[2017] UKFTT 197 (TC)

# TC05685

**Appeal number: TC/2016/01998**

***INCOME TAX – PAYE regulations – effect of regulation 80 determination on consideration of a direction under regulation 72(5)***

**FIRST-TIER TRIBUNAL**
**TAX CHAMBER**

**CHAMPNEYS TRING LIMITED** **Appellant**

**- and -**

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

**TRIBUNAL: JUDGE VICTORIA NICHOLL**
**MR LESLIE HOWARD**

**Sitting in public at Bedford on 27 January 2017**

**Mr Paul Mitchell and Mr Jamie Flarry, Finance Director and Employee Accounting Manager of the Appellant, for the Appellant**

**Ms Hellie Lai, HM Revenue and Customs presenting officer, for the Respondents**

DECISION

1. This is an appeal by the Appellant ("Champneys") against a determination made by the Respondents ("HMRC") on 16 July 2015 under regulation 80 of the Income Tax (PAYE) Regulations 2003 (the "Regulations") in respect of £1527.89 tax which Champneys failed to deduct from the earnings of an employee (the "employee") in the tax year 2013/14.

**Facts**

2. Mr Mitchell and Mr Flarry of Champneys both gave evidence and Mr Flarry presented the case for Champneys. We accepted five pages of further evidence for Champneys at the hearing as they were extracts from Champneys Full Payment Submission ("FPS") for the first payment period for which the employee was paid and two print outs showing no tax code notices were issued in respect of the employee. We find the following facts from the evidence in the tribunal bundle, further evidence and the oral evidence.

3. Champneys joined the Pay as You Earn ("PAYE") scheme on 2 January 1993. It operates through twelve companies and employs over 1,000 employees. Mr Flarry has managed Champneys's payroll issues since he commenced employment with the group in November 2014. The turnover of staff in the tax year 2014/15 was 574.

4. Champneys employed the employee as a receptionist from 23 July 2013 until 16 February 2014. The employee was engaged to work full-time and her employment contract included a clause that she should not take on another employment. The employee had however been employed by another employer since 15 September 2010 and continued to carry out services for this first employer throughout the tax year 2013/14 while she worked full-time at Champneys and after she left Champneys. Due to changes in personnel, it could not be established if any member of Champneys's staff was aware of, or agreed to, the two employments arrangement.

5. Champneys issued a P46 or starter checklist for completion by the employee when she started at Champneys. Champneys then paid the employee on the basis of its assumption that Statement A was applicable as she was contracted to work full-time. This was reflected in the FPS entry for the employee for the first pay period for which she was paid. This resulted in the use of tax code 944L rather than the BR or OT codes.

6. When Mr Flarry joined Champneys in November 2014 he set up new starter procedures to comply with PAYE obligations. These included scanning PAYE forms into electronic filing, issuing starter checklists for new employees to complete and chasing for their return. Mr Flarry put in place a default procedure to operate a BR tax code in the absence of a completed starting statement from a new employee. Some 152 boxes of paper PAYE records were archived.

7. After the end of the 2013/14 tax year and the employee's employment, HMRC sent the employee a P800 on 16 September 2014 showing a shortfall in tax paid for

2013/14. The employee called HMRC on 6 October 2014 and 9 December 2014 and claimed that the under-deduction of tax was Champneys's fault because she had ticked box C on the P46 issued by Champneys as she had an existing employment. She claimed that she expected Champneys to deduct tax at the basic rate. Champneys has carried out searches for this P46 in the 152 archived boxes of payroll records but it has not been located. We find it most likely that the tax form issued was not returned by the employee, and that this reflects the fact that the forms were not always chased up by Champneys in the tax year 2013/14.

8. Following the calls from the employee HMRC wrote to Champneys on 12 January 2015 to ask if it disagreed with the employee's explanation about why the wrong tax code had been operated. HMRC's practice is to consider explanations provided by the employer and employee before deciding whether to make a direction under regulation 72 of the Regulations. Champneys did not respond to this letter and so HMRC wrote a second letter on 16 March 2015. The letter again asked for payment of the tax due or an explanation of why the correct tax had not been deducted. The letter concluded that if HMRC did not receive a response within 14 days of the date of the letter, it would take formal action to collect the tax, plus a possible penalty and interest.

9. Champneys failed to respond to the letters dated 12 January 2015 and 16 March 2015. It claims that the letters were not received because they were addressed to 'Champneys Group Ltd' rather than 'Champneys Tring Ltd'. We find that, on the balance of probabilities, the letters were received as they were addressed to the correct postal address, each letter included Champneys Tring Ltd's payroll reference at the top of the letter and neither letter was returned undelivered.

