



TC01918

Appeal number TC/2011/01461

Income tax – Construction Industry Scheme – failure to make nil returns – whether a person who makes payments – penalties- reasonable excuse- proportionality

**FIRST-TIER TRIBUNAL
TAX**

YURIY KOLEYCHUK

Appellant

- and -

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

Respondents

**TRIBUNAL: CHARLES HELLIER
JULIAN STAFFORD**

Sitting in public in Colchester on 28 October 2011

Ann Burjak for the Appellant

Karen Weare for the Respondents

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. DECISION

1. Introduction

2. Mr. Koleychuk seeks to appeal against a large number of £100 penalties and final
5 penalties of £300 and £600 assessed under the construction industry scheme for his
failure timeously to deliver nil returns under that scheme to HMRC for periods
between March 2009 and January 2010. He also seeks to appeal against a penalty in
respect of the February 2009 period in which he delivered a return late.

3. These penalty determinations were issued in batches in May, July, August,
10 October, and November 2009, and in May and July 2010. The penalty notices
informed the recipient of his rights to appeal and stated that any appeal must be made
within 30 days the date of the notice.

4. Mr. Koleychuk did not make any appeal within those 30 day periods.

5. The first issue before us is whether the tribunal should extend the time in which
15 Mr. Koleychuk should be permitted in respect of any of these penalties to appeal. If
the tribunal decides to extend time, the second issue is whether any of the penalties
should be set aside.

6. We deal with the detail of legislation later. However we should explain at this
stage that the legislation requires a relevant person to make returns of payments he
20 has made to subcontractors in periods ending on the 5th of each month (in this
decision we call the return for the period ending 5 March, the “February return” and
so on). The legislation requires nil returns to be made in certain circumstances. The
returns are required to be made by the 19th of the month in which the return period
ends. If the returns are not made in time a penalty is charged. The penalty is £100 if
25 the return is delayed for one month and a further £100 for each subsequent month the
return is delayed. A larger penalty is payable once a return is more than 12 months
late. The penalties are notified by the sending of penalty notices to the taxpayer.

The Evidence

7. We decided to hear the evidence in relation to all these matters and to reserve our
30 decision in relation to all these issues.

8. Mr. Koleychuk's English was poor. Mrs Burjak acted on his behalf as his
interpreter and also gave evidence of her own of her involvement with his affairs. She
brought no documentation with her and so was unable to produce any written
evidence or to refer to her files to assist with the tribunal's questions. Her evidence
35 about the documents she had received and sent to Mr. Koleychuk was sketchy. The
evidence from her directly and through her translation from Mr. Koleychuk as to the
dates of events was uncertain and occasionally inconsistent. She was a forceful
advocate who would have been a better one if she had come properly equipped and
prepared.

40 The Facts

9. We find the following facts.

10. Mr. Koleychuk works as a building labourer. His main work was, at the relevant times, plasterboard fixing. He worked for contractors on building sites. He would be engaged by a contractor whose site manager would allocate parts of the building to him in which he would be required to fix plasterboard. A different area would be allocated to him each day and his work inspected and monitored. If it was deficient he would be told take it out down and start again. Other areas would be allocated to other workers. The work would continue until the available work at the site was finished. Then he would look for other work on a new site.

11. Work on a site would last from a few weeks to a few months. While working on the site Mr. Koleychuk had no other source of income.

12. Mr. Koleychuk was treated by the contractors as a subcontractor rather than an employee for tax purposes. Tax was deducted from payments made to him under the CIS scheme.

13. In February 2009 Mr. Koleychuk had back problems and as a result could not do all the work required of him. He realised that he would lose his contract and that he should do something. He engaged (and paid) a worker to work alongside him to do the tasks he could not do. This stopped before the end of February 2009. Thereafter he returned to his normal mode of work.

