



TC02212

Appeal number: TC/2012/579

*Construction Industry Scheme – cancellation of gross payment registration -
breaches of compliance test – whether reasonable excuse under para 8(3) sch 11
FA 2004 – whether forgiveness under reg 32 Income Tax (Construction Industry
Scheme) Regulations 2005 (SI 2005/2045) – appeal dismissed*

**FIRST-TIER TRIBUNAL
TAX CHAMBER**

BASE BRICKWORK (a firm)

Appellant

- and -

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

**TRIBUNAL: JUDGE PETER KEMPSTER
Mr GORDON MARJORAM**

Sitting in public at Priory Courts, Birmingham on 21 May 2012

Mr Robert Thorne FCCA for the Appellant

Mr Martin Foster (HMRC Appeals Unit) for the Respondents

DECISION

1. By a notice of appeal dated 19 December 2011 the Appellant (“the Firm”) appealed against a determination by the Respondents (“HMRC”) dated 5 August 2011 cancelling the Firm’s gross payment registration under the construction industry scheme.

The Construction Industry Scheme

2. Legislation cited in this decision notice is as in force at the time of the events relevant to this appeal, and unless otherwise stated statutory references are to Finance Act 2004 and references to regulations are to The Income Tax (Construction Industry Scheme) Regulations 2005 (SI 2005/2045).

3. Chapter 3 of Part 3 FA 2004 establishes the construction industry scheme (“CIS”). For the purposes of the current appeal the CIS may be summarised as follows. The CIS applies to contract payments (s 60) under construction contracts (s 57). The payer is called the contractor (s 59) and the payee is called the sub-contractor (s 58). Contractors are obliged to deduct tax at source from contract payments to sub-contractors (s 61) but sub-contractors may be registered for gross payment (s 63) if they meet specified conditions (s 64 and sch 11). A gross payment registration may be cancelled in certain circumstances (s 66) but the sub-contractor may appeal against such cancellation to this Tribunal (s 67).

4. One of the requirements for gross payment registration of a firm is that the firm and all the partners are compliant with their tax affairs – the compliance test – as set out in para 8 sch 11:

“(1) Subject to sub-paragraphs (2) and (3), each of the persons who are partners at the time of the application must have complied, so far as any such charge to income tax or corporation tax is concerned as falls to be computed by reference to the profits or gains of the firm's business, with—

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

(b) all requests made in the qualifying period to him as such a partner to supply to the Inland Revenue accounts of, or other information about, the firm's business or his share of the profits or gains of that business.

(2) Where a person 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,

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

5 (3) Where a person has failed to comply with such an obligation or request as is referred to in sub-paragraph (1), the firm is to be treated, in relation to that partner, 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—

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

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

15 (4) There must be reason to expect that each of the persons who are from time to time partners in the firm will, in respect of periods after the qualifying period, comply with such obligations and requests as are referred to in sub-paragraph (1).

20 (5) Subject to sub-paragraphs (2) and (3), a person 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-paragraph (1) if there has been a contravention of a requirement as to—

(a) the time at which, or

(b) the period within which,

the obligation or request was to be complied with.”

25 5. One of the circumstances in which the gross payment registration of a firm can be cancelled is where the firm or any partner breaches the compliance test – s 66(1) states:

30 “(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,

35 (b) he has made an incorrect return or provided incorrect information (whether as a contractor or as a sub-contractor) under any provision of this Chapter or of regulations made under it, or

(c) he has failed to comply (whether as a contractor or as a sub-contractor) with any such provision.”

40 6. That places an onerous responsibility on the firm and the partners to keep all their tax affairs up-to-date. Amendments to the CIS since its introduction in 2004 (for example, in 2008) have tightened this responsibility, so it is clear that Parliament has intended the responsibility to be an onerous one. However, some measure of relief is provided by (i) the “reasonable excuse” exception in the compliance test (para 8(3) sch 11, quoted above); and (ii) Reg 32 of the 2005 CIS Regulations, which provides:

“Compliance test

Exceptions from compliance obligations

32—

5 (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.

