Keeping it in proportion

In a FTT case, the Tribunal found that withdrawal of gross payment status from a construction firm was a 'disproportionate' response by HMRC. Robin Williamson explains all

In an interesting First-tier Tribunal case, a judge has found that HMRC's action in withdrawing gross payment status from a construction company eight years after its offence, when it had been compliant for at least the past four or five years, was disproportionate.

The law on gross payment status

Under FA 2004, s 66, HMRC may cancel a person's gross payment registration under the construction industry scheme (CIS) if (among other things) they have made an incorrect return or provided incorrect information or failed to comply with one of the many tax obligations listed in Schedule 11 to that Act and in various regulations. It must also appear to HMRC that an application for gross payment registration would be refused if made at that time.

If the person has a reasonable excuse for the failure, they may be treated as still compliant, provided they remedy the failure without unreasonable delay once the excuse has ceased. Otherwise, the person has 30 days in which to appeal and the effect of cancellation is suspended until the appeal is concluded. The person may not re-apply for gross payment registration again until one year has elapsed since the effective date of the cancellation.

The facts of the RMF case

The case I am considering here is RMF Construction Services Ltd v HMRC [2021] UKFTT 9 (TC), decided in November 2020.

RMF Construction Services Ltd (RMF) had been trading since 1 August 2000. In September 2011, HMRC carried out a Tax Treatment Qualifying Test (TTQT) to determine whether the company had met all its tax obligations in the past year. It emerged that the company's corporation tax return due on 31 July 2011 had not yet been filed, its contractor's returns for May and July 2011 were, respectively, one month and two-and-a-half months late, and there were five other compliance failures including non-filing of the P35 due for the year ended 5 April 2012.

HMRC accepted the company had a reasonable excuse for the late filing of its contractor's returns but not for the other failures, and withdrew the company's gross payment status. The company appealed, but HMRC rejected its appeal because the corporation tax return was still outstanding (it was eventually filed 14 months after it was due). The company requested an internal review, which upheld the withdrawal of gross payment status on the grounds that the compliance failures were not one-off and there was reason to doubt that the company would meet its tax obligations in the future.

The result in JP Whitter

The company appealed to the tribunal, which directed that the appeal be stood behind another case, JP Whitter (Waterwell Engineers) Ltd v HMRC [2018] UKSC 31. In that case, the taxpayer company, having breached various compliance obligations without reasonable

excuse, was appealing against the withdrawal of its gross payment status on the grounds that HMRC had not taken into account the likely effect of that sanction on the company's business. It also relied in its appeal on the European Convention on Human Rights, Article 1 of Protocol 1 (A1P1) (right to peaceful enjoyment of possessions).

The Whitter case was appealed to the First-tier Tribunal, and thence to the Upper Tribunal and the Court of Appeal, and finally to the Supreme Court. Argument revolved around the scope of HMRC's discretion whether to withdraw gross payment registration, based on the use of the word 'may' rather than 'must' in s 66: was the discretion unfettered, or was it limited to matters which related, directly or indirectly, to the requirements for registration for gross payment?

If the former, the company argued that HMRC should have taken account of the financial effect of withdrawal of gross payment status on the company, in that it would lose 60% of its turnover and 80% of its employees.

The company's argument found favour in the First-tier Tribunal but not in the Upper Tribunal or the Court of Appeal. When the case finally reached the Supreme Court, the company's appeal was dismissed on the grounds that the discretion was not unfettered, it was limited and must be exercised consistently with the objects and scope of the CIS. The financial effect upon the appellant was irrelevant and HMRC had no power to take it into account when deciding whether to withdraw gross payment status. As for the human rights ground of appeal, the court held that any interference with the enjoyment of possessions was proportionate and came within the wide margin of appreciation allowed to the State for the enforcement of tax.

The grounds of appeal in RMF

Once JP Whitter was decided, HMRC confirmed the withdrawal of RMF's gross payment registration, even though eight years had now passed since its original appeal and the company had been fully compliant for at least the last four to five years.

The company accepted that the TTQT in 2012 was technically correct, but could not accept that to withdraw gross payment status eight years later, in 2020, was appropriate as the lapse of time was too great. In addition, if it were to apply for gross payment status now, it would succeed as it would comply with all the requirements.

The decision in RMF

The tribunal (Judge Philip Gillett) allowed the taxpayer company's appeal because the withdrawal of CIS gross payment status eight years after the original offence would be disproportionate. The objective of the CIS as a whole was to ensure compliance, not to impose a penalty for non-compliance. That objective (ensuring compliance) was achieved by the mere threat of withdrawal of gross payment status, and to carry out that threat when the company had been fully compliant since that time would serve no purpose whatsoever and would therefore be disproportionate.

Proportionality

The judgment contains some interesting reflections on proportionality with some pertinent quotations from earlier judgments.

Proportionality as a legal concept exists in both English common law (R v Barnsley Metropolitan Borough Council, ex parte Hook [1976] 1 WLR 1052, 1057) and in human rights jurisprudence. In the latter case, it stems from A1P1 (see above) which protects the right to peaceful enjoyment of property but allows the State to interfere with that right if such interference is in the public interest or is 'to secure the payment of taxes or other contributions or penalties'. As Lord Phillips observed in Lindsay v Customs and Excise Commissioners [2002] EWCA Civ 267, at [52], the State's interference must: "strike a fair balance between the rights of the individual and the public interest. There must be a reasonable relationship of proportionality [my italics] between the means employed and the aim pursued…"

Or as Simon Brown LJ put it in International Transport Roth GmbH v Home Secretary [2003] QB 728 at [26] (cited in the recent Upper Tribunal case of Barry Edwards v HMRC [2019] UKUT 131 (TCC) at [79]): "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?"

That question – whether HMRC's action in withdrawing gross payment status from RMF was not merely harsh but plainly unfair – was what the judge had in mind when finding it to be disproportionate.

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