



TC04024

Appeal number TC/2012/05937

VAT- dishonest retention of £586,448.24 in no 2 account- section 9 A Taxes Management Act 1970 enquiry gave rise to increase in income tax liability - non-disclosure of alleged zero rated sale of children's clothes- clothes fabricated through Italian manufacturer and Paris supplier – no record of sale of clothes through retail outlets – no evidence of actual clothes – appellant dishonest - assessment and penalty upheld – appeal dismissed.

FIRST-TIER TRIBUNAL

TAX CHAMBER

TARIQ MAHMOOD t/a PORT STREET FASHION Appellant

- and -

THE COMMISSIONERS FOR HER MAJESTY'S

REVENUE & CUSTOMS Respondents

**TRIBUNAL: JUDGE DAVID S PORTER
MISS SUSAN STOTT**

Sitting in public at Alexandra House, Manchester on 19, 20 and 21 May 2014

Mr Nigel Gibbon, a solicitor, appeared for the Appellant

Mr Luke Connell, a presenting officer, instructed by the General Counsel and Solicitor to HM Revenue and Customs, for the Respondents.

DECISION

1. Mr Tariq Mahmood (Mr Mahmood) appeals against the assessments raised by the Respondents (HMRC) on 12 January 2012 for undeclared VAT made under section 5 73 Value Added Tax Act 1994 (The Act) for the prescribed accounting periods from 02/04 to 01/09 in the sum of £406,989 and against a penalty of £284,892 arising there from. Mr Mahmood disputed that details of his sales of children's clothes had not been properly recorded but, even if they had, as the sales were zero rated no VAT needed to be paid and the assessment and penalty were not due. HMRC stated that Mr 10 Mahmood was dishonest in not disclosing the alleged zero rated sales and had not, on the balance of probabilities, established that the undeclared sales were sales of children's clothes and the appeal should be dismissed.

2. Mr Nigel Gibbon (Mr Gibbon), a solicitor, appeared for Mr Mahmood, who gave evidence and affirmed. He also called Mrs Gurmit Kaur (Mrs Kaur), who gave 15 evidence and affirmed. Mr Gibbon also produced some bundles for the Tribunal. Mr Luke Connell (Mr Connell), a presenting officer, appeared for HMRC and called Jayne Alison Charnock (Mrs Charnock), Andrew Myerscough (Mr Myerscough) and Robert Alan Lenagan (Mr Lenagan) all of whom gave evidence under oath. Mr Connell also produced several bundles prepared by HMRC.

20 3. We were referred to the following cases;

As to children's clothing:

- 2019. *Falcon Sportswear Ltd* MAN/85/374.
- 5760 *Mrs v Cassidy t/a Balou* MAN/90/884.
- 11267. *Charles Owen & Co (Bow) Ltd* MAN/92/623.
- 25 • 11663. *Daungate Ltd* MAN/93/373W.
- 17832. *Smart Alec Ltd* LON/01/1307.
- *CEC v Ali Baba Tex Ltd* 1992 STC 580.
- 18997. *Vidhani Brothers Ltd* MAN/04/0296.

- *H & M Hennes Ltd v CEC* 2005 STC 1749 (Ch D).
- 20758. *Fosters School & Leisure Ltd* LON/2007/1501.
- *Walter Stewart Ltd* 0-499/83.

As to dishonesty and evasion

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- *R v Gosh* [1982] 1QB 1053(CA).
 - *R v Dealy* [1995] STC 217 (CA).
 - *Barlow Clowes International Ltd v Eurotrust International Ltd* [2005] UKPC 37
 - *Mullarkey & Co v Broad & Co* [2007] EWHC 3400 (ch).
- 10
- *Sahib Restaurant Ltd v HMRC* M7X 090 9 April 2008 (ch).
 - *Patrick Conlon v R & C* [2008] UKVAT V20877.

The Law

4. Schedule 8 Value Added Tax Act 1994 (the Act),

Group 16 – Clothing and footwear

15 Item no.

1. Articles designed as clothing or footwear for young children and not suitable for older persons.
2.
3.

20 Section 60

60 (1). In any case where-

- (a) For the purpose of evading VAT, a person does any act or omits to take any action, and
- (b) his conduct involves dishonesty (whether or not it is such as to give rise to criminal liability),

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he shall be liable..... to a penalty equal to the amount if VAT evaded or, as the case may be, sought to be evaded, by his conduct.

60 (2). The reference in subsection (1) (a) above to evading VAT includes a reference to obtaining any of the following sums-

- 5 (a) a refund under any regulations made by virtue of section 13 (5);
- (b) a VAT credit;
- (c) a refund under section 35, 36 or 40 of this Act or section 22 of the 1983 act; and
- 10 (d) 9d) a repayment under section 39,

In circumstances where the person concerned is not entitled to the sum.

60 (3). The reference in subsection (1) to the amount of VAT evaded or sought to be evaded by a person's conduct shall be construed-

- 15 (a) in relation to VAT itself or a VAT credit as a reference to the aggregate of the amount (if any) falsely claimed by way of credit for input tax and the amount (if any) by which output tax was falsely understated; and
- (b) In relation to the sums referred to in subsection 2 (a), (c) and (e) above, as a reference to the amount falsely claimed by way of
- 20 refund or repayment.

60 (7) On an appeal against an assessment to a penalty under this section, the burden of proof as to the matters specified in subsection (1) (a) and (b) above shall lie upon the Commissioners.

The Facts.

- 25 5. Mr Lenagan gave evidence under oath and told us that he was a higher officer with HMRC dealing with enquiries into business tax returns. Mr Mahmood was the owner of Port Street Limited, which was incorporated on 20 June 2002 and which bought and sold ladies garments both retail and wholesale. We have been told that there had been a number of VAT visits to that company and on 9 October 2003 it

was identified that more money was being paid into the bank account that was being declared on the returns. As a result an assessment for £3,750 was raised for the period 1 February 2002 to 30 April 2003. On 29 March 2005 there had been a pre-repayment credibility visit, which concluded that there had been an over claim of imput tax of
5 £33,938.

6. On 5 February 2008, Mr Mahmood's tax return for the period 2005/6 was selected for enquiry under section 9 (a) Taxes Management Act 1970 because it included provisional figures, which had never been updated. A further enquiry was opened into the Tax returns for the period 2006/7 on 23 December 2008. The 2005/6
10 enquiry revealed:

- That Mr Mahmood had a no 2 account with Lloyds TSB numbered 5889080, which had not been disclosed to HMRC, containing £586,448.24 and which had been opened on 25 April 2004. Mr Mahmood made several suggestions as to why the sum had not been
15 entered in the accounts.
 - He suggested that the bankings had been made up of transfers between two accounts. Mr Grover, Mr Mahmood's earlier accountant from WG Ltd Accountants, New Mills, had conceded that Mr Mahmood's explanation did not appear to be correct.
20 ○ Then that some of the purchases invoices had been thrown in to his builders skip and he had been unable to recover them.
 - Mr Lenagan noted that the cost of sales in the accounts was £1.13 million and if Mr Mahmood's explanations were to be
25 believed, they gave rise to serious concerns as that amount was insufficient to sustain the sales. He advised Mr Mahmood that in view of the substantial discrepancies in the tax return he had arranged to extend the enquiry to his VAT returns.
 - As a result of the enquiry, Mr Grover advised that he was no
30 longer prepared to act for Mr Mahmood and he withdrew his services. Mr Tariq Khan of Tariq Khan & Co, accountants, was appointed to act for Mr Mahmood.

purchases it would be difficult to agree the zero rating. Mr Khan had suggested, by way of compromise, that perhaps 50% of the figure could be treated as children's clothes and therefore zero rated.

