



**TC02155**

**Appeal number: TC/2012/00792**

***INCOME TAX– Construction Industry Scheme – cancellation of registration for gross payment status (Finance Act 2004 s66) - failure to meet compliance test – whether there was a “reasonable excuse” for compliance failure – relevance of compliance failures outside qualifying period considered –cumulative effect of extended payments terms on customer contract, bad debt, and difficulties securing overdraft amounted to reasonable excuse - appeal allowed***

**FIRST-TIER TRIBUNAL  
TAX CHAMBER**

**P S R CONTROL SYSTEMS LIMITED**

**Appellant**

**- and -**

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

**Respondents**

**TRIBUNAL: JUDGE SWAMI RAGHAVAN  
SIMON BIRD**

**Sitting in public in Cardiff on 27 March 2012**

**Mr P. Rodger, director of the appellant on behalf of the appellant**

**Ms K. Evans, Higher Officer, HMRC, for the Respondents**

## DECISION

### *Introduction*

1. The appellant appeals against HMRC's decision to cancel its registration to  
5 make gross payments to sub-contractors under the Construction Industry Scheme  
("CIS").

2. HMRC may cancel a contractor's gross payment registration if the contractor  
does not comply with its obligations under the Taxes Acts. HMRC point to the  
appellant's compliance failure in making a late payment of PAYE tax during the  
10 twelve month period preceding their decision to cancel.

3. The appellant argues it has a reasonable excuse for the late payment due to  
cashflow difficulties arising out of the late payment due to it from a customer, a bad  
debt and difficulties securing an overdraft. HMRC disagree the appellant has a  
reasonable excuse.

### 15 *Evidence*

4. We had before us a bundle of copy correspondence between HMRC and the  
appellant. In addition we heard oral evidence from Mr Rodger which HMRC were  
able to cross-examine.

### 20 **Law**

5. The provisions of the CIS Scheme are set out in Finance Act 2004. The relevant  
provisions for the purposes of this appeal are set out below.

#### **63 Registration for gross payment or for payment under deduction**

...

25 (2) If the Board are satisfied that the requirements of subsection (2),  
(3) or (4) of section 64 are met, the Board must register—

(a) the individual or company, ...

for gross payment.

...

#### 30 **64 Requirements for registration for gross payment**

(1) This section sets out the requirements (in addition to that in  
subsection (1) of section 63) for an applicant to be registered for gross  
payment.

...

35 (4) Where the application is for the registration for gross payment  
of a company (otherwise than as a partner in a firm)—

(a) the company must satisfy the conditions in Part 3 of Schedule 11 to this Act, ...

### **66 Cancellation of registration for gross payment**

5 (1) The Board of Inland Revenue may at any time make a determination cancelling a person's registration for gross payment if it appears to them that—

(a) if an application to register the person for gross payment were to be made at that time, the Board would refuse so to register him,

10 ...

(5) On making a determination under this section cancelling a person's registration for gross payment, the Board must without delay give the person notice stating the reasons for the cancellation.

### **Schedule 11 Part 3**

#### **Conditions to be satisfied by companies**

##### *General*

9

20 In the case of an application for a company to be registered for gross payment (whether as a partner in a firm or otherwise), the following conditions must be satisfied by the company.

##### The compliance test

12—

25 (1) The company must, subject to sub-paragraphs (2) and (3), have complied with—

(a) all obligations imposed on it in the qualifying period (see paragraph 14) by or under the Tax Acts or the Taxes Management Act 1970 (c 9); and...

30 (2) A company that has failed to comply with such an obligation or request as—

(a) is referred to in sub-paragraph (1), and

(b) is of a kind prescribed by regulations made by the Board of Inland Revenue,

35 is, in such circumstances as may be prescribed by the regulations, to be treated as satisfying the condition in that sub-paragraph as regards that obligation or request.

