Neutral Citation: [2025] UKFTT 23 (TC)

Case Number: TC09395

FIRST-TIER TRIBUNAL
TAX CHAMBER

Decided on the papers

Appeal reference: TC/2022/00215

Construction Industry Scheme – interaction between CIS and the agency rules – appellant misunderstood the interaction – whether acted with reasonable care – Tribunal's jurisdiction under Condition A of the CIS regs – appeal allowed

Heard on: 30 and 31 December 2024
Judgment date: 9 January 2025

Before

TRIBUNAL JUDGE ANNE REDSTON

Between

HARBRON RECRUIT LIMITED

Appellant

and

THE COMMISSIONERS FOR
HIS MAJESTY'S REVENUE AND CUSTOMS

Respondents

DECISION

INTRODUCTION AND SUMMARY

1. Harbron Recruit Ltd ("HRL") is a family firm, of which Mr James Harbron is the managing director. HRL contracts with end-clients in the construction industry to provide labour and identifies workers to carry out the required tasks. During the time with which this appeal is concerned ("the relevant time") HRL did not engage the workers. Instead, it contracted with intermediary agencies, and those agencies engaged the workers.

2. Historically, HRL treated the agencies as its own subcontractors, and deducted tax from payments made unless the agencies had "gross" status under the Construction Industry Scheme ("CIS").

3. In April 2014, new provisions were introduced which deemed workers to be employed by agencies if they were subject to "supervision, direction or control" by the agency. HRL took appropriate professional advice on how these new rules would affect its business.

4. Mr Harbron understood that as a result of these changes, it did not need to apply CIS to the payments made to the agencies, because the workers were all being paid net of tax under PAYE. HRL therefore made nil CIS returns from 5 May 2017.

5. On 21 October 2020, HMRC opened a "check" of HRL's PAYE, VAT and CIS compliance. On 8 March 2021, HMRC issued HRL with a "Warning Letter" under Reg 13(1) of the Income Tax (Construction Industry Scheme) Regulations 2015 ("the CIS Regs") stating that they would raise determinations on HRL for £483,675 of CIS ("the excess") for the years 2017-18 through to 2021-22 in relation to its payments to the agencies.

6. In response, HRL wrote to HMRC asking for a determination that it was not liable to pay the excess because Condition A or Condition B of Reg 9 of the CIS Regs applied. Condition A is that HRL had acted with reasonable care and Condition B is the agencies had paid the tax due on the related profits.

7. HMRC accepted that Condition B applied to £129,513 of the excess, but refused to apply Condition A. HRL appealed and asked for a statutory review. The review officer upheld the decision, and HRL notified its appeal to the Tribunal.

8. The case was twice listed for an oral hearing, but both hearings were postponed. The parties then asked that the appeal be determined on the papers under Rule 29 of the Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules 2009 ("the Tribunal Rules"), and I considered that it was in the interests of justice to do so.

9. Having considered the facts, the law, and the submissions of both parties, I agreed that HRL had acted with reasonable care, for the reasons explained at §88, and I allowed the appeal.

10. I also considered and rejected a submission made by HMRC that, if HRL won its appeal, the case would be remitted back to HMRC for it to make further decisions on essentially the same facts, see §68ff.

11. All statutory provisions referred to in this Decision are cited only so far as relevant to the issue before the Tribunal.

THE EVIDENCE

12. The Tribunal was provided with a bundle of 1,822 pages, which included:

    (1) Correspondence between the parties, and between the parties and the Tribunal;

(2) print-outs from HMRC's system showing HRL's CIS returns;

(3) HRL's bank statements from December 2019 to January 2020;

(4) HRL's VAT returns for periods 4/20; 7/20; 10/20 and 1/21;

(5) HRL's supplier invoices from April 2017 to November 2020, and from August 2020 to February 2021; and

(6) invoices from one agency from November 2019 to February 2020; and from another from February to October 2020.

13. The Tribunal was also provided with witness statements from Mr Harbron and Mr Richard Clutterbuck. At the relevant time Mr Clutterbuck worked for CIS Tax Advice Ltd ("CISTAL"), the professional firm which provided advice to HRL, although he moved to a new firm, GuildHub Consulting Ltd, before he made his statement.

14. Because this appeal was listed to be decided on the papers, it was not possible for HMRC to cross-examine Mr Harbron or Mr Clutterbuck on their evidence. However, HMRC did not submit that either witness statements was untrue or misleading. I found the evidence contained within both statements to be consistent with other documents in the Bundle and accepted it. The witness statements also included submissions, which I took into account (alongside the submissions made by HMRC) when deciding whether or not to allow the appeal.

15. Although HMRC relied on their CIS guidance as set out in booklet CIS340 ("the CIS Guidance"), the Bundle did not include the version in use during the relevant period. I therefore referred to the current edition, together with the list of updates shown on the landing page of the website. In reliance on that update information, I find that the passages from the CIS Guidance cited in this Decision were present during the relevant period.

16. On the basis of the evidence summarised above, I make the findings of fact in this Decision.

THE CIS PROVISIONS

17. The CIS provisions are found in Finance Act 2004 ("FA 2004"), Part 3, Chapter 3, and in the CIS Regs, which are made under the *vires* given by that Act. FA 2004, s 57 begins:

> "(1) This Chapter provides for certain payments (see section 60) under construction contracts to be made under deduction of sums on account of tax (see sections 61 and 62).
>
> (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 sub-contractor (see section 58); and
>
> (b) another party to the contract ("the contractor") either—
>
> (i) is a sub-contractor under another such contract relating to all or any of the construction operations, or
>
> (ii) is a person to whom section 59 applies.
>
> (3) In sections 60 and 61 "the contractor" has the meaning given by this section.