9. Mr Mahmood had provided evidence of the shops which had been open for the following periods:

- Burnley 1 December 2005 to 6 May 2006.
- Scarborough 21 June 2006 to 29 November 2006
- Nottingham 18 December 2006 to 27 April 2007
- Scarborough 20 June 2007 to 7 February 2008
- Bury 7 May 2007 to possibly 16 August 2008

10. Mr Mahmood had said at a meeting on 4 February 2009 with Mrs Charnock that:

- The customers purchasing from the shops had paid in cash.
- He had also received cash from the wholesale shop in Manchester of between £2000 and £3000 each week.
- Two members of staff had been employed in the Burnley shop which had been open for 6 to 7 months.
- The shops had been exclusively stocked with clothes for children aged 14 to 15 year olds.
- He also suggested that he had frequently paid his French suppliers in cash and paid the full amount by cheque on his return. He then collected the cash that he had paid on his next visit.

11. Mrs Charnock had questioned whether the shop in Burnley could have taken £1,000,000 in the short time that it had been open. If it had it was surprising that Mr Mahmood had not kept the shop open. Mr Khan had explained that the landlord had let the shop initially on a rent free basis for two months. She was not satisfied that the shops had generated the monies giving rise to the £586,448.24 as the Lloyds TSB Account had been opened in April 2004.

12. As Mr Mahmood had suggested that the supplies of children's clothing had come from manufacturers in France, she had arranged for Mr Myerscough to contact

the French authorities to make appropriate enquiries of those suppliers of which she had details. Mr Myerscough confirmed that he had checked 18 suppliers, who appeared to have made supplies in excess of £17,000 each to Mr Mahmood. Mr Mahmood had also obtained details of the supplier invoices from France. These
5 identified the clothes as 'jupe longue', 'T-Shirt dileme' and 'femme fille'. We are satisfied that the information provided through the VAT information Exchange System (VIES) with France, confirmed that children's clothing had not been supplied by the French suppliers. Mr Khan submitted that the French suppliers made no distinction between children's clothes and young adults, and the suppliers had
10 probably misunderstood HMRC's request of the French Authorities. Mr Mahmood maintained that all the clothes from his French suppliers were for children.

13. As a consequence of all her enquiries and the replies supplied by Mr Mahmood and his accountant, Mr Khan on 12 January 2012, Mrs Charnock confirmed the assessment of £406,989 of additional VAT due from Mr Mahmood
15 together with a dishonesty penalty of £284,892. Mr Khan had asked for a review which, when given on 2 May 2012, had upheld her assessment and the penalty.

14. Mr Myerscough gave evidence under oath as to his enquiries through the VIES from the French authorities and confirmed the evidence provided to Mrs Charnock. He had made further enquiries arising from additional supplier information
20 provided by Mr Mahmood. No further information had been made available as the amounts involved had been too small.

15. Mr Mahmood gave evidence and affirmed. Mr Gibbon had taken instructions from Mr Mahmood, at the Tribunal, as Mr Mahmood had not provided a witness statement. Mr Gibbon provided the Tribunal and Mr Connell with a manuscript copy
25 of Mr Mahmood's Statement and that of Mrs Kaur. Mr Mahmood told us that in the 1990s he was involved with a company, Bullet Jeans, where he was the company secretary. The director of the company was Pervaze Chaudary and the company manufactured and sold, on a wholesale basis, male and female jeans for adults and children. Mr Mahmood was employed to source fabrics, designs and customers
30 throughout the world. As a result, he had been constantly 'on the road'. Mr Choudary ran the administration and Mr Grover, of Messrs Ward Grover accountants, was the

accountant to the company. Mr Mahmood had had a disagreement with Mr Chaudhary over the financial administration of the company and he left the company.

16. Mr Mahmood formed Port St Ltd on 3 March 1999 and started trading as 'Port Street Fashion' wholesaling ladies and children's fashion wear with some men's clothing. He registered the business for VAT on 10 March 2000 on that basis. Mr Connell referred Mr Mahmood to the invoice of 8 August 2001 from Fashion Girls and asked whether the invoice was for children's or adult's clothes. Mr Mahmood answered immediately that it was for adults because of the amount of the VAT. There had been no hesitation in his reply. We were impressed that he could immediately identify the clothes from the VAT amount, showing a thorough understanding of the rates.

17. Mr Mahmood told us that he spent most of his working time 'on the road' and relied on his employees, including his younger brother Muhammad Asif, to look after the administration. He asked Mr Grover to act as his accountant and Mr Grover suggested that he appointed Mr Bailey as the firm's bookkeeper. For the first few months of the business Mr Bailey had his own office on the premises. Subsequently, he came to the office on a Thursday where he dealt with all the sales and purchase invoices together with the bank statements which were left for him on his desk. Mr Bailey was in his mid-70s and used a manual system as he was unwilling to convert the bookkeeping to a computerised system.

18. Mr Mahmood told us that one of his wholesale customers, 'Bliss Clothing' in Glasgow, had asked whether Mr Mahmood could supply similar garments to the adult ladies high fashion in children's sizes. Mr Mahmood had made enquiries of his suppliers, who confirmed that they could supply him with children's sizes in the age group 6 to 13. Mr Mahmood had stated earlier, in the meeting with Mrs Charnock on 9 February 2009 (see paragraph 10 above), that the children's clothes were manufactured for children up to 14 years old. The VAT limit for children's clothing is 13 years. He told us that he had an arrangement with Bliss Clothing' in which he effectively operated a concession within the Bliss' shop, selling the smaller sized garments. Bliss Clothing had operated the concession on his behalf and paid him a commission of 40% on the sales. In a letter dated 17 May 2013 K A Javid & Co

confirmed that the franchise arrangement had run from April 2004 to 31 March 2005. The letter carried a logo which stated '10 years of excellence' from 1990 to 2000. HMRC suggested that as a result of the dates specified on the logo the letter could not be relied on as evidence in 2013.

5 19. Mr Mahmood had suggested that some of the undisclosed payments to the Lloyds TSB Account, number 5889080' had come from this source. He had looked at the bank statement and he was able to identify three payments which referred to 'sundry and counter credit'

20. As a result of the concession with K A Javid & Co, Mr Mahmood had decided
10 that there was a market for reduced sized adult ladies fashions for children. He indicated that he had noticed that there was a gap in the market for children's clothes from 6 to 13 years. The large department stores catered for teenagers rather than the younger age group. As a result, he had opened a shop in Burnley and several others followed as indicated in Mrs Charnock's evidence at paragraph 8 above. He had been
15 unable to continue in the shop in Burnley because the landlord had wanted him to sign a 15 year lease and he was not prepared to do so. He had then opened a similar shop in Scarborough.

