[2016] UKFTT 0241 (TC)

TC05017

Appeal no: TC/2015/02430

Income Tax - CIS scheme liabilities and penalties - Appeal substantially allowed

FIRST-TIER TRIBUNAL

TAX

ERIC DONNITHORNE

Appellant

-and-

THE COMMISSIONERS FOR HER MAJESTY'S REVENUE AND CUSTOMS

Respondents

Tribunal: JUDGE HOWARD M. NOWLAN

DR. CHRISTINA HILL WILLIAMS DL

Sitting in public at Fox Court in Brooke Street, London on 7 January 2016

Alastair Kendrick of MHA MacIntyre Hudson and Stephen Godfrey of Godfrey Anderson & Co on behalf of the Appellant

Gill Carwardine of HMRC on behalf of the Respondents

DECISION

1. This Appeal involved an assessment on the Appellant for having failed to make deductions under the Construction Industry Scheme ("the CIS scheme") when making payments to three sub-contractors. It also involved penalties for having made no returns under that scheme.

2. The individuals to whom payments had been made without deduction, and the amount of tax that HMRC claimed should have been deducted in each case were:

Mr. ML Honey	£17,623
Mr. Gill	££2,305
Mr. Warren	£229

The penalties in issue had periodically been varied, but we believe that the final penalty amount sought, essentially for having failed to make CIS returns, was £21,000.

3. The facts were rather unusual.

4. The Appellant, who did not attend the hearing, was the Director of two nursing homes, and he wanted to ensure that various additions or improvements were made to the buildings of one nursing home. He therefore decided that he would take on the role of arranging for the construction work to be done, and it was accepted by his representative that he himself was acting as a contractor, even though he appeared not to be undertaking any of the work himself. It was accepted that he entered into the contracts with the three construction workers, and that if any of the workers had not been paid it was the Appellant who they would have sued for payment. The Appellant's representative conceded that this made the Appellant "an intermediary" for the purpose of the CIS scheme, and that he thus had a potential liability to deduct and account to HMRC for tax under the CIS scheme.

5. We are not going to question that assumption but the result was nevertheless a strange one in that, with a minor difference in form, the conclusion could well have been that there was no question of liability under the CIS scheme on anybody's part. For had the nursing home companies themselves engaged the builders, there would have been no liability on the part of those companies (not being construction companies in any sense) to make deductions on paying for building works in just the manner that there are no such liabilities when an ordinary home owner pays for some building work on his house (as in fact the present Appellant had also done). While the Appellant's present liability resulted from his having adopted the somewhat separate role of arranging for the work to be done and of contracting with the builders, we were also told that the Appellant did not take any form of commission or profit margin when arranging for the work to be done. He was therefore not carrying on a business in any sense since his role was simply to pay a certain sum to the workers and obtain reimbursement of that precise sum from the nursing home company or companies. Even more oddly we were shown all the invoices issued by Mr. Honey and they were indeed all issued to one of the nursing homes. This rather suggested that the Appellant, as a director of the company, was simply acting in his role as a director of the non-construction company that was directly receiving the building services. As we said, however, odd as we considered it to be, we accepted the premise of the Appeal, namely that the Appellant was

liable to comply with the provisions and regulations concerning payments by contractors to sub-contractors.

6. It is clear, however, that the Appellant will hardly have regarded himself as a contractor, and he will certainly not have regarded any of the three workers as his, or indeed anybody's, employees.

The relevant issues under the CIS Regulations

7. On the basis of the acceptance that the Appellant was liable to make CIS deductions from the payments made to the three workers, and that no deductions were made and accounted for, the Appellant is liable to account for the tax that should have been deducted unless either of the exemptions from that liability provided by Regulation 9(4) and 9(3) is in point.

8. Regulation 9(4) eliminates the liability of the contractor to pay the under-deducted amount if HMRC are satisfied that there has been no loss of tax. To date, HMRC have not expressed themselves to be satisfied that there has been no loss of tax, and furthermore no appeal lies to this Tribunal to examine that issue. It was mentioned during the hearing, however, that certainly in the case of the payments made to Mr. Honey, there had been no loss of tax because all the tax in respect of the payments from the Appellant and all the tax in the relevant periods had been paid. There had been a non-payment of tax in respect of some other period but we were informed that the result of a bankruptcy hearing was that that liability had been discharged, with the result that all tax properly owed by Mr. Honey had indeed been paid.

9. While we appreciate that we have no jurisdiction in relation to the saving provision in paragraph 9(4), the Respondents' representative conceded that some of the facts just mentioned had not been appreciated and that HMRC would be perfectly happy to revisit the issue of "loss of tax". The sensible course would appear to be for the Appellant's representative to furnish to HMRC the information briefly mentioned in the previous paragraphs so that HMRC can re-consider the issue.