14. In May 2009 Mr. Koleychuk approached Mrs Burjak's firm for help with his 2008/2009 tax return. Prior to that date he had had some help with his tax affairs from another accountant and had spoken informally to Mrs Burjak. In May 2009 Mrs Burjak realised that Mr. Koleychuk had engaged a subcontractor and advised him to register under the CIS scheme.

15. He was registered under that scheme on 20 May 2009 and received an information pack from HMRC together with return forms. He submitted CIS returns for the periods from February to May 2009 in June 2009. They were received by HMRC on 16 June 2009.

16. Mr. Koleychuk moved house in July 2009. He lived at his new address for the next two years. It was not clear whether or during what period returns and penalty notices had been sent to his old address. Some were sent thither, and from time to time Mr. Koleychuk went there and found or was given some or all of them. It was not clear when or whether Mr. Koleychuk notified his change of address to HMRC.

17. Mr. Koleychuk's form of appeal had annexed to it a copy of a letter dated 5 March 2009 addressed to HMRC. That letter gave a PAYE reference and an HMRC accounts office reference. Those references were not the CIS scheme references later provided by HMRC to Mr. Koleychuk on his registration under the scheme. The letter said "I would like to inform you that in the nearest future I am not going to have subcontractors. I will inform HMRC if I will need to make CIS declarations. Please do not send me monthly returns."

18. The provenance of this letter was unclear. Mr. Koleychuk suggested its writing had been prompted by his first accountant or possibly as a result of informal conversations with Mrs Burjak before he formally engaged her to help with his tax affairs. Miss Weare could not say that HMRC had received the letter and, given the
5 references on it, it seems to us that its receipt would have been unlikely to have been tied to Mr. Koleychuk's records. It was dated after Mr. Koleychuk had made the payments in February to his helper but before the date of his registration under the CIS scheme.

19. We believe that it is likely that the letter was written after 5 March 2009 and that
10 its date referred to the last period in which Mr. Koleychuk engaged a subcontractor (since the return periods for PAYE and the CIS scheme end on the fifth of each month). The PAYE and accounts office references may well have been those of the contractor for which Mr. Koleychuk was working at the time the letter was written. It may have been posted to HMRC at some time after May 2009, but the evidence
15 before us was not sufficient to conclude that it was likely that it had been.

20. Mrs Burjak told us that she had told Mr. Koleychuk to put a tick in the box on the May 2009 CIS return indicating that he would not have any subcontractors in the next six months. She believed he had done so. However the copy of the return produced to us and received by HMRC had no entry in this box. We conclude that Mr. Koleychuk
20 did not make one. We believe that he did not understand the English in the form well enough to make the necessary entry or forgot or misunderstood Mrs Burjak's instructions.

21. After June 2009 Mr. Koleychuk made no further CIS returns until 16 August 2010. In the meantime he was sent blank CIS returns by HMRC and HMRC sent him
25 penalty notices for the failure to deliver returns on time.

22. The following penalty notices were sent:

- (1) on 29 May 2009 10 notices in respect of the delayed returns for February, March and April 2009.
- (2) one notice on 3 July 2009 for the late return for May 2009;
- 30 (3) two notices sent on 31 July 2009 in respect of May and June 2009;
- (4) three notices on 28 August 2009 in respect of the late returns for May, June and July 2009;
- (5) Four notices on 2 October 2009 in respect the late returns for May, June, July and August 2009;
- 35 (6) Five notices on 30 October 2009 in respect of the late returns for May, June, July, August and September 2009;
- (7) Six notices on 27 November 2009 in respect of the late returns for May to October 2009;
- 40 (8) 39 notices on 12 May 2010 in relation to delayed returns for May 2009 to December 2009;

(9) 8 notices on 28 May 2010 for May 2009 to December 2009;

(10) 8 notices on 2 July 2010 for the same period;

(11) and 7 notices on 30 July 2010 for the same period.

