

Case studies for small practitioners

Inadvertent involvement with money laundering

Scenario

Smith & Jones LLP provides compliance services for Acme Limited, a local business which trades in small personal electronics.

As part of their work, Smith & Jones LLP prepares the VAT returns for Acme Ltd. Whilst inputting the VAT return figures, the partner notices that there were high levels of sales to Adder Ltd, a new customer for Acme Ltd. When sending back the VAT return for approval and submission by the managing director of Acme Ltd, the partner asked about Adder Ltd and was told it was a great new customer introduced to the company by another customer. The partner thought nothing more about it.

On preparation of the next VAT return, the sales to Adder Ltd had increased. The partner thought it a bit odd that all the goods shipped to Adder Ltd came through a different supplier and were sent using a different delivery company to that used by Acme for its other customers but was reassured by the client explanation that the delivery company was a group company of Adder Ltd and that they preferred to use it.

This continued for the next VAT quarter. Acme Ltd then had a VAT visit which the partner attended. At that meeting, the VAT compliance officer made some non-specific but pointed comments about Adder Ltd, asking what Acme knew about the company. This struck the partner as odd, but he was reassured by the client who said Adder Ltd had been subject of a VAT enquiry and had had to pay a VAT penalty because they made an error when their tax adviser was ill, but it was all "sorted".

In the follow up letter, the VAT officer made some general comment about being careful in dealings with Adder Ltd. He mentioned concerns about "missing VAT". The VAT officer also attached a leaflet on missing trader intra-community (MTIC) fraud (also referred to as missing trader fraud), which explained how criminals create complex structures of linked companies (known as chains) to abuse VAT rules, whereby a company often at the beginning of the chain and only trading for a short period of time, charges VAT to a customer but does not pay this to the government and then effectively disappears. The partner found the leaflet quite informative.

After two further returns were filed, HMRC wrote to Acme Ltd and to Smith & Jones LLP indicating that they were conducting an investigation into its VAT returns as they suspected VAT fraud. Smith and Jones LLP were also asked for copies of all documents and correspondence supporting the VAT returns.

Questions

What red flags could Smith & Jones LLP have picked up?

1. Although not by itself suspicious, upon being informed that Adder Ltd had been introduced to Acme Ltd by another customer, the partner might have enquired as to the identity of the customer as additional background.
2. Upon discovering the change of supplier and delivery company, the partner ought to have enquired whether any cost savings had been made. Moreover, the knowledge that the delivery company was a group company of Adder Ltd should have prompted further enquiries about the arrangement.
3. The information that Adder Ltd had suffered a VAT penalty should have raised further concerns in the partner's mind, especially as Adder had only recently become a customer of Acme Ltd and the introduction had come through a third party.
4. If the partner was not familiar with MTIC fraud, the mention of "missing VAT" should have alerted the partner that all may not be in order at Adder. Given that Smith & Jones LLP prepared the VAT returns for Acme, the partner would not want either Acme Ltd nor his own practice to fall under suspicion of involvement in VAT impropriety.

What actions should the firm have taken?

With the changed circumstances of the new customer and the increase in turnover, together with the changes in supplier and delivery company, questions should have been asked for further information to be provided. Even if the partner did not know about MTIC fraud, it should perhaps have occurred to him that this was an unusual situation. The firm should have carried out detailed checks to gain comfort over the legitimacy of Acme's supply chain.

The following HMRC guide provides useful tips to help spot missing trader VAT fraud and the type of checks that should be carried out: <https://www.gov.uk/government/publications/vat-missing-trader-fraud>

Where could they have gone for assistance?

It is unclear if Smith & Jones LLP is a firm of Chartered Accountants, but on the basis that this was not the case, they could have made an approach to their own accountants for guidance or sought legal advice. As a firm of Chartered Accountants, they would have been able to contact their professional body for support and advice

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