TC07703

Income Tax (Construction Industry Scheme) Regulations 2005 – failure to submit monthly returns

FIRST-TIER TRIBUNAL
TAX CHAMBER

Appeal number: TC/2016/02355

BETWEEN

David Kinsella **Appellant**

-and-

THE COMMISSIONERS FOR HER MAJESTY'S REVENUE AND CUSTOMS **Respondents**

TRIBUNAL: JUDGE RACHEL MAINWARING-TAYLOR
MS ELIZABETH BRIDGE

Sitting in public at Taylor House, 88 Rosebery Avenue, London EC1R 4QU on 18 September 2017

The Appellant represented himself

Mr S Goulding of HM Revenue and Customs, for the Respondents

DECISION

INTRODUCTION

1. The Appellant appeals against:

   (1) Determinations ('**the Determinations**') made under Regulation 13 of The Income Tax (Construction Industry Scheme) Regulations 2005 (SI 2005/2045) ('**the 2005 Regulations**') for the tax years ended 5 April 2011 and 5 April 2012; and

   (2) Penalties ('**the Penalties**') raised under section 98A(2)(a) of the Taxes Management Act 1970 for failure to submit CIS300 Contractor's Monthly Returns under Regulation 4 of the 2005 Regulations in respect of the tax years ended 5 April 2009, 5 April 2010 and 5 April 2011.

BACKGROUND

2. The Appellant submitted self-assessment tax returns for the years 2008/9 and 2009/10 in which he claimed deductions for Construction Industry Scheme ('CIS') costs. He was not registered as a contractor within the CIS regime.

3. In correspondence during 2011, HMRC informed the Appellant that his circumstances were within the scope of the CIS regime and the Appellant disagreed.

4. HMRC notified the Appellant of the tax liability and fixed penalties it considered were due on 3 August 2011, following which there was a further exchange of information between the parties and the Appellant claimed exemption under Regulation 9(5) of the 2005 Regulations, which HMRC considered and rejected.

5. Further correspondence ensued during which HMRC outlined the reason for the liability and the Appellant's rights to statutory review or appeal. The Appellant disagreed with HMRC's position but did not specifically request a statutory review or lodge an appeal.

6. HMRC issued the Determinations and the Penalties on 6 December 2012 and wrote to the Appellant regarding the Determinations and the Penalties and his rights to appeal on 7 December 2012.

7. HMRC notified the Appellant that they had closed their enquiry on 14 February 2013 as no appeal had been received.

8. On 2 April 2013 the Appellant notified HMRC on form P85 that he had left the UK for Dubai on 24 March 2013 for a period of 5-10 years. He provided no address in Dubai and HMRC continued to use his UK address.

9. The Appellant joined the PAYE/CIS scheme on 20 November 2014 under the trading name Sash Corbel & Beg. CIS monthly returns were filed, the first being on 10 December 2014 in respect of the month ended 5 December 2014.

10. On 16 October 2015 a debt recovery letter was issued to the Appellant and the Appellant wrote to HMRC in response to this letter on 26 October 2015 and further correspondence ensued by telephone and in writing between the parties during which the Appellant asserted that the matter had been resolved in 2012, offered to pay a lesser sum in full and final settlement of the matter, which HMRC rejected, and ultimately wrote a complaint letter to HMRC on 18 March 2016.

11. The Appellant appealed to the Tribunal on 21 April 2016.

RELEVANT LEGISLATION

12. The legal basis for the CIS at the relevant time is sections 57 to 77 of the Finance Act 2004 (FA 2004) and the 2005 Regulations. The CIS requires certain payments by contractors

to sub-contractors to be made subject to the deduction of tax, but the sub-contractors can claim credit for tax withheld under CIS against their tax liability for the year in question.