23. The total penalties assessed and under appeal amount to £10,000.

5 24. As a result of his change of address Mr. Koleychuk may not have received all the
penalty notices immediately after their issue but he told us that he had found some of
them on their visits to his previous house. Mrs Burjak said that she thought that Mr.
Koleychuk first contacted her about the notices in 2010 but she was unable to tell us
10 her. She told us that she had told Mr. Koleychuk that he should fill in the returns and
make an appeal against the penalties, but that if he did fill in the returns (as nil
returns) HMRC would reduce the penalties to nil (as she said had happened with other
clients).

15 25. HMRC's Debt Management unit wrote to the appellant in August, and November
2009 and August and November 2010 about the debt accruing by reason of the
penalty notices.

26. For the period ended 5 February 2010 and 5 April 2010 HMRC accepted that Mr.
Koleychuk had made nil returns by telephone. The penalties originally assessed for
these months were cancelled.

20 27. There was correspondence between Mr. Koleychuk (or his advisers) and HMRC
in 2010. HMRC made an offer to reduce the penalties to £6,400 in total. Mr.
Koleychuk notified his appeal to the tribunal on 21 January 2010.

25 28. In April 2010 Mr. Koleychuk was hit by a car. His shoulder was injured and he
was unable to pursue his normal work. Later in 2010 his wife had serious problems
with a pregnancy.

The parties' arguments

29. Mrs Burjak says that the penalties notified after May 2009 are wholly unfair. Mr.
Koleychuk had no subcontractors and no tax went unpaid. Mr. Koleychuk has
difficulties with English. His income is small and he cannot afford expensive
30 accountancy or legal advice. These penalties amount to half his annual income; they
are not just harsh.

35 30. She says that Mr Koleychuk's difficulties with English mean that it is difficult for
him to deal with HMRC on the telephone and no facilities are provided for face-to-
face discussion. For someone who has difficulties with the language face-to-face
discussion is the only effective way of communicating. Mr. Koleychuk's
circumstances should be taken into account.

31. Miss Weare noted that the appeals were out of time. She noted that no explanation had been put forward for the delay. If the tribunal were minded to admit the late appeals then she made the following points.

5 32. First she said that the tribunal had no jurisdiction to address the proportionality of the penalties. Any proportionality challenge could be by way of judicial review in the High Court only.

33. There was no evidence on which the tribunal could conclude that Mr. Koleychuk had a reasonable excuse for his failure to deliver the returns on time.

10 34. The submission of returns in June 2009 showed that Mr. Koleychuk was aware of the requirements of the CIS regime. He had had the information pack and he was sent the returns.

35. The receipt of the batches of penalty notices during 2009 must have made Mr. Koleychuk aware that he was in default.

The Law

15 36. The construction industry scheme in the form relevant of this appeal was introduced by Finance Act 2004. The primary legislation was supplemented by regulations, namely SI 2005/2045. The scheme provides for certain payments made by a “contractor” to subcontractors to be made under deduction of income tax. Subcontractors who are registered for gross payment may receive payment without
20 deduction.

37. A “subcontractor” is defined by section 58 thus:

“For the purposes of this Chapter a party to a contract relating to construction operations is a sub-contractor, if under the contract-

25 (a) he is under a duty to the contractor to carry out the operations, or to furnish labour ...or the labour of others in the carrying out of operations or to arrange for the labour of others to be furnished in the carrying out of operations; or

(b) he is answerable to the contractor for the carrying out of the operations by others...”

30 36. Regulation 1 of the Regulations defines “contractor” to have the same meaning as in section 57 FA 2004. Section 57 FA 2004 defines "construction contract" and, in subsection (2)(b), “contractor”:

35 “(2) In this chapter "construction contract" means a contract relating to construction operations (see section 74) which is not a contract of employment but where --

(a) one party to the contract is a subcontractor (see section 58); and

(b) another party to the contract ("the contractor") either --

(i) is a subcontractor under another such contract relating to all or any of the construction operations, or

(ii) is a person to whom section 59 applies."

5 37. Section 59 describes 12 classes of person. They include the Crown, the NHS and local authorities. But the first category is:

“(a) any person carrying on a business which includes construction operations”.

