



[2021] UKFTT 115 (TC)

TC08096

VALUE ADDED TAX – appeal against decision to deny right to deduct input tax – HMRC case argued on “alternative” basis: Kittel and “no supply” – application for disclosure of bank statements and purchase invoices held by HMRC – documents sought obtained by HMRC as part of ongoing criminal investigation – documents relevant as related to pleaded fact of circular deal supply chains – documents required for fair determination of issues in the case – application granted

**FIRST-TIER TRIBUNAL
TAX CHAMBER**

Appeal number: TC/2019/00054 A

BETWEEN

VNS WASTE SOLUTIONS LIMITED

Appellant

-and-

**THE COMMISSIONERS FOR
HER MAJESTY’S REVENUE AND CUSTOMS**

Respondents

TRIBUNAL: JUDGE ZACHARY CITRON

Following a case management hearing by telephone (on 7 December 2020), the Tribunal issued directions (on 15 December 2020) asking for further submissions from HMRC on the appellant’s application for disclosure of documents; the appellant was given the opportunity to make comments on such submissions (the deadline for which was subsequently extended). HMRC’s submissions were sent to the Tribunal on 29 January 2021; the appellant made written comments on 30 March 2021. At the case management hearing I heard Mr Sherratt QC, counsel, instructed by the Khan Partnership LLP, for the appellant and Ms Goldring, counsel, instructed by HMRC Solicitor’s Office, for the respondents. The documents to which I was referred at the hearing were a case management bundle and an authorities bundle, both electronic, prepared by the respondents (553 and 441 pdf pages respectively).

DECISION on a CASE MANAGEMENT MATTER

1. This is a decision on an application by the appellant for disclosure of documents held by the respondents (“HMRC”).
2. The context is a consolidated appeal in the “complex” category against two decisions of HMRC of 26 November 2018:
 - (1) a decision (the “input tax disallowance”) to deny the appellant the right to deduct input tax arising on supplies of mixed waste made to the appellant by Construction Supplies and Consumables Ltd (“CSC”) in 29 transactions or “deals” between 24 October 2016 and 28 June 2017; the input tax at stake was £1,818,419.09; and
 - (2) a decision to deregister the appellant from VAT on the basis that it used its VAT registration solely or principally for fraudulent purposes.
3. HMRC state their case on input tax disallowance on an alternative basis; their primary argument (the “*Kittel* case”) is that input tax arising on the supplies is not allowable under the principles in *Axel Kittel v Belgium State*, *Belgium State v Recolta Recycling SPRL* C- 439/04 & C-440/04 (“*Kittel*”) – namely, that the appellant knew or should have known that the supplies were connected with the fraudulent evasion of VAT; their alternative argument (the “no supply” case”) is that the supplies did not in fact occur (and therefore did not give rise to any input tax).
4. It was common ground that the burden of proof falls on HMRC as regards the *Kittel* case. In a decision on a preliminary issue released on 16 March 2021, the Tribunal decided that the burden of proof as regards the “no supply” case lies with the appellant.

THE APPLICATION

5. By application dated 23 November 2020 the appellant sought “specific disclosure” of the following documents to the extent held by HMRC (the “Documents”):
 - (1) bank statements of
 - (a) CSC for October 2016 to January 2017
 - (b) T Davies Utilities Ltd (“T Davies”) for October 2016 to January 2017
 - (c) Chip Logistics Ltd (“Chip”) for October 2016 to August 2017
 - (2) purchase invoices in respect of purchases made by CSC from T Davies or Chip that relate to the subject matter of the deals.

I refer in what follows to certain of the Documents by reference to the above numbering e.g. “Documents (1)” means the Documents in subparagraph (1) above.