21. The shop in Burnley traded as 'TM Stores' as did all the others. He produced
20 confirmation of signage prepared for the shop by 'Budget Signsgraphics'. The signage included the words 'children clothing wholesale direct'. In cross-examination Mr Connell asked about the shops, what sort of tills they had and how the stock was financed. Mr Mahmood appeared to be unclear as to how the shops operated. He said that the staff provided him with weekly details of the stock sales and the till receipts.
25 At the end of each day, two readings were taken and these, together with a ticket from each sale, were put into an envelope marked 'TM Stores' and ultimately left on Mr Bailey's desk, weekly together with the bank statements for him to process them. Mr Mahmood knew the balance at the bank and deducted the overheads from the receipts. He re-ordered the stock every two months. The cash takings from the shops were paid
30 into the account numbered 5889080.

22. Mr Connell suggested that the bookkeeping was very poor. Mr Mahmood agreed, but blamed the failure on Mr Bailey his bookkeeper. Mr Mahmood accepted that he signed all the VAT returns, but he did not pay much attention to them as he relied on Mr Bailey. He conceded, however, that he had signed some of the returns in
5 blank and left them for Mr Bailey to complete. Mr Connell put it to Mr Mahmood that as over £3,000,000 had been paid into the bank account, Mr Mahmood must have known about it. He said that as he was always away buying stock he had left these matters to his staff. On the balance of probabilities we agree with Mr Connell. Mr Mahmood clearly knew how much money he needed to re-stock his shops. He also
10 knew how much he was expending with his European suppliers. He could not have run a business on the scale that he did without an intimate knowledge of its cash receipts.

23. Mr Mahmood explained how he purchased the clothes. The clothes were
15 children's clothes made from the design of fashion items for adults. In a letter dated 18 August 2011 addressed to HMRC Mr Mahmood had suggested that the fact that he was the registered holder of the trademark "Pinkiss" "fashionwear and headwear for female teenagers" indicated that he had acquired and supplied children's clothing. He explained that he sourced most of the children's clothes from France, as evidence
20 from his many trips recorded in his passport. He explained that when he went to Paris he would choose the clothes he liked from the adult range. He would then show them to his supplier and ask if they could make the same clothes but in children's sizes. The clothes were manufactured in Italy and when returned they were on hangers with the size indicated on a plastic tag attached to the hangers.

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24. In cross-examination Mr Connell suggested that the goods could not have been supplied with hangers as suggested by Mr Mahmood as they would have been far too bulky. Mr Mahmood disagreed and said that clothes were always supplied in this way. Mr Connell asked how Mr Mahmood could be sure that his order would be
30 completed correctly given that he did not speak any French and his supplier had to pass the information on to the Italian manufacturers. Mr Mahmood indicated that he

had 25 years' experience in the trade and he had never had any difficulty in obtaining the correct orders.

25. Mr Mahmood produced to the Tribunal samples of the types of clothing he said he had been selling in the shops. He said that the trousers were marked up in sizes 4, 6, 8 and 10 and the tops as small, medium and large. The sizes and washing instructions were sewn in by the manufacturers. We examined the clothing and it appeared that the washing instructions had been very clumsily over sewn onto the sizes. In fact on one garment the over sewn instructions covered the sizes. It appeared to us that the over-sewings must have been done in the shop, as they would have been much neater if they had been sewn in at the manufacturing stage. We found the evidence presented by the clothing to be unsatisfactory. We considered that the labels had been tampered with. We also have no means of knowing whether the clothes presented to us were the same as those purchased as children's clothes from Paris.

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26. In 2010 Mr Mahmood visited 23 of his suppliers and asked them to sign a document prepared by Mr Khan and dated 20 September 2010 The document is in English and reads:

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“TO WHOM IT MAY CONCERN

We the undersigned confirm and solemnly declare that Mr Tariq Mahmood t/a Port Street of Port Street Manchester UK M1 2EQ has been our customer for a number of years, and we further confirm that they bought mainly girl's clothing from us during 2005, 2006, 2007 and 2008. We also confirm that they have been honest and trustworthy in their dealings with us and we have established a very pleasant business relationship over the years.

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As their request for the copy invoices relate to the period over 2 years ago we are trying our best to provide them as much information as possible from our business records.

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Signed and with a Fantaisy stamp

Date 20/09/10

Mr Mahmood had asked them to confirm that they had supplied children's clothing and the suppliers understood his request as he appears to have been the only customer asking for clothes in such small sizes.

27. In 2013 Steve Howard, employed by 'The VAT People', drafted another
5 declaration for the suppliers to sign most of which appear to have been signed in April 2013 and which read:-

“Statement from French Supplier.

We the undersigned confirm that Mr Tariq Mahmood (trading as Port Street
10 Fashions) has been our customer from until.....Although this business made ladies clothing, Mr Tariq Mahmood requested that the business made the clothing that he ordered, to be worn by young girls aged from xxxs to L. It is solely the garments sized accordingly that we sold Mr Tariq Mahmood during the relevant period.

15 I confirm that the sizes made were smaller than the sizes listed on the attached schedule and I sign the attached schedule to confirm the point.

French translation

The same wording appears translated into French and the forms were signed as before.”

20 The schedule sets out the detail for zero rating and refers to sizes which, if the same would take the clothes outside the exemption, hence the comment that the clothes were of less size than those in the schedule. There followed a 4 page document, in English, identifying the usual sizes for Boys and Girls. The sizes are in cm and inches.

25 28. Mr Mahmood told us that the sizes were as follows:

	Trousers	Size 4 is for a 6 year olds. Size 6 for an 8 year olds. Size 8 for a 10 year olds.
30	Blouses	Size 6 = xxxs (very small) Small colours 8 year old = xxs

Small 10 year old = xs

29. Mr Connell cross-examined Mr Mahmood as to why on several of the individual declarations the staple holes did not match. He suggested that where the documents purported to be an integral document he would have expected the staple
5 holes on every leaf to match, which they do not. It was possible that Mr Mahmood had falsified the responses. Mr Mahmood suggested that they might have been unstapled so that they could be photocopied. We consider that there is insufficient evidence one way or the other as to whether the forms had been tampered with. However, we are satisfied that they are of little help to Mr Mahmood as they were
10 completed several years after the periods in question and his suppliers, anxious no doubt to keep his business, might have been prepared to sign the documents since the French do not appear to make a distinction between adult and children's clothes for VAT purposes.

30. Mr Mahmood produced six invoices from Sarl Why Not which described the clothes variously as 'Jupe', 'Jupe longue', 'Sous-pull longue', 'T-Shirt' and
15 'Turnique Pop'. The invoices are dated from 9 May 2005 to 20 February 2006. Why Not had been asked to confirm that the invoices related to children's clothes and they have written on them all 'confection femme fille', which he understood meant children's clothes. Unfortunately, this does not identify the clothes for children from 6
20 to 13 years. The legislation is very specific relating to the exemption as set out in Notice 714 and a general comment such as the above would not be sufficient to establish the sizes of the clothes. If Mr Mahmood had wanted to be sure that he would obtain the relief on children's clothes he should have ensured that the invoices carried the correct information.