13. Section 61 FA 2004 sets out the framework for the deductions the contractor is to make:

> "(1) On making a contract payment the contractor (see section 57(3)) must deduct from it a sum equal to the relevant percentage of so much of the payment as is not shown to represent the direct cost to any other person of materials used or to be used in carrying out the construction operations to which the contract under which the payment is to be made relates.
>
> (2) In subsection (1) "the relevant percentage" means such percentage as the Treasury may by order determine.
>
> (3) The percentage must not exceed [the percentage which is the basic rate for the year of assessment in which the payment is made if the person for whose labour the payment is made is registered for payment under deduction or, if the person is not so registered, the percentage which is the higher rate for that year of assessment]".

14. Regulation 4 of the 2005 Regulations provides for submission of monthly returns to HMRC by a contractor making contract payments or payments which would be contract payments but for section 60(4) of the Act.

15. Regulation 6 provides for a contractor to verify whether a person to whom he is proposing to make a contract payment is registered for gross payment or payment under deduction or is not registered under Chapter 3 of the Act.

16. Regulation 7 provides for payments of deductions to be made by a contractor to HMRC.

17. Regulation 9 provides for recovery from a sub-contractor of an amount not deducted by a contractor and applies if it appears to an officer of HMRC that the deductible amount exceeds the amount actually deducted and condition A or B is met:

> "(1) This regulation applies if-
>
> (a) it appears to an officer of Revenue and Customs that the deductible amount exceeds the amount actually deducted, and
>
> (b) condition A or B is met.
>
> (2) In this regulation-
>
> "the deductible amount" is the amount which a contractor was liable to deduct on account of tax from a contract payment under section 61 of the Act in a tax period;
>
> "the amount actually deducted" is the amount actually deducted by the contractor on account of tax from a contract payment under section 61 of the Act during that tax period;
>
> "the excess" means the amount by which the deductible amount exceeds the amount actually deducted.
>
> (3) Condition A is that the contractor satisfies an officer of Revenue and Customs-
>
> (a) that he took reasonable care to comply with section 61 of the Act and these Regulations, and
>
> (b) that-
>
> (i) the failure to deduct the excess was due to an error made in good faith or

(ii) he held a genuine belief that section 61 of the Act did not apply to the payment.

(4) Condition B is that-

(a) an officer of Revenue and Customs is satisfied that the person to whom the contractor made the contract payments to which section 61 of the Act applies either-

(i) was not chargeable to income tax or corporation tax in respect of those payments, or

(ii) has made a return of his income and profits in accordance with section 8 of TMA (personal return) or paragraph 3 of Schedule 18 to the Finance Act 1998 (company tax return) in which those payments were taken into account, and paid the income tax and Class 4 contributions due or the corporation tax due in respect of such income or profits;

And

(b) the contractor requests that the Commissioners for Her Majesty's Revenue and Customs make a direction under paragraph (5)"

(5) An officer of Revenue and Customs may direct that the contractor is not liable to pay the excess to the Commissioners for Her Majesty's Revenue and Customs.

(6) If condition A is not met an officer of Revenue and Customs may refuse to make a direction under paragraph (5) by giving notice to the contractor ("the refusal notice") stating-

(a) the grounds for the refusal, and

(b) the date on which the refusal notice was issued.

(7) A contractor may appeal against the refusal notice-

(a) by notice to an officer of Revenue and Customs,

(b) within 30 days of the refusal notice

(c) specifying the grounds of the appeal.

(8) For the purpose of paragraph (7) the grounds of the appeal are that-

(a) that the contractor took reasonable care to comply with section 61 of the Act and these Regulations, and

(b) that-

(i) the failure to deduct the excess was due to an error made in good faith, or

(ii) the contractor held a genuine belief that section 61 of the Act did not apply to the payment.

(9) If on appeal under paragraph (7) [that is notified to the tribunal it appears] that the refusal notice should not have been issued [the tribunal] may direct that an officer of Revenue and Customs make a direction under paragraph (5) in an amount the [tribunal determines] is the excess for one or more tax periods falling within the relevant year."