18. Section 58 is headed "Sub-contractors" and reads:

> "For the purposes of this Chapter a party to a contract relating to construction operations is a sub-contractor if, under the contract—
>
> (a) he is under a duty to the contractor to carry out the operations, or to furnish his own labour (in the case of a company, the labour of employees or officers of the company) or the labour of others in the carrying out of the operations or to arrange for the labour of others to be furnished in the carrying out of the operations; or
>
> (b) he is answerable to the contractor for the carrying out of the operations by others, whether under a contract or under other arrangements made or to be made by him."

19. Section 59 defines "contractor" as including by subsection (1)(a), "any person carrying on a business which includes construction operations".

20. Section 60 is headed "contract payments" and begins:

> "(1) In this Chapter "contract payment" means any payment which is made under a construction contract and is so made by the contractor (see section 57(3)) to—
>
> (a) the sub-contractor,
>
> (b) a person nominated by the sub-contractor or the contractor, or
>
> (c) a person nominated by a person who is a sub-contractor under another such contract relating to all or any of the construction operations.
>
> (2) But a payment made under a construction contract is not a contract payment if any of the following exceptions applies in relation to it.
>
> (3) This exception applies if the payment is treated as earnings from an employment by virtue of Chapter 7 of Part 2 of the Income Tax (Earnings and Pensions) Act 2003 (c 1) (agency workers)…."

21. Section 61 then provides that a "contractor" must deduct "the relevant percentage£ from any "contract payment". The Finance Act 2004, Section 61(2), (Relevant Percentage) Order 2007 provides that the "relevant percentage" is 20% unless the subcontractor is not registered for CIS, when it is 30%.

22. Reg 9 reads:

> "(1) This regulation applies if—
>
> (a) it appears to an officer of Revenue and Customs that the deductible amount exceeds the amount actually deducted, and
>
> (b) condition A or B is met.
>
> (2) In this regulation—
>
> "the deductible amount" is the amount which a contractor was liable to deduct on account of tax from a contract payment under section 61 of the Act in a tax period;
>
> "the amount actually deducted" is the amount actually deducted by the contractor on account of tax from a contract payment under section 61 of the Act during that tax period;

"the excess" means the amount by which the deductible amount exceeds the amount actually deducted.

(3) Condition A is that the contractor satisfies an officer of Revenue and Customs—

(a) that he 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.

(4) Condition B is that—

(a) an officer of Revenue and Customs is satisfied that 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 the Commissioners for Her Majesty's Revenue and Customs make a direction under paragraph (5).

(5) An officer of Revenue and Customs may direct that the contractor is not liable to pay the excess to the Commissioners for Her Majesty's Revenue and Customs.

(6) If condition A is not met an officer of Revenue and Customs may refuse to make a direction under paragraph (5) by giving notice to the contractor ("the refusal notice") stating—

(a) the grounds for the refusal, and

(b) the date on which the refusal notice was issued.

(7) A contractor may appeal against the refusal notice—

(a) by notice to an officer of Revenue and Customs,

(b) within 30 days of the refusal notice,

(c) specifying the grounds of the appeal.

(8) For the purpose of paragraph (7) the grounds of appeal are that—

(a) that the contractor 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) the contractor held a genuine belief that section 61 of the Act did not apply to the payment.

(9) If on an appeal under paragraph (7) that is notified to the tribunal it appears that the refusal notice should not have been issued the tribunal may direct that an officer of Revenue and Customs make a direction under paragraph (5) in an amount the tribunal determines is the excess for one or more tax periods falling within the relevant year…"

23. Reg 9 therefore allows HMRC to issue a direction that the under-deducted CIS amount ("the excess") is not collectible from a contractor if either Condition A or Condition B is met. If HMRC refuse to issue a direction, the contractor can appeal to the Tribunal, but only in relation to Condition B. I return to these provisions later in this Decision notice.

24. Reg 13 of the CIS Regs is headed "determination of amounts payable by contractor and appeal against determination", and it includes the following paragraphs:

"(1) This regulation applies if—

(a) …

(b) an officer of Revenue and Customs has reason to believe, as a result of an inspection under regulation 51 or otherwise, that there may be an amount payable for a tax year under these Regulations by a contractor that has not been paid to them, or

(c) an officer of Revenue and Customs considers it necessary in the circumstances.

(2) An officer of Revenue and Customs may determine the amount which to the best of his judgment a contractor is liable to pay under these Regulations, and serve notice of his determination on the contractor.

(3) A determination under this regulation must not include amounts in respect of which a direction under regulation 9(5) has been made and directions under that regulation do not apply to amounts determined under this regulation."

25. It follows from Reg 13(3) that a determination under Reg 13 to collect the excess cannot be made if a direction has already been given under Reg 9(5).

THE AGENCY RULES

26. ITEPA Part 2 Chapter 7 is headed "Application of provisions to agency workers" and together with related provisions and regulations, sets out what are commonly known as "the agency rules". Within that Chapter, s 44 is headed "Treatment of workers supplied by agencies", and since its amendment by Finance Act 2014 ("FA 2014") reads:

"(1) This section applies if

(a) an individual ("the worker") personally provides services (which are not excluded services) to another person ("the client"),

(b) there is a contract between

(i) the client or a person connected with the client, and

(ii) a person other than the worker, the client or a person connected with the client ("the agency"), and

(c) under or in consequence of that contract

(i) the services are provided, or

(ii) the client or any person connected with the client pays, or otherwise provides consideration, for the services.