40 (3) A company that has failed to comply with such an obligation or request as is referred to in sub-paragraph (1) is to be treated as satisfying the condition in that sub-paragraph as regards that obligation or request if the Board of Inland Revenue are of the opinion that—

(a) the company had a reasonable excuse for the failure to comply, and

(b) if the excuse ceased, it complied with the obligation or request without unreasonable delay after the excuse had ceased.

5 ...

(8) Subject to sub-paragraphs (2) and (3), a company is not to be taken for the purposes of this paragraph to have complied with any such obligation or request as is referred to in sub-paragraphs (1) to (6) if there has been a contravention of a requirement as to—

10 (a) the time at which, or

(b) the period within which,

the obligation or request was to be complied with.

**“Qualifying period”**

15 14

In this Schedule “the qualifying period” means the period of 12 months ending with the date of the application in question.

**Income tax (Construction Industry Scheme) Regulations 2005**

20 32—

(1) The obligations and requests prescribed for the purposes of paragraphs 4(3), 8(2) and 12(2) of Schedule 11 to the Act are given in column 1 of Table 3.

25 (2) The circumstances prescribed in which the applicant or company is to be treated as satisfying the conditions in paragraphs 4(1), 8(1) or 12(1) of Schedule 11 to the Act as regards each of the prescribed obligations are given in column 2 of Table 3.

**Table 3**

<i>1. Prescribed obligations</i>	<i>2. Prescribed circumstances</i>
Obligation to pay—  (a) ... (b) tax liable to be deducted under the PAYE Regulations.	(1) Payment is made not later than 14 days after the due date, and (2) the applicant or company— (a) has not otherwise failed to comply with this obligation within the previous 12 months, or (b) has failed to comply with this obligation on not more than two occasions within the previous 12 months.

30

6. In addition the following cases were referred to:

*Ductaire Fabrications v HMRC* [2009] UKFTT 350 (TC)

*Scofield v HMRC* [2011] UKFTT 199 (TC)

*Industrial Contracting Services Ltd. v HMRC* [2011] UKFTT 290 (TC)

5 *Cardiff Lift Company v HMRC* [2011] UKFTT 628 (TC)

*CCE Commissioners v Steptoe* [1992] STC 757

### **Background facts**

#### *Decision to cancel gross payment certificate*

10 7. HMRC made a decision to cancel the appellant's gross payment status under CIS scheme on 8 August 2011.

8. The decision to cancel was made because of a compliance failure during the 12 months preceding the decision to cancel. The appellant had failed to pay PAYE tax for the tax month 5 October 2010. This had been due on 22 October 2010 but was received 75 days late on 4 January 2011.

#### 15 *The business*

20 9. The appellant company is a contractor which carries out specialist electrical control design, manufacture and servicing work in the field of heat and ventilation systems. The work is almost exclusively for commercial clients such as Hoover, Panasonic, and also for local authorities. The company's work was seasonal in the sense that over the summer they were kept busy with longer term contract work while in the winter period work was typically quieter and consisted of work arising from ad hoc maintenance requests and reacting to breakdowns.

25 10. The company was started in 2003 by Mr Peter Rodger who had previously been working in electrical control design for 40 years. The company employs 4 staff including Mr Rodger. As well as being a director of the company and carrying out technical work, Mr Rodger is responsible for the company's administration. Staff are paid weekly and the PAYE amounts are between £3 – 4,000 per month.

30 11. The appellant's standard invoice terms are 30 days. The contracts typically provide for retentions from the invoice sum. This is usually 5 % but can sometimes be 7%. The company normally carries around £12,000 of retentions at any given time.

12. The appellant had from at least 2009 been attempting to get an overdraft facility with its bank, HSBC. Mr Rodger had had to put in £18,000 of his own savings into the company to enable the company to meet its commitments and he had on occasions chosen to take a reduced amount of his own salary. Eventually an overdraft facility of

£12,000 was secured in around March 2011. Since obtaining the overdraft the appellant's cashflow was significantly improved.