10 39. Section 70 deals with periodic returns by “persons who make payments under construction contracts”. It permits the Board of HMRC to make regulations about such returns. Under subsection (1) permission is given to make regulations to require persons "who make payments under construction contracts" to make returns in relation to such payments. Subsection (2) provides that provision made in those regulations may include provision requiring:

15 “(d) a return to be made where no payments have been made in the period to which the return relates.”

20 40. We note that this permits regulations to be made only in relation to “persons who make payments under construction contracts”. There are two points to make. First that if a person is merely a contractor, but not a person who “make[s] payments” then the Regulations cannot make, and *cannot be treated as making*, any provision requiring him to make returns.

25 41. Second, the words “who make payments” implies an element of continuity. In our view, on a proper construction of this phrase, a person who has made payments and will never make them again is not a person who “makes” payments; on the other hand a person who has made payments will continue to be a person who makes payments until there cease to be arrangements by virtue of which he may make them.

30 42. A proper construction of “makes” must of course be made in contemplation of the section as a whole. Subsection (2)(d) is part of the whole. It specifically authorises the making of a requirement to submit returns where no payments have been made in the period. The approach to “makes” outlined above does not deprive this provision of effect: a person who makes a payment in January, and who is subject to arrangements under which he will make payments in March, will, in February, be a person who “makes” payments.

35 43. Nor does it seem to us that the legislative purpose of that subsection requires some broader meaning of “makes” so as to encompass a person who at some past time has made payments but has not given notification of his cessation: once a person has ceased to be someone who makes payments there is no need for HMRC to have any interest in him, but if he simply does not make one in the relevant month, there is an interest in monitoring his actions and, through the return obligation, reminding him of his continuing obligations under the scheme.

40 44. Finally we note that we have paid no heed to the terms of the Regulations in construing the Act: secondary legislation can be no guide to the construction of

primary legislation. The words of Regulation 4(11) quoted below provide a sensible way by which a person who is, or is about to become a person who no longer makes payments, may make his position clear – for his own benefit and that of HMRC. But whilst providing a good workable administrative solution it does not help in
5 construing the words of the Act under which it is made.

45. Regulation 4 (1) provides that a “return must be made to HMRC not later than 14 days after the end of every tax month by a contractor making contract payments”. “Contract payments” are (by section 60 FA 2004 and regulation 1) payments made under construction contracts and made by the contractor to a person who is a
10 subcontractor. A tax month is defined as the period beginning on the 6th day of the calendar month and ending on the 5th day of the next. The return must be made by the 19th of the month following that to which the substantial part of the return relates.

46. Thus an obligation arises to make a return arises only if (a) the person is a contractor, and (b) he is a person who “makes” payments under construction
15 contracts.

47. Regulation 4 paragraphs (10) to (13) are particularly relevant to this appeal. They provide:

"(10) If a contractor who has made a return, or should have made a return, under this regulation makes no payments under construction contracts in the tax month following that return, the contractor must make a nil return
20 not later than 14 days after the end of that tax month. This is subject to paragraph (11).

(11) Paragraph (10) does not apply if the contractor has notified the Commissioners for her Majesty's Revenue and Customs that the contractor will make no further payments under construction contracts within the following six months.
25

(12) Subject to paragraph (13), section 98A TMA (special penalties in the case of certain terms) applies to the requirements in -
paragraph (1), ... [and] ... paragraph (10).

(13) A penalty under section 98A of TMA in relation to a failure to make a return in accordance with paragraphs (1) or (10) arises each month (or part of a month) during which the failure continues after the 19th day of the sixth month following the appointed day.”
30

48. We note that regulation (11) requires no particular form for such notification: it may be by letter, fax, email, phone or face to face.
35

49. Section 98A TMA provides relevantly as follows:

"(2) Where this section applies in relation to a provision of regulations, any person who fails to make a return in accordance with the provision shall be liable --

(a) to a penalty or penalties of the relevant monthly amount each month (or part of a month) during which the failure continues ...