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31. In cross-examination Mr Connell referred to a report of an incident arising from an interception, outbound at Cheriton, of Mr Mahmood's brother, Muhammad Asif, on 20 October 2002. Mr Asif had been in a Mercedes Sprinter Van registration number PJ02 UVB. The report indicates that Mr Mahmood had given his brother, Mr
30 Asif, £35,000 to purchase stock in France. Mr Asif had stated that he was a buyer for Mr Mahmood and that he, Mr Asif, travelled every week and that he had taken

£14,000 out previously. The vehicle had been stopped again on 27 October 2002 and Mr Asif had £43,000 in his possession. The report had been made because the officers were concerned that the monies should be accounted for in Mr Mahmood's books. Mr Mahmood confirmed that the vehicle belonged to him and that Mr Asif is his brother
5 but he had no knowledge of the event. He had had some family trouble around this time and he might have asked his brother to buy some stock for him .We have decided to ignore this evidence because it relates to period before this appeal; it has not been substantiated at the appeal; and no action appears to have been taken against Mr Asif and his colleague who was accompanying him.

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32. Mr Gibbon also called Mrs Kaur, who affirmed. Mrs Kaur had started working for Mr Mahmood at his warehouse in Manchester in April/May 2005. She was employed to sew labels on the clothes. When Mr Mahmood opened the Burnley shop in October 2005, she went to work there as a shop assistant. She said that the shop sold clothes
15 for children in ages 6,8,10 and 12 and in sizes xxxs to small. When cross-examined she confirmed that her wages had been paid by Mr Mahmood, who left the money in an envelope with her name on at the shop. She confirmed that the shop had a sign outside 'TM Stores Children's Clothes'. We note that the sign writer had included the words 'wholesale Direct '(See paragraph 21 above).

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33. She was, however, very vague as to what had been in the shop window, the colours in the window and number of mannequins (if any). She said that it was some time ago and that she could not remember. She could not remember how she worked the till nor did she measure the clothes. 12 to 13 year olds came into the store
25 accompanied by older friends or family. She suggested, but retracted the comment, that some adult clothes were sold in the shop. The garment sizes were on the label and the prices ranged from £10 to £15. She had moved to the Bury shop, which sold exactly the same clothes, in May 2007 until it closed in May 2008. We found Mrs Kaur's evidence less than satisfactory. She was extremely vague about the shop and
30 what merchandise it sold and said that as it was some 8 years ago she had difficulty remembering. Mr Gibbon had indicated that it was hoped that more members of staff would be available, but they did not materialise.

Summing up.

34. Judge Porter had requested written summations as there had been insufficient
5 time at the hearing for them to be presented verbally. Mr Connell and Mr Gibbon
agreed a direction, requested by Mr Gibbon, that Mr Gibbon should provide the
Appellant's submissions by 11 July 2014, which he did. The submissions run to 93
pages and it is proposed to summarise them.

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Mr Connell's submissions.

35. Mr Connell submitted that the issues in dispute were:

- Whether the clothing was designed as clothing for young children or not.
- If so designed, whether the clothing was not suitable for older persons.
- 15 • Whether Mr Mahmood had intended to evade tax or not.
- Whether that conduct was dishonest or not and
- Whether the section 60 penalty was excessive or not.

36. Mr Connell went through the background to the case, as now set out in the
facts above. He then considered the 9 (a) enquiry. He submitted that in the course of
20 the enquiry into his income tax and VAT affairs, and in his testimony at the trial, Mr
Mahmood advanced a series of explanations for the anomalies uncovered, all of
which were unconvincing, not least because he advanced different reasons at different
times. The list of excuses included the following:

- 25 1. "Lloyds TSB Euro account No.86240686 is my supplier's bank
account". On 12 December 2008 Mr Mahmood telephoned officer
Lenagan. He confirmed that he had hidden a second trading account,
Lloyds TSB Euro account No.86240686, for his firm Port Street Fashion
from his accountant.
2. "Balances account No.5889080 are inflated by inter-account transfers".

On 8 December 2008 at a meeting, “following discussions”, the accountant Mr Grover conceded that this explanation did not appear to be correct, there being little evidence of transfers between the two accounts. Mr Grover is now necessarily saying that Mr Mahmood concealed the existence of this second trading account from him and from bookkeeper Mr Bailey

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3. “Records were disposed of in error by a third party”.

On 17 December 2008 Mr Mahmood said that his records had been disposed of in error. But this time he did not say by whom. During his cross examination Mr Mahmood produced various documents from a briefcase. He clearly had kept certain records and had either selectively kept records, or had selectively released his records.

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4. “Children’s clothing: recent fabrication to explain undeclared turnover”. On 22 December 2008, in a telephone conversation with Mr Lenagan, Mr Mahmood, for the first time advanced the “children’s clothing” excuse. He effectively disclosed that he had concealed a retail trade carried on in the relevant period, through several retail outlets operating serially in different towns in the north of England. He also stated that from these retail outlets he supplied “teenage clothes”

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37. Mr Connell submitted that It would not avail Mr Mahmood to say that the “children’s clothes” excuse only became relevant once the direct tax enquiry had become an indirect tax enquiry. The concealed retail trading was as directly relevant to his personal income tax as were the two concealed trading accounts. The VAT zero-rating might be directly relevant to his VAT affairs, but it was indirectly relevant to his personal income tax as it is the difference between profit and loss. There had been several formal occasions prior to this date on which it would have been possible and appropriate to advance the “children’s clothing” explanation, but on which this explanation was not advanced:

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38. At a meeting on 4 February 2009, attended by officers Charnock (VAT) and Lenagan and by Mr Mahmood with his new accountant Mr Khan, Mr Mahmood

confirmed and supplemented his “children’s clothing” excuse. He said the shops were exclusively stocked with “teenage clothing, (ie), to an age range of 14 or 15 at the most and therefore all sales would be zero rated. He also conceded that no records of these sales had been kept in the ‘sales day book’, which had been made available to
5 HMRC.

39. On examination of the accounts, the figure of £595,379.72 representing “Euro purchases missing invoices” was a “balancing figure”. This means that it was in the nature of an estimate rather than a figure based on a complete set of trading vouchers.
10 Mr Connell submitted that, at best, this figure reflected purchases by way of cheques drawn on Lloyds TSB Euro account No.86240686. It would not reflect cash purchases, if any, from the Paris clothing suppliers. Mr Khan and Mr Mahmood treated this figure as reflecting zero-rated acquisitions. This figure was later revised to £614,702.18. Mr Khan was unable to reliably establish the true value of supplies of
15 clothing acquired by Mr Mahmood.

40. In his defence, Mr Mahmood had blamed his first accountant Mr Grover, and also suggested that his bookkeeper Mr Bailey had been overwhelmed by the amount of work he had to deal with and had therefore only recorded transactions that involved
20 VAT. Mr Mahmood had said he did not audit Mr Bailey’s work, but that he did check the weekly bank balance to determine what purchases etc he could make during the following week.

41. Mr Connell said that HMRC had queried whether the retail outlets could be
25 responsible for the large increase in sales in the period from when Lloyds TSB current account 2 No.5889080 or the Lloyds TSB Euro account No. 86240686 were opened in December 2004 to 1 December 2005 when the Burnley shop was opened. Mr Mahmood had been unable to explain the source of deposits into his trading accounts during those periods. Mr Mahmood’s VAT consultant, Mr Rayner had pointed out
30 that if the undisclosed turnover related to zero-rate supplies then there could be no section 73 tax assessment and no section 60 percentage-driven penalty for dishonest evasion.

