



**TC07995**

*Income Tax – construction industry scheme – whether withdrawal of gross status eight years after compliance failures is proportionate – held not – appeal allowed*

**FIRST-TIER TRIBUNAL  
TAX CHAMBER**

**Appeal number: TC/2012/10937**

**BETWEEN**

**RMF CONSTRUCTION SERVICES LTD**

**Appellant**

**-and-**

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

**Respondents**

**TRIBUNAL: JUDGE PHILIP GILLETT**

**The Tribunal determined the appeal on 30 November 2020 without a hearing under the provisions of Rule 29 of the Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules 2009 having received the consent of both parties that the appeal should be determined on the basis of the papers presented to the Tribunal.**

**The Tribunal determined this case on the basis of written submissions from HMRC, primarily contained in a Statement of Case dated 4 February 2020, and submissions from the Appellant dated 16 October 2020.**

## DECISION

### INTRODUCTION

1. This is an appeal against HMRC's decision to withdraw the Appellant's gross payment status under the Construction Industry Scheme.
2. HMRC withdrew the Gross Payment Status because the Appellant ("RMF") failed to comply with their Tax and National Insurance contributions obligations under s66(1) Finance Act 2004 ("FA 2004").
3. It is accepted by HMRC that RMF had a reasonable excuse for failing to submit contractor's monthly returns on time. It is not accepted that the company has a reasonable excuse for the other compliance failures.
4. It is accepted by RMF that the Corporation Tax (CT) return for the Accounting Period Ending 31 July 2010 was filed late. HMRC's ground for withdrawing the gross basis was the late payment of the company's corporation tax liability for the period ended 31 March 2013. This should have been paid on 1 January 2014 but was not in fact paid until September 2014.
5. At the request of HMRC, this appeal was stayed for some time behind the case of *JP Whitter (Water Well Engineers) Ltd v HMRC* [2018] STC 1394. This was finally decided by the Supreme Court in a judgement given on 13 June 2018.
6. Pending the determination of this appeal the appellant has retained gross payment status for the purposes of the Construction Industry Scheme.

### GROUND OF APPEAL

7. RMF has put forward five grounds of appeal:
  - (1) There has been a significant amount of time from the period RMF failed to comply with s66(1) Finance Act 2004. It has been eight years since its appeal was rejected, nine years from the date HMRC carried out their Tax Treatment Qualifying Test ("TTFT") and more than 10 years from the end of the accounting period under initial review by HMRC.
  - (2) The company currently satisfies all of the requirements to be granted Gross Payment Status and has done so for the last four to five years.
  - (3) If the company were to apply for Gross Payment Status now it would comply with the requirements and would be granted Gross Payment Status.
  - (4) The company accepts that the outcome of the review in 2012 was technically correct, but cannot accept that to withdraw Gross Payment Status eight years later, in 2020, is appropriate.

### SUMMARY OF DECISION

8. The tribunal decided that the withdrawal of CIS gross status over eight years after the "offence" of the company's failure to file its corporation tax return on time, together with other minor infringements would be totally disproportionate. The objective of the CIS, ie, the enforcement of compliance, has been achieved by the mere threat of the withdrawal of gross status and to carry through on that threat by withdrawing gross status now, when the company has been fully compliant since that time, would serve no useful purpose whatsoever and is therefore disproportionate.
9. The appeal is therefore ALLOWED.