(2) But this section does not apply if

(a) it is shown that the manner in which the worker provides the services is not subject to (or to the right of) supervision, direction or control by any person, or

(b) remuneration receivable by the worker in consequence of providing the services constitutes employment income of the worker apart from this Chapter.

(3) If this section applies

(a) the worker is to be treated for income tax purposes as holding an employment with the agency, the duties of which consist of the services the worker provides to the client, and

(b) all remuneration receivable by the worker (from any person) in consequence of providing the services is to be treated for income tax purposes as earnings from that employment…"

27. In summary, ITEPA s 44 as amended provides that agency workers who are subject to, or to the right of "supervision direction or control by any person" are deemed to be employed for tax purposes. An equivalent NIC provision, not set out above, came into force around the same time.

28. FA 2014 also introduced a new section 716B into ITEPA, headed "Employment intermediaries to keep, preserve and provide information etc", which begins:

"(1) For purposes connected with Chapter 7 of Part 2 (treatment of workers supplied by agencies) or Part 11 (PAYE), the Commissioners for Her Majesty's Revenue and Customs may by regulations make provision for, or in connection with, requiring a specified employment intermediary

(a) to keep and preserve specified information, records or documents for a specified period;

(b) to provide Her Majesty's Revenue and Customs with specified information, records or documents within a specified period or at specified times.

(2) An "employment intermediary" is a person who makes arrangements under or in consequence of which

(a) an individual works, or is to work, for a third person, or

(b) an individual is, or is to be, remunerated for work done for a third person.

(3) For the purposes of subsection (2), an individual works for a person if

(a) the individual performs any duties of an employment for that person (whether or not the individual is employed by that person), or

(b) the individual provides, or is involved in the provision of, a service to that person…

(4) In subsection (1) "specified" means specified or described in regulations made under this section.

(5) Regulations under this section may

(a) make different provision for different cases or different purposes, and

(b) make incidental, consequential, supplementary or transitional provision or savings."

29. The regulations made under the *vires* given by ITEPA s 716B are contained in the Income Tax (Pay As You Earn) (Amendment No 2) Regulations.

THE CIS GUIDANCE

30. Section 1 of the CIS Guidance is headed "Introduction to the Construction Industry Scheme", and it begins:

> "This section gives a brief introduction to CIS. The scheme sets out the rules for how payments to subcontractors for construction work must be handled by contractors in the construction industry and certain other businesses.
>
> Under the scheme, all payments made from contractors to subcontractors must take account of the subcontractor's tax status, as determined by HMRC. This may require the contractor to make a deduction, which they then pay to HMRC, from that part of the payment that does not represent the cost of materials incurred by the subcontractor."

31. Section 1.2 defines "contractor" as "a business or other concern that pays subcontractors for construction work" and a "subcontractor" as "a business that carries out construction work for a contractor". It then says:

> "Many businesses pay other businesses for construction work, but are themselves paid by other businesses too. When they're working as a contractor, they must follow the rules for contractors and when they're working as a subcontractor, they must follow the rules for subcontractors.
>
> For a more detailed explanation of what is a contractor and what is a subcontractor, read Section 2."

32. After outlining the rules for CIS deductions, the CIS Guidance says at Section 1.8 (headings here and below emboldened in the original):

> "**The scheme does not apply to employees**
>
> For a contract to be within the scheme, it must not be 'a contract of employment'. This means that the scheme applies to workers who are self-employed under the terms of the contract, and who are not employees subject to Pay As You Earn (PAYE).
>
> Employment status depends on general law and it's for the contractor to decide on the individual's employment status when the subcontractor is first engaged. The fact that the subcontractor has worked in a self-employed capacity before is irrelevant in deciding on their employment status — it's the terms of the particular engagement that matter."

33. Section 2 includes the following subsections:

> "**2.10 Subcontractors**

A subcontractor is a person or body that has agreed to carry out construction operations for a contractor. The subcontractor may be carrying out the operations in any way, including:

- carrying out the operations themselves
- having the operations done by their own employees or subcontractors

Subcontractors include:

- companies, corporate bodies or public bodies, as well as any self-employed individual running a business or partnership
- labour agencies or staff bureaux that contract to get work done with their own workforce, or to supply workers to a contractor…

2.11 ….

2.12 Agencies as subcontractors

Where a worker is supplied to a contractor by or through an agency and the worker carries out construction operations under the terms of a contract they have with the agency, the agency supplying the worker will be a subcontractor as far as the contractor is concerned. The contractor must always apply the scheme when making payment to the agency.

Where a worker is merely introduced to the contractor by an agency and subsequently carries out construction operations under the terms of a contract they have with the contractor, the agency is not a subcontractor in this case.

2.13 Rules for agency workers

Special rules apply to agency workers[1] who normally treat the worker as an employee for tax and National Insurance contributions purposes. The business paying the worker should normally deduct tax under PAYE and account for Class 1 National Insurance contributions.

Very exceptionally, the special rules for agency workers do not apply and any payments for construction work will fall within the scheme. The agency will then be a contractor and will need to fulfil its obligations in that role."

THE FACTS

34. I first set out the background facts and then those relating to the dispute.

HRL's business

35. Mr Harbron's parents had previously run a formwork company (a company which specialises in constructing temporary structures to support concrete during construction) and owned a related agency. Those businesses closed during the 1980s recession, but as Mr Harbron had become familiar with the construction business, he relied on that experience to set up HRL. He is HRL's managing director and owns 35% of the shares; his wife and parents own the remainder. It is thus a small family business.