FURTHER FACTUAL BACKGROUND

Ongoing HMRC criminal investigation

6. In addition to the investigation by HMRC that led to the decisions which are the subject matter of this appeal (which HMRC refer to as their “civil investigation”), HMRC are conducting an ongoing criminal investigation into suspected laundering of proceeds of crime. HMRC have separate teams for the civil and criminal investigations. Two directors of the appellant were arrested and interviewed on 11 July 2019 as part of this criminal investigation. The criminal investigation involves a number of suspects and companies and has been going on for a number of years. As at 29 January 2021 (the date of HMRC’s submissions), the case had not been submitted to the Crown Prosecution Service for formal charging advice, but such submission was thought by HMRC to be “imminent”. Any file would take some months to be considered by the Crown Prosecution Service.

Documents obtained by HMRC for civil vs criminal investigations

7. In summary, the Documents are material obtained by HMRC for their criminal investigation rather than for their civil investigation. In further detail:

(1) HMRC obtained, as part of their civil investigation, CSC's bank statements for 31 January 2017 to 1 August 2017. These were disclosed to the appellant as an exhibit to the second witness statement of Lee Bell, an HMRC officer, dated 13 March 2020.

(2) HMRC obtained, as part of their criminal investigation, CSC's bank statements for October 2016 to January 2017 (i.e. Documents (1)(a)). As HMRC do not intend to rely upon (or produce) those bank statements for the purpose of this appeal, they did not include them in their list of documents pursuant to r27 Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules 2009.

(3) As regards Documents (1)(b) and (c), HMRC's submissions stated that these documents are not held by their civil investigation team – but do not say whether or not they are held by any other part of HMRC (e.g. their criminal investigation team).

(4) As regards Documents (2)

(a) HMRC's submissions stated that documents of this description held by their civil investigation team were served with Mr Bell's CSC witness statement dated 24 December 2019 (they cite paragraph 61 and exhibits 34 and 35)

(b) It appears from the statement of case (paragraphs 43 and 46, quoted at [9] below) that HMRC has disclosed documents of this description relating to 11 of the 29 deal chains (deals numbered 1, 3, 4-6 and 8-13)

(c) Documents (2) therefore comprise purchase invoices relating to the other 18 deal chains. HMRC's submissions stated that they are unable to say whether these documents are held by any other part of HMRC (e.g. their criminal investigation team).

HMRC's case in the appeal

8. Under the heading, "Summary of the Respondents' case", the (further amended) statement of case says:

"29. The Respondents' case is that VNS' transactions traced back to a fraudulent VAT default and the Appellant knew or should have known of the connection to the fraudulent tax loss.

30. In the alternative the Respondents' case is that the right to deduct is refused on the basis that there was no taxable supply to VNS."

9. Under the heading "Tax loss, fraud and connection", the statement of case says (inter alia):

"42. Each transaction, which is the subject of this appeal, has been traced back from VNS via [CSC] to the fraudulent defaulting trader [T Davies].

43. Although HMRC do not hold some of the invoices for T Davies, based upon the pattern of transactions in the other deals, on the balance of probabilities the chain of supply commenced with T Davies. In addition, the VAT summaries provided on behalf of CSC demonstrate that T Davies was the main supplier to CSC by a considerable value. At Deal 25 this is the first instance where VNS supply [Chip] as opposed to T Davies.

44. The Respondents case is that the chain of supply is:

T Davies - CSC - VNS - T Davies/ Chip Logistics.

45. The Respondents have denied input tax on 29 deals.

46. The paperwork for Deals 1,3,4-6,8-13 traces as follows in a carousel:

T Davies - CSC - VNS - T Davies

47. The paperwork for Deals 2,7,14-24 traces as follows:

CSC - VNS - T Davies

48. The paperwork for Deals 25, 26 and 27 traces as follows:

CSC - VNS - Chip Logistics

...

49. The paperwork for Deals 28 and 29 traces as follows:

CSC – VNS”

The appellant’s case in the appeal

10. The amended grounds of appeal state:

“7. The Appellant puts the Respondents to proof of chains in relation to their contention that the Transactions are connected to the fraudulent evasion of VAT. The Respondents have failed to particularise the supply chains or where the fraudulent evasion of VAT has occurred.