18. Contractors are required to make a return no later than 14 days after the end of every tax month under section 70 FA 1970 and Regulation 4 of the 2005 Regulations. If such returns are

received after the filing date they are treated as late and the contractor will be liable to a penalty under section 98A TMA 1970, which provides:

> "(1)…regulations under section 70(1)(a) or 71 of the Finance Act 2004 (sub-contractors) may provide that this section shall apply in relation to any specified provision of the regulations.
>
> (2) Where this section applies in relation to a provision of regulations, any person who fails to make a return in accordance with the provisions shall be liable-
>
> (a) to a penalty or penalties of the relevant monthly amount for each month or part of month during which the failure continues, but excluding any month after the twelfth or for which a penalty under this paragraph has already been imposed, and
>
> (b) if the failure continues beyond twelve months, without prejudice to any penalty under paragraph (a) above, to a penalty not exceeding—
>
> …
>
> (ii) in the case of a provision of regulations under section 70(1)(a) or 71 of the Finance Act 2004, £3,000.
>
> (3) For the purposes of subsection 2(a) above, the relevant monthly amount in the case of a failure to make a return—
>
> (a) where the number of persons in respect of whom particulars should be included is fifty or less, is £100…"

19. Under section 100 of TMA 1970, an authorised officer may make a determination imposing a penalty under the provisions of the Taxes Acts; section 100(3) requires notice of such determination to be served on the person liable. So far as material, section 100 provides as follows:

> "(1) Subject to subsection (2) below and except where proceedings for a penalty have ben instituted under section 100D below…an officer of the Board authorised by the Board for the purposes of this section may make a determination imposing a penalty under any provision of the Taxes Acts and setting it at such amount as, in his opinion, is correct and appropriate.
>
> …
>
> (3) Notice of a determination of a penalty under this section shall be served on the person liable to the penalty and shall state the date on which it is issued and the time within which an appeal against the determination may be made.
>
> (4) After the notice of a determination under this section has been served the determination shall not be altered except in accordance with this section or on appeal…"

20. Section 100B of the TMA 1970 sets out the relevant right of appeal and the extent of the Tribunal's jurisdiction. It provides, so far as is material:

> "(1) An appeal may be brought against the determination of a penalty under section 100 above and, subject to the following provisions of this section, the provisions of this Act relating to appeals shall have effect in relation to an appeal against such a determination as they have effect in relation to an appeal against an assessment to tax, except that references to the tribunal shall be taken to be references to the First-tier Tribunal.
>
> (2) On an appeal against a determination of a penalty under section 100 above sections 50(6) to (8) of this Act shall not apply but--

(a) in the case of a penalty which is required to be of a particular amount the First-tier Tribunal may--

(i) if it appears that no penalty has been incurred, set the determination aside,

(ii) if the amount determined appears to be correct, confirm the determination, or

(iii) if the amount determined appear to be incorrect, increase or reduce it to the correct amount,

(b) in the case of any other penalty, the First-tier Tribunal may--

(i) if it appears that no penalty has been incurred, set the determination aside,

(ii) if the amount determined appears to be appropriate, confirm the determination,

(iii) if the amount determined appears to be excessive, reduce it to such amount (including nil) as it considers appropriate, or

(iv) if the amount determined appears to be insufficient, increase it to such amount not exceeding the permitted maximum as it considers appropriate."

21. Section 118(2) of TMA states that where a person had a reasonable excuse for not doing anything which was required to be done, he shall be deemed not to have failed to do it if he did it without unreasonable delay after the excuse ceased:

"(2) For the purposes of this Act, a person shall be deemed not to have failed to do anything required to be done within a limited time if he did it within such further time, if any, as the Board of the tribunal or officer concerned may have allowed; and where a person had a reasonable excuse for not doing anything required to be done he shall be deemed not to have failed to do it unless the excuse ceased and, after the excuse ceased, he shall be deemed not to have failed to do it if he did it without unreasonable delay after the excuse had ceased."

22. Under section 102 of TMA 1970, HMRC has a specific power to mitigate penalties:

"The Board may in their discretion mitigate any penalty, or stay or compound any proceedings for a penalty, and may also, after judgment, further mitigate or entirely remit the penalty."

