential risks were considered, in particular, and of relevance: EC acquisitions, imports, margin scheme and records and controls. The report summary of the risks makes no express assessment of EC acquisitions but notes that imports "appear credible" and that the Margin Scheme was "satisfactory". The detail of the report notes:

> "Discussed issues about sales and purchases and items that should not be included on schemes … Wrote to acct … received letter … from acct. The purchase and sales invoices trace to copy of the stock book and imports and EC sales and purchases appear credible.
>
> …
>
> CONCLUSION AND COMMENTS ON CREDIBILITY: It was difficult to trace sales & purchase through the stock book … It would not be financially viable to continue the visit and athought [sic] the records were poor the checks undertaken, and records inspected tend to suggest that credibility of the traders [sic] records is satisfactory."

(2) The visit report of a second visit was made to A&M on 17 July 2014 following receipt of a SCAC request concerning A&M's trade with SAS Di Andrea Ubaldi. The visit note reports that it took 13 attempted contacts over 4 weeks before a visit could be arranged. It also states that EP and ZC were available at the meeting and that all records were made available. The report sets out the information necessary to enable HMRC to respond to the SCAC request. At that visit it was identified that A&M had not completed box 9 (that for intracommunity acquisitions) on its VAT returns since 05/11. The explanation reported as given was that there had been problems with the accountant. The report notes that ZC agreed that the A&M's returns would be amended, and the EC acquisitions information provided. EP emailed AHC following the visit as did HMRC and AHC confirmed that he would "ensure vat return boxes [were] correctly completed". However, it was evident from a subsequent review of the VAT returns that no acquisitions were declared by A&M following that visit or at any time before the end of the period covered by the Assessments.

Commencement of enquiry leading to Assessments

38. The present investigation began following receipt of a SCAC request from the Italian tax authorities concerning supplies received by A&M from Piccinini Srl (**Piccinini**). The initial contact was by telephone on 1 September 2017.

39. We were provided with a copy of the SCAC request and telephone attendance note which RP also summarised in his statement. The SCAC request identified that watches had been sent by Piccinini directly to A&M but that the invoices for supply of the relevant

watches had been issued to other companies including Credit Foncier, UAB Credit Fiduclaire Europe, Timepiece Group, Montecarlo Trade et Finance and others. The request identified that the watches sold by Piccinini were new and that A&M sold them on their website. The Italian authorities sought answers to the following questions: "1.Why [A&M] received the watches? 2. To whom they were resold?" and indicated that they suspected A&M to be involved in "tax fraud (including MTIC VAT Fraud)".

40. The attendance note of the call records that ZC confirmed that he had dealt with Piccinini both directly and via intermediaries who may have purchased large quantities of stock from Piccinini. That Piccinini continued to hold the stock purchased by the intermediaries such that when A&M purchased via the intermediary supplier the watches would be delivered directly from Piccinini but were invoiced by the intermediary who A&M paid for the goods. ZC identified the intermediaries with whom he dealt as Credit Foncier and Timepiece Group. The note records that ZC said that Credit Foncier "used to be called UAB Credit". Mr Kazakos cross examined on the note; such cross examination was limited to confirming that ZC had "volunteered" the information regarding Credit Foncier and UAB Credit. RP confirmed that appeared to be the case as identified in the note.

41. After the call there was a visit on 13 September 2017. Again we were provided with the meeting note, a schedule of transactions with intermediaries who had supplied watches then delivered by Piccinini and RP's summary of the meeting. The note records that ZC, and his mother Gayle Coles (**GC**) were present. They confirmed that they purchased watches from Piccinini but not directly. They explained that the watches purchased from Piccinini were purchased via an intermediary introduced through an individual named Mariana. The note records that HMRC were told that discounts could be obtained through Mariana. The note also records that GC stated that she visited all suppliers to do their own vetting and perform due diligence checks and that Mariana also did her own checks; it was stated that detectives were employed if necessary. A&M are recorded as having confirmed that UAB C and Credit Foncier together with a company Cortlin were Mariana companies. As with the previous telephone note Mr Kazakos cross examined RP to elicit confirmation that ZC had volunteered the relationship with Cortlin. We do not have a record of any question in cross examination about the volunteering of Mariana's name. We also note that in his witness statement ZC makes no mention of employing detectives in order to provide due diligence on suppliers or that it was his mother who carried out any checks. Neither point was put to ZC in cross examination.

42. We understand that A&M were asked to provide details of transactions with the intermediaries who had supplied watches from Piccinini stock. Following this meeting EP provided a spreadsheet and some apparently associated purchase and resale documentation for watches that had been delivered by Piccinini. The spreadsheet refers to the following intermediaries: Sarle France Montres, First Electronic Commerce, Timepiece Group, Montecarlo Trade et Finance, Delta West Finance. The spreadsheet identified that there had been three watches also supplied directly by Piccinini.

43. The emails sent with the spreadsheet purport to provide the purchase and sales documentation in respect of the watches identified on the spreadsheet. However, we note that none of the purchase invoices appear to be from the intermediaries identified in the spreadsheet provided. We list below a summary of the purchase invoices sent to accompany the spreadsheet:

(1) The largest volume of invoices were from Credit Foncier and showed a VAT number and the rubric "sale made under Art 718 margin scheme. Pre-owned and pre used, MARGINE INVOICE, INPUT TAX DEDUCTION HAS NOT BEEN AND

WILL NOT BE CLAIMED BY ME IN RESPECT OF THE GOODS SOLD ON THIS INVOICE" or similar.

(2) The majority of the invoices for supplies by Cortlin Ltd showed a Cypriot VAT number and that the goods were preowned with the sale made under Art 718 margine scheme.

(3) The invoice provided for Societe Generale Overseas Limited indicated that the supplying entity had a UK address. The invoice does not have a supplier VAT number on it. It does not refer to Art 718 but despite being from a company based in the UK has the same spelling of "margine invoice".

(4) Invoices from Fedest Transport & Logistic SL do not show a VAT number but show the same rubric as those from Credit Foncier.

(5) Andmorabance Ltd (**A'bance**) invoices for supplies made on 17/02/15 do not show a VAT number but contain the same rubric as for CF and are in substantially the same format. The supplies made on 08/06/2015 do show a VAT number.

(6) There were invoices from the following suppliers: Padaliaka Andrei, Halynski Kanstantsin, Halynski Petr, Ardita Salvatore, Zhlukto Ivan, Kohoeva Kate, Shytsik Alsana, Ostertag Willy, Larysa Antsukevich, Halybskaya Iryna, Rkukina Maria. The invoices from those suppliers were all in identical format, layout and general appearance and generally concerned supplies of multiple watches per invoice and by multiple invoices. The invoices identify the manufacturer and serial number of the watches; each of them shows VAT charged at 0% they do not bear a VAT number and do not include the required margin scheme declaration.

(7) UAB Credit Fiduclaire European. These invoices were in identical format to those referred to at (6) above.

44. The carbon copy sales invoices describe all watches included in the schedule said to have been delivered by Piccinini as "unworn" and they have been sold under the margin scheme.

45. Shortly thereafter EP provided documentation demonstrating payment of the various purchase invoices. The documents demonstrate that payments were made on A&M's behalf by Afex in Euros and Afex was paid through A&M's bank account with Barclays. The documents enable the payments to be traced.

46. A&M also provided sales analysis sheets for August in each year 2013 – 2015. These illustrate that in August 2013 of a total value of transactions of £806,025.91, £795,495.43 (i.e. 98.69% were under the second-hand margin scheme) and a further 4.94% under the global margin scheme. The comparative figures are 92.34% second hand margin scheme in August 2014 and 96.27% for 2015 (though we note that the dates listed in each of the spreadsheets all say 2013).

47. We understand that following the provision of this information HMRC responded to the SCAC request, but we do not know on what date, and we were appropriately not provided with a copy of the response.

RP's mindset in the investigation

48. Before proceeding to consider the detail of the documents introduced and explained by RP, we address the general challenge that ran throughout cross examination as to RP's mindset when undertaking visits and when raising the Assessments.

49. Mr Kazakos cross examined RP extensively as to RP's mindset and whether the monitoring visits were MTIC focussed with repeated lines of questioning which asserted that RP's judgment was clouded by a view that A&M and ZC were associated with fraudulent activities rather than being open minded. Mr Kazakos put to RP that there must have been an MTIC focus because: 1) the decision to monitor A&M had been taken following the Italian SCAC request; 2) the team to which RP was attached was an MTIC team; 3) the opening letter informed A&M of HMRC's MTIC concerns; 4) each of the monitoring visits was recorded on a visit template headed "post registration – summary of MTIC assurance activity"; 5) VAT Notice 726 was issued and 6) many of the questions put to A&M in the various monitoring meetings appeared to indicate that HMRC were investigating A&M as potential MTIC fraudsters.

50. RP resisted all such propositions. RP consistently maintained that he was open minded and that the assessments were raised on the basis of all of the evidence available to HMRC at the time the Assessments were raised, and that further evidence had been considered as presented by A&M. RP also readily accepted that it was for HMRC to establish, as necessary, whether there was fraudulent activity, and it was not for a taxpayer to prove that there was no fraud in the chain.

51. Mr Kazakos also cross-examined RP about a visit to the shop by RP prior to the investigation. We understand from the cross examination and responses that the visit was whilst RP was a child and was with a family member who wanted to purchase a watch. Mr Kazakos put to RP that he had said, at some point (we are not clear whether it was alleged to have been when he visited as an adolescent (aged 12 – 15) or in the monitoring visits), that the watches could be sourced more cheaply in the middle east. RP confirmed that he had visited the shop but could recollect little of it; he did not accept that he had said that the stock could have been purchased more cheaply.

Trader monitoring

52. Following the September 2017 meeting A&M was put on trader monitoring which resulted in monthly visits from HMRC. RP's involvement commenced at this point. A letter dated 15 December 2017 was sent. The letter appeared to be a standard opening letter and referenced the risk of MTIC fraud. RP stated that despite the terms of the letter the monitoring was part of a supply chain concern generally and not MTIC specific.

53. We were provided with and have reviewed the meeting notes of each of the trader monitoring meetings. RP confirmed that the meeting notes had not been shared with A&M prior to the present litigation. Mr Kazakos cross examined RP extensively on these meeting notes. We make the following observations as to their contents and by reference to the answers given in cross examination (we also, where relevant refer to cross examination of ZC on these meeting notes).

Visit on 8 February 2018

54. A&M were informed that HMRC proposed to trace deals from start to finish.

55. ZC confirmed that he was a buyer for the business and completed the stock book, EP was the bookkeeper and AHC the accountant who prepared the VAT returns.

56. EP provided a supplier spreadsheet and ZC explained that he met suppliers through attendance at exhibitions and networking but had been in the industry a long time. It was explained that he would seek to source specific watches requested by buyers who often purchase them for investment purposes.

57. The note records that the stock mix at that time was 50:50 new/unworn:used and that there was a discussion regarding the meaning of unworn and new which reflects the correct

VAT position i.e. that an unworn watch may be the subject of a margin scheme transaction if it has previously gone into consumption. What represents a new verses an unworn watch was also the subject of cross examination. RP confirmed that a watch which was unworn and held as an investment, but which had entered the chain of consumption, was eligible to be traded under the margin scheme. However, he also confirmed that the age of a watch would not necessarily determine whether it had entered the chain of consumption.

58. However, the note also records that ZC had stated that if the watch had been purchased from a dealer abroad it was treated as used. That section of the note was not put to ZC and RP was not challenged on it.

59. ZC is said to have confirmed that he understood the margin scheme and terms of Notice 718 having discussed it with his accountant over 2-3 days. Again this section was not the subject of cross examination and, unlike other matters in the visit reports, ZC did not claim that he had been mis-recorded. We record below the terms of ZCs response to questions put to him regarding his understanding of Notice 718.

60. There is a record of a discussion concerning verification of suppliers which indicates that ZC would only deal with long established traders and would not deal with traders of which he was not sure. The note then records that "he always checked VIES".

61. The relationship with Mariana is recorded to have been explained by ZC. It is noted that Mariana is used to acquire specific stock for customer orders and not for stock generally. The benefits of using her are described as her access to more rural small businesses and because she obtains good discounts. The note records that ZC had spoken to her only once. In cross examination ZC denied that this is what he told HMRC (see paragraphs 122 to 126 below for a summary of his position on communications with Mariana).

62. At the meeting HMRC are recorded as raising their concerns about suppliers established in one country but with bank accounts in another. The meeting note records that RP described such a situation as "iffy". When cross examined on whether he had ever described the arrangements as iffy RP did not consider that he had but accepted that the note recorded it.

63. The concluding risk assessment of the visit, as further explained by RP, confirmed that no MTIC awareness letter was required to be issued because one had previously been issued and that there was no basis, at that time, to set a repayment inhibit, block the VAT number or deregister A&M.

64. Records for VAT period 11/17 were requested.

Visit on 14 March 2018

65. ZC, GC, EP and AHC were in attendance on behalf of A&M. A memory stick onto which A&Ms records for period 11/17 were saved was provided to HMRC.

66. The visit report records that EP informed HMRC that there was no set way for sales to be described, she explained that the purchase invoice usually showed a product code and serial number. EP explained that where there was no sum of VAT charged by the invoice, then the margin scheme was used.

67. RP sought to understand whether due diligence procedures had been improved since the last monitoring visit. Rather than indicate what enhanced due diligence would be undertaken ZC merely indicated that there had been no new suppliers in the month. ZC confirmed that he also visited all his suppliers and would not continue to deal with them if he had concerns. The note records that ZC said that he undertook companies house searches and background checks on his suppliers and purchasers but retained no records to support that assertion.

68. At the meeting HMRC established that, at least, Wonderful Invest OU, Maiko Trade OU, Veranika Kavaliova, Luxury International Fze Ltd, Anisenka Anastasiya and Ibercaja International Trade Ltd were companies acting through Mariana. We note that some of these companies were not recognised by ZC when cross examined.

69. The records provided at this meeting were included in the hearing bundle. Examination of the carbon copy sales invoices identified that each invoice was handwritten. The invoices identified the name of the purchaser, full details of the watch purchased including its serial number. The watches were almost invariably described as "unworn". The price was entered as "total second hand" and no VAT was shown. In the main, each sales invoice was also accompanied by a post-it note in which was written the serial number of the watch and a brief description. The purchase price of the watch was not recorded on the post-it. However, also shown on most of them were four other items of information three of which were later confirmed both to RP and to us as:

(1) The date on which the watch was received by A&M

(2) Details of the warranty: jurisdiction (i.e. EU) and the effective date, occasionally the dealer which had commenced the warranty

(3) An abbreviation identifying the supplier

Visit on 17 April 2018

70. The visit report records that RP asked A&M whether there had been any changes to the business model or practices. The meaning of the question was challenged by GC and RP confirmed that it related to the period since the previous visit and concerned due diligence practices. In light of the clarification, it was confirmed that no changes had been made. Mr Kazakos sought to understand why this question had been asked. RP explained it was a routine question.