10. The second saving provision from the liability of the contractor to make a payment to HMRC of the hitherto under-deducted tax is contained in Regulation 9(3). This provides that:

> *"[The contractor shall not be liable for the under-deducted tax if] the contractor satisfies an officer of HMRC:*
>
> > *(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."*

11. During the hearing we had not seen the documents that had in fact been supplied to the Tribunal and we were told that it was unnecessary to read the Appellant's witness statement. We were certainly given the impression that the Appellant had been totally and honestly

unaware of any potential liability to deduct tax under the CIS regulations, and indeed that he thought that Mr. Honey, and probably Mr. Gill as well, had paid or would be paying tax on their net profits. Our initial conclusion, therefore, was that the Appellant's mistake in not deducting tax had plainly been an honest mistake and a very understandable one, particularly in the light of the points made in paragraphs 5 and 6 above, but as a pure matter of interpretation we found it difficult to conclude that the Appellant could be said to have taken reasonable care to comply with section 61 and these Regulations (so as to satisfy paragraph (a) of Regulation 9(3)) if the Appellant had been totally unaware of the CIS regulations. We accordingly concluded that we could not decide that the Appellant's liability was nullified by Regulation 9(3), though this was certainly an odd conclusion when the Appellant had first honestly known nothing about the Regulations, and secondly had understood that Mr. Honey at least would be properly paying his tax.

12. On subsequently reading the Appellant's witness statement, however, we see that he said the following:

> *"We agreed terms and method of payment for the work to be undertaken. Mr. Honey told me that he was self-employed and registered with the Inland Revenue. As a result of that it never occurred to me that I would have to make deductions from the payments that I would be making to him."*

13. The extract just quoted certainly stops short of suggesting that the Appellant specifically considered compliance with section 61 and the Regulations, and it does not specifically say that he considered anything about any obligation to deduct tax at source, other than the implicit reference to the fact that as the Appellant had been told that Mr. Honey was self-employed he would have no obligation to deduct tax under the PAYE Regulations. We are also unclear as to what the Appellant meant by referring to Mr. Honey being "registered with HMRC", and we suspect that he simply meant that he understood Mr. Honey to be making his own self-assessment tax returns and paying his tax, rather than that the registration implied the right for a contractor to make gross payments to him under the CIS legislation.

14. While there was no suggestion that the Appellant did actually consider the obligation to deduct tax under the CIS machinery, we are still struck by the statement, that we fully accept, that it simply did not occur to the Appellant that he would have a liability to deduct tax on any other basis, once he had concluded that PAYE obligations were not in point. He expressly said that it never occurred to him that he would have to make deductions from the payments to Mr. Honey. Similarly (as we quote in paragraph 16 below when referring to the payments to Mr. Gill), he said that he regarded Mr. Gill as being *"registered with the Inland Revenue and so [he] felt that [he] did not need to make any deductions from him."* When it is inevitably the case, when seeking to apply Regulation 9(3)(a) that there will have been a failure to deduct tax, and an honest failure to deduct tax, we consider it reasonable to conclude in this case that there was no "want of reasonable care" on the part of the Appellant in failing to comply with the CIS Regulations. We reach this conclusion on the four grounds that:

- it was entirely understandable that the Appellant, having considered and correctly rejected the issue of deducting tax under the PAYE Regulations, should have failed to note any other potential obligation to deduct tax at source, when the Appellant's technical status as a "contractor" was far from intuitive;
- it is also appropriate to test the required level of "reasonable care" by considering whether the payer was a trader (generally a trader in the construction industry) that must have been, or certainly ought to have been, fully aware of the CIS Regulations, or whether the payer was someone who would have been most unlikely ever to have heard of them;
- the previous point is particularly compelling in the light of the points made in paragraphs 5 and 6 above that indicate that it is only by accident that the Appellant may have been liable to deduct CIS tax at all, if indeed it was indeed right to assume that he was technically liable to do so; and
- finally, we do accept the Appellant's claim that his reference to Mr. Honey's self-employed status and that of registration with the Inland Revenue, left him oblivious to any other obligation to deduct tax.

15. As a result of the points made in the previous paragraph we decide that on the unusual facts of this case, there was no want of reasonable care on the part of the Appellant in relation to any obligation to deduct tax at source from payments made. The Appellant then unquestionably satisfied both limbs of Regulation 9(3)(b), and we accordingly decide that Regulation 9(3) is satisfied in this case and that the Appellant's liability to account now for CIS payments is discharged in relation to the payments made to Mr. Honey.

16. Very little attention was given in the hearing to the payments made to the other two workers. We were also told that, *"as an act of good faith"*, the Appellant had paid £3,859, perhaps reflecting the tax and interest payable in respect of the other two workers. He did say however that in a similar manner he regarded Mr. Gill as being *"registered with the Inland Revenue and so I felt that I did not need to make any deductions from him."* We do not know whether Mr. Gill also paid his tax, but our decision is that essentially the same declaration made in relation to the payments to Mr. Gill should result in the elimination of the Appellant's CIS liability in respect of those payments.

17. Only a minor amount was paid to the third worker and the witness statement made no mention of that payment, or of whether the Appellant considered that Mr. Warren was also *"registered with the Inland Revenue"*. We therefore make no finding or decision in relation to the small payment to Mr. Warren.

The penalty

18. In view of the manifest honesty on the part of the Appellant, all parties were effectively in agreement that the penalties should be quashed, quite apart from the outcome of the substantive point in relation to the non-deductions and the failure to make CIS returns. We were invited to conclude within paragraph 16 of Schedule 55 to the Finance Act 2009 that in view of the special circumstances in this case, the liability for penalties should be entirely eliminated. That is our decision.

Right of Appeal

19. This document contains full findings of fact and the reasons for our decision in relation to each appeal. Any party dissatisfied with the decision relevant to it 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.

HOWARD M. NOWLAN

TRIBUNAL JUDGE

RELEASE DATE: 7 APRIL 2016