



[2020] UKFTT 0033 (TC)

TC07539

Appeal number: TC/2019/00866

CONSTRUCTION INDUSTRY SCHEME - penalties for late filing of returns - the director of the appellant Company believed that “project management” services provided by the Company did not fall within the CIS and that there was no obligation to deduct tax from payments made to sub-contractors or file monthly returns - whether the appellant Company had a reasonable excuse for its failures - no - appeal dismissed

**FIRST-TIER TRIBUNAL
TAX CHAMBER**

T ARDERN LIMITED

Appellant

- and -

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

Respondents

**TRIBUNAL: JUDGE MICHAEL CONNELL
MEMBER MOHAMMED FAROOQ**

**Sitting in public at Sheffield MJC, Castle Street, Sheffield, S3 8LU
on 4 November 2019**

Mr Richard Smith, director of the Appellant Company

Ms Victoria Halfpenny, officer of HMRC, for the Respondents

DECISION

The Appeal

1. This is an appeal by T Ardern Limited (“the appellant”) against a decision of the Respondents (“HMRC”) dated 3 July 2018 refusing a claim under Regulation 9(3) (Condition A) of the Income Tax (Construction Industry Scheme) Regulations 2005 (“the CIS Regulations”). The refusal resulted in an amount of £405 (£192 falling in the tax year 13-14 and £213 falling in the 14-15 tax year) becoming chargeable for non-declared CIS liability.
2. The appellant company also appeals penalties of £3,671 imposed by HMRC under Schedule 55 Finance Act 2009 for its failure to make monthly returns by the due dates under the CIS for various periods between 6 April 2012 and 5 November 2014.
3. The points at issue are:
 - i. Whether the appellant took reasonable care to comply with s 61 of the Finance Act 2004 to make deductions from contract payments made by the company to sub-contractors engaged by it, and
 - ii. Whether the appellant has a reasonable excuse for the failure to submit CIS returns.

The CIS penalty regime

4. The CIS is a tax compliance scheme for businesses operating in the construction industry.
5. The legal basis of the CIS regime, in force from 6 October 2011, is the Finance Act 2009, Schedule 55 paragraphs 1, 8-13 and 23 (“FA 2009”); ss 57-77 of the Finance Act 2004 (“FA 2004”) and the Income Tax (Construction Industry Scheme) Regulations 2005 (SI 2005/2045) (the “2005 Regulations”). The regime came into force for CIS monthly returns with effect from 6 October 2011 and applies to returns due to be filed on or after 19 November 2011.
6. Sections 57-59 FA 2004 replaced the provisions of sections 559-561 of the Income and Corporation Taxes Act 1988 with regard (inter alia) to the definition of ‘contractors’ and a ‘construction contract’.
7. Contractors in the construction industry are required to make deductions from construction payments made to sub-contractors in accordance with s 61 FA 2004 and pay over those deductions to HMRC under Regulation 7(1) of the CIS Regulations. The sub-contractors are entitled to claim credit for tax withheld under CIS against their tax liability for the tax year in question.
8. Under Regulation 9(3) of the CIS Regulations the contractor may make a claim to be absolved from making the deductions if HMRC are satisfied that the contractor:

“(a) ...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.”

9. Under Regulation 9(4) of the 2005 Regulations HMRC may ‘relieve’ the contractor of the requirement to pay over deductions which should have been made if was satisfied that:

“(a) 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 or 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 corporation tax due in respect of such income or profits;

and

(b) the contractor requests that HMRC make a direction under paragraph (5).”

10. Contractors are required to make a return no later than 14 days after the end of every tax month (a “monthly return”) (reg 4 of the 2005 Regulations). For these purposes, a tax month means the period beginning with the 6th day of a calendar month and ending on the 5th day of the following month. A monthly return must therefore be received by HMRC no later than the 19th day of the month. Nil returns are also required (reg 4(10) of the 2005 Regulations).

11. If a monthly return is received after the filing date, it will be treated as late and the contractor will be liable to a penalty under Schedule 55 FA 2009 as follows:

If a CIS return is 1 day late, an initial fixed penalty of £100 is payable.