71. Payment arrangements are shown as having been discussed. RP questioned why some banking records showed bulk payments without reference to particular invoices. ZC explained that multiple invoices from one supplier might be settled in one payment without that being recorded on the banking record but that it was then recorded in the A&Ms books.

72. The markup of the business and the basis on which prices were determined was recorded as having been discussed. Mr Kazakos put to RP that the questions were asked in order to establish whether the markup and/or selling prices were pre-ordained as would be expected in an MTIC deal chain. The inference derived from what was a reasonably extensive line of questioning was that despite there being no evidence of MTIC (in the sense that A&M traded in physical goods which were factually received and supplied on to identified consumers) at the previous two monitoring visits RP continued to pursue a "mission" to establish that A&M participated in deal chains resulting in a loss of VAT with a clouded mindset. RP was clear that they were questions to better understand the business.

73. At this visit HMRC asked for contact details for Mariana. These were subsequently provided by email. It was established in cross examination that HMRC had not made any attempt to contact Mariana.

74. A particularly contentious part of the note records that RP "asked what percentage of watches were unworn new and what were pre-owned worn". The answer is recorded as "ZC said and discussions with [EP] approx. 80% new and 20% used." Both RP and ZC were cross examined on this aspect of the note. RP did not recollect that part of the conversation ZC denied that he had said that 80% were new. EP was not asked.

75. A&M were informed that HMRC intended to issue SCAC requests of other tax authorities.

Visit on 21 June 2018

76. As with the other meeting notes the stencil template used is for "Post registration – summary of MTIC activity". As regards this visit report Mr Kazakos sought to establish that its use indicated that RP continued to pursue a line of enquiry to confirm RP's view that A&M were engaged in MTIC fraud. RP explained that the template was standard for post registration VAT visits.

77. The visit report records that questions like those asked on previous occasions concerning changes to the business structure and operation were asked together with questions concerning markup and pricing. The relevance of these questions at this meeting were not the subject of specific cross examination in the way that they were in respect of the April visit, but we see nothing in that.

78. There was discussion about the business generally and changes to trade over time. ZC indicated that Brexit, a general downturn in the market for luxury goods and the effect of exchange rate movements had caused a £5m reduction in turnover as compared to 2016.

79. A&M's dealing with Maiko Trade OU (**Maiko**) are shown as having been discussed. RP is recorded as having indicated that there was no valid VAT number on the invoice such that the watches to which it related should not have been sold using the margin scheme. ZC and EP are recorded as having agreed that there was no VAT number, and promised to make enquiries of Mariana. Mr Kazakos was interested to understand whether correspondence from the Estonian VAT authorities dated 7 May 2018 (see discussion below in respect of communications with other tax authorities) had prompted RP to investigate this invoice. RP could not recall whether he had seen the Estonian correspondence prior to the meeting (even though it predated the meeting) but indicated that whether, or not, there was any concern with the deal chain leading to the issue of the Maiko invoices A&M should not have used the margin scheme because there was no evidence that Maiko were a VAT registered business. RP again resisted Mr Kazakos's assertion that the line of questions concerning Maiko was further evidence of a MTIC mindset.

80. Mr Kazakos sought to establish with RP whether A&M had been advised by HMRC that the margin scheme could have been used for Maiko purchases if A&M had issued their own self-billing invoices. RP confirmed that where the purchase was made from an unregistered trader A&M were entitled to issue their own invoice to substantiate accounting for VAT under the margin scheme but that he had not offered the option to A&M. Two explanations were given: 1) the goods might have been new and 2) the deficiencies in the Maiko invoice. Mr Kazakos correctly pointed out that the first reason could not be sustained by refence to the terms of the invoice as supported by the information from the Estonian authorities (see paragraph 93.(1) below) and that the second reason could not preclude the issue of an A&M purchase invoice because it was the very reason for it. In response to these points RP refused to accept that he did not offer the facility to issue a purchase invoice because he believed A&M to be engaged in fraudulent activities but did not provide any further explanation as to why he did not advise that purchase invoices could be issued. In re-examination RP articulated that the principal reason that A&M were not invited to issue purchase invoices was the sheer number that would have been required given the volume of trade with intermediaries who were not VAT registered.

81. The meeting note records the examination of further invoices from other suppliers either showing no VAT number or demonstrating that the supplies were acquisitions. These aspects of the note were not subject to cross examination despite having also been

summarised in RP's witness statement. Nor was the section in which RP recorded that he had serious concerns regarding A&M's use of the margin scheme.

82. It appears that warranties were first raised at this meeting; RP identifying that it appeared that warranties for watches sold as second hand appeared to start co-terminously with, or very shortly before, and in some instances after, the onward sale of the watch by A&M. There is no record of any explanation provided by ZC.

83. RP requested that a newly received parcel containing a watch be opened by ZC. The watch in question included a warranty from 2017 showing an individual's name. By cross examination Mr Kazakos sought to ascertain whether RP had requested that the parcel be opened in an attempt to prove that ZC was in fact selling new watches. RP's response was that the request was part of the visit and concerned the assets of the business.

84. The meeting note also records that in response to indications that more due diligence in relation to both the goods and suppliers was required ZC had indicated that if that was the way it had to be it would be the end of the business and that GC could retire. Again, there was no cross examination or denial from ZC regarding this part of the note.

Visit on 26 September 2018

85. This meeting is reported in the same way as the previous monitoring meetings but was promoted by a complaint having been made by A&M. Rather than being at A&M's premises it was held at HMRC offices.

86. We observe that in response to a question concerning the preparation of sales invoices ZC was noted as saying that he and GC prepared them. No mention is noted of other sales staff though it is apparent from the considerable number of sales invoices we saw comparatively few were prepared by ZC or GC.

87. In response to what was forming a common opening series of questions about the business ZC confirmed that there had been no changes to suppliers. ZC confirmed that due diligence processes would be followed in respect of any new supplier. However, the note identifies that watches had recently been purchased from Oriamo Ventures Ltd (**Oriamo**) for what was apparently the first time. There was apparently no due diligence by reference to which the integrity of the transaction for VAT purposes could be ascertained despite the absence of a VAT number on the invoice. Further issues with any identified due diligence are noted with transactions with PLD Managed Services Limited (**PLD**), another apparently new supplier of watches (again without a VAT number on the invoice), the due diligence for which appeared to be limited to ZC knowing the director historically.

88. Concerns were raised again concerning Maiko's changed bank accounts. ZC is recorded as having no concerns on the basis that bank accounts may be moved to take advantage of free banking but also that he was not particularly aware of the issue because he paid through Afex.

89. In one contentious part of the note it is recorded that GC would have been happy to pay for a handbag purchased from Debenhams where payment was made to a country other than where the shop was located, and the invoice came from a third. We acknowledge that the example is an unnecessary and unrealistic one the response cannot therefore fairly represent any basis for a decision to assess. We deal below with our factual findings on the asserted reliance on this response.

90. The report also notes that various invoices were put to ZC and GC. In particular an invoice from deBling, a UK supplier which had added VAT to the invoice at 20%. The VAT had been reclaimed by A&M, but the onward supply had been taxed under the margin scheme. ZC accepted that had been in error.

Supplier verification

91. We next consider the various correspondence with European VAT authorities and RP's evidence in respect of them. Before doing so we set out our understanding of the SCAC system in order to set the context and relevance of the evidence. We understand that pursuant to Articles 7, 15, 16 and 25 – 7 Council Regulation 904/10 concerning administrative cooperation and combating fraud in the field of value added tax the various tax authorities within the EU (at the time the including the UK which remained part of the EU) HMRC could ask or be asked to provide information regarding traders and transactions in their own states. We were provided with SCAC reports both received and issued by HMRC. In total we were provided with seventeen SCAC reports. Mr Kazakos cross examined in respect of nine of them and we set out in more detail the relevant contents of those reports and the matters on which RP was cross examined.

92. The remaining reports were summarised in RP's statement. By way of brief summary these reports demonstrate that:

(1) The Italian authorities made a SCAC request of HMRC in respect of Piccinini as referred to in paragraph 39. HMRC provided a response which we have not seen but then made a request of the Italians. The response from the Italians stated that the watches sold by Piccinini were all new and that Piccinini was an official dealer of new watches and classification of watches as used was incorrect such that the use by them of the margin scheme was suspected to be fraudulent.

(2) The Spanish authorities confirmed that all supplies by Galax Memory SI (**Galax**) were taxed as intracommunity supplies.

(3) Edwards Lowell Ltd of Malta was confirmed as selling new watches as intracommunity supplies.

(4) A'bance was confirmed by the Cypriot authorities as having been registered for VAT until 23 February 2017. The company was deregistered for fraudulent activities.

(5) Through the Italian authorities, HMRC identified that certain purchases made through Watch Distribution SAS Di Andrea Ubaldi & Co (**Ubaldi**) were of apparently preowned watches but that the supplier to the Italian company, Swiss Watch Centres Limited (**SWC**) was a defaulting trader in the UK.

(6) Hottinger Merchant Shipping & Trade SRO (**Hottinger**) was only registered in Slovakia as a recipient of services and not as a registered supplier of goods. It apparently acted as an intermediary for a supplier which shipped preowned goods with activated warranties directly to A&M.

(7) The Greek authorities confirmed that Gofas Jewellery (**Gofas**) traded in unused and new watches purchased directly from a main distributor but sold to A&M accounting for VAT on the basis that the supplies were intracommunity transactions.

(8) The Austrian authorities reported that Pi. Gi Bi Handels Gmbh (**Pi**) imported watches from Hong Kong and sold them on to A&M as intracommunity supplies.

(9) UAB Laurenas was confirmed by the Lithuanian authorities to have never been registered for VAT and to therefore have wrongly stated that supplies were made under the margin scheme. The authorities also reported that the directors of the company were apparently resident in Belarus and that the goods in question were shipped directly from Bulgaria.

(10) Authorities in the Republic of Ireland reported that Oriamo was not registered for VAT and with no presence in Ireland, the director being a Greek national also linked to SWC.

93. Where there was cross examination on the reports, we deal with each in more detail and in the order in which Mr Kazakos cross examined on them rather than in chronological order. We note that RP was not named as the requestor in any of the SCACs issued by HMRC.

(1) The UK issued a SCAC to the Estonian authorities on 26 March 2018; a response was provided on 7 May 2018. HMRC requested information on Maiko. The concern expressed by HMRC was that A&M had received invoices bearing no VAT number, but which referred to the margin scheme. The Estonian authorities were asked to indicate how Maiko could use the margin scheme, what action was being taken against Maiko, information regarding the trade between Maiko and A&M including whether the watches supplied were genuinely second hand and what due diligence appeared to have been carried out on Maiko by A&M. The Estonian authority response appears to have followed engagement with Maiko. The Estonian authorities confirmed that the watches sold were stated to have been preowned and that they had been purchased from a further intermediary. The authorities confirmed that Maiko was not registered for VAT and had not applied to be so registered despite (and by reference to the trade with A&M alone) exceeding the registration threshold. Due to other defaults in corporate registration it was confirmed that Maiko was to be deleted from the corporate register. RP accepted in cross examination that he had been able to trace the purchases made from Maiko to watches sold by A&M and was also able to establish that A&M had paid Maiko for the watches supplied but he confirmed that the invoices received from Maiko did not permit A&M to use the margin scheme when selling the goods on.

(2) Also on 26 March 2018 the UK issued a request to the Spanish authorities concerning Tableros Barnices y Colas Del Sur SL (**Tableros**). In this request it was stated that invoices had been received from the Spanish trader by A&M showing supplies under the margin scheme. The request proceeds "upon inspection of these goods it is believed these watches are new with manufacturers' warranty". Mr Kazakos challenged RP as to the accuracy of the information provided in the request. RP confirmed that the only goods ever seen physically by him had been those on show in the retail premises, all of which were used, and the single box opened and referred to in paragraph 83; the statement was therefore established as inaccurate. Mr Kazakos sought an explanation for the discrepancy. RP's response was initially that the assertion that the goods had been inspected might have been cut and paste from another report and when it was established that that could not have been the case, he accepted that the statement was an error. In the request the Spanish were asked to confirm whether the second-hand margin scheme had been used for the sale and why they appeared as EU intracommunity goods in VIES. The response confirmed that as the invoices did not reference the second-hand margin scheme and had been taxed under the general VAT regime as intracommunity supplies no visit had been undertaken. That the supplies were treated as intra-community supplies was confirmed by the VIES entries further, our examination of the invoices confirmed that each referenced PVD Article 138 and the implementing provisions in Spanish law. Considering the response from the Spanish authorities, RP sought to marginalise the error in the request as irrelevant.

(3) The SCAC to Latvia in respect of supplies made by Dimaxi was dated 20 March 2018. This request stated: "UK trader has invoices from your trader stating the supply has been made under the VAT margin scheme and not an EC supply. These goods are

being sold on by the UK trader as secondhand [sic] using the VAT margin scheme but upon inspection of these goods it is believed these watches are new with manufacturers warranty, EU trader is declaring these sales on VIES as standard EC supplies, is this correct". The request indicates that the information would assist the UK "in combating and disrupting any future fraud and also assist us in the identification of new MTIC traders". Mr Kazakos cross examined on the statement that the goods from Dimaxi had been inspected receiving the same response as in respect of Tableros. He also questioned regarding the reference to assistance in identifying MTIC fraud. RP's response, though not by reference to the obviously wider terms of the request, was that he was concerned with supply chain fraud generally and not only MTIC fraud. The Latvian response followed interaction with Dimaxi. The response reported that Dimaxi had confirmed that they had supplied from 2008 stocks of new watches to A&M but had not retained their own purchase information as records were retained for only 5 years. The sales had been zero rated as intracommunity supplies. This was confirmed by the VIES report and each invoice references Article 138 PVD. RP stated that his view when receiving the response was that A&M had incorrectly accounted for VAT in respect of the Dimaxi supplies on the basis that Dimaxi had sold them accounting for VAT as intracommunity supplies and that simply because it was old stock did not mean that it had previously entered the chain of consumption as confirmed by the SCAC response.