10. On 22 May 2015 HMRC notified the employee that as her former employer had failed to respond she did not need to take any further action about the unpaid tax. HMRC had determined that a direction under regulation 72 of the Regulations would not be appropriate in the absence of a response from Champneys. On 16 July 2015 HMRC issued an assessment of the tax due under regulation 80 of the Regulations for £1527.89. The assessment did not include a penalty.

11. Mr Flarry contacted HMRC by telephone on receipt of the assessment and he wrote to appeal against the determination on 23 July 2015. He advised HMRC that Champneys had actioned the tax code that it believed to be correct at the time and that the P46 referred to by the employee could not be found. On a further call with HMRC on 11 September 2015 Mr Flarry claimed that the unpaid tax should not fall on Champneys because the employee had not queried the tax code it had applied and HMRC had not flagged the incorrect tax code under the RTI system,

12. HMRC wrote to Champneys on 14 September 2015 to advise that the regulation 80 determination would stand as it had failed to comply with its responsibilities to operate PAYE. This decision was reviewed by HMRC at Champneys's request on 11 March 2016, but it concluded that the decision to raise the tax determination was correct. Champneys appealed against the decision on 6 April 2016.

## The law

13. Regulation 68 of the PAYE Regulations ("regulation 68") determines how much tax an employer must pay or can recover in respect of payments to an employee for a tax period. If the total amount of tax which the employer was liable to deduct from relevant payments to the employee in the tax period, plus the total amount of tax for which the employer was liable to account in respect of notional payments, exceeds total amount which the employer was liable to repay in the tax period, the employer must pay the excess (the "excess") to HMRC.

14. Regulation 46 of the PAYE Regulations ("regulation 46") provides:

> "(1) This regulation applies if –
>
> (a) An employee commences employment without giving the employer Part 2 and 3 of Form 45 and
>
> (b) A code in respect of the employee has not otherwise been issued to the employer.
>
> (1A) The employee must provide the following information in Form P46.
>
> (1B) The information is –
>
> (a) the employee's national insurance number (if known),
>
> (b) the employee's full name,
>
> (c) the employee's sex,
>
> (d) the employee's date of birth, and
>
> (e) the employee's full address including postcode.
>
> …
>
> (2) The employee must indicate in Form P46 which …of the following statements applies
>
> Statement A: that the employment referred to in paragraph (1)(a) is the employee's first employment since the preceding 6th April, and the employee has not since that date received –
>
> (a) jobseeker's allowance, incapacity benefit or employment and support allowance which is subject to income tax, or
>
> (b) a retirement pension or an occupational pension:
>
> Statement B: that the employee is not receiving a retirement pension or an occupational pension and since the preceding 6th April –
>
> (a) has had another employment, but is not now in receipt of employment income from it, or
>
> (b) has received jobseeker's allowance, incapacity benefit or employment and support allowance which is subject to income tax, but payment of that allowance or benefit has ceased;
>
> Statement C: that the employee either has another employment (which is continuing) or is in receipt of a retirement pension or an occupational pension.

….

(2A) A Form P46 must be –

(a) Signed by the employee; or

(b) Delivered by the employer by an approved method of electronic communications after he has complied with paragraph (2B).

(2B) To the extent that the information contained in it relates to the employee, the employer must verify the content of the Form P46 before it is delivered.

(2C) If, despite the requirements of paragraphs (2) to (2B), a Form P46 is sent or delivered to an officer of Revenue and Customs without the requirements of those paragraphs being satisfied, the employer must deduct tax on the non-cumulative basis using code OT from the employee's earnings. …"

15. We note that following the introduction of RTI, HMRC replaced form P46 with starter checklists to gather the information required to submit an FPS. The starter checklists do not have to be sent to HMRC but regulation 97 of the Regulations provides that they must be retained by the employer for not less than three years after the end of the tax year to which they relate.

16. Regulations 47, 48 and 49 of the Regulations provide that if Statement A applies the employer should deduct tax on the cumulative basis using the emergency code, if Statement B applies the employer should deduct tax on the non-cumulative basis using the emergency code and if Statement C applies the employer should deduct tax on the cumulative basis using the basic rate code.