## THE FACTS

10. I received a Statement of Case from HMRC and submissions from Mr McGee, the director of RMF, both of which contained statements of facts. Mr McGee, in his submissions states that given the passage of time he cannot remember in any detail specific events from the relevant time such as might enable him to refute HMRC's statement of the facts. There is therefore no disagreement between the parties as to the essential facts. I therefore find the following as matters of fact.
11. The company was incorporated on 5 July 2000 and commenced trading on 1 August 2000. The company undertakes construction work.
12. On 8 September 2011 HMRC carried out a Tax Treatment Qualifying Test (TTQT), or Scheduled Review, to ensure that the company was meeting its tax obligations during the period from 2 September 2010 to 2 September 2011.
13. HMRC identified three failures during the period examined:
  - (1) The company's Corporation Tax Return due on 31 July 2011 in respect of the accounting period ended 31 July 2010 was not received until 5 October 2012 and was therefore 431 days late.
  - (2) The company's Contractor's Return due on 19 July 2011 was not received until 5 October 2011 and was therefore 78 days late.
  - (3) The company's Contractors Return due on 19 May 2011 was not received until 22 June 2011 and was therefore 34 days late.
14. HMRC wrote to the company on 27 September 2011 advising of the failures and requesting an explanation. HMRC also advised that documentary evidence must be supplied at this stage if this supports the reasons for the apparent failures.
15. The company's agent replied on 21 October 2011 informing HMRC that:
  - (1) They were in the process of dealing with the CT Returns.
  - (2) The CIS Returns were a genuine mistake by the Appellant's CIS clerk which had now been rectified.
16. HMRC wrote to the agent on 16 November 2011 stating that their explanation for the compliance failures could not be accepted because it was not accepted that they had a reasonable excuse for the failure to submit the CT Return on time. HMRC also withdrew Gross Payment Status on the same date.
17. On 29 November 2011, an appeal was sent to HMRC by the agent, but this was not received. A further copy was sent to HMRC on 30 March 2012.
18. On 17 May 2012, HMRC rejected the appeal as the CT return was still outstanding.
19. On 24 August 2012, HMRC wrote to the company accepting the reasonable excuse for the failure to submit contractors monthly returns, but noted five other failures during the period following the review, from September 2011 to August 2012, which involved the CT returns for the accounting periods ended 31 July 2011 and the P35 due for the year ended 5 April 2012.
20. In the light of this, HMRC noted that they had reason to doubt that the company would continue to meet their tax obligations, and upheld the withdrawal of Gross Payment Status.
21. On 25 September 2012, the company requested a review of the decision. The review was concluded on 7 November 2012 when HMRC wrote to the company advising that the decision to withdraw gross payment status was upheld. The reasons given for this were:

(1) The reasons given for the late submission of the CT Return for the accounting period ended 31 July 2010 were that it was an oversight, records were misplaced, work pressures & family problems. HMRC does not consider this demonstrates a Reasonable Excuse which lasted over the full 14 month period for which the return was outstanding.

(2) Once the Reasonable Excuse no longer existed the failure should be remedied as soon as possible.

(3) Gross Payment Status is a privilege for those contractors who comply with the statutory tests. Those who do comply, and have to compete with those who do not, are trading at a disadvantage.

(4) There were compliance failures which continued, and new failures that arose, after the date of the TTQT. HMRC considered that this was not a one-off situation, and that despite HMRC warning the company in the past they had still failed to meet their obligations within the scheme.

22. On 6 December 2012, an appeal was made to the Tribunal.

23. The Tribunal then directed that the matter should be stood behind the case of *JP Whitter (Waterwell Engineers) Ltd v HMRC* [2018] STC 1394.

## **THE LAW**

24. The requirements for registration for gross payment status under the CIS are set out in s64 Finance Act 2004 as below:

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

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

(2) Where the application is for the registration for gross payment of an individual (otherwise than as a partner in a firm), he must satisfy the conditions in Part 1 of Schedule 11 to this Act.

(3) Where the application is for the registration for gross payment of an individual or a company as a partner in a firm—

(a) the applicant must satisfy the conditions in Part 1 of Schedule 11 to this Act (if an individual) or Part 3 of that Schedule (if a company), and

(b) in either case, the firm itself must satisfy the conditions in Part 2 of that Schedule.

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

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

(b) if the Board of Inland Revenue have given a direction under subsection (5), each of the persons to whom any of the conditions in Part 1 of that Schedule applies in accordance with the direction must satisfy the conditions which so apply to him.

(5) Where the applicant is a company, the Board may direct that the conditions in Part 1 of Schedule 11 to this Act or such of them as are specified in the direction shall apply to—

(a) the directors of the company,

- (b) if the company is a close company, the persons who are the beneficial owners of shares in the company, or
  - (c) such of those directors or persons as are so specified, as if each of them were an applicant for registration for gross payment.
- (6) See also section 65(1) (power of Board to make direction under subsection (5) on change in control of company applying for registration etc).
- (7) In subsection (5) “director” has the meaning given by section 67 of the Income Tax (Earnings and Pensions) Act 2003 (c. 1).”
25. Section 66 Finance Act 2004 then goes on to set out the circumstances in which registration for gross status may be withdrawn:

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

- (1) The Board of Inland Revenue may at any time make a determination cancelling a person’s registration for gross payment if it appears to them that—
- (a) if an application to register the person for gross payment were to be made at that time, the Board would refuse so to register him,
  - (b) he has made an incorrect return or provided incorrect information (whether as a contractor or as a sub-contractor) under any provision of this Chapter or of regulations made under it, or
  - (c) he has failed to comply (whether as a contractor or as a sub-contractor) with any such provision.
- (2) Where the Board make a determination under subsection (1), the person’s registration for gross payment is cancelled with effect from the end of a prescribed period after the making of the determination (but see section 67(5)).
- (3) The Board of Inland Revenue may at any time make a determination cancelling a person’s registration for gross payment if they have reasonable grounds to suspect that the person—
- (a) became registered for gross payment on the basis of information which was false,
  - (b) has fraudulently made an incorrect return or provided incorrect information (whether as a contractor or as a sub-contractor) under any provision of this Chapter or of regulations made under it, or
  - (c) has knowingly failed to comply (whether as a contractor or as a sub-contractor) with any such provision.
- (4) Where the Board make a determination under subsection (3), the person’s registration for gross payment is cancelled with immediate effect.
- (5) On making a determination under this section cancelling a person’s registration for gross payment, the Board must without delay give the person notice stating the reasons for the cancellation.
- (6) Where a person’s registration for gross payment is cancelled by virtue of a determination under subsection (1), the person must be registered for payment under deduction.

(7) Where a person's registration for gross payment is cancelled by virtue of a determination under subsection (3), the person may, if the Board thinks fit, be registered for payment under deduction.

(8) A person whose registration for gross payment is cancelled under this section may not, within the period of one year after the cancellation takes effect (see subsections (2) and (4) and section 67(5)), apply for registration for gross payment.

(9) In this section "a prescribed period" means a period prescribed by regulations made by the Board."

26. Extensive conditions for registration are contained in Sch 11 Finance Act 2004 and, in particular, what is referred to as the compliance test, for companies, is set out in para 12 Sch 11 as follows:

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

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

(b) all requests made in the qualifying period to supply to the Inland Revenue accounts of, or other information about, its business.

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

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

(b) is of a kind prescribed by regulations made by the Board of Inland Revenue, is, in such circumstances as may be prescribed by the regulations, to be treated as satisfying the condition in that sub-paragraph as regards that obligation or request.

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

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

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

(4) The company must, if any contribution has at any time during the qualifying period become due from the company under—

(a) Part 1 of the Social Security Contributions and Benefits Act 1992 (c. 4), or

(b) Part 1 of the Social Security Contributions and Benefits (Northern Ireland) Act 1992 (c. 7),

have paid the contribution when it became due.

(5) The company must have complied with any obligations imposed on it by the following provisions of the Companies Act 1985 (c. 6) in so far as those obligations fell to be complied with within the qualifying period ..."

27. Some relief is provided from these strict requirements under Regulation 32 of SI2005/2045. In particular this provides some flexibility in respect of, inter alia:

(1) Three late submissions of the CIS return – up to 28 days late,

- (2) Three late payments of CIS/PAYE payments – up to 14 Days late, and
- (3) One late payment of corporation tax – up to 28 days late.

## DISCUSSION

28. It is common ground between the parties that the company did not submit its CT return for the year to 31 March 2010 and that there had been a number of other failures at that time in respect of CT returns, CIS returns and a P35 return. HMRC have accepted that the company did have a reasonable excuse for failing to submit contractor's monthly returns on time, but they do not accept that the company had a reasonable excuse for the other compliance failures.

29. Moreover RMF has accepted that the outcome of the review in 2012 was technically correct, but cannot accept that to withdraw Gross Payment Status eight years later, in 2020, is appropriate.

30. Given this mutual acknowledgement of the position regarding reasonable excuse I do not need to consider this further. In any case, the director of RMF, Mr McGee, states in his submissions that the time elapsed makes it impossible for him to recall specific events from that time. In addition he says that the company has changed its advisor twice since the period in question and that he is no longer in contact with the advisor at that time, a Mr Alam. Mr McGee states that he cannot recall with any certainty the events leading up to the conclusion of the review by HMRC in 2012. He says that, as is typical in these cases, he was heavily reliant on the tax advisor doing the job he was paid to do.