8. The Appellant puts the Respondents to strict proof of the chains of supply said to lead to the fraudulent evasion of VAT, including (but not limited to):

8.1. the integrity of those chains;

8.2. the evidence of due diligence undertaken by the parties in each of those chains;

8.3. the integrity of the documents relied on by parties in those chains in support of their respective claimed rights of deduction;

8.4. the proportionality of allowing other parties in those chains to exercise their right of deduction of input VAT and the denial of that right to the Appellant;

8.5. the existence of a tax loss in those chains; and

8.6. the fraudulent nature of the tax loss in those chains.

9. The Appellant denies the allegation that, at the time when it entered into the Transactions, the Appellant had, or had the objective means to acquire, the requisite knowledge, the Respondents are put to strict proof of:

9.1. whether it is alleged that the Appellant (a) knew of the fraudulent evasion of VAT, and/or (b) had the objective means to know of that fraud (or intended fraud), and whatever the case, will be put to strict proof thereof in every particular;

9.2. insofar as not comprised within 9.1 above, any further facts and matters relied on by the Respondents to support the conclusion that the Transactions formed part of the fraudulent evasion of VAT;

9.3. insofar as it is alleged that the Appellant had the objective means to acquire the requisite knowledge, what fact(s) in the real world it is alleged that the Appellant should have known, and how it is said that it should have acquired that knowledge.”

11. In the application, the appellant said that its case was that it genuinely believed it was engaged in a legitimate supply chain, which it understood to be: CSC – VNS – T Davies (and later Chip) – “Broad”. It said the appellant and its investors were victims of a sophisticated fraud by its trading counterparties; it believed its funds were used “effectively in a carousel to gain the appellant’s confidence before dissipation by the counter-parties”.

RELEVANT LAW

Tribunal procedure rules

12. Under r5(3)(d), the Tribunal may by direction require a party to provide documents to the Tribunal or a party.

13. Under r16(1)(b), the Tribunal may order any person to produce any documents in that person's possession or control which relate to any issue in the proceedings.

14. The Tribunal must seek to give effect to the overriding objective – being to enable the Tribunal to deal with cases fairly and justly – when it exercises any power under the rules or interprets any rule or practice direction (r2(3)). Dealing with a case fairly and justly includes (inter alia)

- (1) dealing with the case in ways which are proportionate to the importance of the case, the complexity of the issues, the anticipated costs and resources of the parties (r2(2)(a))
- (2) avoiding unnecessary formality and seeking flexibility in the proceedings (r2(2)(b))
- (3) avoiding delay, as far as compatible with proper consideration of the issues (r2(2)(e)).

***McCabe v HMRC* [2020] STC 2148 – recent Upper Tribunal (“UT”) authority**

15. The UT considered, insofar as they were relevant to the appeal before it:

- (1) what principles were material to disclosure of relevant documents in the case
- (2) what does ‘relevant’ mean and can a document be of ‘low relevance’

16. The UT at [22] agreed with the First-tier Tribunal (“FTT”) that in a ‘high-value complex dispute’ the starting proposition was that HMRC should disclose relevant documents to the taxpayer unless there was a good reason not to.

17. The UT said at [23] that the FTT must exercise its discretion to order additional disclosure under r 16 so as to give effect to the overriding objective: r 2(3)(a). That objective of dealing with a case fairly and justly includes dealing with it in a way which is proportionate

18. Relevance is to be assessed by reference to the issues in the case and the positions of the parties: [25]

19. There are degrees of relevance: “There is clearly a substantive difference between, say, a document which is agreed to be probative of a primary fact pleaded by one of the parties and one which might possibly prompt a train of enquiry by the other party. The FTT could not discharge its duty to take into account the overriding objective if it was forbidden to distinguish between these two examples of different degrees of relevance in considering the need for and proportionality of the disclosure sought” - [35].