(4) On 27 March 2018 a SCAC request was sent to the Italian authorities concerning supplies of watches to A&M by Angela Ripa SRL (**ARipa**). The request on this occasion said "My trader has invoices from your trader stating the supply has been made under the VAT margin scheme and not an EC supply. The VIES declarations state that the supply was made under normal EC supply. My trader is selling these watches on as second hand or preowned which clearly, they are not. Please explain." A series of questions were asked as to whether the watches were new and the basis of VAT accounting in Italy. The Italian authorities confirmed that ARipa was a licenced Omega dealer selling new and used watches. The invoices supplied do not reference the PVD but refer to Art 41 of the Italian VAT legislation providing for zero rating of intracommunity supplies. In cross examination RP confirmed that he had not undertaken any investigation regarding the listed serial numbers of the watches to establish the age of the watches. He explained that he was not obliged to do so in accordance with best judgement and in any event the goods could not be taxed by A&M under the margin scheme because ARipa had sold them and accounted for VAT on the basis of intracommunity supplies.

(5) The SCAC request in resect of Credit Foncier was made to the Cypriot authorities on 26 March 2019 and the response received on 18 June 2019 i.e. after the date on which the Assessments were originally made but before they were revised on review. As with some of the previous SCAC requests the narrative of the request refers to the goods having been inspected. As previously RP conceded that was not the case. By the time of the request Credit Foncier had been deregistered for VAT for some considerable period. The UK sought information as to whether the watches were new and more generally regarding the trading relationship between A&M and Credit Foncier. It appears that the Cypriot authorities sought information from the Italian authorities before responding but confirmed that Credit Foncier had been deregistered for VAT on 31 December 2014. Despite this Credit Foncier issued invoices to A&M after deregistration continuing to show a VAT number and, as accepted by RP, in all regards appearing to represent a valid tax invoice. In cross examination RP was clear that whilst not expecting taxpayers to do the work of the tax authorities it was

appropriate to expect a taxpayer to check VIES to ensure that counterparties were registered for VAT particularly where, as in the case of the Credit Foncier invoice there were other red flags i.e. banking in a different member state. RP refused to accept that his approach in refusing to allow margin scheme treatment for Credit Foncier invoices post deregistration was because his driver was proving MTIC fraud.

(6) A SCAC request concerning Giemmeci SRL (**Giemmeci**) was made on 26 March 2018. It too referenced the inspection of the goods. The request was in very similar form to the others made at that time and sought confirmation as to the VAT treatment applied in Italy and whether the watches supplied were new or used. RP conceded the same error was made in the request. The response confirmed that used watches has been imported by Giemmeci from Hong Kong subject to Italian import tax and that the supplies made by Giemmeci to A&M were intracommunity supplies and not made under the margin scheme despite no formal reference to art 41 of the Italian VAT code. The authorities note that Giemmeci would be sanctioned for this failure. In cross examination RP accepted that there was nothing on the invoices which identified the supplies as intracommunity and suggested that where it was unclear as to the basis on which there was no charge to VAT the appropriate course of action would have been for A&M to establish the basis from the supplier. In re-examination RP identified that one of the Giemmeci invoices referred to Art 41. We note however than none of the invoices included any reference to the margin scheme as would be required if the supplies had been made under the margin scheme.

(7) The Cypriot authorities were sent a SCAC request concerning Ibercaja International trade Limited (**Ibercaja**) on 28 March 2018. This request included the inaccurate statement that there had been inspection of the goods. Concerns were identified regarding Ibercaja's banking arrangements and the authorities were asked to confirm whether the watches were genuinely second hand. The response confirmed that the watches had been purchased by Ibercaja from 6 individuals and that the goods were sold under the margin scheme to A&M. RP explained that he had not allowed the supplies of these watches under the margin scheme because further enquires had revealed that the purposed sellers to Ibercaja could not be verified and that there were other concerns about Ibercaja, in particular that they traded from the same address as other companies introduced to A&M by Mariana including A'bance. RP accepted that it would not have been possible for A&M to have confirmed the legitimacy of the supplies made to Ibercaja, but he considered that there were nevertheless indications that there was a significant risk of fraud in the supply chain through the other identified issues.

94. In addition to the SCAC requests HMRC undertook additional verification in respect of other suppliers:

(1) Enquiries were made of the Swiss authorities in respect of HBP Milestone SA (**HBP**) who confirmed that the goods had been accounted for directly as exports to the UK.

(2) It was identified that PLD Management Services Ltd (**PLD**) had been deregistered for VAT purposes as at the date on which margin scheme invoice were issued to A&M. The director of this company was also associated with several other companies which were deregistered for VAT owing significant sums of money. One such company was Watchtraderuk Ltd about whom ZC claimed to have undertaken due diligence before transacting. There was only one invoice from this supplier and whilst

it noted that the goods had been sold as second hand under the margin scheme it bore no VAT number.

(3) Elite Luxury Watches Ltd was visited by HMRC. At the time of the visit all stock was noted as having been imported. It was assessed to VAT for having incorrectly used the margin scheme and HMRC had applied to wind up the company.

95. Not all suppliers were verified individually. However, RP also considered VIES information in respect of all suppliers and identified that in excess of £20.5m of intracommunity supplies had been declared as made to A&M in the period 1 April 2014 to 30 September 2018 but had not been correctly accounted for by A&M. Mr Kazakos sought to establish through cross examination that the value of VIES data was dependent on the accuracy of the declarations made by the suppliers concerned. Whilst RP accepted the theoretical premise of the question, he maintained that VIES was a reliable source of data.

Analysis of uplifted records

96. At the trader monitoring visits in March (for 11/17), April (for 02/18) and September (for 05/18) HMRC uplifted the VAT records of A&M. These records were analysed before being returned at the next visit.

97. Those for period 11/17 revealed that all sales in that period had been accounted for under the margin scheme. There were no acquisitions declared. This was so despite examination of the underlying purchase invoices showing that a significant proportion of supplies had been zero rated as intercommunity supplies.

98. Consideration of the sales invoices and the accompanying post-it notes caused RP to be concerned that the description of a watch as "unworn" did not support a conclusion that the watch in question was preowned. RP considered the warranty information provided on the post-it notes and identified that the warranty for many watches either had not previously been activated or was activated during the period in which A&M owned the goods. RP also identified that there had been several imports on which VAT had been claimed but for which VAT had been declared under the margin scheme on the subsequent sale of the watch.

99. In cross examination RP was asked whether he had undertaken any exercise to establish the age of the watches and/or the position on the warranties. He was taken to a specific set of documents concerning the purchase and sale of a specific Rolex watch with a serial prefix C. Mr Kazakos put to RP that the prefix C indicated that the watch was manufactured in 1992. No evidence was produced to confirm the information put in that question. RP was asked if he had undertaken any checks of serial numbers to confirm the age of watches sold by A&M and he confirmed that he had not. Similarly, he confirmed that he had not investigated how and when warranties were activated. RP did, however, indicate that he understood that A&M may have issued top up warranties but was not able to provide any further detail in this regard.

100. RP's analysis of the information shown on the sales invoices identified that 10.58% by value of total sales in the 11/17 period were shown as preowned as distinct from unworn.

101. A similar exercise was undertaken for each of the VAT periods 02/18 and 05/18. The same pattern was identified with no VAT accounted for on acquisitions, the second-hand margin scheme used for the overwhelming volume of sales (with limited use of the global margin scheme). The proportion of sales by value shown as "preowned" were 9.16% for 02/18 and 10.81% for 05/18.

102. By reference to the investigations undertaken RP established to his satisfaction the following regarding each of the suppliers to A&M in the periods 11/17 – 05/18:

(1) ARipa – referenced that the supplies were taxed as intracommunity supplies stating that they had been zero rated pursuant to the provisions of the Italian legislation implementing Art 138 PVD (Art 41 of Reg 331).

(2) Edwards Lowell & Co Ltd – VAT at 0% and no charge to VAT but no margin scheme declaration or statement that the supply was an intracommunity supply.

(3) Galax – only total price shown together with a declaration in Spanish referring to Article 138 PVD and article 13 of the Spanish legislation.

(4) Giemmeci – invoices refer to Art 41 of the Italian legislation, the provision implementing Art 138 PVD.

(5) Gofas – VAT stated to have been charged at 0% in accordance with Art 138 PVD.

(6) Pi – invoices state that they are made "tax free intracommunity delivery – preowned watches".

(7) Dimaxi – reference to reference to Art 138 PVD.

(8) Tableros – only total price shown together with a declaration in Spanish referring to Article 138 PVD and article 13 of the Spanish legislation.

(9) Ubaldi – reference to Art 41 Italian legislation implementing Art 138 PVD.

(10) Piccinini – declared as a non-taxable transaction pursuant to Art 41 Italian legislation implementing Art 138 PVD.

(11) Think Time Limited – reference to Art 138 PVD.

(12) Alexios Ousta & Co – reference to Art 138 PVD.

(13) Vaggi Sergio E Figli SRL – reference to Art 41 Italian legislation implementing Art 138 PVD.

(14) Leonardo Watch limited – company based in Hong Kong, no reference to VAT at all.

Annual accounts comparison

103. RP compared the annual accounts to the declared turnover for A&M and identified the following discrepancies:

Accounts y/e	**Turnover**	**VAT Returns**	**Outputs**
August 2014	£10,607,421	11/13 – 08/14	£2,650,000
August 2015	£10,806,436	11/14 – 08/15	£6,466,171
August 2016	£11,918,379	11/15 – 08/16	£6,456,619
August 2017	£ 7,392,805	11/16 – 08/17	£4,743,467
August 2018	£ 3,892,088	11/17 – 08/18	£3,565,677

The Assessments

104. On the evidence gathered through the various visits, supplier verifications undertaken and analysis of prime records, it appeared to RP that there had been significant failures in VAT accounting:

(1) intracommunity acquisitions had been treated as supplies eligible under the margin scheme;

(2) import VAT had been declared and claimed as input tax but the onward supply of the imported goods had been treated as margin scheme supplies;

(3) a significant number of the purchase invoices bore no VAT number, but the invoices had nevertheless been used as the basis for taxing the onward supply under the margin rather than A&M issuing their own purchase invoice;

(4) there was a significant concern that goods described as "unworn" were goods which had not entered the chain of consumption and were therefore not goods eligible to be supplied under the margin scheme.

105. Considering these specific concerns and more generally RP determined to assess VAT for the period from 08/14 to 08/18. The assessment was raised on 19 November 2018 and as such the earliest period assessable under normal time limits was 08/14. In cross examination RP stated that he had assessed for the whole period as there was nothing to indicate that the nature and pattern of trade and VAT accounting had changed over that period.

106. The Assessments were calculated allowing 11% of sales by value to be taxed under the second-hand margin scheme, 11% being the highest percentage identified in the three analysed periods. That percentage was applied to the annual turnover as declared in the annual accounts. The total assessment for each year was allocated to quarters on a straight-line basis.

107. Mr Kazakos sought to establish by way of cross examination why RP had limited his analysis to the final three quarters of the full period covered by the Assessments particularly as the annual accounts showed that there had been some considerable variation in turnover across the four years of assessment, with the final year also being significantly lower than in other years. RP responded that he considered that there had been a consistency in the nature of the trade despite the fluctuation in annual turnover and that over the period there was nothing to demonstrate any relevant or significant change, certainly no change had been raised by ZC or GC either in the monitoring visits. We note that although RP limited his answers to the monitoring visits a review of the 2011 and 2014 visit report outline the trade carried on and provide a sense of the business over the period from 2011 to 2018 when taken with the more detailed monitoring visit reports.

108. RP was also cross examined on the reasonableness of his failure to have offered a facility to A&M to issue their own purchase invoices for all the purchases made from traders who were unregistered for VAT. RP maintained that given the volume of transactions for which such invoices would have been required it was not, in his view, necessary to make the offer. ZC had said in visits he was familiar with the terms of Notice 718 which provided that a trader must issue purchase invoices in those circumstances. We also note that A&M did make purchases from individuals and, in those situations, made out purchase invoices themselves. That occurred in circa 9.5-11% of situations by value in the three periods examined and so appears to have been a procedure familiar to A&M.

Review of the Assessments

109. Following the issue of the Assessments A&M submitted a detailed report challenging the basis of them. The main arguments presented in that report addressed A&M's concern in relation to HMRC's conduct in the investigation and a claim that, by refence to the conclusion of previous visits, A&M had a legitimate expectation limiting any recovery action HMRC were entitled to take. As indicated, we have no jurisdiction to consider these allegations and they do not form part of this appeal.

110. The report provided analysis of the VAT quarter 05/15 by reference to which it was contended that in that quarter 48% of sales by value had legitimately been treated as margin scheme supplies. A&M accepted that the margin scheme had been incorrectly used for all purchases treated by the supplier as an intracommunity supply and where import VAT had been declared and claimed.

111. An explanation was provided for the discrepancy between the annual accounts and the VAT turnover figures: incorrect VAT coding had been used within the sage accounting software such that the sales price was taken as the margin and not the actual price agreed with the customer.

112. Following receipt of the report RP undertook a comprehensive review of the 05/15 VAT records applying the same principles that he applied in respect of periods 11/17 – 05/18. And calculated the correct margin scheme rate became 8.25% (rather than 48%). RP determined to leave the allowable percentage at 11% as originally assessed.

113. The Assessments were then subject to a formal review. The substance and rationale of them was upheld but a comparatively minor calculation error was identified which led to a reduction in the Assessments as identified in paragraph 1.(1) above.

114. Subsequently, and as part of these proceedings, a further analysis was undertaken on behalf of A&M of the 05/15 period by AP acting as expert appointed on behalf of A&M in these proceedings. Following receipt of AP's report RP examined every purchase and sales invoice in the period. He was able to trace 660 purchase invoices (58%) and 1061 (92%) of the sales invoices (together with the associated post-it notes) to the stock book for the period and thereby to AP's report.

115. He identified that save in one specific but significant regard his analysis coincided with the view formed in AP's report. The difference concerned the resale of watches purchased from Credit Foncier and A'bance. RP noted that in the stock book all purchases from these companies were shown as having been purchased from "cf". RP considered that as, in 11/15 no VAT number was quoted on the invoices and/or that the company was not registered for VAT, A&M were not entitled to account for VAT on the relevant resale of watches under the margin scheme. Having carried out this more forensic exercise the percentage of sales correctly taxed under the margin scheme fell to below 5%.