23. Schedule 55 to the Finance Act 2009 introduced a new penalty regime that applied to the late filing of returns, including CIS monthly returns due to be filed on or after 19 November 2011. In light of this new regime, in November 2010 HMRC revised its existing policy on mitigating penalties under section 102 TMA 1970 to the effect that it would compare penalties that fell to be charged under section 98A with the level of penalty that would have applied had Schedule 55 applied instead and, if the Schedule 55 penalty would have been lower HMRC offered to mitigate the section 98A penalty to that lower amount.

24. The way this policy works is as described by the Upper Tribunal in *Anthony Bosher v HMRC* [2013] UKUT 0597 (TCC):

"HMRC's policy results in one of three outcomes:

1. If a contractor accepts the lower penalty amount, the penalties are reduced under s 102 of TMA.

2. If a contractor wishes to challenge the fact that a penalty is due despite the offer of mitigation, he can appeal in the normal way. However, HMRC will not reduce the amount beforehand. If the tribunal determines at the higher figure, once the appeal process has been exhausted, HMRC will reduce the amount of the penalty under s

102 of TMA in any event. If the contractor feels that further mitigation is due for reasons such a hardship, this will be considered in the normal way.

3. If a contractor agrees that a penalty is due but feels that it should be mitigated further, his reasons will be considered in the normal way."

EVIDENCE

25. HMRC provided evidence as to the circumstances and way in which the Determinations and Penalties were raised and issued.

26. The Appellant gave evidence as to why he felt the Determinations and Penalties should not have been issued.

AGREED FACTS

27. The key facts are not disputed.

28. The parties agree that the Appellant did not file monthly CIS returns during the relevant period.

29. The parties agree that the Appellant did not withhold and pay over to HMRC a percentage of the contract payment he made to the subcontractors.

30. The Appellant does not dispute that he came within the CIS rules during the relevant period. (He maintains that he was not aware of his obligations under it.)

ISSUES

31. Were the Determinations raised correctly? If so, does this Tribunal have power to change the Determinations and, if so, are the legal grounds for it to do so?

32. Were the Penalties raised correctly? If so, does this Tribunal have power to change the Determinations and, if so, are the legal grounds for it to do so?

APPELLANT'S CASE

33. The Appellant's arguments were:

(1) He was not aware of the CIS rules;

(2) HMRC did not advise him of the CIS rules despite having a full description of his trade;

(3) He stopped using sub-contractors as soon as he was made aware of his obligations under the CIS rules;

(4) All invoices have been supplied to HMRC for their verification of payment by him in full;

(5) The contractors have paid their own taxes and therefore no taxes are outstanding;

(6) He has paid all his taxes on time and in full;

(7) There is no allegation of fraud, tax evasion or criminal activity on his part;

(8) He has acted honestly and correctly for all his business life and it is unfair and malicious of HMRC to level fines in circumstances where there has been no loss of revenue; and

(9) HMRC's procedures are flawed as their decisions and reviews are not independent, being made 'in house'.

34. The Appellant explained that he was not aware of the CIS rules, HMRC did not make him aware of them despite him providing them with comprehensive information about his

business in his own returns. As soon as he was aware, following the correspondence in 2011, he ceased trading on that basis so that he was no longer within CIS.

35. The Appellant accepted that he had made a mistake but felt that the level of penalty imposed was excessive in the case of a genuine mistake, particularly when there was no loss of revenue to HMRC.

36. The Appellant believed he had taken reasonable care to operate within the law and had demonstrated this to HMRC.

HMRC'S CASE

37. The CIS provides for payments by contractors to sub-contractors within the CIS to be subject to the deduction of amounts on account of the subcontractors' tax. The deductions are paid to HMRC and count as advance payments towards the sub-contractors' tax and National Insurance bill.

38. The Appellant was legally required to make the CIS deductions under section 61 Finance Act 2004 and to pay such deductions to HMRC under Regulation 7(1) of the 2005 Regulations. It was the Appellant's responsibility to do this and he did not.