17. Regulation 80 of the PAYE Regulations ("regulation 80") provides:

> "(1) This regulation applies if it appears to [HMRC] that there may be tax payable for a tax year under regulation 68 by an employer which has neither been—
>
> (a) paid to [HMRC], nor
>
> (b) certified by [HMRC] under regulation 76, 77, 78 or 79.
>
> (2) [HMRC] may determine the amount of that tax to the best of their judgment, and serve notice of their determination on the employer.
>
> (3) A determination under this regulation must not include tax in respect of which a direction under regulation 72(5) has been made; and directions under that regulation do not apply to tax determined under this regulation.
>
> [(3A) A determination under this regulation must not include tax in respect of which a direction under regulation 72F has been made.]
>
> (4) A determination under this regulation may—
>
> (a) cover the tax payable by the employer under regulation 68 for any one or more tax periods in a tax year, and

(b) extend to the whole of that tax, or to such part of it as is payable in respect of—

(i) a class or classes of employees specified in the notice of determination (without naming the individual employees), or

(ii) one or more named employees specified in the notice.

(5) A determination under this regulation is subject to Parts 4, 5[, 5A] . . .and 6 of TMA (assessment, appeals, collection and recovery) as if—

(a) the determination were an assessment, and

(b) the amount of tax determined were income tax charged on the employer,

and those Parts of that Act apply accordingly with any necessary modifications."

18. Regulation 72 of the Regulations ("regulation 72") provides that if certain conditions are satisfied HMRC may direct under regulation 72(5) that the employer is not liable to pay the excess of the amount of tax owed over the amount of tax deducted from payments made to an employee. In these circumstances the excess income tax is payable by the employee. The conditions to be satisfied are that either:

Condition A: the employer satisfies [HMRC] –

(a) That the employer took reasonable care to comply with the PAYE regulations, and

(b) That the failure to deduct the excess was due to an error made in good faith.

OR

Condition B: [HMRC] are of the opinion that the employee has received relevant payments knowing that the employer wilfully failed to deduct the amount of tax which should have been deducted from those payments.

19. Regulation 72A gives an employer the right to request HMRC to make a direction under regulation 72(5). If HMRC refuse to make a direction under regulation 72(5) that the employer is not liable to pay the excess to the HMRC, the employer may appeal by setting out the evidence that it did take reasonable care to comply with the Regulations and that the failure to deduct the excess tax was due to an error made in good faith. On appeal, the Tribunal has jurisdiction to direct that HMRC make a direction under regulation 72(5) if it appears that it should not have been refused.

**Submissions**

20. Champneys submit that the employee did not query the tax code applied by her employer or suggest that more tax should have been deducted from her pay because she had another employment. Champneys completed the FPS to the best of its knowledge and operated code 944L in good faith. HMRC should have flagged that

Champneys was using an incorrect tax code under the RTI system or issued an amended coding notice.

21. HMRC submit that Champneys did not comply with its responsibilities to operate PAYE correctly. The regulation 80 determination was correctly raised as Champneys failed to provide any valid reasons for why the PAYE was not operated correctly. HMRC noted that the RTI system does not flag up incorrect tax codes and that it is for the employer to determine the tax code to be applied to the earnings of a new starter. HMRC referred us to the cases of *Paringdon Sports Club Ltd v The Commissioners for Her Majesty's Revenue & Customs* (TC/2015/00613) and *Poole Leisure Ltd v The Commissioners for Her Majesty's Revenue & Customs* {2015] UKFTT 0109 (TC) (" *Poole Leisure*").

**Discussion**

22. The PAYE regulations set out the procedures and obligations on employers to deduct and account to HMRC for tax on certain payments made to employees. In this case Champneys failed to obtain and/or retain a form 46 or a starter checklist in respect of the employee and there was an under-deduction of £1527.89 due under regulation 68. Champneys has not sought to challenge these facts but the reasons why they arose.

23. Regulation 80 provides that HMRC may direct an employer to pay tax due under regulation 68 which has not been paid to HMRC. The regulation 80 the subject of this appeal was made in respect of the £1527.89 excess tax which arose under regulation 68 because the provisions of regulation 46 were not followed. Regulation 80(5) provides that a determination under regulation 80 may be appealed under section 50(6) Taxes Management Act 1970 as if the determination were an assessment. This provision allows the Tribunal to reduce an assessment to the extent that the appellant is overcharged, but provides that otherwise the assessment "shall stand good". We find that Champneys has not discharged the burden of proof to show, on the balance of probabilities, that it was overcharged as the amount of the excess tax due under regulation 68 has not been disputed and is found to be correct. We find that the regulation 80 determination should stand good.