31. I am not therefore required to consider the question of reasonable excuse and the only arguments before me are the grounds of appeal put forward by RMF as follows:

- (1) There has been a significant amount of time from the period RMF failed to comply with s66(1) Finance Act 2004. It has been 8 years since its appeal was rejected, 9 years from the date HMRC carried out their Tax Treatment Qualifying Test ("TTFT") and more than 10 years from the end of the accounting period under initial review by HMRC.
- (2) The company currently satisfies all of the requirements to be granted Gross Payment Status and has done so for the last 4 to 5 years.
- (3) If the company were to apply for Gross Payment Status now it would comply with the requirements and would be granted Gross Payment Status.
- (4) The company accepts that the outcome of the review in 2012 was technically correct, but cannot accept that to withdraw Gross Payment Status 8 years later in 2020 is appropriate.

32. Essentially RMF is asking me to consider the questions of staleness and proportionality.

33. As regards the question of staleness I would note that the main, if not the only, reason for the delay of eight years is that HMRC requested that the appeal be stayed behind *JP Whitter (Water Well Engineers) Ltd v HMRC* [2018] STC 1394, which has only recently been decided by the Supreme Court.

34. However, I can find no reference to the issue of staleness as such either in the legislation or the case law on this subject.

35. In the Supreme Court, Lord Carnwath suggested in *Whitter* that the tribunal should exercise some flexibility. In *Whitter*, at [21] and [22], Lord Carnwath said:

"21. Attractively though the appeal has been argued, I have no doubt that the Court of Appeal reached the right conclusion, substantially for the reasons they gave. Apart from the Convention, the company's submission comes down to a short point: that is,

given the existence of a discretion in section 66, it must in the absence of any specific restriction be treated as an unfettered discretion. That to my mind overlooks the basic principle that any statutory discretion must be exercised consistently with the objects and scope of the statutory scheme.

22. Like Henderson LJ, I cannot read the power as extending to matters “which do not relate, directly or indirectly, to the requirements for registration for gross payment, and to the objective of securing compliance with those requirements” (para 60). He rightly emphasised the highly prescriptive nature of the scheme. This starts with the narrowly defined conditions for registration in the first place, among which the record of compliance with the tax and other statutory requirements is a mandatory element, allowing no element of discretion. The same conditions are brought into the cancellation procedure by section 66. **The mere fact that the cancellation power is not itself mandatory is unsurprising. Some element of flexibility may be desirable in any enforcement regime to allow for cases where the failure is limited and temporary (even if not within the prescribed classes) and poses no practical threat to the objectives of the scheme.** It is wholly inconsistent with that tightly drawn scheme for there to be implied a general dispensing power such as implied by the company’s submissions.”

36. Thus Lord Carnwath undoubtedly suggested that there was room for some flexibility, in the case of a **limited and temporary** failure, but he also stated that it would be wholly inconsistent with the CIS for there to be a general dispensing power on the part of HMRC. In any case, there is already provision for some flexibility for minor non-compliance contained in Regulation 32, but the failures in this appeal did not fall within those limited exceptions. In addition I do not consider that a delay of 431 days in making a corporation tax return, together with the other failures around the same time, can constitute a limited and temporary failure.

37. I am however more persuaded by the question of proportionality.

38. In *Whitter*, at the First Tier Tribunal, the company’s appeal was successful and an important part of the FTT’s consideration was that loss of gross status would likely lead to a loss of around 60% of the company’s turnover and the dismissal of around 80% of its employees. The FTT decided that it was wrong on the part of HMRC not to take account of the likely impact on the company’s business when coming to its decision to withdraw registration, on the basis that the word “may” in s 66 gave HMRC a general unfettered discretion to take account of the impact of cancellation on the company’s business. The Upper Tribunal and The Court of Appeal took a different view, as perhaps best expressed by Henderson LJ in the decision of the Court of Appeal, where he said, at[60]:

“60. As a matter of first impression, I cannot find any indication in this tightly constructed statutory scheme that Parliament intended HMRC to have the power, and still less a duty, to take into account matters extraneous to the CIS regime, when deciding whether or not to exercise the power of cancellation in section 66(1). By ‘matters extraneous to the CIS regime’ I mean in particular, in the present context, matters which do not relate, directly or indirectly, to the requirements for registration for gross payment, and to the objective of securing compliance with those requirements. My preliminary view, therefore, is that consideration of the financial impact on the taxpayer of cancellation would fall well outside the intended scope of the power.”

39. This makes it quite clear that HMRC have no obligation, nor indeed any ability, to take into account the financial consequences of the withdrawal of gross status.