10 (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 submit monthly contractor return within the required period.	(1) Return is submitted not later than 28 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.
Obligation to pay— (a) the amount liable to be deducted under section 61 of the Act from payments made during that tax period, or (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.
Obligation to pay income tax.	(1) Payment is made not later than 28 days after the due date, and (2) the applicant has not otherwise failed to comply with this obligation within the previous 12 months.
Obligation to submit a return under regulation 73, 74 and 85 of the PAYE Regulations (annual returns) within the required period.	Return is submitted after the due date.
Obligation to pay corporation tax for which the applicant or company is liable.	(1) Payment is made not later than 28 days after the due date, and (2) any shortfall in that payment has incurred an interest charge but no penalty.
Obligation to submit a self-assessment return within the required period.	Return is submitted after the due date.
Obligations and requests referred to in paragraphs 4(1), 8(1) and 12(1) of Schedule 11 to the Act.	The failure to comply occurred before the appointed day and was within section 562(10), 564(4) or 565(4) of ICTA (conditions to be satisfied: minor and technical failures).
Obligation to make a payment under the Tax Acts or Taxes Management Act 1970.	Late, or non-payment of an amount under £100.

Background

7. The Firm comprises three partners: Mr Etherson, Mr Aslam and Mr Sargent. Mr Sargent no longer takes an active part in the business.

5 8. As part of HMRC's routine compliance checks on the operation of the CIS, the Firm was selected for review of its gross payment status for the twelve month period ended 21 May 2011. On 9 June 2011 HMRC informed the Firm that several late payments had been noted, and invited any explanations. The Firm replied on 20 June 2011 apologising for the late payments; stating they were unaware of the impact this would have on their gross payment status; and explaining the cash flow problems
10 suffered by the business.

9. On 5 August 2011 HMRC formally notified the Firm of cancellation of its gross payment registration, listing the following breaches of the compliance test;

- (1) Self-assessment second payment on account due on 31 July 2010 was not paid in full on time.
- 15 (2) Self-assessment first payment on account due on 31 January 2011 was not paid in full on time.
- (3) Self-assessment balancing charge due on 31 January 2011 was not paid in full on time.
- (4) PAYE payment due for the tax month ended 5 May 2010 was not paid in
20 full on time.
- (5) PAYE payment due for the tax month ended 5 June 2010 was not paid in full on time.
- (6) PAYE payment due for the tax month ended 5 July 2010 was not paid in full on time.
- 25 (7) PAYE payment due for the tax month ended 5 August 2010 was not paid in full on time.
- (8) PAYE payment due for the tax month ended 5 September 2010 was not paid in full on time.
- (9) PAYE payment due for the tax month ended 5 October 2010 was not paid
30 in full on time.
- (10) PAYE payment due for the tax month ended 5 November 2010 was not paid in full on time.
- (11) PAYE payment due for the tax month ended 5 February 2011 was not paid in full on time.
- 35 (12) PAYE payment due for the tax month ended 5 March 2011 was not paid in full on time.

10. On 6 September 2011 the Firm's accountant wrote to HMRC explaining the cashflow problems experienced by the Firm in the relevant period. On 26 September

HMRC replied that they did not consider there to have been a reasonable excuse for the late payments. The accountant requested a formal internal review of the cancellation decision and, on 7 November, made further representations. On 9 December 2011 HMRC gave its review decision, upholding the original decision. On 5 19 December the Firm appealed to the Tribunal.

Submissions

11. For the Firm Mr Thorne submitted as follows:

10 (1) The construction industry was badly affected by the current economic recession. The Firm had a single main customer (“the Customer”) who had continued to award contracts to the Firm but had taken longer to pay for work performed. Payment had slipped from one week to two, then eventually to eight weeks – the Customer had “moved the goal posts”. That meant the Firm had to fund eight weeks’ labour costs from its own resources. A new temporary overdraft facility had been granted by the Firm’s bank and had been used in full. 15 In May 2010 the partners had put £20,000 additional capital into the business, which had entailed remortgaging their homes (against the wishes of their respective wives). The PAYE liabilities for December 2010 and January 2011 had been paid on time because the wage bills for those months had been low – December had severe weather and then there was the Christmas and New Year shutdown – and payments were being received from the Customer in respect of work done eight weeks earlier, hence the bank balance was healthier. The cashflow position deteriorated again after February 2011. 20