42. Mr Connell referred to the various declarations from the Paris suppliers in relation to the children's clothes and submitted that, as they had appeared to have been tampered with, they were not reliable evidence as to their contents. In any event, HMRC had made its own enquires of the French Authorities, who had revealed that the suppliers questioned had not supplied children's clothes. Mr Mahmood had said that the clothes supplied to him by his Paris-based suppliers were in fact small sized European garments that in the UK are equivalent to a child's size". Nor had HMRC been able to accept that because Mr Mahmood was the registered holder of the trade mark "Pinkiss" fashion wear and head wear for teenagers, that Mr Mahmood necessarily supplied children's clothing.

43. Mr Connell submitted that at the appeal Mr Mahmood had said that he was a hard-working salesman with limited VAT knowledge and no time to check up on the compliance activities of Mr Bailey and Mr Grover. He knew little about VAT compliance. Although Mr Bailey was 78 years old and unwilling to move to a computerised system, he had retained his services for sentimental reasons. Mr Connell suggested that in those circumstances it was probable that the replacement of Mr Grover was tactical, to support the excuse of blaming a professional agent for the evasion.

44. Mr Connell submitted that the burden of proof is on Mr Mahmood to show that the section 73 assessment is wrong. The purpose of item 16 of Schedule 8 (zero-rating) was to relieve children's clothing of the tax liability which would otherwise attach to it and, in accordance with ordinary principles, as it operated as an exemption it should be narrowly construed. HMRC's interpretation of the legislation in item 1 of Group 16 of Schedule 8 to VATA 1994 is set out in Public Notice 714 (zero-rating young children's clothing). This notice does not have the force of law. It originates in general sectorial agreement and is generally accepted by litigants and tribunals as a correct interpretation of the legislation.

45 The suitability test need only be considered if Mr Mahmood is able to prove that
the clothes supplied were designed as clothing for young persons. Mr Connell
submitted that not suitable for older persons means “not suitable for persons older
than a young child”. The test is whether the items are not suitable for older persons. In
5 the case law, suitability can be a matter of:

- a. Visual appearance. Taking into account fashion and style;
- b. Size. If a garment is larger than the dimensions of a young child then it is
suitable for older persons. But the mere fact that a garment is within the
dimensions of a young child, it does not mean that the garment is not
10 otherwise suitable for older persons.

46. Mr Mahmood should bear the burden on suitability. If the point is in doubt, it
must be remembered that Mr Mahmood has provided absolutely no records at all.
This is not a matter like so many in the reports where an appellant has produced
15 during the enquiry, and in tribunal, the actual garments, or the actual price lists,
labels, advertising etc. The kind of proof required is appellant-generated and within
the power of an appellant to keep as part of his records. Mr Mahmood cannot dispose
of or withhold his records and then seek to hide behind a legal technicality in the form
of the burden of proof. He submitted that Mr Mahmood cannot be allowed to create
20 by his own evasive behaviour, the circumstances of impunity.

47. The statutory basis for the French Authorities report, for the relevant period, is
set out in Council Regulation (EC) No. 1798/2008. Mr Connell submitted that Article
41 stated that information furnished in a report may be used for the purpose of
25 establishing the assessment base or the collection or administrative control of tax. He
submitted that the evidence from the French Authorities was to be preferred from that
of Mr Mahmood. Furthermor, as Mr Mahmood has challenged the rate on which the
assessment is based he bears the burden of proving that he supplied clothing designed
for young children, which were not suitable for older children and therefore entitled to
30 be zero-rated.

48. Mr Connell submitted that it was unlikely that Mr Mahmood would have known what the Paris wholesaler ordered from its Italian manufacturer as Mr Mahmood had no contact with the Italian manufacturer. As a result, because the order was for scaled-down adult clothes' the clothes ultimately supplied could not have
5 been designed for young children. Even if the Pinkiss labels were sown into the designs, this would not convert them to designs for young children. Mr Mahmood said in cross-examination that the clothes supplied to him by his Paris-based suppliers "were in fact small sized European sized garments that are the UK equivalent to a child's size". It was not until the second set of certificates were produced that any
10 sizes complying with the Notice 714 were provided.

49. Mr Connell submitted that Mr Mahmood kept no general VAT records relevant to the Paris supplier's transactions, and no records or evidence relevant to design. In particular, during the enquiry he failed to produce any labels, price lists,
15 size tables, advertising or the like, or even any garments which it had acquired and supplied. HMRC do not accept that the garments produced during the trial, with no explanation as to why they were not produced during the enquiry, are reliable evidence of the kind of garments acquired and sold during the relevant period. In the circumstances Mr Mahmood had not discharged the burden of proving that the
20 garments were designed as clothes for young children.

50. Mr Connell submitted that statutory returns (European Sales Lists recording details about intra-EU transactions (ESLs)) must be completed by despatchers of
25 goods to traders located elsewhere within the European Union. In the case of Mr Mahmood's Paris suppliers, those returns detail their trade with Mr Mahmood in the relevant period. Those returns contribute to the data captured to the VIES. All ESLs are stored on the VIES database (The database is able to or enables a tax authority officer to match up related returns e.g. French supplier return with UK recipient
30 return).

51. Some or all of Mr Mahmood's Paris-based suppliers duly filed their ESL returns, and officer Myerscough was able to access the details off the VIES and identify Mr Mahmood's trade with his Paris-based suppliers. If a Paris-based supplier did not appear on VIES when officer Myerscough interrogated that data base on or
5 about 30 July 2010, then the probabilities are either that the Paris suppliers are non-compliant or evaders and therefore not credible witnesses, or they did not trade with Mr Mahmood in the relevant period.

52. Mr Connell submitted that the evidence of the witnesses for HMRC should be preferred as they were carrying out their normal administrative duties. In contrast, Mr Mahmood's explanations during the enquiry were vague and therefore unreliable, and on several important points dishonest. He gave a series of explanations, which during the enquiry he had to concede were false. Mrs Kaur's evidence was no better. She avoided several questions relating to the setup of the shop front window, size of the
15 mannequins in the window, label content and design, by saying that she could no longer remember the detail, and to this extent at least her evidence is unreliable.

53. Mr Connell submitted that the correct rate was applied to the facts determined to best judgement and the appropriate calculation methodology was used. The
20 assessment under section 73 was lawful and accurate. In the circumstances, HMRC also conclude that the clothing supplied to Mr Mahmood was not "children's clothing" as defined and so was not eligible for zero-rating. Mr Mahmood should have charged VAT at the standard rate on the full sale price of the clothing. The failure to do so meant that Mr Mahmood's output tax was understated, leading to a
25 loss of revenue for HMRC. He was able to under-cut his trade competition by an amount bearing a relationship to the difference between standard rate VAT on the full sale price and standard rate VAT on the profit margin. The appeal should be dismissed.

30 54. As to the dishonesty and the penalty, Mr Connell submitted that Mr Mahmood had acknowledged that he was an experienced businessman. He said that he was travelling most of his business life, but as the owner of the business he had been

advised as to the VAT responsibilities and had employed both an accountant and a bookkeeper to assist him. Mr Grover had been straightforward and ceased to act for Mr Mahmood when he considered that Mr Mahmood was not being honest.