5 (b) if the failure continues beyond 12 months, without prejudice to any penalty under paragraph (a) above, to a penalty not exceeding... (ii) in the case of a provision of regulations made under section 70(1)(a) or 71 [FA]2004, £3000.

10 “(3) For the purposes of subsection (2)(a) above, the relevant monthly amount in the case of the a failure to make a return -- (a) where the number of persons in respect of whom particulars should be included in the return is 50 or less, £100 ...”

50. Section 118(2) TMA provides:

15 "(2) ... 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 ceased."

Discussion

51. We consider first whether appeals should be permitted out of time.

20 52. Mrs Burjak indicated that, if permission was given to appeal out of time , the appellant did not wish the case to be referred for a formal review by HMRC, and that the appeal should be considered by the tribunal.

25 53. In deciding whether to permit Mr Koleychuk to appeal out of time the tribunal must seek to act justly and fairly. That involves taking into account all relevant factors and performing a balancing exercise. Rule 3.9(1) of the Civil Procedure Rules contains a list of factors to be taken into account by a court in similar circumstances. We should also normally have regard whether the applicant has a good prima facie case; in this case we had the advantage of hearing all the parties' evidence and submissions so we are therefore able to be clearer in our assessment of the strength of
30 the case. The following considerations appeared to us to be relevant:

- (1) that the administration of justice was generally best served by the adherence to time limits prescribed by statute;
- (2) that the failure to appeal promptly did not appear to us to have been intentional but arose as a result of Mr Koleychuk's limited means, limited
35 English, and lack of understanding of the system;
- (3) that the penalties at issue are in aggregate very large in relation to Mr Koleychuk's means and would bear heavily on him;
- (4) that in relation to the later penalties it seemed to us that there was a good case that they were not exigible;

(5) that HMRC would not in the circumstances be put to extra expense if we extended the time limit for appeal, nor would uncertainty be created over its tax collection, although it could lose the benefit of the assessed penalties.

5 54. In our judgement these factors indicated that an extension of time should not be allowed in relation to the penalties notified on 29 May 2009. At that time Mr Koleychuk was dealing with, and could reasonably have sought advice from his accountant . In relation to those penalties he has in our view no reasonable excuse for his delay and no tenable argument that they are not due.

10 55. By contrast in relation to the penalties notified on and after 3 July 2009, Mr Koleychuk's move and the consequent late receipt of at least some of the penalty notices, his limited means to pay for advice, from April 2010 his injury, and the strength of the case that the penalties were not due caused us to conclude that an extension of time to appeal should be granted.

15 **The Merits**

56. In February 2009 Mr. Koleychuk was a party to a contract relating to construction operations (plaster boarding) and under that contract was under a duty to carry out the operations or to furnish labour to carry out those operations. As a result he was, for the purposes of section 59, a subcontractor.

20 57. We then asked whether the contract between Mr. Koleychuk and the worker he engaged was a "construction contract" within section 57. It would be such a contract only if:

(1) it was not a contract of employment;

(2) one party (the worker) was a subcontractor; and

25 (3) the other party (Mr Koleychuk) was a subcontractor under another such contract or a person carrying on a business which included construction operations.

30 58. There was no evidence before us as to whether the contract between the worker and Mr. Koleychuk was or was not a contract of employment. If it was a contract of employment it could not be a construction contract. But, given that the February 2009 CIS return was made on the advice of his accountant, it seems likely that there was some evidence that the worker was not an employee. On the evidence before us we find that it was not proved that he was not an employee.

35 59. On the bases that the contract between Mr. Koleychuk and his worker was not one of employment, and that Mr. Koleychuk himself was not an employee (which was not questioned by Mrs Burjak) that contract would be a construction contract because the worker would be a subcontractor within section 58 and Mr. Koleychuk would also be a subcontractor by reference to his contract with his main contractor.