Evidence of deliberate behaviour

116. The decision was taken to penalise A&M on the basis that the errors were deliberate and prompted and subsequently to issue a PLN on the basis that such conduct was attributable to ZC. RP explained that the substantive basis of that conclusion was that A&M (and ZC) were aware of the terms of operation of the second-hand margin scheme. RP considered that A&M had wilfully misused the scheme in several regards. He considered that the acceptance that the scheme had been incorrectly used for goods purchased by way of intracommunity supplies on its own demonstrated deliberate behaviour. Particularly so given that in the period prior to 2011 acquisitions had been declared and following the visit in 2014 where the issue had been flagged and in circumstances in which the accounting support provided to A&M had been consistent throughout the period from 2011 – 2018.

117. Similarly for goods which had been imported though, in RP's view, perhaps an even clearer example of deliberate misuse of the scheme as A&M was claiming input tax on the imports and then including them in the margin scheme.

118. RP's statement addressed his concern that A&M through the auspices of ZC wilfully failed to carry out due diligence on its suppliers; in particular, those with whom Mariana was associated. We address below ZC's evidence on what due diligence he undertook. RP's

view of its adequacy and the implications for A&M's liability to a penalty are now of little relevance. RP was particularly concerned regarding the connection evident between a number of traders with whom A&M dealt through Mariana.

ZC's evidence

119. We found much of ZC's evidence to have been self-serving and, in parts, evasive. Following lines of cross examination through many of his final responses can only be described as incredible given his earlier responses and thereby unbelievable. In the main, we were unable to accept his evidence as reflecting his true knowledge or understanding of the circumstances in which the margin scheme was actually used by A&M. Plainly, however we did not disbelieve everything he said.

120. At the outset we record, because of its central importance to the case, that ZC was asked whether he had read Notice 718 concerning the operation of the margin scheme. ZC confirmed that he had read it and was aware of its terms. He had been making sales using the margin scheme since 1994/5. He accepted that he was aware that it was an optional scheme and that to make supplies under the margin scheme its terms had to be complied with and, absent compliance, normal VAT accounting rules would apply. He specifically confirmed that he was aware:

(1) that only goods which had been preowned by private individuals were eligible under the scheme and that A&M was required to raise a self-billed invoice for purchases made from such individuals;

(2) of the requirement for a purchase invoice from another taxable dealer to include a declaration that the supply had been made pursuant to the margin scheme. In this regard we note that paragraph 7.1.2 of Notice 718 states that the margin scheme declaration should refer to Article 313 PVD or the relevant domestic implementing provisions;

(3) A&M were required to maintain a stock book that met the terms of the Notice.

121. ZC confirmed he was the only person who made entries into the stock book. The stock book had various columns including those for date of sale, watch detail including a description model and serial number, selling price, name of purchaser from A&M, name of supplier to A&M, selling price and margin.

122. ZC's statement provides an explanation of the Appellants' relationship with Mariana who he describes as a person well known in the industry. In cross examination ZC stated that he had first become aware of her through James Peter Coop one of the original shareholders in the corporate entity owning and developing the iconicwatches.com website. ZC explained that Mr Coop met with her and established that she assisted other traders in the UK many of whom spoke well of her. That included a business in Bishop Stortford the owner of which was known to ZC who had confirmed that Mariana did what she said she would do. ZC considered that her ability to speak many languages and her network of connections was particularly valuable to A&M. He explained that personal relationships are very important in the watch trade and accessing new relationships through personal contacts was critical.

123. There is a conflict of evidence regarding his personal contact with Mariana. In his statement it is recorded that: "personally, I did not have any contact with Mariana". The meeting note referred to in paragraph 61 recorded that he had spoken to her once, but he denied the accuracy of that note and in cross examination he was adamant that he had spoken with her by phone on three occasions. ZC could provide no explanation for these discrepancies.

124. ZC stated that Mariana operated an "open book" business model. That phrase was not explained in the statement but in re-examination ZC stated that such a business model means that Mariana applied a fixed percentage mark up to the watches supplied through the introductions she made. He accepted that she did not herself buy the watches and supply them to A&M she merely identified sellers able to meet A&M's requirements for particular watches who then supplied them directly. From this evidence we understand that A&M paid Mariana a fixed commission in addition to the price agreed with the supplier. However, we were provided with no evidence regarding these commission payments.

125. ZC explained that even in respect of companies with which A&M had direct dealings they would not have cut Mariana out even where she effected a transaction with a supplier A&M dealt with directly as the trade in watches relies on trust and to do so would be a breach of trust with significant reputational issues. We were told that Mariana acted in this capacity between A&M and a group of different companies but in cross examination ZC could not name the companies with whom A&M dealt through her.

126. The statement confirms that payments were made to the suppliers introduced by Mariana (and others) via Afex and that ZC understood that Afex undertook thorough anti money laundering and other checks on the recipients of funds routed through them. It is at least inferred from the statement that ZC therefore considered he could rely on Afex's willingness to process payments to these supplies as some verification as to their integrity.

127. ZC narrates his relationship and dealings with the following suppliers in his statement and as supplemented by oral evidence:

(1) Gofas – ZC claimed this company was a Greek supplier of part exchanged watches with whom he reached a mutually beneficial arrangement following a visit to Greece for which he exhibited a flight itinerary to Athens. ZC explained to us that Gofas was precluded from selling part exchange watches from manufacturers for which they were not authorised dealers. However, the facility of offering to part exchange was important. A&M were able to offer an outlet for these part exchanged watches. We note that the Gofas invoices were all printed in Greek. HMRC supplied translations of the invoices, and the translated documents plainly show that the supplies were zero rated as intracommunity supplies but without a knowledge of Greek or a translation of the document that was not immediately discernible from the invoices themselves.

(2) HBP – a Swiss supplier in respect of which ZC produced two invoices indicating that two particular watches had been supplied to A&M following refurbishment by Rolex. ZC also asserted that A&M had dealt with this supplier over many years and HMRC should have flagged if there was an issue following previous visits. ZC exhibited further invoices which demonstrated that HBP had taxed the supplies as exports to the EU.

(3) Galax, Tableros and others – all Spanish companies apparently controlled by "Pepe" who, ZC stated, chose to run his business through several small businesses rather than one because it was easier to get smaller sums of credit for each company. ZC asserted that HMRC had historically confirmed that the margin scheme could be used in respect of supplies from these suppliers but subsequently changed their mind in June 2019 (i.e. after the issue of the assessments). As regards the due diligence undertaken by A&M, ZC produced copies of emails confirming that he had made a trip to Basel to a jewellery fair where he said that he met Pepe and it was only following this meeting that ZC agreed to trade with them. ZC states that at the meeting Pepe confirmed that supplies were not made on an intracommunity basis but under the margin scheme. We observe (as set out at paragraph 92.(1) in respect of Galax and 93.

(2) in respect of Tableros) all supplies were confirmed by the Spanish authorities having been treated as intracommunity supplies.

(4) Maiko – ZC indicated that he was told that Maiko had applied for VAT registration and a VAT number was pending, as the invoices included a margin scheme declaration, he considered he was entitled to account for VAT on the resale of such watches under the margin scheme. He explained that a similar situation had arisen in respect of another of his suppliers in respect of which he had been told that HMRC were comfortable for the trader to continue to trade. He considered the same permission would apply in respect of Maiko. However, it appears that the period in which ZC was prepared to accept that the VAT number was pending spanned many months in which he did not question the basis on which he was accounting or make further enquiry of Maiko. ZC also stated that he was also unconcerned about the fact that Maiko changed its bank account three times in 5 months.

(5) PLD management Services Ltd – a UK company which, in his statement, ZC claimed that he believed the supplier to be registered for VAT at the time of the transaction with it. ZC provided no evidence of any enquiry or VIES check to confirm that the company was in fact registered. However, later in the statement and in cross examination ZC accepted that the invoice from PLD was deficient as the VAT registration number of the supplier was missing and that he was aware of that at the time as he chased the supplier for it to be reissued.

(6) ARipa – ZC openly admitted that he asked this Italian company to adapt the format of its invoice to a form he considered had been signed off by HMRC as appropriate when accounting under the margin scheme. We note however that all ARipa invoices refer to Article 138 PVD and Article 41 Italian VAT code and not to the margin scheme.

(7) Pi – purchases were apparently made from or through a UK trader/broker, but A&M were asked to pay the broker's supplier directly.

(8) Ubaldi – A&M traded with this supplier on the basis that it was a creditable supplier of a long-standing Cheshire Jewellers.

(9) Piccinini – An Italian company that ZC repeatedly asserted he never dealt with and that all watches sent by Piccinini to A&M were purchased via another intermediary. He maintained this position in cross examination. There were however significant discrepancies in ZC's evidence as to who A&M dealt with in respect of watches sent to them by Piccinini. Variously it was said that A&M had never paid Piccinini for any watches with payments always made to one of the companies to which they were introduced via Mariana and at other times denied any connection between Piccinini and Mariana. In any event, we note that despite these vehement assertions the information provided by EP as set out in paragraph 42 above demonstrates that three identified purchases were made directly from Piccinini).

(10) Dimaxi – ZC claimed in his statement that when he visited the supplier in November 2014 (as apparently supported by a flight itinerary from Manchester to Riga) he had been informed that the supplies made by them qualified for the margin scheme. ZC explains that Dimaxi used A&M's website to market its stock retaining title until a buyer placed an order which would then be sold to A&M and onward to the buyer.

(11) A'bance – was a Mariana company, ZC claimed that when A&M traded with them, they were registered for VAT and that trading ceased in 2017 after the Cypriot authorities deregistered A'bance. In his statement he made no mention of the absence

of a VAT number on the invoices. Ms Vicary cross examined ZC thoroughly regarding A&Ms dealings with A'bance.

(a) She put to ZC that the A'bance invoices clearly indicated that A'bance was acting as an intermediary for the purchase of watches from other supplies as those other suppliers were noted on the invoices themselves. ZC initially sought to provide some other explanation for this identified information but subsequently seemed to accept that the invoices did state for each watch the supplier from where it was to be sourced.

(b) ZC accepted that there was no direct evidence that watches sold by A'bance and described as unworn had previously been owned by a non-taxable person. He explained that the unworn description was adopted by him following a visual inspection of the goods for any signs of wear.

(c) For margin scheme purposes he relied exclusively on the description of the watches on the purchase invoices.

(d) Ms Vicary took him to some of the post-its which described A'bance watches as "new unworn" and asked for an explanation as to that description (particularly in the context that the resale of such goods was then accounted for under the margin scheme). ZC's response was that the post-it had incorrectly recorded the condition of the watch in these situations and that the invoice prepared had correctly recorded the watches as simply unworn.

(e) The nomenclature of "cf" was used in the stock book to relate to A'bance purchases because it was convenient shorthand for the companies that A&M made purchases from through engagement with Mariana. He could not think of an alternative abbreviation for A'bance and the whole word was too long to fit in the available box in the stock book ledger. In so doing he explicitly accepted that he had not complied with the strict requirements particularised and having force of law in Notice 718 as purchases from A'bance were misrepresented as purchases from a separate legal entity: Credit Foncier, though continued to assert that there had been practical compliance because he knew what the shorthand meant.

(12) Credit Foncier – As with A'bance ZC claimed that he ceased dealings after deregistration whilst accepting that there was one post deregistration invoice. In respect of that invoice ZC's evidence was inconsistent, in his statement ZC asserted that there was no communication from either the Cypriot or UK authorities that Credit Foncier had been deregistered and as the invoices otherwise complied as margin scheme invoices there was no basis on which he could have been alerted to the change of status. However, in cross examination he stated that he had been told by Credit Foncier that it was to be deregistered about a or two week prior to deregistration; standard procedures caused the invoice to be paid but the sums were returned by Credit Foncier via Mariana, ZC then asked for the invoice to be reissued.

(13) Giemmeci – ZC claimed that he had not understood at the point of purchase that he was trading with Giemmeci as he had dealt with a man called Dante Cenci. It was only when the invoice arrived that he appreciated Dante had been acting as a broker. ZC claimed that the watches purchased had not been manufactured for many years and must therefore have been second hand. We note that HMRC have not disputed that the Giemmeci watches were second hand, but as they were supplied to Giemmeci from Hong Kong subject to import VAT procedures Giemmeci could not make an onward

supply under the margin scheme. As identified at 93.(6) the invoice from Giemmeci did not include the margin scheme declaration.

(14) Ibercaja – ZC indicates that there is nothing on the invoice which could possibly have alerted him to any issue or risk with the supplies from this supplier as each watch was identified as second hand with a margin scheme calculation and VAT number of the supplier. He did not consider it of any particular note that Ibercaja shared an address with A'bance but was not clear he had even noticed.

(15) Ubaldi – ZC's statement asserts that he knew the supplier well, they had accompanied him to his club, had met in Italy and had supplied to Mark Worthington Jewellers for many years. Thus inferring that A&M should be entitled to trade with them. Again we note that HMRC have not asserted any issue with the integrity of this Italian supplier, the margin scheme was refused because the supplier zero rated its supplies to A&M as intracommunity supplies.

(16) SWC – ZC claimed that he knew the owner of SWC well and had visited the UK premises. He was aware that they had been investigated by HMRC. ZC was aware that the VAT number had been subsequently withdrawn but understood that HMRC permitted the supplier to continue to trade. The due diligence undertaken appeared to represent a LinkedIn search and company check performed on 19 November 2018 (i.e. after the Assessments were raised). In an email exchange prompted by AHC (who had questioned why VAT was showing at 0% rather than being excluded from the invoice) the owner informed ZC that the supplier's accounting package did not support margin scheme sales, so the supplies were treated as zero rated but that "he had never had a problem with it".

(17) Oriamo – it appears from the documents annexed by ZC supporting his due diligence on SWC that the owner of the business was also connected with Oriamo, an Irish company. ZC stated that the owner had informed him that Greeks were moving their businesses to other EU jurisdictions to remain in the EU. No explanation is provided for this view though we note and recollect that shortly after the Brexit vote there was debate about Grexit. Oriamo's invoices did not bear a VAT number but included a margin scheme declaration. ZC had been told that this was because the VAT number had been suspended but that the company remained entitled to trade without it. ZC said that despite knowing this he continued to use the margin scheme and given that he held an invoice for the supply did not consider it would have been "transparent" to have also made out a self-billed purchase invoice.