5 55. Mr Connell submitted that in the cases reports, the usual introduction to the element of evasion is to begin with a quotation from the judge's direction to the jury in R v Dealy, a criminal case on evasion:

10 "so far as the law is concerned, if the person concerned to send in the VAT Returns and the money when the time has come to do it, ... knows that the time has come, deliberately does not want to send them in, in order not to pay the tax because he does not want to, then, from that moment onwards, he is, in law, evading the tax";

15 56. Mr Connell submitted that the test for dishonesty is both subjective (as regards the dishonest act or omission) and objective (as regards the moral standard).

1. The subjective test: Did the controller know all the facts which together constitute the relevant business conduct? A controller armed with the correct moral template cannot apply it to facts of which he or she is unaware.
- 20 2. The objective test: Would ordinary people think the relevant business conduct or behaviour under examination was dishonest? Although a dishonest state of mind is a subjective mental state, the mental element is knowledge of the ordinary moral standard, not some personal opinion or standard. In other words, the personal moral standards of the trader are
25 irrelevant.

57. Section 70 of VATA 1994 provides for reduction of the section 60 penalty percentage, in proper circumstances. Section 70(1) states:

30 "Where a person is liable to a penalty under section 60 ... the Commissioners or, on appeal, a tribunal may reduce the penalty to such amount (including nil) as they think proper."

In exercising the discretion to reduce a civil evasion penalty, HMRC has reduced the penalty liability to 70% of the tax on the basis of Mr Mahmood's co-operation with HMRC during its investigations giving rise to a penalty of £284,892. HMRC's officers applied their minds properly to the facts and the law. They took account of relevant facts and did not rely on irrelevant facts, had a clear understanding of the law, acted reasonably and without bias and reached an appropriate decision. The assessment under section 60 is lawful and appropriate. The tribunal is invited to dismiss the appeal.

10 **Mr Gibbon's submissions.**

58.. Mr Gibbon submitted that section 77 (4A) of the Value Added Tax Act 1994 (the Act) extends the time limit for assessments made under section 73 to 20 years from the end of the proscribed accounting period where the loss of VAT was occasioned deliberately by Mr Mahmood otherwise the period is 4 years (see section 15 77 (1). As a result, the assessments for the prescribed accounting periods 02/04 to 10/07 in a total sum of £344,188 are out of time and invalid.

59. If HMRC proves that Mr Mahmood was guilty of fraudulent evasion of VAT then all the VAT assessments are valid in the total sum of £406,989. If it does not then Mr Mahmood will be liable for the VAT assessments for the periods 01/08 to 20 01/09 in the sum of £62,801. The time limit under section 77(2) for the assessment of a civil penalty pursuant to section 60 of the Act is two years and as the VAT assessment was issued on 12 January 2012 the penalty was in time as it was issued on the same day as the assessment.

60. It is for Mr Mahmood to prove that the clothes were zero rated and, if so 25 proved, the VAT is to be discharged. If the full assessment and penalty are to be confirmed, then HMRC has to prove that Mr Mahmood was dishonest. Although the standard of proof with regard to the penalty is on the balance of probabilities HMRC have to produce compelling evidence. In *re H and others* [1996] 1 All ER at 17 Lord Nicholls said:

30 "The flexibility built into the preponderance of probability standard in respect of the seriousness of the allegation does not mean that where a serious

allegation is in issue the standard of proof is higher. It means only that the inherent probability or improbability of an event is itself a matter to be taken into account when weighing the probabilities and deciding, whether, on balance the event occurred.”

5 61. In *Secretary of State for the Home Department v Rehman* [2002] 1 All ER at 141 Lord Hoffman said:

“It would need more cogent evidence to satisfy one that the creature seen walking in Regent’s Park was more likely than not to have been a lioness than to be satisfied to the same standard of probability that it was an Alsatian. On
10 this basis, cogent evidence is generally required to satisfy a civil tribunal that a person has been fraudulent or behaved in some other reprehensible manner.”

62. In *Glenda Candy* (TC02544 and [2013] UKFTT 146 (TC) the tribunal confirmed the position in relation to dishonesty;

“...we can see no reason why the standard (balance of probabilities) should not
15 apply in cases such as this, because the issue of dishonesty by the taxpayer arises and because the consequences of the finding of dishonesty gave rise to potentially serious penalties, we consider that we should not be satisfied with anything less than a high degree of probability.”

63. Mr Gibbon submitted that he agreed with the tests of dishonesty as proposed
20 by Mr Connell, but the Tribunal should consider the weight and quality of the evidence and should not be satisfied with evidence that amounts to little more than conjecture, supposition or innuendo.

64. Mr Mahmood’s case is that the undeclared takings, which are the basis of the assessments, resulted from retail sales of children’s clothing which qualified for zero
25 rating, resulting in an under-declaration of VAT. Mr Mahmood said that he saw a gap in the market for designer style fashionable female children’s clothes after Bliss Clothing had asked towards the end of 2003 if Mr Mahmood could provide children’s clothing similar to the design of the adult clothing. At the Tribunal, Mr Mahmood had

said that at that time female teenagers from the age of 14 were well catered for by the high street stores but that there was little provision for younger children.

65. As a result in 2005 Mr Mahmood had opened a shop in Burnley selling high fashion clothing for girls aged 6 to 13. HMRC do not appear to take issue with the fact that Mr Mahmood opened the various shops. Mr Mahmood also said that he would not have opened shops for adult customers as this would have seriously affected his wholesale business. Trousers were sized in the age suitable for sizes 6, 8, 10 and 12. Tops were sized XXXS (6 year olds), XXS (8 year olds) XS (10 year olds) and s (12 year olds). Jackets were on a similar sizing system.

66. Mr Mahmood was away a lot of the time buying clothing for his shops and the wholesale business. As a result, he left the day to day running of the shops to his managers. The details of the sales and monies received were taken to the wholesale shop where Mr Bailey made the appropriate entries. Bank statements were also made available separately to Mr Bailey.

67. Mr Mahmood told the Tribunal that he would look at adult garments on the racks and ask if they could be made in specified smaller sizes. It is not clear whether he specified or not that the clothing should be for children, but it can be inferred from the size range. Although the clothing was scaled down versions of adult fashions, it would be made in sizes appropriate for young children to the age of 13 and not appropriate for older children or adults.

68. Mr Gibbon concede that the original design of a particular garment was for adult females, however, if a garment by its very small size, would not fit an adult then it cannot be said to be *designed* for adults just because the original design was for adults. Reference should be made to the design/pattern/size used by the actual manufacturer to determine what category of person the design of the particular garment was for. If this was not so, Mr Gibbon submitted that a scaled down version to fit a 2 year old child will always be standard rated – which is a nonsense.

69. Mr Connell in his submission appears to accept that an item would be designed for young children either on the basis of the items' physical measurements or on the body size of the child it is intended to fit. HMRC also accepted that if the

items of clothing fit within the list of measurements for various garments contained in Notice 714 they will also be for young children. Mr Mahmood has been able to confirm that the clothes were for young children from the two sets of certificates he had arranged to be signed by his suppliers. The second set of certificates, as
5 recommended by HMRC, were signed by 12 of Mr Mahmood's suppliers and have been produced to the Tribunal. They indicate that the clothes sold to Mr Mahmood were all in the various sizes referred to in Notice 714.