36. HRL identifies workers suitable for roles within construction projects in the local area, ranging from general operatives, machine operators, carpenters, bricklayers, plasterers and electricians right up to senior site managers, quantity surveyors and account directors. Once workers are accepted as suitable by the end-client, HRL directs them to an agency, which engages them. The contractual chain is thus as follows:

[1] This appears to be an error for "special rules apply to agencies who…"

(1) Construction company contracts with HRL to supply workers;

(2) HRL contracts with agency to supply workers;

(3) Agency contracts with workers to provide services to end-client.

The change to the agency rules

37. In 2014, the agency rules changed. As noted above, ITEPA s 44 was amended to provide that agency workers who were subject to, or to the right of "supervision direction or control by any person" were deemed to be employed for tax purposes.

38. HRL received a large number of newsletters and other information from external firms, such as human resource companies and payroll providers, warning that if a worker was not correctly identified as a deemed employee, but was instead treated as within CIS, the agency could be liable for all the under-deducted PAYE and NICs.

The staff changes and the accountants

39. At around the same time, Mr Harbron's mother, who had been responsible for the operation of CIS, had to retire for health reasons, and the other two experienced finance staff also left the business. Mr Harbron recognised he did not have the skills necessary to deal with finance issues, as his role had always been in business development and sales. He instructed HRL's accountants, Darnells, a well-known and respected local firm, to manage the function while new staff were recruited, and to interview the applicants to ensure that the candidate who was appointed had the necessary skills.

40. Mr Harbron also recognised that specialist advice was required in the light of the change to the agency rules, and he instructed CISTAL to carry out a complete review of HRL's operations, including compliance with its obligations under CIS and the agency rules. CISTAL is a subsidiary of Francis Clark LLP ("Francis Clark"), a large and reputable accountancy practice based in the West Country. CISTAL was set up by Francis Clark specifically to provide specialist advice on CIS and related issues.

41. CISTAL's review was carried out by Mr Clutterbuck; he had previously worked for over thirty years for HMRC, initially as a Compliance Officer and then a Senior Manager; he dealt predominantly with CIS and employment tax. Given his role and background, I find as a fact that he had read and was familiar with:

(1) the CIS legislation and regulations;

(2) the CIS Guidance; and

(3) the agency rules.

42. Mr Clutterbuck carried out a health check on HRL and identified only minor issues. One of HRL's directors then designed a program to ensure that workers who were within the agency rules were identified as such. This was a significant financial investment, and Mr Harbron instructed CISTAL to carry out a further review. Mr Steve Ashworth, Tax Director at Francis Clark, subsequently confirmed in correspondence with HMRC that CISTAL was being engaged to and actually did provide support "in relation to both aspects", ie both CIS and the agency rules, and I find this to be a fact.

43. Mr Clutterbuck carried out that further review, and having done so, confirmed that HRL's software met the legal requirements. He also advised that HRL should make reports to HMRC under s 716B, because it was an employment intermediary as defined under s 716B(2), namely "a person who makes arrangements under or in consequence of which (a) an individual works,

or is to work, for a third person, or (b) an individual is, or is to be, remunerated for work done for a third person". The agencies told HRL that they were applying ITEPA s 44; deeming the workers to be employees, and deducting PAYE and NICs.

44. Around the same time as CISTAL was carrying out its review, Mr Harbron decided to transfer overall responsibility for advising on HRL's accounting and tax issues from Darnells to Francis Clarke. HRL also recruited a new senior member of staff with a strong construction background, including experience of CIS; when she left, her replacement was another finance manager with similar background and experience.

The change of approach

45. Having taken advice both from an external specialist firm and from internal experienced finance staff, Mr Harbron understood the position to be as follows:

(1) the workers being contracted were subject to supervision direction and control;

(2) they were thus deemed to be employed by the agencies and were not within CIS;

(3) PAYE and NIC was deducted and paid over to HMRC by the agencies;

(4) by completing the detailed returns required under ITEPA s 716B, HMRC were being provided with information relating to the workers; and

(5) HRL therefore did not have to operate CIS in relation to its payments to the agencies.

46. As a result, in May 2017 HRL changed its approach, and completed CIS returns on a nil basis. Mr Ashworth subsequently accepted that the advice given to HRL "may have lacked clarity in certain elements", while Mr Harbron acknowledged t he had misunderstood the position. Nevertheless, during the next three years, the error was not identified by any of HRL's external or internal professionals.

HMRC compliance checks

47. On 18 May 2017, HMRC opened a check into HRL's compliance with its CIS obligations, and arranged to visit the premises. However, that visit was postponed by HMRC and subsequently cancelled. HRL heard nothing further and were never told why HMRC had not taken any further action in relation to this compliance check.

48. On 21 October 2020, Officer Jason Purdy opened a second compliance check, this time into HRL's PAYE, VAT and CIS compliance as part of an exercise to prevent businesses being "caught up in" fraudulent supply chains.