If HMRC have still not received that return:

- 2 months after the date it was due, a second fixed penalty is payable of £200.
- 6 months after the date it was due, a further penalty of £300 or 5% of any liability to make payments that should have been shown in the return is payable.
- 12 months after the date it was due, a second further penalty is payable – the amount of this penalty depends on why the return was late. The amount

HMRC charge will be either £300 or 5% of any liability to make payments, or a ‘higher’ penalty of up to 100% of any liability to make payments.

12. Paragraph 23 of Schedule 55 makes provision as to what may or may not constitute a reasonable excuse.

“23(1) Liability to a penalty under any paragraph of this Schedule does not arise in relation to a failure to make a return if P satisfies HMRC or (on appeal) the First-tier Tribunal or Upper Tribunal that there is a reasonable excuse for the failure.

(2) For the purposes of sub-paragraph (1)-

(a) an insufficiency of funds is not a reasonable excuse, unless attributable to events outside P’s control,

(b) where P relies on any other person to do anything, that is not a reasonable excuse unless P took reasonable care to avoid the failure, and

(c) where P had a reasonable excuse for the failure but the excuse has ceased, P is to be treated as having continued to have the excuse if the failure is remedied without unreasonable delay after the excuse ceased.”

13. Section 57(2) Finance Act 2004, states that:

“(2) In this section ‘Construction Contract’ means a contract relating to construction operations, which is not a contract of employment but where

(a) One party to the contract is a sub-contractor and

(b) Another party to the contract (‘the contractor’) is either –

(a) ...

(b) Is a person to whom s 59 applies.”

14. Section 59 (1) (a) Finance Act 2004 provides that:

“Contractors

(1) This section applies to the following bodies or persons –

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

Background Facts

15. The appellant has been an incorporated Company since 1994, and during all periods in question provided “project management/quantity surveying services to industrial or commercial organisations”. The Company has only one employee being the sole director, Mr Richard Smith. In the accounts period ended 31 March 2015 the Company had a turnover of £392,232. It mainly undertakes work for existing customers. It occasionally employs sub-contractors and sometimes purchases materials where sub-contractors are working direct for the client.

16. On 8 December 2016 HMRC opened an enquiry into the Company's return for the period ended 31 March 2015.

17. During the course of those enquiries it became apparent that the Company had been paying sub-contractors to undertake work involved within the construction industry from at least the trading year commencing 2012-13.

18. On 27 June 2017 a meeting was held between the parties to discuss the findings of the investigation. The enquiry into the Corporation Tax was concluded with no discrepancies identified. However, Mr Smith agreed that the Company had failed to make deductions from payments made to sub-contractors and had failed to make the necessary returns.

19. The failures arose because Mr Smith believed the CIS regulations did not apply to the Company's activities. He did not realise that the Company was 'a contractor, carrying on a business which includes construction operations', and as such obliged to file monthly returns. Mr Smith also believed that the CIS regime did not apply because the Company mainly dealt with sub-contractors who were 'exempt from CIS deductions', [that is, they had 'gross payment status', although there is no assertion on his part that he ever made on-line checks, as he could have done, to determine the status of sub-contractors]. Mr Smith says that he had checked HMRC's guidance when the Company was initially set up in 1994 and concluded that because it would not be directly engaged in construction operations the CIS regime will not apply to it.

20. Mr Smith has not identified which guidance he checked, but in any event now agrees that his interpretation of the guidance must have been incorrect. His grounds of appeal are that he made an honest mistake, that there has been no loss to HMRC, that he cooperated fully with the investigation and that the penalties are disproportionate insofar as they include periods where relief has been given under Regulation 9(4). He asserts that the Company has a reasonable excuse for the failures and that the penalties should be waived in all the circumstances.

Non-declared CIS liability

21. HMRC 'relieved' the appellant of the requirement to pay over £6,317 of the deductions which should have been made as HMRC decided that the appellant satisfied the provisions of Regulation 9(4) of the 2005 Regulations.