20. At [37] the UT said “ it is appropriate for the FTT to evaluate and weigh the likely effect on the determination of the case of ordering disclosure of a document. The starting point in the FTT in a complex, high-value case may be that a document which is relevant (in the broadest sense) should be disclosed unless there are good reasons to the contrary, but that is only a starting point. On an application for disclosure, the tribunal will need to consider the degree of potential relevance of the document and whether there is a need for disclosure in order to enable a fair determination of the issues to take place. Further, in taking into account the overriding objective, what might amount to ‘good reasons’ for refusing to order disclosure of documents that are relevant are likely to differ depending on whether a document is

materially adverse to a party's case or merely a background document or one which might lead to a train of enquiry."

PARTIES' ARGUMENTS

21. The appellant submitted the Documents were relevant material which might advance its case or undermine HMRC's case, as they touched on the circularity of the deal chains (as pleaded by HMRC) and shed light on the wider fraud of which the appellant claimed to be a victim.

22. HMRC's primary argument was that the Documents were not relevant to the appeal and that the application was a "fishing expedition". They submitted that if the appellant considered that HMRC's case as regards the deal chains was undermined due to Documents (1)(a) not being produced, then the appellant could assert that in the course of the proceedings; and Documents (1)(b), (c) and (2) had no relevance to the appellant's state of knowledge, the main issue in the *Kittel* case.

23. In their written submissions of 29 January 2021, HMRC submitted that disclosure of the Documents would adversely impact their ongoing criminal investigation; and that disclosure of Documents (2) would be disproportionate in the circumstances. In further detail, they submitted that:

(1) provision to the appellant of any material currently held by their criminal investigation team at this "pre-charge" stage "carries a real risk of impeding the success of the criminal investigation";

(2) it would be "inappropriate" to disclose material that has been obtained for the purposes of their criminal investigation before HMRC decide what information will be relied upon as evidence (if a prosecution is brought);

(3) there was "concern" that disclosure of material from their criminal investigation at this stage will mean that criminal suspects may obtain the material and be in a position to "frustrate or influence" HMRC's criminal investigation;

(4) their criminal team and the Crown Prosecution Service were treating all suspects and their representatives the same way - disclosure of material to the appellant would undermine this position "as one suspect could claim to have material that the others do not, which has adverse consequences for the criminal investigation".

24. HMRC said that if bank statements were disclosed, they would redact them to show only the appellant's transactions.

25. As regards Documents (2), HMRC submitted:

(1) they could not confirm whether these Documents were held by their criminal investigation team, as they were working with a large amount of material (including from approximately 60 mobile phones and 40 computer devices), consisting of several million "strings of data"; they said the material was not readily searchable and extractable;

(2) they needed to prioritise making a charging decision;

(3) consequently, they could give no useful time estimate for attempting to conduct the required searches for Documents (2); and

(4) therefore, even if Documents (2) were relevant (which HMRC did not accept), the time and resources required to locate and disclose them would be disproportionate in the circumstances.

26. HMRC said that if the Tribunal orders disclosure, they would be likely to seek a stay of proceedings pending a charging decision. They would not however make this application for now, pending the Tribunal's determination of whether the material sought is otherwise disclosable.

DISCUSSION

27. I begin by considering the relevance of the Documents, by reference to the issues in the case and the positions of the parties.

28. The issues in the case as regards input tax disallowance are

(1) as regards the *Kittel* case, whether there was a tax loss due to fraudulent evasion of VAT and, if so, whether the appellant knew, or should have known, that the deals were connected with such fraudulent VAT evasion;

(2) as regards the "no supply" case, whether supplies of waste were in fact made to the appellant.