(18) Hottinger – ZC's statement claimed that full due diligence was performed on this supplier but provided no evidence of it. ZC explained that the supplier dealt with other respected traders. ZC noteed that as regards the watches sold by this trader the warranties were commenced prior to A&M taking possession of the watches. We were unable to verify the warranty position. However, we note that Hottinger was confirmed by the Slovakian authorities as having a limited registration and, we infer, thereby unauthorised to issue margin scheme invoices (see paragraph 92.(6) above).

(19) Alexios Ouster & Co – ZC explained that he had personally agreed the deal with this supplier when visiting their retail premises. He stated that he expressly agreed the form of the invoice. ZC exhibited email correspondence regarding the arrangements for the visit to the retail shop. There was no evidence as to a discussion regarding the form of the invoice, but we note that the invoice exhibited to RP's statement is dated 1 March 2018 shortly before the arranged visit and the invoice references Article 138 PVD and not the margin scheme.

(20) Patseas – was not addressed specifically in the witness statement but in cross examination ZC was taken to invoices which, albeit in Greek, showed that VAT had been declared at 23%. ZC explained that when AP undertook his review of period 11/15 these invoices had been identified and that it was AP's view that domestic Greek VAT had been incorrectly charged on them. However, as this was not identified until some years after the event A&M had not sought repayment of the incorrectly charged VAT or rectification of the invoice. This was so despite ZC also saying that he had a personal relationship with the owner of Patseas, who had invited him to the christening of the owner's child, and that the deal was arranged through Mariana (though the latter position was then contradicted by ZC saying that Patseas was not a Mariana supplier).

(21) MM – again this company was not addressed in the witness statement. Ms Vicary took ZC to invoices from this supplier. They demonstrably did not bear a VAT number for the supplier which was accepted by ZC.

(22) UAB Laurenas – also not referred to in the statement but transactions between A&M and this company were the subject of cross examination pursuant to which ZC accepted that the invoices bore no VAT number for the supplier (as was apparent from the invoices themselves).

128. Throughout the statement ZC repeatedly asserted that they did not generally deal in "new" watches and that the business "dealt with a mix of unworn and used" watches only. He denied that he had ever said (as per the visit report for 2 February 2018) that the new:used split of sales was 50:50 or (as per the visit report for 17 April 2018 that the split was 80:20.

129. When asked how he verified that goods purchased were, as a matter of fact, second hand ZC stated that he essentially relied on the description on the purchase invoices. Where those invoices stated that the goods were preowned, he accepted that to be the case. No further checks were undertaken. However, when the watches were received ZC stated that he examined them, if there was any sign of wear, he would reject them or seek a discount to cover the cost of repairs.

130. A brief explanation of warranties is given in the statement. ZC explains that warranties are often left blank and that fraudulent warranty cards could easily be purchased. In cross examination ZC was, at best sketchy and at worst evasive, on how A&M dealt with warranties. ZC said that there was no company policy on completion of warranty cards. He provided no adequate explanation at all for the dates entered where those dates were after receipt of the watches by A&M. In response to most of the examples he was presented with where there was a warranty activation during the period it was in A&M's possession he stated that he had not "witnessed" the date being added to the post-it note and could not comment. He volunteered no evidence regarding top-up warranties and was not cross examined on the availability or procedures concerning top-up warranties. However, he accepted in response to a question put to him by me that for the date to be during the period between purchase and sale it must have been completed by A&M staff.

131. Ms Vicary systematically took ZC through invoices issued by the majority of suppliers. Where invoices were not in English ZC stated that he had been unable to read them. He confirmed that he had not sought to translate their terms. Where relevant Ms Vicary pointed out that the majority of the EU suppliers issued invoices showing VAT at 0% and referred to Article 138 PVD. Despite these references ZC maintained that he understood and believed at the time he completed the stock book that all the invoices received supported entitlement to use the margin scheme. He indicated that he expected AHC to have checked the invoices and to have confirmed that he was correctly maintaining the stock book.

132. With regard to invoices from suppliers based outside the EU, ZC claimed that he was unaware that he could not use the margin scheme for imported goods; this was so despite having confirmed that he had previously read and understood the importance of Notice 718 which, at paragraph 8.1 confirmed that the margin scheme was not available for imports. However, he did accept that he was aware that the margin scheme could not be used where input tax had been claimed on the purchase and that import VAT had been claimed as input tax by A&M in connection with imported watches.

133. ZC's statement is explicit that "virtually all potential and actual suppliers were visited by a member of the A&M team" and that there were "scores" of suppliers with whom A&M were not prepared to transact because they considered that "ethically" or pragmatically" they were not businesses with which A&M wanted to deal.

134. Ms Vicary asked ZC what due diligence A&M undertook over the lifecycle of a relationship with suppliers and in respect of frequent bank account changes, common addresses between suppliers etc. ZC's response was that he either did not notice or if he did, did not question such issues. He posited that companies may have been changing bank accounts to take advantage of free banking offered for an initial period.

135. ZC stated in cross examination that he did not perform VIES checks and relied on AHC who always did them. ZC claimed that AHC had told him as much. He indicated that had AHC informed him that any supplier had not been VAT registered he would only continue to trade with the business if he knew the supplier personally.

136. In his statement and when put to him in cross examination ZC denied that A&M had deliberately rendered inaccurate VAT returns or abused the margin scheme to gain a commercial advantage. He objected to any assertion that A&M had not taken instruction or guidance from HMRC at previous visits to adapt to become compliant. In his view, at the visit in 2014, HMRC had confirmed that the business was compliant. However, under cross examination he accepted that HMRC will rely on VAT returns rendered and that it is important to ensure that returns are accurate.

137. Ms Vicary explored with ZC how the business was operated on a day-to-day basis. ZC explained that he was the principal buyer and ran the business. A&M employed six staff who attended to customers whether online or in person at the retail premises by appointment. He confirmed that the staff were all trained on the process of receiving watches including the information to be transcribed onto the post-it notes, storage of the boxes on shelving and securing the watches themselves, completion of sales invoices. However, he also stated that it was not him who trained them.

138. ZC confirmed that he had retained AHC as the company's accountant throughout the period covered by the assessment and from 2010. He accepted that he had seen and signed the VAT returns and authorised the annual accounts. However, he stated that he accepted what was shown in them relying on AHC as a professional to prepare them accurately. He confirmed that he did not verify the accuracy of the return and simply authorised the payment the return indicated required to be made to HMRC.

139. When it was put to him that up to period 05/11 A&M had been accounting for VAT on acquisitions but then stopped, he could provide no explanation and invited Ms Vicary to take the point up with AHC (see below paragraph 149 for AHC's response when Ms Vicary did so).

EP's evidence

140. We found EP to be a straightforward and honest witness. Having left her employment with A&M in 2018 her recollection was, at times, entirely expectedly, unclear. However, we

accept that she answered all questions put to her to the best of her recollection and refused to "fill any gaps" where she was unsure.

141. EP was A&M's bookkeeper for approximately 6 years and throughout the period 2014 – 2018. In that capacity she would calculate the margin on sales of watches and maintain the VAT account on the SAGE accounting software from which AHC would prepare the VAT returns. She would also assist in the shop and regularly completed sales invoices; we saw a number of invoices bearing her name. She also, on occasion, would complete the post-it notes. She explained that the post-it note would be written on receipt of the watch and by reference to the purchase invoice and information included in the watch package; the post-its were attached to the watch boxes which were stored on shelving with the watches being put in a safe. The description and serial number together with warranty details, supplier names and date of receipt would be recorded on the post-it. She informed us that she had been trained on how to complete the post-it notes and had been told to record that the watches were "unworn". My handwritten note of her evidence records that Ms Brown asked her what she meant by "unworn" and her response (as recorded in my note) was "can't remember always unworn".

142. When completing sales invoices EP confirmed that where the post-it indicated that the watch was unworn the sales invoice was prepared on the basis that the sale was under the margin scheme.

143. EP was asked about warranties. She candidly stated that she knew the basics on how warranties worked but no more; the post-it notes were completed on instruction reflecting the warranty information provided with the watch in question.

144. Similarly, EP indicated that she did not know much about the details of VAT accounting under the margin scheme and largely followed the process of bookkeeping that she was instructed to follow. She did not know what Article 138 of PVD was. She was referred to an email she had sent to a contact at ARipa in which ARipa was asked to adopt a model of invoicing similar to of a Spanish supplier. EP had no recollection of sending the email but the chain to which it belongs indicated that ZC and AHC had asked her to contact ARipa (then a new supplier) and ask them if they were prepared to follow a particular invoicing rubric. It is not clear from the bundle what invoice was sent to ARipa (the image scan in the body of the email is almost unreadable but the invoice included in the same section of the bundle is demonstrably not the one in the scanned image). However, and in any event, as we note above the ARipa invoices all referenced Article 138 PVD and Article 41 of the Italian legislation; they were not margin scheme invoices.

145. In her statement she confirmed that she had never performed any due diligence checks on suppliers; in oral evidence she confirmed that ZC undertook all due diligence on suppliers. However, she did communicate by email with Mariana. The communications were professional but friendly. They principally concerned shipping and tracking of watches. There was nothing which caused EP to question Mariana's integrity.

AHC's evidence

146. We found AHC to be a credible and honest witness. He has been A&M's accountant since 2010. Originally, he serviced them as an employee of Alexander Gow (Blackburn) Ltd but in 2013 when he left that employment and set up his own business A&M followed him. He was responsible for completion of the VAT returns and preparation of the annual accounts throughout the period. The returns and accounts were (and continue) to be prepared from source records provided to him by A&M. He explained that the VAT returns are principally prepared from the information contained in the stock book, purchase invoices (for purchases other than of watches) and records of Afex payments/bank statements.

147. In his statement AHC states that at the second monitoring visit he "stated that the VEIS [sic] system was used to check suppliers and valid VAT numbers". It also states: "I was under the impression that when a supplier was verified by A&M the client would check the supplier in several ways. Either Companies House, VEIS [sic] for VAT numbers ([EP] did this or asked me to do it over email), checking with other people in the industry that they have heard or dealt with the suppliers until they were satisfied that they were a genuine business and there wasn't any cause for concern with the supplier." The statement also indicates that periodically A&M would seek ad hoc advice from AHC regarding individual supplier invoices. When cross examined by Ms Vicary he confirmed that he had only rarely been asked to undertake a VIES check and not in the period post his departure from Alexander Gow.

148. The explanation noted above at paragraphs 111 regarding the discrepancy between the annual accounts and turnover as declared on the VAT returns was reiterated by AHC in his statement and was further explained when cross examined.

149. Under cross examination AHC accepted that when preparing the VAT returns, he worked from the stock book such that if the book noted a transaction as within the margin scheme that was the basis on which it was reported in the VAT return. This was the explanation for why, from 2011, and even post the visit in which the issue was raised in 2014, acquisitions continued to be accounted for as margin scheme supplies. With no indication in the stock book that the purchases were intracommunity supplies there was no reason for AHC to report the purchase as an acquisition or to exclude the onward sale outside the margin scheme.

150. We note that AHC's witness statement referred to his view that A&M had never traded as a pawn broker. Ms Vicary did not cross examine on that part of the statement. Mr Kazakos sought to re-examine in relation to it asking AHC to comment on the terms in which it was raised by HMRC during the monitoring visits. Ms Vicary objected as the question did not arise from any matter explored in cross examination. I upheld the objection for the reason expressed by Ms Vicary, also expressing concern that the question put sought to establish RP's "tone" when the issues was said to have been discussed. I considered the tone of the question to be irrelevant to the issues we needed to determine and was concerned as to the motivation of the question. Mr Kazakos assured me there was not negative motivation to the question which I accepted however, the question was not relevant to an issue we had to decide and did not arise from cross examination.

AP's evidence

151. AP was appointed as an expert on behalf of A&M. His statement was prepared broadly in accordance with the provisions of Part 35 Civil Procedure Rules. We say broadly as there was no disclosure of the instructions sent to AP. Indeed it was not even clear from whom the instructions had been provided but he confirmed that he had never been provided with a copy of counsel's opinion. AP openly informed us that he had never previously given evidence as an expert witness and that this inexperience may be reflected in his witness statement. He informed us that he had previously been a witness of fact for HMRC in relation to other appeals and when preparing such statements he had been guided by his superiors and Solicitor's Office; he had no such similar assistance in the preparation of his expert statement. His experience and expertise was gained over 31 years with HMRC as a visiting officer. He confirmed he had no particular expertise in the second-hand margin scheme. He stated that he had some experience visiting traders operating the scheme but indicated all those visited operated the second hand card scheme which applies to second hand card rather than the wider scheme applicable to other goods. He understood that his overriding duty was to this Tribunal and not to A&M. We consider that AP met that duty; it was clear on

occasions that he did not have deep experience or expertise in some of the finer aspects of the operations of the margin scheme and had to be led to them by Ms Brown, but he had a familiarity with it generally.

152. AP was asked by A&M to reconstruct the margin scheme calculations and associated VAT declarations for period 11/15. He created a spreadsheet from A&M's stock book and then traced a sample of 317 (28% of the total) purchase and sale invoices. He told us that the sample size was determined by cost constraints. The 317 selected were those that he could trace in a cost-effective way so were random only in that sense. Of the sample traced he was satisfied that 41% of sales had correctly been taxed under the margin scheme.

153. It was explained that on examination of purchase invoices AP would accept that the margin scheme applied if the invoice showed a margin scheme declaration and otherwise complied on its face with the requirements of the scheme. He confirmed that where the invoice referred to zero rating, Article 138 PVD (or the relevant domestic implementing provision) confirming an intracommunity supply he had excluded it as ineligible for the margin scheme.

154. Concerning the sales invoices, AP confirmed that where he had looked at them, he accepted each at face value and ZC's explanation that unworn meant preowned but kept for investment value. He admitted that he only looked at sales invoices where he could not trace the sample watch transaction from the purchase invoice to the stock book and on to the sales invoice. His primary source of reference in determining whether a particular watch was preowned was therefore the purchase invoice.

155. However, AP also indicated that he had some awareness of the post-it notes which accompanied the sales invoices. He accepted that he understood that the post-its included the date the warranty had been activated. He readily accepted the proposition that where the post-it indicated that a warranty had been activated whilst in the ownership of A&M it was likely that the watch was not simply unworn but rather that the watch in question was new. He was taken to a purchase invoice from A'bance which was described as a particular Omega watch as preowned and then to the associated sales invoice and post-it which described the watch as unworn but for which the warranty commenced after receipt by A&M. He conceded that had he looked at or considered the whole suite of documents relating to that watch he would have concluded it was in fact a new watch not eligible under the margin scheme. He thereby acknowledged that the working assumption that the purchase invoices were a reliable basis on which to determine eligibility under the margin scheme was not an adequate foundation for the analysis he had undertaken and, on that basis, that his calculation of the correct VAT due in period 11/15 was likely to be under stated.