40 60. As we have noted, section 70 permits regulations to be made requiring returns to be made by "persons who make payments under construction contracts". On the basis

recorded above that neither Mr. Koleychuk nor the worker were employees, the payments made by Mr. Koleychuk to his worker would have been payments under a construction contract, and as a result Mr. Koleychuk would in February 2009 have been such a person and the regulations could apply to him.

5 61. In March 2009 we believe that Mr. K could still properly be called a person who “makes payments under construction contracts”. He had made such payments in the previous period and the reason that he had made them (his bad back) had only just ceased.

10 62. In April 2009 the shadow of his previous need for help, and the possibility that it might recur, persuades us that Mr Koleychuk could still properly be described as a person who made such payments and was therefore a person to whom the regulations could apply.

15 63. But by May 2009, two months had passed since Mr Koleychuk engaged another person to do construction work in his stead. By then the problems with his back were history and he was, we believe, working on his own again. By then the arrangements which gave rise to his having made payments had clearly ceased and he could not properly be described as a person who makes payments under construction contracts. His activity was providing his own labour in controlled circumstances for another, and did not encompass arranging for others to work him.

20 64. From May onwards we do not believe that Mr Koleychuk could properly be described as such a person.

25 65. As a result in our judgement from May onwards Mr Koleychuk could not be, and was not, required by the regulations to make any returns. As a result his failure to make them was not a failure to which regulation 4(13) could apply, and no penalty arose under section 98A in respect of any such failure.

30 66. However Mr Koleychuk was a person to whom the regulations did apply in February and March and April 2009. In those months he failed to provide a return by the stipulated time and regulation 4(13) applied. As a result the penalties of £400 in respect of the February return, £300 in respect of the March return, and £200 in respect of the April return were properly exigible unless he had a reasonable excuse for his failure.

35 67. We do not believe that Mr Koleychuk had a reasonable excuse for his failure. He may not have been aware of his obligations to make returns but ignorance of the law cannot be a reasonable excuse. No other reason for his failure was advanced in relation to the period before June 2009 other than perhaps his difficulty with English. But no link was made between that difficulty and his failure to make these early returns.

68. We therefore find that the penalties in respect of the February, March and April returns were properly chargeable. Section 118 TMA does not provide an escape.

69. Miss Weare suggested that this tribunal did not have jurisdiction to deal with the question of proportionality. We disagree. Section 7 of the Human Rights Act 1998 provides that "a person who claims that a public authority has acted ... in a way which is made unlawful by section 6 (1) may ... rely on the Convention right in any legal proceedings." Proceedings before this tribunal constitute legal proceedings and this tribunal therefore has the power and the duty to consider the effect of any such claim of unlawful action.

70. Section 6(1) provides that it is unlawful for a public authority to act in a way which is incompatible with a Convention right. If the assessment of the penalties under appeal was made unlawful by section 6(1) the tribunal would have to take account of that fact.

71. However section 6(2) provides that section 6(1) does not apply to acts of an authority which are compelled by primary legislation or which were to give effect to such legislation. In *Bysermaw* [2007] UK SPC 644 the Special Commissioners found that as a result of this provision section 7 HRA could not be relied on in relation to CIS penalties.

72.

73. However, we have found that only some £1000 of penalties are exigible in respect of his failure to deliver returns on time. It is clear to us that a penalty of £1000 bears harshly upon Mr Koleychuk but it does not seem to us to be wholly unfair in the circumstances. As a result it cannot be disproportionate and we have no need to consider the application of section 7(1) of the Human Rights Act.

Conclusion

74. We allow the appeal in respect of the penalties issued after 29 May 2009.

75. Had we extended time for appealing the earlier penalties we would have dismissed the appeal in relation to the penalties levied in respect of the periods ending on 5 February, March, and April 2009 and allowed the appeal in respect of the penalty for the period 5 May 2009. The appeals in relation to these periods are struck out.

76. The result is that in aggregate penalties of £1,000 are properly payable.

Rights of Appeal

77. 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.

CHARLES HELLIER

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TRIBUNAL JUDGE
RELEASE DATE: 09 February 2012

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