70. Mr Gibbon states that there was nothing sinister in the staple markings. The documents must have been taken to pieces for copying purpose and then re-stapled
10 together. Nor can the evidence from the French authorities help. Those provided by Sari Chichi merely state that the clothes were "vetements de sexe feminine", which does not assist one way or the other.

71. HMRC says that the certificates from Fantasy stated "Absence of sales children's clothing" drawn from the fact that the invoices did not specify children's
15 clothing – but they did not specify adult clothing either. The supplier has also stated he sold "vetements pour femme", but again this could merely mean that the clothes were for females rather than males and says nothing about the age.

72. HMRC accept that children's clothes are not zero rated in France. A French manufacturer would not be used to differentiating between adult and children's
20 clothing, nor were they asked by HMRC about the sizes in accordance with Notice 714. The invoices for 'Why Not' were identified by the French authorities as "confection adult femme". The same 8 of the invoices produced by Mr Mahmood for 'Why Not' bore the manuscript addition "confection femme fille".

73. The manuscript writing on HMRC's and Mr Mahmood's invoices appears to
25 be in the same hand save that Mr Mahmood went to see 'Why Not' and got them to sign his invoices as "confection femme fille". It is, however, significant that Mr Mahmood's invoices were signed in September 2010 and HMRC's several weeks later. Mr Gibbon therefore submitted that the subsequent notation does not affect Mr Mahmood's evidence.

74. The second test for zero rating is that the clothing must not be suitable for older children. This test can be met by ensuring that they are “held out for sale” for young children and therefore unsuitable for older people. Mr Gibbon submitted that the point is that a garment which could conceivably fit a very small adult female will
5 be treated as being unsuitable for older persons if it is held out for sale for children under 14 and the sizes are within the body measurements listed in paragraph 4.2.2 of Notice 714. He also submitted that the evidence relating to the clothes was that the clothes were held out for children:

- The shop signage was TM Stores and underneath “Children Clothing
10 Wholesale Direct”.
- Each garment carried a tag label showing children’s sizes.
- The clothes were delivered on hangers carrying similar sizes.
- This evidence was confirmed by one of his employees Mrs Kaur.

75. The income tax enquiry for the years 2005/6 was initiated on 5 February 2008
15 and extended to cover 2006/7. 2004/5 was never the subject of an enquiry, but it was agreed that it would be treated as a year in which there was neither a profit nor loss and revised accounts were not requested. As a result, Mr Gibbon submitted that Mr Mahmood cannot be criticised for not explaining the source of income into the “no 2” account 5889080 during that tax year.

20 76. The “no 2” account was opened in April 2004 but the euro account 86240686 was not opened until April 2005. HMRC stated that it was difficult to accept the evidence from K A Javid accountants in their letter of 17 May 2013 as it carried the logo testifying to ‘10 years of excellence’ from 1990 to 2000. Mr Gibbon submits that the accountants had merely not updated their letterhead.

25 77. He also noted that Mr Mahmood had telephoned Mr Lenagan on 22 December 2008 and advised him about the retail shops and the fact that they were selling children’s clothes. He had sacked Mr Glover, his first accountant, because he considered that he had not been acting professionally. In any event, Mr Grover has not been called to give evidence so that Mr Mahmood does not know what he said to
30 HMRC in the 10 months before December 2008. The lack of professionalism is also

confirmed by the fact that Mr Glover knew about the “no 2” account in September 2008 and payments, entered by Mr Bailey into the purchase day book, appear to have been made out to that account in respect of the main wholesale business.

5 78. Mr Gibbon submits that in spite of the fact that the enquiry lasted four years it did not answer the questions as to whether the goods the subject of that enquiry were children’s clothes and not therefore liable to VAT. Even if it is established that Mr Mahmood was dishonest, it has not been established that his dishonesty was to avoid VAT as he contended that all the sales giving rise to the increase in his turnover were of children’s clothes and, as a result, he had not evaded any VAT. The test is whether
10 Mr Mahmood believed that the clothes he was selling were children’s clothes or alternatively did he know that they did not qualify for zero rating.

79. In the light of all the evidence, Mr Mahmood says that the clothing which was sold from his retail shops was zero rated for VAT and as a result he had not under-declared output tax on those sales and there had been no consequential evasion of
15 VAT. The only evidence that HMRC have put forward as to the type of clothing is the evidence from the French Authorities, which is not cogent evidence, that the clothing supplied by the 3 suppliers was NOT children’s clothing. The appeal should be allowed in full and the Tribunal should also allow the appeal against the civil penalty.

20 **The decision**

80. We have consider the law and the facts and we dismiss the appeal. We accept that where dishonesty is alleged that cogent evidence thereof is required. We are satisfied that there is such evidence as identified at paragraph 86 below. The case law has considered the meaning of dishonesty. In *R v Dealy*, in 1994, *McCowan LJ*,
25 although by reference to the Value Added Tax Act 1983, stated:

“ However, the point is that there comes a time when the person who is concerned to send in the firm’s VAT return, or his own if he is an individual, and the cheque for the amount owing, knows that the time has finally come when he must pay by the 31st of the month, or soon afterwards, anyway, and, if
30 that person deliberately does not send in the VAT return, and the money, at the

time when he takes the decision, quite deliberately, not to send in the return, because he does not want to pay, he is, in law, evading the tax.”

81. In *Sahib Restaurant Limited*, in 2008, His Honour Judge Pelling QC said in relation to dishonesty:

5 “.It is common ground that the relevant test is that set out in *R v Dealy*. This establishes a bipartite test with HMRC having to prove to the requisite standard¹ (a) evasion and (b) dishonesty. In relation to dishonesty, the first question is whether objectively and judged by the standard of ordinary reasonable people, what the taxpayer did was dishonest. If the Tribunal considers this to be
10 established then the second question whether the tax payer might have thought, quite honestly, that he had a perfect right to do as he did.”

82. In *R V Gosh*, in 1982, Lord Lane CJ gave the example:

 “Take for example a man who comes from a country where public transport is free. On his first day here he travels on a bus. He gets off without paying. He
15 never had any intention of paying. His mind is clearly honest: but his conduct judged objectively by what he has done, is dishonest.... Parliament cannot have intended to catch dishonest conduct in that sense, that is to say conduct to which no moral obloquy could possibly attach.”

83. Mr Gibbon, in his summing up, does not appear to address in any detail the
20 position with regard to the enquiries and the resultant increase in Mr Mahmood’s income tax liability. He suggests that if Mr Mahmood can establish that the clothes giving rise to that increase were children’s clothes, then the VAT liability will not arise, because the sales would have been zero rated. We are satisfied from the evidence that Mr Mahmood intended to conceal the fact that he had accumulated
25 £586,448.24 in the number 2 Account. Mr Gibbon submits that Mr Grover told HMRC of the account in December 2008. It was not for Mr Grover to tell HMRC about the account, but for Mr Mahmood to disclose it as and when he opened it.

¹ Balance of probabilities.

84. As Mr Connell has submitted, Mr Mahmood had put forward various reasons for the discrepancies in the accounts over the periods:

- The No 2 account 5889080 was his supplier's bank account.
- 5 • The Balances on account No.58 89080 were inflated by inter-account transfers
- His records were disposed of in error into a skip by a third party.
- His Paris purchases and subsequent United Kingdom sales were of children's
10 clothing.
- Mr Grover and Mr Bailey concealed the receipts and excluded the income from the two trading accounts.
- 15 • Mr Bailey omitted the supplies from the returns because they were zero rated and, as a result, there was no VAT due.
- Mr Mahmood spend a large amount of his time abroad and left the management of the finances of his business to his staff and the accountants.