29. One of the facts pleaded by HMRC is that all 29 deal chains were circular, with T Davies (and later Chip) being not only the appellant's customer (as is common ground) but also the supplier to CSC (the supplier to the appellant in the deals). The appellant is putting HMRC to proof on its case generally, and on the deal chains in particular.

30. The circularity of the deal chains is not itself an issue in the case but is, in my view, an important fact in the determination of those issues. This is because circular deal chains can be an indicator of fraud, and, furthermore, it is well established in *Kittel*-related case law that the taxpayer's state of knowledge regarding VAT fraud in a chain of supply can, and, where appropriate, should, be inferred from the surrounding circumstances – and a circular deal chain is the kind of surrounding circumstance from which such inference might be made.

31. In my view the Documents are relevant to, and potentially probative of, the circularity of the 29 deal chains as asserted by HMRC. I accept that bank statements (Documents (1)) record movements of money and not supplies of goods or services as such – but movements of money are, at a minimum, a significant indicator of such supplies. Purchase invoices (Documents (2)) are more direct documentation of a supply.

32. My starting point here is therefore the one described in *McCabe*: relevant (in the broadest sense) documents in a high-value, complex appeal (like this one) are to be disclosed, unless there is a good reason not to. I now consider the degree of potential relevance of the Documents and whether there are good reasons not to disclose them.

33. In my view the degree of potential relevance is high: the circularity of the deal chains is a pleaded fact in the case, and the Documents are potentially probative of that circularity; equally, the Documents might contain evidence against circularity of the deal chains (for example, if Documents (1) do not show payments reflecting the deal chains, or if Documents (2) do not exist or refer to different subject matter to that in the deals). The likely effect on the determination of this case of requiring disclosure of the Documents is in my view material: it may well confirm or undermine HMRC's case that all the deal chains were circular and cast meaningful light on the alleged fraud. In my view, the Documents do not fall into the less important categories of documents mentioned in *McCabe*, such as mere "background documents" or those which might lead to a train of enquiry.

34. HMRC's submissions as summarised at [23] and [25] above give reasons not to disclose the Documents. It is difficult for the Tribunal to evaluate HMRC's assertion that disclosure of the Documents raises a "real risk" of prejudicing their criminal investigation – on the face of it, it seems somewhat surprising that disclosure to the appellant of such "straightforward"

documents as bank statements and purchase invoices, in circumstances where documents of a similar character have already been disclosed to it (because similar documents were obtained in HMRC's civil investigation), should have that effect. But even if HMRC's assertions are taken at face value, the Tribunal is left with its overriding objective of dealing with the case before it fairly and justly. Hence the test, as was said in *McCabe*, is whether the Documents are required to enable a fair determination of the issues in this case. In my view, given their high degree of relevance, they are.

35. As for the time and effort that HMRC say they will have to expend to identify Documents (2): the Tribunal, again, cannot easily evaluate HMRC's assertions – although it again seems somewhat surprising that HMRC have no reasonable means of searching through the large volume of information that they have gathered, given that one would have thought they would have developed some reasonable method of searching through it, in order to progress their criminal investigation. However, in my view, given the Documents' high degree of relevance to the case, and the fact that this is a high-value complex case, it is proportionate to require disclosure of Documents (2) as well, provided HMRC are given a reasonable period of time.

DECISION

36. The application is granted: the Tribunal will give directions, on or around the date of this decision, that HMRC provide the Documents (or submit a written statement that they are not in their possession or control) within eight weeks (which I consider a reasonable amount of time, given the logistical difficulties HMRC describe). Documents (2) shall be referred to more specifically in the directions, as “purchase invoices in respect of purchases made by CSC from T Davies or Chip that relate to deals 2, 7, and 14-29”; and HMRC will be permitted to redact documents to remove references to matters unrelated to the deal chains.

RIGHT TO APPLY FOR PERMISSION TO APPEAL

37. 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.

**ZACHARY CITRON
TRIBUNAL JUDGE**

RELEASE DATE: 16 APRIL 2021