13. In April / May 2010 the appellant had carried out work for Noelty James (Newport). The sum due was around £14,000. Despite chasing for this debt it went  
5 unpaid and in December 2010 / January 2011 it had to be written off.

14. In the summer of 2010 the company had been working flat out on a contract for Abertillery comprehensive school. This work was invoiced in October 2010. The local authority's payment terms were 90 days.

#### *Appellant's arguments*

10 15. Keeping gross payment status under the CIS scheme was important to the company's reputation. It had recently won certain contracts and was in negotiations for another. Loss of gross payment status would jeopardise this.

15 16. There were exceptional circumstances outside of the appellant's control which meant the appellant had a reasonable excuse for non-compliance. These were the difficulties in arranging finance with HSBC, bad debts the company had suffered, seasonality of the company's work, and the level of retentions that were held back on invoice payments.

#### *Respondents' arguments*

20 17. The late payment of PAYE tax due on 22 October 2010 but not received until 4 January 2011. This constituted a compliance failure for the purposes of the relevant legislation.

25 18. The appellant did not have a reasonable excuse for the compliance failure. While the concept of reasonable excuse was not defined in the legislation, in HMRC's view there had to be exceptional circumstances which were beyond the taxpayer's control. That was not the case here. Cashflow difficulties are not a reasonable excuse as the appellant should make appropriate contingency plans to deal with these.

19. In addition to the compliance failures described above the annual review carried out on 28 June 2010 showed there had been 5 late payments of PAYE tax (due dates between 22 September 2009 to 22 March 2010).

30 20. The appellant had been warned by a letter from HMRC on 17 November 2009 of the consequences of compliance failures on its gross payment status but had not heeded this warning.

#### *Discussion*

35 21. There are a number of tests required for a contractor to be granted gross payment status within CIS, these comprise the business, turnover, and compliance

tests. Once such status has been granted HMRC may make a determination cancelling a person's registration for gross payment if it appears to them that —

“if an application to register the person for gross payment were to be made at that time, the Board would refuse so to register him...”

5 22. The particular test in issue in this appeal is the compliance test and accordingly whether the appellant has complied with its obligations under the Taxes Acts in the “qualifying period”. That period is defined in the legislation as the “period of 12 months ending with the date of the application in question”. In the context of a determination by HMRC to cancel gross payment status this means the qualifying  
10 period is the 12 months preceding the determination to cancel which in this case took place on 8 August 2011.

23. The particular compliance failure relied on by HMRC is that PAYE tax which was due on 22 October 2010 was paid late on 4 January 2011. The fact that payment was made late not being in dispute, the key issue for the Tribunal to determine is  
15 whether the appellant had a reasonable excuse for the failure.

*Meaning of reasonable excuse*

24. We disagree with HMRC’s argument that there must be exceptional circumstances in order for there to be a reasonable excuse. That term must, we think, be given its ordinary meaning. Whether there is a reasonable excuse has to be  
20 assessed against the backdrop of the particular facts and evidence before the Tribunal.

25. A large part of the appellant’s arguments and evidence were directed towards the effect withdrawal of gross payment status would have on its business. HMRC submit that this factor is irrelevant to considering whether there is a reasonable excuse for the compliance failure, and drew our attention to First-tier Tribunal decision of  
25 *Ductaire Fabrications* in support. We agree with this submission and therefore have not taken the effect on the business of withdrawal of gross payment status into account.

*Relevance of previous compliance failures*

26. HMRC have in the course of their submissions drawn our attention to previous compliance failures of the appellant in paying PAYE tax late which they maintain  
30 occurred between 22 September 2009 and 22 March 2010. There was no indication that the facts of these late payments had been agreed with the appellant and no evidence beyond a letter from HMRC to the appellant stating the amounts and dates of the late payments.