24. As we explained at the end of the hearing, while this outcome of the appeal against the regulation 80 determination appeared unfair to Champneys, it should be considered against the background of both HMRC and the Tribunal considering whether a direction could be made to relieve Champneys of the liability under regulation 72. We noted that HMRC had considered whether to exercise their discretion under regulation 72 to direct that Champneys is not liable to pay the excess PAYE due before it made its determination under regulation 80. As HMRC accepted that Condition B of regulation 72 was not in point, it asked Champneys for evidence so that it could determine whether Condition A was in point on the basis that the employer took reasonable care to comply with the Regulations and the error was made in good faith. HMRC accepted on the facts that any error made was made in good faith but when Champneys failed to respond to these letters with evidence of

taking reasonable care, HMRC concluded that it had not taken reasonable care to comply with the Regulations and issued the regulation 80 determination.

25. HMRC treated the initial correspondence from Champneys after the regulation 80 determination as an appeal against the determination but, as this correspondence included Champneys's evidence to support its claim that it should not be liable to pay the excess tax due, we consider whether it could or should be treated as an appeal against the refusal to make a regulation 72(5) direction or as a request under regulation 72A. As however regulation 80(3) states that no direction can be made under regulation 72(5) in respect of tax which is the subject of a determination under regulation 80, we have to consider the relationship between regulation 72 and regulation 80.

26. We consider first whether Champneys could make a request under regulation 72A after a regulation 80 determination had been made. We note that Judge Clark in *Poole Leisure* commented, but did not proceed to decide on the facts of that case, that it is not clear if a regulation 80 determination can be made when a regulation 72(5) decision remains open.

27. On the facts of this case, HMRC had considered but did not exercise their discretion to make a direction under regulation 72, and then went on to make the regulation 80 determination. Further, we find that even if Champneys had intended to request a direction under regulation 72A after the regulation 80 determination had been made, its correspondence did not meet the requirements set out in regulation 72A(2) as it failed to state how it took reasonable care to comply with the Regulations. No notice of request can therefore be regarded as having been given.

28. We note for completeness that if a request under regulation 72A had been made, we would need to consider whether the Regulations allow HMRC to make a regulation 72(5) direction after a regulation 80 determination has been made. In this respect we respectfully adopt Judge Raghavan's clear analysis in paragraph 32 of *Ridgecrest Cleaning Services Pendergate Ltd v The Commissioners for Her Majesty's Revenue & Customs* [2016] UKFTT 0778 (TC) and agree that the Regulations only allow this in the limited factual circumstances in which a regulation 80 determination does not cover the full amount of the excess tax so that a regulation 72(5) direction can be made in respect of the remainder because it is not subject to the determination. As the regulation 80 determination was in respect of the full amount of the excess tax due in this case, there was no scope for a regulation 72(5) direction to be made in any event.

29. Notwithstanding our conclusion that there was no scope for HMRC to make a direction under regulation 72, we consider whether Champneys's correspondence after the regulation 80 determination can be treated as an appeal against the original decision not to make a regulation 72(5) direction. Champneys was asked to provide the evidence requested to show how it "took reasonable care to operate PAYE, by saying what HMRC guidance was followed despite the error occurring and what checks were in place to prevent the errors happening". Champneys responded that it had actioned the tax code which it believed to be correct, that neither the employee

nor HMRC had corrected the error and that the business should not be responsible for the employee's tax. HMRC took Champneys's failure to provide the evidence requested as sufficient to confirm both its decision not to make a direction under regulation 72 and its regulation 80 determination.

30. We have had the benefit of hearing oral evidence from Champneys about its starter procedures in 2013/14. We find that Champneys assumption that any new full-time starter should come within Statement A demonstrated a lack of reasonable care in compliance with the Regulations. As there has been a change in personnel since this action was taken it is not possible to establish what steps were taken to check this information, but even assuming that no second employment was allowed, we note that Champneys has no record of checking what the employee said at her interview to explain why Statement A was applied rather than Statement B (which assumes that some of the personal allowance has already been used). Further, as the P46 or starter checklist was not obtained and/or retained, regulation 46(2C) required Champneys to operate an OT code. This is accepted by Champneys as Mr Flarry noted that he put procedures in place after he joined in November 2014 to ensure that these starter procedures and codes were followed and applied.

31. On the basis of this evidence we find that Champneys could not have met paragraph (a) in Condition A of regulation 72 because it failed to exercise the reasonable care expected of a reasonable and prudent taxpayer in operating new starter procedures in relation to the employee. In these circumstances, we agree that there was no basis on which HMRC could have made a direction under regulation 72(5) to relieve Champneys of the liability even if the regulation 80 determination had not been made in the full amount of the excess tax due before HMRC received evidence from Champneys.

**Decision**

32. For all the reasons set out above the regulation 80 determination is confirmed and the appeal is dismissed.

33. 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.

**VICTORIA NICHOLL**
**TRIBUNAL JUDGE**

**RELEASE DATE: 27 FEBRUARY 2017**