20 85. We agree with Mr Connell, Mr Mahmood could not have run a business turning over £3,000,000 and not know what was taking place in the shops and wholesale business We noted that he was able to answer Mr Connell's questions about the type of clothing involved in the invoice without any hesitation at all, simply by looking at the amount of VAT. (See paragraph 16 above). We would not have expect such a
25 quick answer from somebody who purported to be unaware of his VAT liabilities. His wholesale business had been subjected to earlier enquiries arising from a failure to disclose all the receipts. Mr Mahmood also confirmed that he needed to collect data from his shops to be able to assess how much he had to spend on his next trip for stock. We are satisfied that Mr Mahmood was dishonest in relation to his self-
30 assessment returns with the consequent increase in his tax liability and with regard to his VAT for the period 02/04 to 01/09 in deliberately failing to account for the retail sales of the clothes through his shops that he alleges he had purchased from Paris..

86. It is ingenuous of Mr Gibbon to suggest that there can be no dishonesty where the VAT is concerned, because the clothes involved, rather than the financial returns,
35 were children's clothes and as such did not give rise to a VAT liability. No evidence

was provided to show that Mr Mahmood kept records of the clothes and he provided no invoices for the purported sales from his shops. He was fully aware that he had made such sales, as he has sought to advise us throughout this appeal. His VAT returns were incomplete as he well knew, not least because he was prepared to sign the returns in blank and leave it to Mr Bailey to complete them.

87. We have therefore decided that “judged by the standard of ordinary reasonable people” what Mr Mahmood did was dishonest. We are also satisfied from his actions and his various reasons given for the funds in the number 2 account, that he knew that he was not completing his VAT returns correctly and that he deliberately omitted the details giving rise to the monies in the number 2 account.

88. In *Smart Alec Limited*, in 2002, Chairman Adrian Shipwright stated at paragraph 19:

“19. Other than the declaration that the child was under the age of 14 made by the person placing the order we have no evidence before us as to who was to wear the clothing. However, this is not the relevant question. The relevant question is “were the articles designed as clothing or footwear for young children?”. There is no evidence before us that the manufacturer (whom we consider is the designer here..) as the designer, intended the articles in question were designed as clothing or footwear for young children. Accordingly we cannot find that they were so designed.”

89. In *H & M Hennes Ltd v Customs and Excise Commissioners*, in 2005, Sir Donald Rattee stated at paragraph 17:

“17. As to the appellant’s submission that on its proper construction in its context the phrase ‘young children’ does not mean children below a certain age but children of whatever age who have not reached puberty, I have already recorded how the tribunal rejected, and in my view rightly rejected, a similar argument put before it on behalf of the appellant. It is in my judgement impossible to reconcile the argument with the ordinary meaning of the words used in item 1 of Group 16 in Schedule 18 of the 1994 Act. Those words clearly contrast young children and older persons. The distinction drawn is one

of age and not the stage of physical development reached by the relevant person, which stage different children reach at different ages.”

He concluded that a 14 year old is not a young child, which he considered to be an eminently reasonable conclusion.

5 90. Mr Mahmood has sought to convince us that he had only bought children’s clothes and that the sale of those clothes through his shops accounted for the £586,448.24 in the no 2 account. This in spite of the fact that he had suggested that some of the undisclosed payments to the account had come from the commission he received from the ‘Bliss Clothing’ arrangement. (See paragraph 19 above).

10 91. He also sought to identify the payments to the number 2 account on the following basis:

- He produced to the tribunal clothes, which he said are similar to those that he had made up for children’s clothes some 5 to 10 years ago. Those samples appeared to have been tampered with and were of no assistance in evaluating the clothes he actually bought in the periods 02/04 to 01/09 as we have no means of knowing whether they were similar or not. We would suspect not, given the time that has passed. We have the same difficulty that Chairman Adrian Shipwright had in the case of *Smart Alec Ltd*.
- 15 20 • He explained, at great length, how he purchased the clothes in Paris. The children’s clothes that had been manufactured, we understand in Italy, were reduced samples of the adult clothes that he wished to have copied. He conceded that the French were unconcerned with regard to the size of the clothes as the sizing of children’s clothes differs to that used in the United Kingdom.
- 25 30 • Given that the French were unconcerned about the sizing of children’s clothes it is not surprising, if they wished to keep his custom, that they would sign not one but two of the certificates prepared for Mr Mahmood. It is of no help to Mr Mahmood that the certificates provided by HMRC did not say that they were ‘adult’ clothes. As the invoices we have seen from his suppliers have incomplete details on them, we are unable to accept that they were necessarily

children's clothes. We have, however, decided that the information provided formally through the French authorities is the more likely to be correct.

- We have had difficulty establishing from the evidence provided what clothes Mr Mahmood was buying. The evidence from his shop assistance, Mrs Kaur did not assist. She clearly could not remember what went on at the shop and inadvertently mentioned, although she retracted the comment, that some adult clothes were sold in the shops. (See paragraph 33 above.)
- Mr Mahmood also has a wholesale business and we have no means of knowing whether some of the clothes, he ostensible purchased in Paris, were also sold through the wholesale business. We accept that he told us that the wholesale business only dealt with adult clothes, but he also accepted that some smaller women might well be able to fit into the larger children's clothes.
- Mr Mahmood admitted that he signed the VAT returns without giving them much thought as he relied on Mr Bailey to complete them correctly. He even confirmed that he had signed some of the returns in blank and had allowed Mr Bailey to complete them as he thought fit.
- As we have no evidence about to the types of clothes that were being sold we have no means of knowing what the sizes were. We were told that the sizes appeared on the garments, although the ones we saw had the washing instructions sewn somewhat haphazardly over them. The sizes were also on the coat hangers. No coat hangers have been produced. We were told the sizes on the coat hangers were English sizes although the clothes had been imported from Italy through Paris. Without seeing the coat hangers for the actual clothes, we are unable to say what size appeared on them. We do, however, accept that the clothes were supplied with coat hangers.

92. We have decided that, as we are unable to ascertain what clothes were purchased in Paris and sold through the shops, we do not need to decide whether they were designed as clothing for young children and as a result not suitable for older person. The only clothing produce to the tribunal were quite large and in our judgment would have fitted a person of 14 years or more. Given the confusion about

the size of the clothes, we have no evidence as to who was to wear them. The fact that we were told that the clothes were designed for adult females originally, then, at Mr Mahmood's request, reduced in size, is relevant as we have no evidence that the Italian manufacturer intended the clothing for young people.

5 93. We have also decided that the section 60 penalty was not excessive. Given Mr Mahmood's various reasons for the huge sum of money that was in the number 2 account and his unhelpful efforts thereafter to account for it, we consider that a 30% reduction was, in the circumstances, generous. For all the above reasons we dismiss the appeal, and we confirm the assessments and the penalty.

10 94. 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
15 "Guidance to accompany a Decision from the First-tier Tribunal (Tax Chamber)" which accompanies and forms part of this decision notice.

20 **DAVID S PORTER**
TRIBUNAL JUDGE

RELEASE DATE: 23 September 2014

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