40. However, I consider that this tribunal should be able to consider whether or not the “punishment” of withdrawing gross status would be proportionate, considering the significant lapse of time since the “offence” of non-compliance was committed.

41. Following the various failures in 2011 and 2012 it has, apart from a very minor failing a few years ago, fulfilled all its obligations under the Taxes Acts.

42. The withdrawal of gross status at this time would therefore serve no useful purpose whatsoever and may even result in the commercial failure of the company, with the significant loss of jobs which that would entail. In addition, it would be able to reapply for Gross Status immediately, which, in accordance with the normal rules, would be granted. Thus the effect of withdrawing Gross Status at this time would cause additional administrative work, for both the company and HMRC, but would serve no further purpose.

43. The objective of the compliance regime for the CIS is to encourage compliance. It is not its purpose to punish non-compliance. This objective has already been achieved by the mere threat of withdrawal of gross status. The company has successfully complied with its obligations for a number of years.

44. The principle of proportionality can be derived from the long held common law concept of proportionality, as applied in the well-known case of *R v Barnsley Metropolitan Borough Council, Ex parte Hook* [1976] 1 WLR 1052, 1057. Alternatively the principle can be derived from Article 1 of the First Protocol to the European Convention on Human Rights. A1P1 of the Convention provides:

“Every natural or legal person is entitled to the peaceful enjoyment of his possessions. No one shall be deprived of his possessions except in the public interest and subject to the conditions provided for by law and by the 15 general principles of international law. The preceding provisions shall not, however, in any way impair the right of the state to enforce such laws as it deems necessary to control the use of property in accordance with the general interest or to secure the payment of taxes or other contributions or penalties.”

45. This was summarised by Lord Phillips in *Lindsay v Customs and Excise Commissioners* [2002] EWCA Civ 267, at [52]:

“...Under Article 1 of the First Protocol to the Convention such deprivation will only be justified if it is in the public interest. More specifically, the deprivation can be justified if it is ‘to secure the payment of taxes or other contributions or penalties’. The action taken must, however, strike a fair balance between the rights of the individual and the public interest. There must be a reasonable relationship of proportionality between the means employed and the aim pursued ... I would accept [counsel’s] submission that one must consider the individual case to ensure that the penalty imposed is fair. However strong the public interest, it cannot justify subjecting an individual to an interference with his fundamental rights that is unconscionable.”

46. The Upper Tribunal recently considered the question of proportionality in the case of *Barry Edwards v HMRC* [2019] UKUT 131 (TCC) at[79], where it said:

“The Upper Tribunal has previously considered the question of proportionality in the context of the VAT default surcharge regime in *HMRC v Total Technology (Engineering) Limited* [2012] UKUT 418 (TCC). In that case the Upper Tribunal referred at [11] to what Simon Brown LJ had said in *International Transport Roth GmbH v Home Secretary* [2003] QB 728 at [26], setting out the test for assessing proportionality in the context of a scheme which imposed significant penalties on lorry drivers and haulage companies

who intentionally or negligently allowed clandestine immigrant entry into the United Kingdom as follows:

“... it seems to me that ultimately one single question arises for determination by the court: is the scheme not merely harsh but plainly unfair so that, however effectively that unfairness may assist in achieving the social goal, it simply cannot be permitted? In addressing this question I for my part would recognise a wide discretion in the Secretary of State in his task of devising a suitable scheme, and a high degree of deference due by the court to Parliament when it comes to determining its legality. Our law is now replete with dicta at the very highest level commending the courts to show such deference.”

47. The question I must address therefore is whether or not the imposition of what amounts to a penalty in this case is “not merely harsh but plainly unfair”. In addition I must address this question in the context of the objectives of the CIS.

48. As I have stated above, the objective of the CIS is to ensure compliance, it is not to impose a penalty for non-compliance.

49. In my view, the withdrawal of CIS gross status over eight years after the relevant offences would be totally disproportionate. The objective of the scheme, ie, the enforcement of compliance, has been achieved by the mere threat of the withdrawal of gross status and to carry through on that threat by withdrawing gross status, when the company has been fully compliant since that time would serve no purpose whatsoever and is therefore, in my view, disproportionate.

#### **DECISION**

50. For the reasons set out above therefore I have decided that the company’s appeal should be ALLOWED.

51. 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.

**PHILIP GILLETT  
TRIBUNAL JUDGE**

**Release date: 15 January 2021**