39. The Appellant does not qualify for relief under Regulation 9(3) because he does not satisfy the statutory conditions: that HMRC be satisfied that the contractor has taken reasonable care to comply with section 61 FA 2004, that the failure to deduct was due to an error made in good faith and that the contractor held a genuine belief that section 61 did not apply to the payment.

40. HMRC considered the Appellant's claim under Regulation 9(3) fully and notified the Appellant that they were not satisfied he had taken the required care and attention. Although the Appellant appealed HMRC's decision, he supplied no further information to enable them to reconsider.

41. The refusal of a claim under Regulation 9(4) is not an appealable decision. The claim was dealt with properly in accordance with the legislation by an independent officer (not the decision maker). HMRC were not satisfied that Condition B under Regulation 9(4) had been met i.e. that the subcontractors had made returns of their income or profits, in accordance with section 8 of TMA 1970 or para 3 of Schedule 18 to FA 1988 in which the contractors payments were taken into account, and had paid the income tax and National Insurance Contributions or corporation tax due.

42. Relief under Regulation 9(5) should not be granted and the Determinations were correct.

43. HMRC is not seeking payment that is not legally due or has already been paid. The total CIS deductions due were £100,066.68 but after appropriate relief the balance payable is £2,779.51.

44. Penalties legally due under section 98A(2) total £102,300 but HMRC agree to reduce the amount of the penalties under section 102 TMA 1970 to £12,852 which is the amount that would be charged under Schedule 55 of the Finance Act 2009.

45. HMRC relies on the Upper Tribunal decision in *HOK Ltd v HMRC* [2012] UKUT 363 (TCC) ("***HOK***")at para 36:

> "In particular, neither that provision nor any other gives the tribunal a discretion to adjust a penalty of the kind imposed in this case, because of a perception that it is unfair or for any similar reason. Pausing there, it is plain that the First-tier Tribunal has no statutory powers to discharge, or adjust, a penalty because of a perception that it is unfair.

46. The Determinations were correctly raised and the claim for relief has been correctly considered.

47. The Penalties were correctly raised.

48. The appeal should be dismissed.

DISCUSSION

49. The issue here is essentially one of fairness. The Appellant feels that he has been treated harshly: he never intended to breach the rules, paid his own tax in full and on time and believed those he contracted with were doing the same. In those circumstances he feels aggrieved that HMRC should insist on recovering the amounts in the Determinations and the Penalties from him.

50. We believe that the Appellant acted honestly throughout. However, this Tribunal has no general power to cancel charges issued by HMRC. It has only those powers granted to it by statute, as was made clear in *HOK*.

The Determinations

51. In this case, the Appellant not having filed the monthly returns and withheld and paid over to HMRC the percentages of contract payments due under the 2005 Regulations, HMRC had power to issue determinations under Regulation 13.

52. The Appellant effectively requested mitigation under Regulation 9(5) and HMRC considered mitigation under Condition A as set out in Regulation 9(3) and Condition B in Regulation 9(4).

53. Condition B in Regulation 9(4) allows HMRC to reduce the amount otherwise payable by a contractor (i.e. the amount he should have deducted and paid over to HMRC) where HMRC is satisfied that the tax due has in fact been paid in full by the subcontractors. This is essentially the power the Appellant is asking HMRC to exercise when he argues that there has been no loss as the subcontractors all paid their own tax in full.

54. Before issuing the Determinations, HMRC exercised its powers under Regulation 9 to reduce the amount of the deductions due from the Appellant under section 61 FA 2004 in relation to contract payments made by him during the period by the amount of tax it (HMRC) was satisfied had been paid by the subcontractors in respect of those contract payments. Using the terms of Regulation 9, the deductible amount of £100,066.68 was in this way reduced to £2,779.51.