49. HRL provided extensive information in response to Officer Purdy's questions, and on 9 December 2020, Officer Purdy wrote back, saying:

> "Harbron Recruit Ltd are of the understanding NIL submissions are correct as they use intermediary companies. You have detailed that the company offers construction specific roles and make supplies of labour to the construction sector. I refer to section 2.12 in the Construction Industry Scheme Guide (CIS 340) which details how contractors such as Harbron Recruit Ltd should treat payments to sub-contractors who supply workers via an agency.
>
> I have attached a link to the CIS 340 guide…This confirms that a contractor, in this case Harbron Recruit Ltd must always apply the Construction Industry Scheme (CIS) when making a payment to an agency. For CIS purposes this is a contractor and sub-contractor relationship, therefore NIL submissions are

> incorrect and payments made to agencies/sub-contractors should take account of their tax status as determined by HMRC.
>
> I take on board Harbron Recruit Ltd comments on quarterly intermediary reports for HMRC and that the intermediaries pay the workers via PAYE however this is not relevant in determining if payments fall under scope of the Construction Industry Scheme (CIS). Whether a payment falls within the scope of the CIS scheme is determined by the type of work carried out and from the information provided it appears that the company is supplying workers for construction work. Therefore, all payments made by Harbron Recruit to agencies for construction related activities within the scope of the CIS scheme should take account of the subcontractor/agencies tax status as determined by HMRC."

50. On 4 March 2021, a telephone conference ("the Meeting") took place between Officer Purdy and another HMRC officer on the one hand, and Mr Harbron, together with Mr Ashworth and Mr Bishop of Francis Clark on the other. The meeting discussed both CIS and VAT issues.

51. On 8 March 2021 (updated on 29 March 2021) HMRC issued a "Warning Letter" under Reg 13(1) of the CIS Reg stating that they would raise determinations on HRL for £483,675 for the years 2017-18 through to 2020-21 as set out below.

Year	**Subcontractor**[2]	**Excess**
2017-18	C Ltd	£129,513
2017-18	P Ltd	£104,302
2018-19	P Ltd	£110,947
2018-19	PC Ltd	£69,174
2018-19	PC Ltd	£1,554
2019-20	PC Ltd	£25,988
2019-20	AC Ltd	£39,815
2020-21	PP Ltd	£2,382
Total		£483,675

52. On 28 April 2021, Mr Ashworth wrote to HMRC, asking them to direct that either or both of Condition A or B of Reg 9 applied. As set out earlier in this Decision, Condition A was that HRL was not liable to pay the excess because it had acted with reasonable care; Condition B was that the subcontractors had paid income or corporation tax on the related profits.

53. On 2 June 2021, Officer Lin Hale issued HRL with a direction that Condition B applied to the excess relating to C Ltd for 2017-18 of £129,513. In a separate decision letter of the same date, she refused to apply Condition A to the remaining sum of £354,162. She said:

[2] The names of the subcontractors have been anonymised, as they are not a party to the appeal and their names are not required to understand this decision, see *Mr A v HMRC* [2015] UKFTT 189 (TC) at [4] and *Unwired Planet International Ltd v Huawei Technologies Co Ltd (No 2)* [2017] EWHC 3083 (Pat) at [24(iv)].

> "I am not satisfied the criteria in Regulation 9(4) Condition B of the Income Tax (Construction Industry Scheme) Regulations 2005 have been met and I am now notifying you of my decision."

54. On behalf of HRL, Mr Ashworth appealed against the refusal to apply Condition A. He said:

> "Our client now fully appreciates that this understanding was not correct, but this does not change the facts that during the period under review it was genuinely believed that nil CIS returns were appropriate because employment intermediaries reports were being submitted. This was a genuine mistake."

55. Mr Ashworth also asked for a statutory review, following which Officer Hale issued a "view of the matter" letter, in which she said:

> "You failed to operate the Construction Industry Scheme on payments made to subcontractors engaged by you. You have not demonstrated that you took reasonable care in finding out your obligations under the scheme.
>
> I do not consider that the further explanation about the failure to operate the Construction Industry Scheme has provided any additional information for me to consider that the original decision not to grant relief was incorrect, therefore I have not changed my view of the matter."

56. Officer Telfer carried out that statutory review. He set out the "point at issue" as being "whether the company took reasonable care to comply with section 61 of the Finance Act 2004 and the CIS Regulations" and then said:

> "The Regulation 9(6) refusal notice was issued because it was not considered that the company had met the requirement at Regulation 9(3)(a) of the CIS Regulations that reasonable care had been taken to comply with section 61 of the Finance Act 2004 and the CIS Regulations."

57. Officer Telfer went on to uphold Officer Hale's decision, and on 6 January 2022, HRL notified its appeal to the Tribunal. The parties then entered ADR, but this was unsuccessful. The case was twice listed for an oral hearing, but both were postponed. The parties then asked for the appeal be determined on the papers under Rule 29 and it was listed before me.

WHAT IS (AND WHAT IS NOT) IN ISSUE

58. I next set out what points are not in issue, and what matters are to be decided by the Tribunal.

The underlying technical issue

59. By or soon after the Meeting, there was no dispute that HMRC were technically correct. Payments between HRL and the agencies were within CIS, even though the workers were deemed to be employed by the agencies. This Decision thus does not address the technical issue except in so far as relevant to the reasonableness of HRL's actions.

The quantum

60. The statutory review letter and HMRC's Statement of Case each said that the amount in dispute was £483,675. Both therefore overlooked the fact that Officer Hale had issued a direction on 2 June 2021 that Condition B applied in relation to £129,513 of the excess. As a result, the amount under appeal is £354,162 (£483,675 less £129,513). For the avoidance of doubt, this Decision would have extended to the £129,513 had it remained in issue.

Condition B

61. HMRC refused to direct that Condition B applied to the remaining amounts, but Reg 9 does not give a person a right of appeal against that refusal. This was described as "odd" by Judge Berner in *Hoskins v HMRC* [2012] UKFTT 284 (TC), given that whether or not a subcontractor (here, the agencies) had paid the correct tax was "a straightforward issue" on which a Tribunal could make a finding of fact.