156. When calculating the tax due in the period 08/14 – 08/18 as compared to the Assessments AP extrapolated on a uniform basis.

157. AP also rebuilt the records for VAT periods 11/17 – 05/18. His statement did not describe the exercise he undertook but stated that the tracing exercise in these quarters as "impossible" where there was no individual value or serial number recorded on the purchase invoice. In oral testimony he explained that he had examined all purchase invoices in this period but traced only 167 watches through the stock book. He then assumed that if the traced watch had been correctly treated as second hand, all purchases from the same supplier would also have been correctly treated. Based on this exercise he formed the view that of the order of 20% of sales should properly be treated as margin scheme supplies over the period 11/17 – 05/18.

158. AP was shown the relevant pages of the stock book and asked what he understood the entry "cf" to mean in the supplier name column. He explained that it was a shorthand entry

and may mean any one of a number of companies from whom A&M purchased stock. He understood that all "cf" entries would be stock purchased using a contact known as Mariana and would include, in the 11/15 period, Credit Foncier and A'bance and in the later periods also included Maiko. He accepted that it also included other companies across the full period under consideration. He confirmed that the global use of "cf" to represent a wider group of companies than simply Credit Foncier failed to meet the specific requirements of Notice 718 which had force of law. He indicated as a VAT inspector he might have invited the taxpayer to rectify the stock book but accepted that there was no statutory or other legal basis to do so. He accepted that for any entry in the stock book that showed the supplier as "cf" which was not in fact Credit Foncier there was no legal right for the onward supply to be taxed under the margin scheme.

159. When asked whether he had been aware that Credit Foncier had been deregistered for VAT in Cyprus he confirmed that he had not known that at the time he undertook his analysis but that in the periods he analysed he had also not seen any Credit Foncier invoices.

160. Critically, AP accepted that in light of the challenges put to him in cross examination his analysis for period 11/15 had incorrectly treated the supplies of watches purchased from A'bance as eligible under the margin scheme. This was on the basis that the stock book was wrong, and it could not reliably be said that the goods were preowned. Following this concession, in re-examination, AP indicated that, in his view as an ex-HMRC officer, A&M might reasonably have relied on the purchase invoice declaration as to the margin scheme and that as a VAT officer he may have allowed them to correct the stock book rather than assess.

SUBMISSIONS OF THE PARTIES

161. The essence of the dispute in this case centred on the interpretation of the evidence. It is therefore appropriate to set out the submissions of the parties prior to setting out our factual findings. We are grateful to all Counsel for their clear skeletons, submissions, and willingness to engage with our questions. We set out below our summary of those submissions. The parties however, should be assured that when preparing this judgment the terms of the skeletons were reread and the full handwritten notes fully reviewed. Because we do not deal specifically with any point does not mean that it was not considered in the round when reaching our decision.

Appellants' submissions

Best judgment

162. As indicated A&M's principal contention in this case is that HMRC, through RP, failed to make the Assessments in exercise of their/his best judgment. The Appellants' first line of attack in this regard was to challenge RP's credibility as a witness. The second appeared to be founded in either bias or an unrelenting conviction that A&M were engaged in MTIC fraud despite it being abundantly clear (as accepted by RP) that the watches were physically bought and sold. It was contended that RP did not approach the investigation with an open mind to such an extent that it could not be said that the Assessments and Penalties were the product of the reasonable behaviours of HMRC. Put in terms of the case law: that HMRC had acted in a way which no reasonable body of commissioners could have acted or, put another way, had been vindictive, dishonest or capricious.

163. Mr Kazakos relied on the visit reports from 2011 and 2014 as indicating that HMRC had been satisfied following both visits that A&M was a compliant trader satisfactorily using the margin scheme. By 2017 following a SCAC request from the Italian Authorities concerning Piccinini HMRC had become fixated to tying A&M in to potential MTIC fraud rather than simply assessing A&M's mechanical entitlement and use of the margin scheme. In support of this contention Mr Kazakos relied on the more reasonable approach taken by

AP in the context of his 31-year career with HMRC. It was said that AP had adopted a neutral mindset through which he had examined the records for the randomly selected period of 11/15 and subsequently for periods 11/17 – 05/18. That exercise had revealed inaccuracies, but those inaccuracies were understandable given the complexity of the issues in question. A&M had readily accepted the errors so identified.

164. A further attack to best judgment was made on the basis that save for periods 11/15, 11/17, 02/18 and 05/18 HMRC did not have sufficient evidence to have raised any assessment thereby failing to meet the *Van Boeckel* test and amounting to an unreasonable and random guess as to potential liability to tax for all periods in respect of which there had not been a detailed consideration of the transactions taxed under the margin scheme. This, it was said, infected HMRC's decision to assess for the full 4 years permissible under normal time limits based only on examination of the three of the final four quarters of the Assessment period. The unsuitability of the approach was also said to be supported by the significant variation in turnover across the period and failed to consider of the possibility of a changing pattern of suppliers.

165. Mr Kazakos also contended that in order have any realistic possibility of showing that they had raised a best judgment assessment for a full 4 year period HMRC had to rely on their assertion of connection to fraud, through their unproven allegations regarding trade through Mariana. He submitted that such a case fell at the first hurdle: HMRC had not presented a case to the standard normally offered and expected in a fraud case; and, in his submission, HMRC could not, on the case presented, meet the burden of proof.

166. It was also submitted that it was impermissible for HMRC to now justify the assessments by reference to analysis effectively undertaken by their Counsel as alternative bases for denying the use of the margin scheme. We were invited to focus on the documentation prepared contemporaneously by RP, which was restricted to a single spreadsheet for the examined periods. That spreadsheet had allowed or disallowed the use of the margin scheme solely by reference to the description of the goods as preowned or unworn (the margin scheme being permitted only in the case of watches recorded as preowned). It was said that the decision to disallow any transaction referenced as unworn was motivated by the view that A&M were involved in fraudulent MTIC transactions. Such motivation demonstrated by a plethora of evidence (including the SCAC requests and the monitoring visit reports) all of which recorded the lines of enquiry being followed all of which were demonstrably rooted in a fixation on an assumption that A&M knew or should have known of fraud and thereby a desire to raise the maximum assessment possible.

167. To the extent that we were properly permitted to consider the SCAC documentation, we were invited to focus only on the SCAC requests and not any responses. This was on the basis that internal HMRC guidance (no copy of which was provided to us) states that HMRC's Solicitor's Office has, in Mr Kazakos's view correctly, determined that the responses provided in such reports represent only the opinion of the overseas authorities and is thereby hearsay evidence. Without the opportunity to cross examine the respondent it was asserted that little weight should be given to the responses generally. In this case it was asserted that the SCAC responses were next to valueless because some were paper based without any interaction with the supplier in question.

168. Our attention was also drawn to the inadequacies of RP's investigation. It was submitted that by his own admission he had not sought to contact Mariana (or requested another authority to do so) a critical step that would have materially assisted in the present case.

169. In the alternative, A&M contend that the Assessments are all overstated essentially for the same reasons

170. As to deliberate conduct it was contended ZC had every reason to believe that the way A&M operated the margin scheme was considered to be satisfactory by reference to the previous visits. Given the history it was contended that any error in the operation and application of the scheme was careless.

171. It was submitted that HMRC had inappropriately issued the PLN following A&M's hardship application. It was contended that an indication that A&M could not pay the assessment should not have been used as justification for circumventing the proper means of collecting any assessment or penalty found to have been payable from A&M in the first instance.

172. No formal submissions were made as to mitigation of the penalty.

HMRC's submissions

173. Ms Vicary was clear that HMRC's primary case was not predicated on an allegation of involvement (either because A&M knew or should have known) in fraudulent supply chains. In her submission this case is one in which we must determine whether, in the periods covered by the Assessment, HMRC were entitled to conclude that A&M were ineligible to use the margin scheme except in circa 11% by value of the sales made. She highlighted that based on AP's evidence and analysis of the records for period 11/15 the Appellants had made substantial concessions and that, at least for that period, the only supplies which were disputed were those concerning sales of watches purchased by A&M from A'bance. For the accounting periods originally examined by RP (11/17 – 05/18) it should be assumed that similar concessions would be made with the disputed purchases being limited to other Mariana introduced intermediaries. The critical question for us therefore is limited to whether the purchases made from Credit Foncier, A'bance, Maiko and UAB Larenas in the periods for which there was evidence were made in circumstances which permitted the onward sale to be made under the margin scheme.

174. In the circumstances it was HMRC's contention that this case came nowhere near the bar which needed to be met for the Assessments to be struck down for want to best judgment. In the first place it was immediately apparent that there were material errors in VAT accounting. A&M had ceased to account for acquisitions in 2011. When the absence of acquisition accounting was raised in 2014 there was no indication that acquisitions had ceased and an acceptance that the position needed to be regularised. It had not been so regularised, and the errors were therefore glaring. Stopping there, HMRC had just cause to consider an assessment for the period back to 2014. However, there were substantial concerns beyond the treatment of acquisitions which further justified further investigation and subsequent assessment.

175. She contended there was no basis for contending that HMRC lacked information or evidence on which to base an assessment. A thorough and detailed investigation had been undertaken led by RP. The investigation had identified further concerns regarding whether watches were new or used for which A&M had been unable to provide any adequate response.

176. There were also material concerns regarding counterparties with whom A&M purchased watches, particularly the moving feast of apparently connected intermediaries for whom Mariana acted.

177. By reference to these concerns singly or taken together HMRC contended that there was a more than adequate basis on which to proceed to an assessment which could not be undermined by any asserted bias.

178. In support of the Assessments Counsel for HMRC produced a summary table which explained in respect of each of the suppliers to A&M the basis on which use of the margin scheme had been denied. In closing submissions the basis for refusal was prioritised to demonstrate that the appeal could be dismissed without our needing to determine whether A&M knew or should have known about fraud said to arising in the supply chain. The Appellants did not accept the table even as a summary of HMRC's arguments.

179. By reference to that table and the prioritisation HMRC submitted:

(1) As accepted by A&M any supply made of goods purchased by way of intracommunity supply could not be resold under the margin scheme. The suppliers who supplied A&M exclusively by way of intracommunity supply were: Piccinini (when supplying directly and when supplied through Credit Foncier), Dimaxi, Gofas, Edwards Lowell, ARipa, Ubaldi, Galax, Tableros, Giemmeci, Pi, Think Time ltd., Alexios Ousta, Vaggi Serio and Supermaderos.

(2) Similarly for the supplies made by HBP and Leonard Watch which were imports from outside the EU.

(3) All supplies examined within the Assessment periods received from A'bance, Credit Foncier, Maiko, Ibercaja, MM, Patseas, PLD UAB Larenas and Oriamo were ineligible to be included in the margin scheme because of record keeping deficiencies. These deficiencies ranged from a failure to show a valid VAT number, errors in the stock book, VAT shown on the invoice and others.

(4) HMRC also contended that it was reasonable to conclude that supplies made by A'bance, Credit Foncier Piccinini, Dimaxi, Gofas, HBP, Edward Lowell, ARipa and Ubaldi were or included supplies of watches that were not previously owned.

(5) There was evidence that supplies by A'bance, Credit Foncier, Piccinini, Ibercaja were connected with fraud.

180. HMRC contended that it had long been confirmed in the courts and tribunals that it was not for them to do the taxpayer's work for them. Provided an assessment is soundly based on some information and issued in good faith it would be a best judgment assessment. A best judgment assessment may materially overstate the tax due but where that was the case it was for the taxpayer to adduce evidence to demonstrate this. Here A&M adduced an expert who undertook a limited sampling exercise of one further period. For that period AP identified only one area (A'bance purchases) in which he formed a different view to RP and, in cross examination, accepted that all purchases from A'bance had been mis described as from "cf" in the stock book. As a consequence there was simply no evidence in this appeal, which would enable us to reduce the assessment.

181. As regards the penalties HMRC contended that A&M, through ZC, had deliberately mis-recorded acquisitions, imports and misdescribed the supplier in the stock book. Whilst HMRC do generally accept that where there are multiple errors of different types the root/cause of each error is considered independently here all errors were margin scheme errors and each of material errors in terms of quantum were independently deliberate. As such the correct basis of the penalty was that the inaccuracies were deliberate and prompted but not concealed thereby justifying a penalty in the range of 30 – 70%. As the conduct giving rise to the penalty was properly attributed to ZC the PLN was appropriate.

182. HMRC maintained that a 56% penalty was appropriate.

FINDINGS OF FACT

183. From the above evidence and by reference to the submissions made we make the following findings of facts. Under each section we set out our finding both as the underlying VAT positions and as to A&M/ZC's knowledge/conduct.

Eligibility under the margin scheme

Operation of the margin scheme

184. We accept ZC's evidence that he was familiar with the terms and operation of the margin scheme as provided under Notice 718. We do so despite not accepting much of his other evidence. It appears to us obvious that ZC was aware of the criteria and mechanics for operation of the scheme as accepted by him in cross examination. He had worked in the business with his parents over many years; the business trades in second hand goods and familiarity with the scheme was thereby essential.

185. On that basis, and by reference to his cross examination answers we find he knew that:

(1) the margin scheme was an optional facilitation for businesses trading in second hand goods;

(2) for VAT to be declared by A&M under the margin scheme the goods in question must have been previously owned by a non-taxable person (i.e. a private individual or an unregistered business);

(3) a purchase invoice was required to be issued by A&M when making a purchase from a non-taxable person;

(4) all purchase invoices, whether prepared by the supplier or by A&M, were required to include a margin scheme declaration and for there to be no reference to any amount of VAT on the invoice, and in all other regards were required to comply with the specifications for an invoice;

(5) the record keeping requirements for the margin scheme, and in particular the precise requirements of the stock book, had to be met in order to be entitled to account for VAT under the scheme;

(6) the margin scheme was not available for goods purchased as intracommunity supplies or imports;

(7) where any of the above requirements were not met in respect of any particular transaction VAT had to be declared under normal VAT accounting rules and, on the basis that A&Ms customers were, in the main, private individuals in the UK, subject to VAT at 20%.