25 (2) In July 2010 Mr Etherson had realised the Firm had insufficient funds to meet that month’s PAYE liability, and had personally visited HMRC’s office in Coventry to discuss the position. As he had no appointment he was dealt with by an internal telephone call from a booth in the foyer; he was told a first late payment of PAYE attracted no penalty but further defaults would carry penalties. No advice had been given about time-to-pay arrangements. The PAYE had been paid in full, a few days late. The monthly returns had been filed on time throughout. The Firm appreciated that there may be penalties and interest on late payments. There was the same funds problem the following month so Mr Etherson again visited HMRC and was told that PAYE penalties would escalate from 1% to 4% depending on the number of late payments. The PAYE was paid in full 14 days late. The funds problems continued but no further visits were made to HMRC because the advice already received had been clear and consistent. At no time was the possibility of cancellation of gross payment status mentioned by HMRC; there had been no warning letter from HMRC intimating this might happen. The Firm had not appreciated the potentially serious consequences of late payment on its gross payment status and, if it had been made aware, may have been able to avoid or mitigate the late payments. Since being made aware of the true position by HMRC all PAYE liabilities had been paid on time. 30 35 40

(3) The Firm had done everything expected of a reasonable person; the partners had put in substantial additional capital; HMRC had been kept

informed of the position and advice sought; all the liabilities had been met in full; the maximum delay had been 19 days. The consequences of cancellation of gross payment status would be very serious; work and workers would have to be laid off; twenty years' of hard work could be destroyed; new contractors had been won but required possession of a gross payment certificate; the Firm would be unable to take on apprentices.

12. For HMRC Mr Foster submitted as follows:

(1) The number of late payments demonstrated a serious failure of the compliance test. The Firm and all three partners had made late payments in the period under review.

(2) HMRC had properly considered whether the explanations put forward to them could constitute a reasonable excuse for any of the late payments. HMRC considered that only unexpected or unusual events would qualify. The Firm had continued to accept work from the Customer despite the increased delays in payment of invoices; the impact on cashflow was not unexpected and should have been understood.

(3) Although the statutory regime was strict, it was important that it be applied evenly for all sub-contractors. There was no obligation on HMRC to issue warning letters. A comprehensive information pack would have been provided to the firm when it was first registered under the CIS. No record of the conversation at the Coventry tax office was available and it may be that the officer was not even aware that the Firm was within the CIS.

Consideration and conclusions

13. The breaches of the compliance test in the year ended 21 May 2011 fell into three categories:

(1) *Nine late payments of PAYE liabilities* – The Tribunal considered that, on balance, the Firm had a reasonable excuse (within the meaning of para 8(3) sch 11) for these late payments taking together (a) the unilateral extension of payment terms imposed by the Customer, and (b) the apparent failure by HMRC's telephone adviser to advise on the possible availability of a time-to-pay arrangement.

(2) *Late payment by all three partners of the July 2010 income tax instalment* - The Tribunal considered that, on balance, the partners had a reasonable excuse (within the statutory meaning) for these late payments considering the unilateral extension of payment terms imposed by the Customer.

(3) *Late payment by all three partners of the January 2011 income tax instalments* - The Tribunal considered that by this time the exceptional impact of the change of terms by the Customer had been replaced by a more general cashflow problem for the partners. The Firm had managed to pay its PAYE liabilities on time for a couple of months. While those difficulties were understandable and unfortunate, they could not constitute a reasonable excuse (within the statutory meaning) for these late payments. Regulation 32 permitted

the “forgiveness” of a single failure but only if the lateness of the payment did not exceed 28 days. Here at least one of the partners (certainly Mr Sargent and perhaps also Mr Etherson) had exceeded that latitude in late payment.

14. As the compliance test had been breached, HMRC were correct to cancel the Firm’s gross payment registration. While the consequences of that action might be very serious for the Firm, the Tribunal has no discretion to take that into account in reaching its decision: *Barnes v Hilton Main Construction* [2005] STC 1532.

Decision

15. For the reasons stated at ¶ 14 above, the appeal is DISMISSED.
16. This document contains full findings of fact and reasons for the decision and replaces the summary decision notice issued to the parties on 13 June 2012. 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.

**PETER KEMPSTER
TRIBUNAL JUDGE**

RELEASE DATE: 22 August 2012