62. I also note that as drafted Condition B only gives relief where the subcontractor has paid corporation tax or income tax on its own profits, and does not extend to cases where tax and NICs are paid by employees (including deemed employees) of the subcontractor.

63. Notwithstanding those points, the statute does not allow HRL to appeal against HMRC's refusal to apply Condition B to its other subcontractors, and the Tribunal has no related jurisdiction.

VAT

64. As is clear from the findings of fact, Officer Purdy's compliance check also included VAT, and the Bundle included numerous related documents. Mr Harbron's witness statement said that:

(1) HMRC raised VAT assessments as the result of the compliance check;

(2) HRL appealed on the basis that it had taken reasonable care; and

(3) the assessments were subsequently cancelled.

65. As a result, this Decision does not address any VAT matters.

Condition A

66. In consequence of the foregoing, the only issue for me to decide is whether HMRC were right to refuse to direct that Condition A applied, and the only grounds of appeal I can consider are those set out at Reg 9(8), namely that HRL:

> "(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) [HRL] held a genuine belief that section 61 of the Act did not apply to the payment."

67. One of HRL's grounds of appeal was that HMRC had initiated the first compliance check because they had identified the error in the CIS returns, but had then allowed the business to go on making incorrect returns for three further years. Mr Harbron said that this was a breach of HMRC's obligations to taxpayers. However, that submission is not one of the permitted grounds set out in Reg 9(8), so cannot be considered by the Tribunal.

68. There is one further issue to be resolved in relation to the scope and application of Condition A. HMRC's Statement of Case says:

> "HMRC submits that this case concerns whether reasonable care was taken by the Appellant and only if this can be satisfied then can consideration be given as to whether the failure to deduct the tax was due to an error made in good

> faith or the Appellant held a genuine belief that section 61 did not apply to payments he had made."

69. This implies that if the Tribunal finds that HRL took reasonable care, the case will revert to HMRC to make further decisions as to (a) whether the error was made in good faith and (b) whether there was the necessary genuine belief. I disagree for the reasons explained below.

The Officer is required to set out the grounds for the refusal

70. Reg 9(6) reads (my emphasis):

> "If condition A is not met an officer of Revenue and Customs may refuse to make a direction under paragraph (5) by giving notice to the contractor ("the refusal notice") stating—
>
> (a) **the grounds for the refusal**, and
>
> (b) the date on which the refusal notice was issued".

71. Officer Hale's decision letter issued on 2 June 2021 said that the refusal notice was issued on the grounds that she was "not satisfied that the criteria in Regulation 9(4) Condition B of the Income Tax (Construction Industry Scheme) Regulations 2005 have been met". In her subsequent "view of the matter" letter, she said that, having considered further information provided, she had not "changed [her] view" because HRL "have not demonstrated that [it] took reasonable care in finding out [its] obligations under the [CIS] scheme".

72. These two letters, taken together, show that the *only* criterion which in Officer Hale's view had not been met was that HRL had not demonstrated reasonable care. Officer Telfer, who carried out the statutory review, confirmed that this was the position when he said:

> "The Regulation 9(6) refusal notice was issued because it was not considered that the company had met the requirement at Regulation 9(3)(a) of the CIS Regulations that reasonable care had been taken to comply with section 61 of the Finance Act 2004 and the CIS Regulations."

A single procedure

73. There is no suggestion in any of the three letters referred to above that HMRC had reserved their position in relation to "good faith" or "genuine belief". This would in any event be impermissible, because:

(1) Reg 9(6) requires HMRC to set out their grounds for refusal;

(2) the company has the right to appeal against that refusal; and

(3) Reg 9(9) then provides that the Tribunal "may direct that [HMRC] make a direction under paragraph (5) in an amount the tribunal determines is the excess for one or more tax periods falling within the relevant year".

74. Thus, Reg 9 sets out a single procedure, as the result of which the Tribunal determines whether the company is responsible for the excess and the correct amount of any excess. Nothing in the statute supports HMRC's submission that there is a two or three stage process, under which HMRC have a second or third bite of the cherry if they lose the initial appeal.

No case law support

75. HMRC's Statement of Case also does not refer to any case law which would support this two or three stage approach. Having reviewed previous FTT judgments, I have not identified any previous decision in which HMRC have put forward this view of the law, let alone one which upholds this approach.

Interests of justice

76. Moreover, if HMRC were to be correct, the decision and appeal process would be extremely time-consuming and inefficient, with matters of fact being decided long after the events in question, and the parties potentially bringing the same dispute before the Tribunal on two or three sequential occasions. That would plainly not be in the interests of justice.

Observations

77. For completeness, I add the following observations about the other parts of Condition A:

(1) In relation to "genuine belief", it is clear from the findings of fact made in this Decision that Mr Harbron genuinely believed he was acting correctly, and this has never been challenged or disputed by HMRC.

(2) In relation to "good faith", as Peter Smith J said in *R&C Commrs v Infinity Distribution* [2015] UKUT 219 (TCC) at [11], "it is well established that an allegation of lack of good faith is tantamount to an allegation of fraud". No such allegation has been made by HMRC; none of the evidence provided for this appeal would support such an allegation, and the burden of proving a lack of good faith would be on HMRC.

In summary

78. The refusal decision at issue in this case was made because Officer Hale considered that HRL had not acted with reasonable care, and for no other reason. That is the decision which is now before the Tribunal. If HRL succeeds in its appeal, HMRC cannot then make further decisions about HRL's lack of "genuine belief" and/or "good faith".