Purchases from non-taxable persons

186. When taking part exchanges or otherwise making purchases from private individuals A&M made out purchase invoices. ZC admitted that he was informed two weeks prior to the date on which Credit Foncier was to be deregistered for VAT that it would be so deregistered. He also knew that Oriamo and Maiko were not VAT registered. Yet in neither case did he prepare VAT invoices for purchases from those traders. ZC told us that he believed that despite knowing that Oriamo and Maiko were not registered for VAT he understood that he could nevertheless continue to account for VAT under the margin scheme without raising a valid margin scheme invoice. We have carefully considered this evidence, but we cannot accept that it provides an adequate explanation for the use of the margin scheme without A&M issuing a purchase invoice to themselves. The terms of Notice 718 paragraph 2.9 and

the table at paragraph 4 make it clear that an invoice must be raised by the purchaser where the purchase is made from either a private individual or an unregistered business. ZC knew the last invoice from Credit Foncier and that from Oriamo and all those from Maiko were from traders who were not VAT registered, and we therefore find that he knew that the margin scheme should not have been used on the resale of the watches purchased under those invoices. Given that Maiko was in this group that represented a significant proportion of purchases.

187. The invoices from MM, PLD and Maiko did not bear VAT numbers and thus were deficient. ZC's evidence was not clear as to whether he looked at these invoices and/or was aware that they were deficient or that the suppliers were not registered for VAT. However, he was the sole person who completed the stock book. To do so we consider that he must have had sight of the purchase invoices because they were the only documents on which the purchase price was recorded (purchase prices were not on the post-it notes). Whilst we were not told that he checked the invoices for general compliance when completing the stock book we find that he at least had the opportunity to do so and, given his awareness of the requirements of the margin scheme, was well aware that he needed to be sure that the invoice received was from a VAT registered business and where there was no evidence that the business was so registered that A&M needed to raise their own invoice. We therefore find that he knew or at least closed his mind to the risk that A&M were not entitled to use the margin scheme in respect of items purchased from these suppliers. This is so irrespective of a failure to establish whether the suppliers were registered as to which see paragraph 222 below.

Stock book inadequacies

188. When ZC completed the stock book in respect of purchases made from wholesale suppliers introduced to him by Mariana he chose to record the supplier as "cf". For supplies from A'bance, Maiko, Ibercaja, UAB C and UAB Laurenas, (in the periods 11/15, 11/17, 02/18 and 15/18) and other companies in the wider period covered by the Assessments (Cortlin, Wonderful Invest OU, Luxury International Fze Eood, Vernika Kavaliova and Anesenka Anastasiya) he did so knowing that Credit Foncier was not the supplier. As indicated above we consider his explanation of the reason for doing so is entirely incomprehensible (as evidenced by this judgment an abbreviation for Andmorabance Ltd, Maiko Trade OU and Marcus Millebourg was easily found). However, we do not need to find an explanation for the decision to record everything as "cf" in order to determine this appeal. Whatever the reason for doing so every entry made as "cf" which was not in respect of a purchase from the corporate entity Credit Foncier is mis recorded in the stock book. Use of the margin scheme was precluded for each such entry in accordance with Notice 718.

189. We do not accept ZC's evidence that he believed there to have been practical compliance with the terms of Notice 718 paragraph 5.2. "cf" was used for all Mariana connected companies; as such, and without refence to individual purchase invoices it was impossible for ZC, HMRC and us to know who the supplier was. We consider that it is abundantly clear that the stock book is the principal record which must be kept ensuring margin scheme compliance and it must therefore be accurate. An entry which grouped supplies of at least 6 suppliers under one identifier cannot objectively have been considered to be compliant with the requirements under the scheme.

Use of margin scheme for goods purchased as acquisitions/imports

190. As accepted by A&M any invoice which referenced Article 138 PVD or the corresponding domestic implementation of that provision and/or which showed VAT as calculated as due at 0% were taxed by the supplier as an intracommunity supply and the

onward supply of any watch purchased in these circumstances was ineligible to be taxed under the margin scheme.

191. In the periods 11/15, 11/17, 02/18 and 05/18 and by reference to the invoices reviewed by RP and AP the invoices from: Piccinini, Dimaxi, Gofas, Edwards Lowell Ltd, ARipa, Ubaldi, Galax, Tableros, Giemmeci, Pi, Think Time Ltd, Alexios Ousta, Vaggi Sergio and Supermaderas all showed, on their face, that they had been taxed as intracommunity supplies by reference to Article 138 PVD, the domestic implementing legislation and in many cases VAT due at 0%.

192. It is clear to us from the evidence that A&M deliberately chose to tax acquisitions of watches under the margin scheme rather than to tax them correctly on their full value. This conclusion is based on the following evidence:

(1) A&M now concedes that it incorrectly accounted for VAT on acquisitions;

(2) Until 2011 the A&M had correctly accounted for VAT on acquisitions;

(3) The need to account correctly for VAT on acquisitions was specifically raised with A&M in 2014, at which point both ZC and AHC confirmed that they would be accounted for correctly going forward, but they were not.

(4) In the March 2018 monitoring visit (at which ZC was present) EP confirmed that the margin scheme was used for any purchases where VAT was not shown on the purchase invoice.

193. In cross examination ZC refused to accept that he was aware that invoices referring to Art 138 were not margin scheme supplies. In the main, we do not accept that evidence. The vast majority of the invoices refer to Art 138 PVD, Notice 718 explains that a margin scheme declaration would be by reference to Art 313 PVD. Where the invoices did not refer to the PVD and only to domestic legislation we consider that ZC was either well aware that the supplies were not margin scheme supplies or deliberately turned a blind eye to the fact that they were not margin scheme supplies. A simple google search of “VAT Art 41 Italy” would have revealed that Art 41 implemented Art 138 and not Art 313.

194. The only exception we see could have been the invoices in Greek from Gofas which are substantively more difficult to read than invoices even in a foreign language that use roman characters. However, we consider we can take notice that for many years even telephones have had the ability to translate on them. Further, we consider that where a purchaser does not know the basis on which a supply has been made to them and it is inherently vital that the basis is established to turn a blind eye to doing so represents deliberate conduct.

195. A&M also accepted that the supplies from HBP and Leonardo Watch were imports from outside the EU on which import VAT had been claimed. ZC said he was not aware they were imports when completing the stock book but did know that the VAT had been declared as import VAT. We resolve this conflict of evidence against ZC. We prefer the evidence that he treated the onward supply of the watches purchased from these suppliers as margin scheme supplies either knowing or at least turning a blind eye to the fact that the purchases had been declared as imports and knowing that Notice 718 thereby excluded them from the margin scheme.

New v used goods

196. As to whether the goods themselves were eligible goods under the margin scheme, the Assessments are based on a conclusion that 11% of the goods purchased by A&M were both eligible goods and had been purchased in circumstances in which A&M was entitled to use the margin scheme. But that is not to determine what proportion of the remaining 89% of

goods were pre-owned goods and which might have been eligible for the margin scheme but for other features precluding the use of the scheme.

197. There is no question that HMRC had concerns that ineligible goods were being sold by A&M under the margin scheme and we consider rightly so. By reference to the evidence of EP goods were treated as preowned unworn whether or not the purchase invoices so stated. The training given to her was that all goods were margin scheme goods where the post-it notes indicated that the goods were unworn.

198. ZC denied that he was aware of the training which was given to sales staff. Whilst we are prepared to accept that ZC may not have witnessed the training given by his mother or others to the sales staff we do not accept that he was unaware of the basis on which it was given. He was aware that watches were generally described as "unworn" on the post-it notes and the sales invoices. He knew that sales invoices were all prepared on the basis that the margin scheme applied whether or not in respect of any particular watch it did so apply. We therefore consider that he cannot absolve himself on knowledge or responsibility that the process adopted from the moment the watches were received to the moment a sales invoice was completed in respect of them was aimed at supporting the sale of the watches under the margin scheme (whether or not such watches were so eligible).

199. Whilst there was some inference that the serial number of a watch might be used to establish that it was not new, we do not find that to be made out on the evidence. First of all there is no evidence that serial numbers were ever checked and certainly we were not provided with information or evidence that would have enabled us to make such a finding. We might have taken a view that a watch manufactured many years earlier had been previously owned but the indication from the Latvian authorities that in the mid-2010s Dimaxi were supplying stocks of new watches manufactured in 2008 is likely to have required us to have more concrete evidence of ownership for us to have concluded the point in A&M's favour.

200. As regards the contentious excerpt of the visit report for the 17 April 2018 visit and the recorded acceptance that 80% of watches were new. We consider that the note is at best ambiguous. The question is recorded as conflating new and unworn with the answer as indicating 80% of watches were new. Whilst, of course, we cannot know for certain we consider that there was either a miscommunication/misunderstanding or the note is not a full record of what was said. We consider it most likely that ZC did say, or at least meant, that 80% of the watches were unworn. On the evidence presented to us we consider it most likely that 80% were unworn but it is not the status of being unworn that qualifies for the VAT on the sale to be accounted for under the margin scheme. A new watch is unworn, and a watch purchased by a non-taxable person as an investment may well be unworn (or show no signs of wear) but only the latter watches may be taxed under the margin scheme. A watch purchased from an intermediary may be either new/unworn or unworn having entered into consumption. The question and the answer were therefore not ones which were particular meaningful in establishing whether the A&M incorrectly used the margin scheme.

201. We do not need to determine whether the watches purchased by way of acquisition/imports or from Mariana companies which were mis-recorded as "cf" were new as A&M has no entitlement to use the margin scheme for those watched in any event. However, and for completeness we note, by reference to the SCAC responses, that the watches sold by the following suppliers were not, on the balance of probabilities, used watches: Piccinini, Dimaxi, Gofas, Edwards Lowell, and Ubaldi. The Swiss authorities provided a similar confirmation that watches sold by HBP were also new. The SCAC report for ARipa indicates that this supplier sold both new and used watches and we cannot

therefore be as confident that all watched were new, though we consider it is more likely than not that at least some were new. As regards Ubaldi the Italian authorities identified one example of used goods, the others being of new goods; we note that none of the invoices stated that the goods were used. As with ARipa we conclude that it is more likely than not that some watches sold by Ubaldi were new.

202. Had our decision depended on a conclusion whether goods were new we consider that it would have been appropriate to have regard to the SCAC report responses. We acknowledge that the responses represent the view reached by an overseas tax authority by reference to the investigations they consider appropriate. However, on the basis that the strict rules of evidence do not apply we would not have excluded or ignored the evidence but may have placed less weight on those which expressed an opinion rather than recited a fact. Where there was evidence referenced that the goods were either new or used we would have been prepared to accept that evidence.

203. HMRC were particularly concerned that the watches sold by A'bance and Credit Foncier were not used goods. There was a very significant volume of such goods purchased from these suppliers, for Credit Foncier these were in the prescribed accounting periods up to deregistration on 31 December 2014 (and one invoice thereafter) and for A'bance from January 2015 through to its deregistration in February 2017 (when Maiko become the substantive supplier from Mariana's suppliers). Through the diligence of RP HMRC identified there were 541 watches purchased from A'bance in quarter 11/15. Of those 229 of the post-its provided warranty data. We have roughly evaluated that data and it indicates that 86 of the 229 warranties were activated contemporaneously with the sale by A&M (by which we mean within the period beginning a month before through to sometime after the sale by A&M). AP accepted that in these circumstances it was entirely reasonable to conclude that the watch was new. We therefore conclude that at least some, and possibly all, of the watches sold by A'bance were new. As all were described as preowned and sold subject to a margin scheme declaration, it is impossible to determine generally which were new and which were used; accordingly, we consider that HMRC were entitled, to conclude that all sales of watches purchased from A'bance should be excluded from the margin scheme as ineligible unless and until it was established that the watches were in fact preowned.

204. We were not provided with similar data for Credit Foncier. However, it is necessary for us to determine whether supplies made by Credit Foncier in the period from 1 September 2014 to the date on which it was deregistered (31 December 2014) are eligible (as not all these watches are excluded for other reasons). On the basis: (1) that almost immediately upon the deregistration of Credit Foncier Mariana introduced A'bance to A&M; (2) the fact that both Credit Foncier and A'bance traded from the same premises (apparently consecutively); (3) both companies used substantively the same format of invoice in terms of layout, typeface and rubric for the margin scheme declaration; and (4) each apparently acted as a wholesale intermediary for the same suppliers who each then delivered the watches directly to A&M, we consider it more likely than not that the pattern of trade of the two companies was the same and at least some, if not all, of the watches supplied by Credit Foncier were new. As such, and as for A'bance, we consider it is not unreasonable to conclude that all watches supplied through Credit Foncier should be excluded from the margin scheme as ineligible goods, subject to the production of evidence by A&M that the watches were preowned, none having then been adduced.

205. Based on the evidence of ZC we consider that he closed his mind to the possibility that the goods he was being sold by intermediaries were new and had never entered the chain of consumption. He accepted the description of the goods as preowned or used but was principally interested in selling only watches that were in exceptional condition and looked

unworn. It appears to us that the most likely scenario in which a watch looks unworn is when it is new. We accept that there are investors who buy and hold watches but for the margin scheme to apply those investors must be individuals/unregistered business and not VAT registered traders. We would expect that some care would need to be taken to verify that a watch had been purchased by an individual (rather than a trader) in such circumstances particularly when then sold by a trader wholesale or as an intermediary. ZC gave no evidence that he made any enquiry to establish that the goods were preowned and A&M cannot therefore establish that for any particular watch the decision to exclude it from the margin scheme was wrong.

Responsibility for preparation of VAT returns

206. There was a conflict of evidence as to the distribution of responsibility between ZC and AHC when completing the VAT return. ZC sought to contend that any inaccuracy in the VAT return was essentially attributable to AHC as a professional aware of the requirements of the margin scheme. AHC was clear that his instructions were limited, and he accepted that ZC had sufficient awareness of the margin scheme to have correctly recorded sales in the stock book. We prefer the evidence of AHC. AHC was not in the room when ZC gave his evidence; he openly responded to questions, he gave no sense that he felt vulnerable or exposed professionally and we believe that he was not so exposed. If we were to have any criticism of AHC at all we would say that it having been identified that VAT accounting for acquisitions had gone awry he could have sought to understand why acquisitions had apparently seemed to have ceased particularly in the context of supplier names that were plainly not traditionally English. But, in the end, it does not diminish ZC's responsibility for having provided records and instructions to AHC that led to the VAT returns being incorrect.

207. Accordingly, we conclude that ZC provided instruction to AHC to prepare the VAT returns by reference to the stock book and thereby directly determined the basis on which VAT declarations were made to HMRC. He did so knowing that the terms of Notice 718 had not been complied with in the vast majority of transactions and thus his conduct led directly and deliberately to the rendering of inaccurate VAT returns.