55. The Appellant argued that the amount should have been reduced to nil on the grounds that the subcontractors had all paid their own tax in full to HMRC. HMRC said that it had made the reduction it considered appropriate after full consideration of all the facts. The Appellant provided no evidence that the subcontractors in respect of whose contract payments the Determinations were ultimately made had paid in full the tax (and Class 4 contributions) due on them. HMRC said it was unable to provide detailed information relating to the tax affairs of those subcontractors as it was inappropriate and would be a breach of their duties when dealing with taxpayers' personal data.

56. Looking at the wording of Regulation 9(4), HMRC may reduce the amount sought "if an officer of Revenue and Customs is satisfied that the person to whom the contractor made the contract payments…had made a return in respect of his income or profits…in which those payments were taken into account, and paid the income tax and Class 4 contributions due or the corporation tax due in respect of such income or profits".

57. In this case HMRC are not satisfied and there is no provision in the legislation allowing the Tribunal to substitute its own view if it did come to a different conclusion.

58. HMRC also considered Condition A in Regulation 9(3), which allows them to reduce the amount which would otherwise be due if "the contractor satisfies an office of Revenue and Customs- (a) that he took reasonable care to comply with section 61 of the Act and these Regulations, and (b) that (i) the failure to deduct the excess was due to an error made in good faith or (ii) he held a genuine belief that section 61 did not apply to the payment".

59. HMRC's view is that the Appellant did not take reasonable care. HMRC accordingly issued a refusal notice under Regulation 9(6) against which a contractor may appeal under Regulation 9(7), as the Appellant has effectively done.

60. The grounds of an appeal under Regulation 9(7) are limited to the requirements set out in Condition A i.e. that the contractor took reasonable care and either the failure was a genuine error made in good faith or the contractor held a genuine belief section 61 did not apply.

61. This Tribunal does have power to consider the appeal under Regulation 9(8) and if it appears that the refusal notice should not have been issued to direct HMRC to reduce the amount of the Determination under Regulation 9(5).

62. This does not permit the Tribunal to simply consider whether it would have granted the relief had it been in HMRC's place. In order for the Tribunal to direct HMRC under this provision it must find that "the refusal notice should not have been issued", that is that HMRC issued it incorrectly.

63. We believe that the Appellant intended to meet all his legal and tax obligations and did not fail to comply with the CIS rules deliberately or dishonestly. However, this is not the same as taking reasonable care to comply with them. We have not seen or heard evidence that the Appellant took active steps to inform himself of the tax rules that applied to him. The CIS rules were not a new concept at the time and no compelling reason for the Appellant believing that they did not apply to him has been given. We are therefore unable to conclude that the Appellant took reasonable care, objectively, or that HMRC should not have issued the refusal notice.

The Penalties

64. A contractor who failed to file a monthly CIS return on time during the periods relevant in this case was liable for a penalty under section 98A TMA 1970. The Appellant failed to file returns and so was liable for a penalty. HMRC served the penalty notice in accordance with section 100 TMA 1970.

65. Section 98A penalties are required to be of a fixed amount and so the Tribunal's jurisdiction in relation to such penalties is very limited. Under section 100B(a) TMA 1970:

> (1) If the penalty was not incurred, we can set it aside. In this case, as stated above, the Appellant did fail to file the returns and so the penalty was incurred;
>
> (2) If the amount of the penalty is incorrect, we can increase or reduce it to the correct amount and if the amount of the penalty is correct we can confirm it.

66. The amount of the Penalties was correctly calculated in accordance with the provisions of section 98A. The Tribunal has no discretion to alter them based on any view of what is fair. We note that although the Tribunal has no discretion (as is clear from *HOK* and *Bosher*), HMRC have exercised their own discretion under section 102 to reduce the Penalties from £102,300 to £12,852.

CONCLUSION

67. For the reasons set out above, the Appellant's appeal is dismissed.

RIGHT TO APPLY FOR PERMISSION TO APPEAL

68. 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.

JUDGE RACHEL MAINWARING-TAYLOR
TRIBUNAL JUDGE

Release date: 13 May 2020