79. The issue I have to decide is therefore whether HRL, acting through Mr Harbron, "took reasonable care".

WHAT IS "REASONABLE CARE"

80. In *HMRC v* Hicks [2020] UKUT 12 (TCC), the Upper Tribunal held at [120] that:

> "Whether acts or omissions are careless involves a factual assessment having regard to all the relevant circumstances of the case. There are many decided cases as to what amounts to carelessness in relation to the completion of a self-assessment tax return. The cases indicate that the conduct of the individual taxpayer is to be assessed by reference to a prudent and reasonable taxpayer in his position: see, for example, *Atherton v HMRC* [2019] STC 575 (Fancourt J and Judge Scott) at [37]."

81. In *Perrin v HMRC* [2018] UKUT 156 (TCC) ("*Perrin*") the UT considered the test for a "reasonable excuse", and held at [81(3)] that the Tribunal had first to find the facts, and then decide:

> "…whether, viewed objectively, those proven facts do indeed amount to an objectively reasonable excuse for the default and the time when that objectively reasonable excuse ceased. In doing so, it should take into account the experience and other relevant attributes of the taxpayer and the situation in which the taxpayer found himself at the relevant time or times. It might assist the FTT, in this context, to ask itself the question "was what the taxpayer did (or omitted to do or believed) objectively reasonable for this taxpayer in those circumstances?"

82. In *Hextall v HMRC* [2023] FTT 00390 (TC) at [74] the Tribunal (Judge Sinfield and Mr Howard) held at [74] that there was no "meaningful distinction" between the two criteria of "reasonable care" and "reasonable excuse". I agree: in both the Tribunal must find the facts,

and then on the basis of those facts, determine whether the taxpayer acted as a prudent and reasonable taxpayer (who was in the same situation as the taxpayer and who had same experience and relevant attributes) would have acted.

THE PARTIES' SUBMISSIONS

83. I first set out HMRC's submissions, and then those made on behalf of HRL.

Submissions made by HMRC

84. HMRC's position was that in submitting nil CIS returns HRL had failed to take reasonable care, because:

(1) it was clear from the CIS Guidance at Sections 2.10 and 2.12 that subcontractors include agencies;

(2) "nowhere is it suggested" in legislation or guidance that the agency rules "include payments for work done in the construction industry";

(3) HRL's decision to change its procedures because of the agency rules was "a clear indication that the company did not [take] reasonable care to comply with its obligations" in relation to CIS; and

(4) although HRL did seek advice from CISTAL, it did so because it was confused by the new agency requirements, and did not ask CISTAL about CIS.

85. HMRC also said that "it is well established that ignorance of the law is not a defence, and the Tribunal has routinely exercised [sic] that view".

Submissions made on behalf of HRL

86. Mr Harbron and Mr Clutterbuck submitted that HRL had acted with reasonable care, for the following reasons:

(1) Mr Harbron's focus throughout had been on making sure that correct tax approach was applied.

(2) He had read the information about the changes to the agency rules and realised he was out of his depth.

(3) He instructed CISTAL, an accountancy firm specialising in the construction industry, to advise HRL and ensure the company remained compliant.

(4) HRL had invested a significant amount of time and money in seeking to establish whether the workers engaged to carry out the tasks for the end-clients were subject to supervision, direction and control.

(5) The interaction of the agency rules and the CIS provisions was complex.

(6) Having taken advice, Mr Harbron had done his best to understand both sets of provisions, and believed that as the workers were all deemed to be employed, HRL would meet its compliance obligations by submitting returns under ITEPA s 716B.

(7) Mr Harbron had also ensured that appropriately skilled staff were recruited for the relevant roles within the company.

(8) None of the external or internal professionals had identified (until this was pointed out by HMRC) that HRL was wrong to submit its CIS returns on a nil basis, and this too showed that the interactions were complex.

87. Mr Harbron also rejected HMRC's assertion that this was a case about ignorance of the law; he said it was instead about misunderstanding how two sets of provisions interacted.

THE TRIBUNAL'S VIEW

88. I have set out my view under the following headings:

(1) Ignorance of the law.

(2) The CIS Guidance and the legislation.

(3) Interactions between CIS and the agency rules.

(4) Reliance on advisers.

Ignorance of the law

89. Submissions about "ignorance of the law" are typically raised where the taxpayer has not known about a particular provision, such as a statutory obligation to report gains on residential property, or to notify liability to the High Income Child Benefit Charge. Mr Harbron was not ignorant of CIS or the agency rules; he knew about both sets of provisions. Instead, he misunderstood the law.

90. In any event, HMRC are wrong to say that (a) ignorance of the law cannot be a reasonable excuse, and (b) the Tribunal has "routinely" endorsed that view. In *Perrin*, the UT said at [82]:

> "…It is a much-cited aphorism that 'ignorance of the law is no excuse', and on occasion this has been given as a reason why the defence of reasonable excuse cannot be available in such circumstances. We see no basis for this argument. Some requirements of the law are well-known, simple and straightforward but others are much less so. It will be a matter of judgment 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."

The CIS guidance and the legislation

91. HMRC say that it was not reasonable for someone in Mr Harbron's position to think that the CIS requirements were displaced by the agency rules, because it was clear from the CIS Guidance at Sections 2.10 and 2.12 that subcontractors include agencies.