35 27. In any event, even if we had been able to make findings of fact in relation to the earlier failures alleged it was not made clear to us what the relevance of these failures was to the issue of whether the appellant had a reasonable excuse for the late payment of its October 2010 PAYE tax.

28. Even if the fact of the previous failures was established we doubt that would assist us in the determination before us as the issue of whether the appellant had a reasonable excuse for any such previous failures has not been tested.

5 29. Also, given the legislation clearly envisages a cut-off point for assessing the compliance test in the form of a 12 month qualifying period, it is questionable whether consideration of compliance failures prior to that period, even if their purpose is to illuminate the circumstances of a compliance failure within the 12 month period can be consistent with the scheme of the legislation.

*Did the appellant have a reasonable excuse?*

10 30. The appellant did not put any documentary evidence before us, but its director Mr Rodger did give extensive oral evidence which was subject to cross examination by HMRC. Mr Rodger also assisted the Tribunal with its further questions. Mr Rodger had set the appellant company up, and ran the company. He was very knowledgeable about its affairs. We found him to be a credible witness and were able  
15 to make findings of fact on the basis of his evidence.

31. In so far as the appellant's contention was that he had a reasonable excuse for the late payment due to cashflow difficulties we accept HMRC's submission that this in and of itself does not amount to a reasonable excuse. It is necessary we think to explore the reasons for the cashflow difficulties and to consider what actions the  
20 appellant took to prepare for and mitigate those difficulties.

32. In this appeal there are several circumstances which we think are relevant to the issue of whether the appellant had a reasonable excuse. First, the lengthier than usual payment terms of the Abertillery school contract which was invoiced at the beginning of October 2010. We accepted Mr Rodger's evidence that the payment terms for this  
25 particular contract turned out to be 90 days whereas the appellant's standard invoice terms stipulated 30 days. Second, we accepted Mr Rodger's evidence that there was a crystallisation of a bad debt amount of around £14,000 in December 2010/January 2011 which the appellant had been chasing for for a number of months previously. Third, there was an ongoing issue of the appellant not being able to secure an  
30 overdraft facility with HSBC which would have helped to alleviate its cashflow issues. We accepted Mr Rodger's evidence that he been in negotiations to secure an overdraft facility for the appellant but these were prolonged and as at the period of the failure to pay the PAYE tax in issue, the overdraft was not in place. He had not therefore passively accepted the situation the company was in but was attempting to  
35 improve matters.

33. In assessing whether the appellant has a reasonable excuse we think it is reasonable to expect that a business should plan for the contingencies it may face and that it should take into account the particular environment in which it operates. It should take steps to organise its affairs in such a way that tax payments are made on  
40 time. When the taxpayer does not pay over the PAYE deductions it has made on time this effectively amounts to the taxpayer unilaterally taking credit, at the expense of the general body of taxpayers. As has been pointed out by other tribunals this also puts

the late payer at a competitive advantage to those who do organise their affairs so as to pay on time. The seasonal nature of the type of the work the appellant does and the amounts of contract retentions are things which we think it is reasonable for the appellant to plan for appropriately in order that payments can be made on time.

5 *Conclusion*

34. In relation to the extended payment terms of the school contract, the bad debt and the difficulties securing an overdraft, we are doubtful that any of these matters when viewed individually would amount to a reasonable excuse for the whole of the period of the late payment (October 2010 to January 2011). However we are of the  
10 view that when considered cumulatively, these matters amount to circumstances which constitute a reasonable excuse and further that they constitute a reasonable excuse which subsisted during the period October 2010 through to January 2011.

35. We accordingly allow the appellant's appeal.

36. This document contains full findings of fact and reasons for the decision. Any  
15 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  
20 "Guidance to accompany a Decision from the First-tier Tribunal (Tax Chamber)" which accompanies and forms part of this decision notice.

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**SWAMI RAGHAVAN  
TRIBUNAL JUDGE**

**RELEASE DATE: 27 July 2012**

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