Annual accounts

208. A&M accepted that there was a very significant discrepancy between the annual accounts and the VAT returns. This was obvious on a simple comparison of the documents (as set out in paragraph 103 above). We find that there was such a discrepancy and that the turnover declared in the annual accounts more accurately reflects the turnover of A&M in the relevant period.

Best judgment

209. As indicated above whilst we generally accept RP's evidence there were answers given in cross examination which made little sense in the face of the evidence presented to him, for example:

> (1) his answer to why MTIC meeting visit stencil templates were used. As indicated in paragraph 76 RP said the template was a used as standard for post registration VAT visits. That is plainly incorrect, as demonstrated by the form of the 2014 visit reports alternative stencil templates are used. This was a standard template for a post registration visit by the FIS/MTIC team we do not understand why RP resisted what was a reasonably obvious conclusion;
>
> (2) his answers when challenged about the reference in the various SCACs to having inspected the goods. RP knew that he had not inspected the goods. He accepted this in cross examination. His answer that the reference to an inspection was by way of cut

and paste (easily proven to be wrong) or in error was difficult to understand in the circumstances. In this regard his evidence was not credible.

210. Despite this we do not consider that the integrity of RP (and thereby HMRC) can be impugned. As RP accepted there had been no inspection of the relevant goods and the statement was categorically wrong. As RP was not the author of any of the documents the error cannot be directly attributed to him, and Mr Kazakos did not put to RP that the error had been made by the authors in consequence of any inaccurate input from RP. We are concerned that each SCAC request in which the error was made is likely to have given a false impression of the HMRC investigation. However, whether the goods were new or used is a precedent fact. The EU tax authorities were asked to confirm the status of the goods and did so. Some confirmed the goods supplied to A&M were new and some confirmed that used goods had been supplied. As such we consider it to be an unfortunate but immaterial error. That does not excuse sloppiness on HMRC's part; it is their responsibility to ensure that when requests of this type under principles of mutual assistance (now usually under the provisions of relevant double tax treaties) are accurate.

211. We have carefully considered RP's evidence taken as a whole and by reference to the specific matters put to him and recorded above concerning bias. We wholeheartedly reject that RP was "out to get" A&M or ZC because of a preconceived prejudice associated with his having been to the premises as a child or arising from any previous trading activity of the business.

212. As regards RP's approach to the investigation generally, we find that RP's remit was to undertake the careful monitoring of A&M's business to identify whether it had correctly accounted for VAT in connection with sales of watches purchased through a complex network of suppliers. A&M initially denied any failures in its margin scheme accounting, later rescinded as it is now accepted that VAT was incorrectly accounted for in respect of all acquisitions and imports. That somewhat belated acceptance justified HMRC's concern that there were substantial VAT accounting errors requiring investigation.

213. Initial enquiries identified the use of what we consider to be highly suspect wholesale intermediaries for the purchase of significant volumes of watches. Mariana was said to have introduced A&M to suppliers with whom A&M already dealt. When Credit Foncier became deregistered for VAT in Cyprus an alternative intermediary (A'bance) operating from the same business park, using all but identical invoicing was offered as an alternative. When A'bance was deregistered Maiko were introduced (though we note that Maiko was not established in Cyprus and adopted a different format of invoicing – Maiko were however, never registered for VAT). Other intermediaries were also introduced who showed classic characteristics of fraudulent behaviour, using similar addresses and more particularly frequently changing bank accounts about which we consider it is reasonable to have expected A&M to be concerned given its status as a High Value Dealer for anti-money laundering purposes.

214. We accept what was conceded by RP, that in a traditional sense there was no evidence of MTIC fraud because real goods were being traded. There was, however, ample evidence that the supply chain selling to A&M was likely to represent a risk to the proper collection of VAT. Something which would have been obvious to A&M/ZC had they not deliberately turned a blind eye to it.

215. In this context, we do not find, that HMRC placed any particular reliance on GC's answer to the question discussed in paragraph 89 above. Whilst it was specifically identified in RP's witness statement, it is a neutral recitation of what is shown in the meeting note over 4 lines as part of a 47-page witness statement. Further, and in any event, ZC's answers in

cross examination were that he had no concerns dealing with a company that regularly changed its bank account and which had bank accounts in countries other than the one in which it was established. We consider that suppliers that have multiple bank accounts in different countries are objectively a matter of concern, and it is something that should concern any counterparty; HMRC would be rightly concerned if this was considered entirely innocuous as A&M and ZC appeared to think.

216. ZC and GC claimed that each supplier was thoroughly investigated before A&M would deal with them using private detectives, companies house, VIES etc. But there was no evidence at all that any due diligence was undertaken. Latterly ZC produced a small number of flight itineraries for trips to Italy, Switzerland and Lithuania but in our view, they provide nothing more than corroboration that ZC travelled to those countries. He may even have met the suppliers; but meeting a supplier is not the same as effecting satisfactory due diligence as to the integrity of that supplier, and whether they are involved in supply chain fraud, or not.

217. We reject Mr Kazakos's assertion that having appropriate due diligence documentation is never enough for HMRC who often assert that such documentation is manufactured as a fig leaf. We accept RP's evidence that such documentation is necessary but not always sufficient to represent a justified defence to an allegation of known or should have known where there is established supply chain fraud. RP's persistence in looking to ascertain what due diligence processes were adopted does not indicate to us a preconceived view of A&M's activities but represents a necessary part of a thorough investigation into A&M's entitlement to account under the margin scheme (either as a consequence of the simple mechanics or by way of abuse of it).

218. We find that the decision to assess for the full four-year period for which normal time limits apply, to have been founded on what later became the admitted errors in margin scheme accounting. No acquisitions had been declared since 2011 and their absence had been raised in a VAT visit in July 2014 (prior to the start of the period covered by the Assessment). Annual account discrepancies were also identified throughout the entire period. We consider it entirely reasonable to conclude given those errors that all errors later identified in the examined quarters were likely to have subsisted throughout the period from 1 September 2014.

219. On the evidence before us and taken as a whole, we do not consider the RP/HMRC's conduct at any point during the investigation bore the hallmarks of being dishonest, vindictive, capricious, unreasonable or without basis. On the contrary we consider that RP was thorough and diligent. His response to the expert report went above and beyond that required of him or any HMRC officer.

Evidence of involvement in fraudulent transactions

220. As indicated above we do not need to determine this issue however, we record our findings on the evidence before us to assist the Upper Tribunal in the event of any appeal. We deliberately do not draw any conclusions from these findings as we have no need to.

221. HMRC's presentation of the evidence in this case was not that usually followed in a supply chain fraud case. There was no deal chain analysis presented. However, Ms Vicary contended that with respect to each of the suppliers who were not registered for VAT for some or the whole of the period (Credit Foncier, A'bance, Maiko, Oriamo and PLD) each of the supplies made to A&M purportedly under the margin scheme demonstrated a tax loss. This was not a complicated case of tracing deal chains; the tax loss arose on the supply to A&M and had been confirmed by the relevant overseas authority. We agree.

222. On the processes adopted by A&M in the context of a risk of supply chain fraud we find:

(1) There is no evidence to support the assertion recorded in the meeting note that GC or Mariana undertook supplier checks. There is no evidence that detectives were ever employed. We find that detectives were not employed to check suppliers.

(2) As set out in paragraph 60 the HMRC monitoring report for 08/02/2018 records that "the Accountant said he always checks VIES". That correlated with ZCs evidence before this Tribunal. However, when giving evidence AHC said that he did not check VIES except when asked, the number of times he had been asked was limited and predominantly prior to 2013. The meeting note was not put to AHC. On balance we accept AHC's sworn testimony that he did not check VIES because he was not asked to. We prefer this evidence to the answer recorded in the meeting note because we consider that the meeting note is not precisely clear as to who "he" was, it might have been a reference to ZC and might have been a reference to AHC. However, we consider that at the meeting A&M were likely to have been keen to reassure HMRC that their due diligence processes were adequate and less likely to have reflected the true position than the evidence given in this Tribunal.

(3) We find that no relevant background checks were undertaken into suppliers. There is no record of any companies' house search or other investigation. ZC persistently reassured HMRC during the monitoring visits that due diligence was undertaken and the need for it appreciated and yet in period 08/18 after A&M had been in trader monitoring for 5 months, when Oriamo and PLD was first used as suppliers there was no evidence of any due diligence having been undertaken. In our view A&M were at best cavalier and at worst knew or strongly suspected turning a blind eye to the risk that their suppliers were acting unlawfully.

DISCUSSION

223. In the end this matter was one which was easy for us to determine.

Best judgment

224. As set out in paragraphs 9 to 13 it is a very high hurdle for an appellant to jump to satisfy a Tribunal that an assessment is not made to best judgment. The hurdle will be higher still where the expert tendered on behalf of the taxpayer accepts that there were material inaccuracies in the VAT returns rendered leading to a substantial underpayment of tax which would go unrecovered following a finding that the assessment were not to best judgment. That is not to say that even in such circumstances a contrary to best judgment finding would be precluded where the evidence supported vindictive, dishonest or capricious behaviour by HMRC. However, here, there is no such evidence. As we have determined RP was diligent and thorough. HMRC had legitimate concerns regarding A&M's use of the margin scheme generally and specifically and there was a wider concern that A&M were participants in fraudulent supply chains. We consider that the investigation was proportionately carried out considering these concerns and the Assessments raised in exercise of best judgment.

Quantum

225. There is no legal entitlement to use the margin scheme for purchases made by way of acquisition or import with the consequence that sales of watches purchased from Piccinini, Dimaxi, Gofas, Edwards Lowell, ARipa, Ubaldi, Galax, Tableros, Giemmeci, Pi, Think Time ltd., Alexios Ousta, Vaggi Serio and Supermaderos or any other supplier selling to A&M by way of intracommunity supply.

226. In view of our findings of fact we consider that A&M incorrectly recorded all the Mariana companies as "cf" in the stock book thus depriving themselves of the entitlement to use the margin scheme in connection with any purchases of used watches made from those suppliers.

227. In addition to the reasoning at 226 there was no entitlement to use the margin scheme on sales by Maiko because it was unregistered for VAT, a matter which could easily have been verified by A&M by undertaking a VIES check.

228. Similarly, there was no entitlement to use the margin scheme for MM, Oriamo, PLD and Credit Foncier (in the latter case from 1 January 2015).

229. It therefore follows that HMRC's decision with regards to each of the suppliers for which they refused the use of the margin scheme was correct in the periods they examined, and we need not consider whether any of those watches were new and/or whether there was fraud in the supply chain of which A&M knew of should have known.

230. However, as set out in paragraphs 196 to 205 we also consider it more likely than not some or all of the watches were new.

231. We consider that it was entirely reasonable for HMRC to extrapolate their findings to all periods 1 September 2014 to 31 August 2018. This is on the basis that in that period A&M had not accounted correctly for acquisitions; A&M have not contended that the group of suppliers from which they purchased varied materially, though there was a change in the identity but not business operation of the companies introduced by Mariana particularly Credit Foncier, A'bance and Maiko. There was also an annual accounts v VAT return discrepancy throughout the period.

232. We reach this conclusion acknowledging that in the period from 1 September 2014 to 31 December 2018 Credit Foncier was a supplier who was registered for VAT and whom we understand provided invoices which, on their face, were compliant. Nevertheless, and for the reasons set out in paragraph 204 above we consider that there is sufficient uncertainty that the sales were of used goods that extrapolation to that period is reasonable.

233. We therefore conclude that there is no evidence on which we can conclude that the quantum of the assessment is overstated.

Penalties

234. As set out above we find that A&M, through the actions of ZC deliberately (actual or blind eye):

(1) Used the margin scheme for goods purchased by way of import or acquisition;

(2) Mis-recorded in the stock book the name of the supplier of all purchases bought from Mariana connected companies other than Credit Foncier;

(3) Recorded new purchases as "unworn" and then accounted for all unworn stock as preowned.

235. A deliberate penalty is therefore appropriate.

236. Little was submitted about the inaccuracies in respect of purchases made by way of acquisition/import. In contrast, much was made by Mr Kazakos of the apparent compliance of invoices by A'bance and Credit Foncier (until each was deregistered) and Ibercaja with the terms of the margin scheme. It was said that each of the invoices bore all the hallmarks of a legitimate margin scheme invoice: each was from a trader which was, at the time, registered for VAT, contained the usual particulars for a VAT invoice, a description of the goods as pre-owned and a margin scheme declaration.

237. So it was put, A&M were perfectly entitled to rely on the invoice when making onward supplies of the goods under the margin scheme. Those submissions, taken alone, would call in to question the actual or imputed knowledge of A&M/ZC. It is certainly correct that a trader who has undertaken all appropriate due diligence regarding a supplier is entitled to rely on invoices at face value.

238. However, for the reasons already given the inaccuracies in VAT recording sales as margin scheme supplies were deliberately made. That conduct cannot be excused or ignored because, on his evidence AP indicated that whilst working for HMRC he might have permitted records to be amended or purchase invoices to be belatedly issued. He accepted there was no legal basis for him to have provided such facilitation and it is not within our jurisdiction to consider whether HMRC might, in other circumstances, have offered such a facilitation.

239. Therefore, on the facts as we have found them, we have no hesitation in concluding that the inaccuracies in the returns and which are assessed by way of the Assessments were brought about deliberately through the conduct of ZC. Accordingly, HMRC were entitled to issue the PLN pursuant to paragraph 19 Schedule 24 FA 07. Of course if A&M pay the penalty HMRC will have no cause to look to ZC to collect it but that will be a matter between him and A&M.

240. We have no hesitation in rejecting the submission made at paragraph 171 above. The power to issue a PLN requires only that a deliberate penalty issued to a corporate entity be attributable to the behaviour of the company officer to whom the notice is issued. HMRC have the power to issue a PLN irrespective of the financial standing of the company and do not need to justify their decision on any other basis.

241. For completeness and absent any submission that the mitigation permitted was insufficient we consider that a 40% mitigation of the penalty for telling, giving and helping was a fair reduction in the circumstances. We do so despite the apparent acceptance by RP that ZC had volunteered information at meetings. We are not clear that the information was volunteered as the meeting notes indicate that the officers were working through SCAC reports which mentioned the parties about which it was asserted ZC had volunteered information. However, and in any event, HMRC gave 40% mitigation which, in our view, adequately reflected any information which was volunteered.

RIGHT TO APPLY FOR PERMISSION TO APPEAL

242. 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.

AMANDA BROWN KC
TRIBUNAL JUDGE

Release date: 20th AUGUST 2024