22. However, £405 could not be relieved under Regulation 9(4) of the CIS Regulations because two sub-contractors involved had not paid their tax liability (£192 and £213, and possibly any related Class 4 NI contributions). The refusal notice pursuant to Regulation 9(6) of the CIS Regulations was issued to the appellant on 3 July 2018.

Failure to make CIS returns.

23. Under Regulation 4 of the 2005 Regulations the appellant was required to submit a Contractor's Monthly Return ("CIS300") by the 19th day of the month. The returns that should have been made are as follows:

Period	CIS deductions that should have been declared on a monthly return
05/05/2012	£810.00
05/06/2012	£556.00
05/07/2012	£216.00
05/08/2012	£120.00
05/12/2013	£792.00
05/01/2014	£648.00
05/02/2014	£1,176.00
05/03/2014	£660.00
05/04/2014	£636.00
05/05/2014	£348.00
05/06/2014	£474.00
05/09/2014	£213.00
05/11/2014	£70.00
Totals	£6,719.00

24. None of these amounts have been challenged by the appellant, and no alternative figures proposed.

25. All of the CIS returns for the periods listed were made late on 23 May 2017.

26. Penalties were charged as follows:

- £100 for each of the 13 periods for being one day late - £1,300.
- £200 for each of the 13 periods for being two months late - £2,600.
- 5% of the liability that should have been declared for each of the 13 periods for being six months late - £335.95.
- 5% of the liability that should have been declared for each of the 13 periods for being twelve months late – £335.95.

27. The total penalties were £4,571.90 but HMRC capped the total of the £100 and £200 penalties to £3000 which resulted in reduced total penalties of £3,671.90.

28. In October 2018 the appellant asked HMRC to reconsider their findings. On 10 January 2019 HMRC reviewed their decision but concluded that the Regulation 9(3) claim should remain refused and that the penalties should not be reviewed.

29. On 5 February 2019 the appellant submitted an appeal to the Tribunal.

Burden of Proof

30. With regard to HMRC's decision to refuse the Regulation 9(3) claim, the burden of proof is on Mr Smith to show that he had taken reasonable care to comply with s 61 FA

2004 and that any failure was due to an error made in good faith or that he had a genuine belief that s 61 did not apply. With regard to the Schedule 55 penalties the burden of proof is on HMRC to show that a penalty is due and that the notice of the penalty was correctly issued. The burden then shifts to the appellant to show there was a reasonable excuse for the failure by the Company to submit its returns by the due dates.

31. The standard of proof is the civil standard; on the balance of probabilities.

Appellant's contentions

32. The appellant's grounds of appeal are stated in the notice of appeal as follows:

“Although CIS deductions are due for just two payments, the penalties cover a 13 month period.

A genuine mistake has been made, which HMRC have known about through the Annual Returns. The Company has made no financial gain from this error, and HMRC has not lost any revenue. As such we would ask that the penalty is reduced to a level which reflects just two incorrect payments. HMRC has discretion to reduce penalties if [they] think it is right because of special circumstances.

HMRC [should] reduce the penalty to say £500, making the amount payable £947 (CIS £405, interest £42, penalty £500). Given the evidence that this was a genuine mistake which was never hidden, the co-operation given, the excessive time-period this has been a live investigation, the value of CIS, we believe these are special circumstances to allow the penalty to be reduced.”

33. At the hearing Mr Smith said that he had employed a reputable firm of accountants who knew his business extremely well. They prepared and filed the Company's accounts and annual returns and had never indicated during all the Company's trading years that it may be caught by the CIS regulations.

HMRC's Contentions

34. Mr Smith no longer disputes that the relevant payments fell within the CIS or that the Company should have made deductions of CIS tax from them. Further he now accepts that CIS returns should have been made.

35. HMRC cannot “have known about” the discrepancy in question purely based on information contained in the annual Company returns. The legal obligation to submit an accurate return in any tax regime is squarely on the taxpayer. In the case of *Nicholson v Morris* L.J. Walton states:

“...the Taxes Management Act, throws upon the taxpayer the onus of showing that the assessments are wrong. It is the taxpayer who knows and the taxpayer who is in a position (or, if not in a position, who certainly should be in a position) to provide the right answer, and chapter and verse for the right answer, and it is idle for any taxpayer to say to the Revenue, “Hidden somewhere in your vaults are the right answers: go thou and dig them out of the vaults”. That is not a duty on the Revenue.”