92. That is true as far as it goes. However, it is also relevant that:

(1) Section 1.8 of the CIS Guidance says that "the scheme does not apply to employees";

(2) Section 2.13 states that "special rules apply to agency workers who normally treat the worker as an employee for tax…purposes";

(3) the CIS legislation itself, at FA 2004, s 60, provides that a payment under construction contracts made by a contractor is not within CIS if "the payment is treated as earnings from an employment by virtue of Chapter 7 of Part 2 of the Income Tax (Earnings and Pensions) Act 2003 (agency workers)"; and

(4) ITEPA s 716B(2) defines an employment intermediary "for purposes connected with Chapter 7 of Part 2 (treatment of workers supplied by agencies)" as "a person who makes arrangements under or in consequence of which (a) an individual works, or is to work, for a third person, or (b) an individual is, or is to be, remunerated for work done for a third person". HRL was responsible for arranging for the provision of workers to fill the roles required by the end-clients.

93. Thus, the CIS Guidance and the legislation, read as whole, show that the interaction of CIS provisions and the agency rules is not straightforward.

Interactions between CIS and the agency rules

94. HMRC also say that HRL's decision to change its procedures because of s 44 was "a clear indication that the company did not [take] reasonable care to comply with its obligations" in relation to CIS, given that "nowhere is it suggested" that the agency rules "include payments for work done in the construction industry".

95. HMRC are wrong to say that the agency rules do not apply to those working in construction. They apply whenever the conditions set out in ITEPA s 44 are met, so a construction worker who is subject to "supervision, direction or control by any person" is a deemed employee under the provisions of that section. As Mr Harbron said, whether or not the agency rules apply requires a detailed consideration of the facts of each worker's case.

96. Unsurprisingly, given the scope and effect of ITEPA s 44, HMRC are also wrong to say that it has never been suggested that the agency rules "include payments for work done in the construction industry". Around the time that ITEPA s 44 was amended, HMRC published numerous examples as to how the provisions applied; these remain available on the gov.uk website[3]. Example 4 is John, a joiner/carpenter who works on small-scale construction jobs. Depending on the particular fact pattern, John is either inside or outside the agency rules.

97. The failure of HMRC's own officers to appreciate the wide scope of the agency provisions serves to support HRL's case that the interaction between the two sets of rules is not straightforward.

98. The agency rules mattered to HRL because its role was to identify suitable workers to fit the roles required by the end-clients. HRL therefore took responsibility for deciding whether those workers were inside the agency rules. but it overlooked the fact that, because the agencies were interposed in the contractual chain, HRL continued to be required to pay them under CIS.

Reliance on advisers

99. HMRC rightly accepted that:

(1) the statutory test requires consideration of how the reasonable taxpayer in Mr Harbron's position would have acted;

(2) Mr Harbron knew he lacked the knowledge and understanding to know how to respond to the changes to the agency rules; and

(3) Mr Harbron acted as the reasonable person in his position would have acted when he instructed CISTAL.

100. However, HMRC go on to say that Mr Harbron sought advice only about the agency rules, and not about CIS. That is not, however, factually correct see §42: HRL requested and received advice about both sets of provisions.

The Tribunal's view

101. I have no hesitation in agreeing with Mr Harbron and Mr Clutterbuck that HRL, acting through Mr Harbron, acted with the level of care which the reasonable person in his position would have showed. That is for the following reasons:

[3] https://assets.publishing.service.gov.uk/media/5a7c2a9fed915d26a930179b/Definition_of_Supervision_Direction_or_Control_with_supporting_examples.pdf

(1) The interaction of the two sets of provisions was technically complex.

(2) Mr Harbron recognised that this was the case, and realised he was out of his depth.

(3) He acted reasonably when he instructed CISTAL, a subsidiary of a highly reputable large firm and a specialist in CIS and employment taxes.

(4) He also acted reasonably in relying on Mr Clutterbuck, a former HMRC Senior Manager with over thirty years experience in CIS and employment law who was familiar with the law and guidance on CIS and the agency rules.

(5) HRL asked for and received professional advice about both CIS and the agency rules.

(6) Mr Harbron also ensured that the staff within HRL were professionally qualified and had the requisite skills, and it was reasonable to rely on them as well as on CISTAL.

102. This case is a clear example of a situation where, despite Mr Harbron doing his best to ensure that the correct steps were taken, a mistake was nevertheless made. However, a mistake does not prevent Condition A being met. As HMRC themselves say in their Compliance Manual at CH1140:

> "People do make mistakes. We do not expect perfection. We are simply seeking to establish whether the person has taken the care and attention that could be expected from a reasonable person taking reasonable care in similar circumstances, taking into account the ability and circumstances of the person in question at the time the irregularity was submitted to HMRC."

CONCLUSION

103. For the reasons set out above, HRL's appeal is allowed. In accordance with Reg 9(9) of the CIS Regs, I direct that an officer of HMRC make a direction under Reg 9(5) in an amount of nil in relation to each of the years as set out below.

Year	Subcontractor	Excess under appeal	Excess after appeal
2017-18	P Ltd	£104,302	nil
2018-19	P Ltd	£110,947	nil
2018-19	PC Ltd	£69,174	nil
2018-19	PC Ltd	£1,554	nil
2019-20	PC Ltd	£25,988	nil
2019-20	AC Ltd	£39,815	nil
2020-21	PP Ltd	£2,382	nil
Total		£354,162	nil

104. HMRC are reminded that (despite the position taken in their review letter and their Statement of Case) a direction has already been issued by Officer Hale on 2 June 2021 under Reg 9(5) that HRL is not liable to pay the "excess" in relation to C Ltd for 2017-18 of £129, 513.

105. As a result of that earlier direction and this Decision, all the “excess” originally identified by HMRC has been reduced to nil.

RIGHT TO APPLY FOR PERMISSION TO APPEAL

106. 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 Rules. 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.

Release Date: 09th JANUARY 2025