36. The onus to ensure that the responsibilities of a Company are discharged falls on the proprietor. At the very least HMRC consider a diligent trader would have contacted HMRC to verify that its obligations were being complied with. There is no record on file of the appellant ever contacting HMRC with regard to its CIS obligations.

37. The returns for the periods in question were eventually submitted and received on 23 May 2017, long after their due date. It follows that under Schedule 55 FA 2009, penalties are chargeable.

38. Although the amount of penalty may at first appear to be incommensurate to the amount of the actual liability, this needs to be viewed in the context of the actual amounts that were not declared under the CIS returns. It is the total amount of the non-declared CIS deductions that should have been ‘returned’ that is the relevant factor, not the amount after relief (as provided by virtue of Regulation 9(4) of the Regulations) is given.

39. Under Schedule 55:

- Paragraphs 8 and 9 apply a fixed penalty of £100 and £200 respectively, for the initial failure and subsequent 2 months failure.
- Paragraphs 10(2)(a) and 11(5)(a) apply a 5% penalty at 6 months and 12 months respectively based on “...any liability to make payments which would have been shown in the return in question...”.

40. The penalty amounts have been ‘capped’ by virtue of paragraph 13(2)(b), to £3,000 for the initial late filing and 2 months late filing penalties. The penalty amounts are chargeable at 5% rather than £300 for each return by virtue of Paragraph 13(2)(a) for the 6 month and 12 month failures.

41. There is nothing within Schedule 55 or other legislation which allows for mitigation (under CIS) for the co-operation of the appellant or the quality of disclosure.

42. The fact that there may or may not be a loss to the revenue is immaterial. Schedule 55 refers to “any liability to make payments which would have been shown in the return in question”. It is irrelevant that the Regulation 9(3) refusal notice is in question - the granting or refusal of relief would not disturb the Schedule 55 penalty amounts in any case.

43. The amounts of the non-declared returns are not disputed, therefore the penalty is determinable by statute. In *HMRC v Hok Ltd* the Upper Tribunal considered whether

the jurisdiction of the First-tier Tribunal includes the ability to discharge a penalty on the grounds of unfairness, and concluded that the Tribunal has the power to:

“... set aside a penalty which has not in fact been incurred, or to correct a penalty which has been incurred but has been imposed in an incorrect amount, but it goes no further ... it is plain that the First-tier Tribunal has no statutory power to discharge, or adjust a penalty because of a perception that it is unfair.”

44. The Upper Tribunal case of *HMRC v Christine Perrin* sets out a 4-test approach to apply to arguments of Reasonable Excuse:

i. Establish what facts the taxpayer asserts give rise to a reasonable excuse - the appellant relies on them not being aware of their obligation to comply with the CIS Regulations. HMRC contend that the onus is on a contractor to ascertain whether it is called by the CIS regime and if so, how it operates in order to comply with the Scheme.

ii. Decide which of those facts are proven. The appellant is actively involved in the Construction Industry. It engaged the services of and subsequently paid sub-contractors within that industry. The Company did not register for the CIS, and subsequently made no returns. The appellant did not seek any advice from HMRC or other tax professional.

iii. Decide whether, if viewed objectively, those proven facts amount to an objectively reasonable excuse, taking into account the experience and other relevant attributes of the taxpayer and the situation in which the taxpayer found himself at the relevant time. The appellant has been trading for over 20 years in an industry where knowledge of the strict necessity to adhere to the CIS Regulations is fundamental. CIS Regulations have received wide publicity. There is information available, in the public domain, not least on the government website. It is almost inconceivable that as the appellant Company proprietor was not aware of the existence of the Regulations. No explanation had been given as to why he did not obtain a definitive answer as to whether the Company was liable to comply with the CIS Regulations.

iv. If any reasonable excuse existed, whether the taxpayer remedied the failure without unreasonable delay after that time. HMRC do not accept that a reasonable excuse existed at all.

45. Taking into account the experience and other relevant attributes of the appellant's proprietor, Mr Smith, and in the situation in which he found himself at the relevant time, he should have known that the Company may have been subject to CIS Regulations. As an absolute minimum he should have sought clarification if there was any uncertainty. Mr Smith should not have assumed that the Company would not be caught by the Regulations.

46. Special Reduction has been considered by HMRC under paragraph 16 of Schedule 55, but there is nothing in the arguments put forward by the appellant which would

warrant a special reduction. In reaching this decision HMRC have taken into account all the facts and all of the points raised by the appellant

47. In *HMRC v Christine Perrin* the Upper Tribunal decided [at 82] that there is no general rule that ignorance of the law cannot constitute a reasonable excuse but warned that:

“Some requirements of the law are well-known, simple and straightforward but others are much less so. It will be a matter of judgement for the FTT in each case whether it was objectively reasonable for the particular taxpayer, in the circumstances of the case, to have been ignorant of the requirement in question, and for how long.”

Conclusion

48. Mr Smith believed that the work his Company was undertaking and the engagement of sub-contractors was outside the CIS. We accept that his belief was genuinely held.

49. With regard to the guidance which Mr Smith says he referred to some 15-20 years previously, he now accepts that he must have misinterpreted that guidance. The general principles of engaging and paying sub-contractors in the construction industry and whether the CIS applies, whether under the current scheme or former scheme, have not materially changed, if at all. Given that sub-contractors within the construction industry were frequently employed albeit mainly those holding gross payment status, there was a clear obligation on Mr Smith to check whether his Company was caught by the CIS Regulations. It appears that because the appellant Company was not directly engaged in construction activities, the possibility that it may be subject to the CIS was never considered. It is unfortunate that his accountants made the same assumptions.

50. We concur with HMRC’s reasoning and arguments as set out in paragraphs 34-46 above. In our opinion Mr Smith has not demonstrated that he took sufficient care in deciding whether he should operate within the CIS. Ignorance of the scheme rules is not a sufficient excuse to relieve a contractor of its obligations under that scheme. It is the contractor’s responsibility to make himself aware of the scheme rules and to apply them appropriately.

51. Whilst we accept that Mr Smith believed the Company did not have to register for the CIS, it was not objectively reasonable for him to hold that belief. He had engaged sub-contractors to perform duties on behalf of the Company in the construction industry. To be ignorant of the requirement to register under the CIS is not considered to be a reasonable excuse.

52. We consider that HMRC’s refusal to make a direction under Regulation 9(5) of the CIS Regulations is correct as the appellant has not satisfied HMRC for the purposes of Regulation 9(3)(a) that he took reasonable care to comply with s 61 of the Act.

53. The penalties are calculated on the original amounts of the CIS liability, before the relief allowed under the Regulation 9(4) legislation. The penalties charged under Schedule 55 are therefore in the correct amounts. Although in this particular regard we

have some sympathy for Mr Smith, we have to find that he has not shown a reasonable excuse for the Company's failure to submit its returns on time.

54. A penalty can be reduced where the application of the law produces a result that is clearly contrary to the legislative intention. In other words that there are special circumstances. Special circumstances must be something that is uncommon or exceptional, and clearly recognisable as such. However, the circumstances must apply to the particular individual/Company and should not be general circumstances that may apply to many taxpayers by virtue of the penalty legislation. Whilst accepting that Mr Smith made a genuine error, the circumstances which led to the failures cannot be described as uncommon, exceptional or special.

55. The proportionality which the penalties bear to the amount of the CIS deductions is not considered to be a special circumstance. In any event the structure and level of penalties where legislated by Parliament issues of proportionality are not within the jurisdiction of this Tribunal to consider.

56. The appeal is accordingly refused and HMRC's decisions to refuse the Regulation 9(3) claim and impose the penalties under Schedule 55 for the late filing of CIS returns are confirmed.

57. 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.

MICHAEL CONNELL

TRIBUNAL JUDGE

RELEASE DATE: 16 JANUARY 2020