TC02042

Appeal number TC/2010/07760

Contract of employment or contract for services – no written terms - notice under section 8 of the Social Security Contributions (Transfer of Functions etc) Act 1999 - determination under regulation 80 of the Income Tax (Pay As You Earn) Regulations 2003 - appeals allowed

FIRST-TIER TRIBUNAL
TAX CHAMBER

SLUSH PUPPIE LIMITED

Appellant

- and -

THE COMMISSIONERS FOR HER MAJESTY'S REVENUE AND CUSTOMS **First Respondents**

ROSS SANDFORD

Second Respondent

TRIBUNAL: Judge Malachy Cornwell-Kelly
Mrs Shawar Sadeque

Sitting in public at 45 Bedford Square London on 26 & 27 April 2012

Ms Nicola Smith of Accountax Consulting for the Appellant

Ms Karen Weare of HMRC for the Crown
The second Respondent appeared in person

DECISION

Introduction

1 These are appeals against:-

(i) a notice under section 8 of the Social Security Contributions (Transfer of Functions etc) Act 1999 issued to Slush Puppie Limited ('SPL') on 28 May 2010 that the second respondent, Mr Ross Sandford, was an 'employed earner' of theirs for the period 6 April 2002 to 5 April 2007, and that the total amount due from the company in that regard for primary and Class 1 contributions in respect of that employment is £32,312.23;

(ii) a determination under regulation 80 of the Income Tax (Pay As You Earn) Regulations 2003 issued to SPL in respect of income tax due pursuant to Mr Sandford's employment for the year 2006-07 amounting to £6,309.

2 We heard oral evidence from SPL's managing director, Mr Mark Peters and from Mr Steve Coyne, their Service Supplier Manager, and from Mr Sandford on behalf of the Crown. We regarded all three witnesses as honest. In addition, we had two substantial bundles of agreed documentation, including signed notes of HMRC interviews with Mr Sandford. On the basis of this evidence, we find the following facts established at least on the balance of probability, except where it is explicitly stated to the contrary.

Legislation

3 Section 2(1) of the Social Security Contributions and Benefits Act 1992 defines 'employed earner' and 'self-employed earner' as follows:-

> *2 Categories of earners*
>
> (1) In this Part of this Act and Parts II to V below—
>
> (a) "employed earner" means a person who is gainfully employed in Great Britain either under a contract of service, or in an office (including elective office) with general earnings; and
>
> (b) "self-employed earner" means a person who is gainfully employed in Great Britain otherwise than in employed earner's employment (whether or not he is also employed in such employment).

4 Regulation 80 of the Income Tax (Pay As You Earn) Regulations 2003 provides:-

> *80 Determination of unpaid tax*
>
> (1) This regulation applies if it appears to the Inland Revenue that there may be tax payable for a tax year under regulation 68 by an employer which neither has been-
>
> (a) paid to the Inland Revenue, nor
>
> (b) certified by the Inland Revenue under regulation 76, 77, 78 or 79.
>
> (2) The Inland Revenue may determine the amount of that tax to the best of their judgment and serve notice of their determination on the employer.

Facts

5 'Slush Puppies' are a type of non-alcoholic drink made from crushed ice to which flavours have been added. Mr Sandford and members of his family were directors and shareholders of a family company in Lanarkshire, Scotland, called Cambusnethan Confectionary Company Limited ('CCC'). The family relationship between those who owned SPL and those who owned CCC went back many years and, since the 1980s, CCC had held appointment as a Slush Puppie distributor for part of Scotland.

6 In 2001, CCC agreed with SPL to sell the distributorship business to it. A draft sale agreement exists but, surprisingly, neither side can produce the final version even though there was significant negotiation over it. It was clear, however, that SPL wanted to keep the business running under their new ownership and that they wished the transition to be as smooth as possible, both because of the longstanding family relationship and for obvious commercial reasons as well.

7 We find that the sale agreement was originally intended as an asset sale which transferred CCC's physical assets and intellectual property rights to SPL, for a consideration consisting of payments over five years from the profits of the business so purchased. Those profits were to be paid to CCC, of which Mr Sandford was to remain a shareholder; and he himself would therefore share an interest in the successful outworking of the sale. The draft agreement in evidence did not provide for CCC's employees to go over with the assets, but in the event that is what in fact happened as SPL wanted the takeover to work for everyone and made every effort to find each person a job. All the staff became employees of SPL except for Mr Sandford.

8 A reason for this was that SPL's service engineers of Mr Sandford's type were all self-employed and Mr Sandford accepted that that was the way in which he could continue to work with the business, though he claimed that his preference was to have been taken on as an employee. There was a conflict of evidence over whether Mr Sandford had wanted to be an employee, but had had to accept self-employment (his account), or whether he had always wanted to be self-employed (SPL's understanding).

9 The contemporary documentation, SPL's clear desire to be as accommodating as possible in the transition, and the fact that they did have employed engineers doing work overlapping with Mr Sandford's, lead us to conclude that, whatever he had started out as wanting, self-employed status was something that Mr Sandford was ultimately willing to agree to and did agree to. Despite promises of a formal agreement defining his status, no formal contract was ever drawn up and Mr Sandford settled down to working ostensibly as a self-employed service supplier maintaining the equipment, principally freezers, used by what were by then SPL's distributors.

10 Mr Sandford's agreed daily rate was £120, while other self-employed service suppliers like him only got £80, but the higher rate reflected the terms of the sale negotiations and the fact that the area covered by Mr Sandford in Scotland was particularly extensive. (SPL's *employed* service technicians were paid an annual salary which equated to an average 'daily rate' of £67.94.) In addition, Mr Sandford had enjoyed health insurance and pension benefits from CCC, and SPL agreed to pay him a monthly 'consultancy fee' of £236.58 plus VAT to reimburse CCC the cost of

continuing that cover. That description was chosen by SPL in order to conceal from their other service suppliers that Mr Sandford was getting a benefit that they were not getting.

11 Mr Sandford's actual conditions of work were as follows:-

- an unincorporated consultancy business called Keyakin Mhor Consulting was set up by Mr Sandford and he invoiced SPL for the agreed daily rate and his monthly 'consultancy fee'; there was inconsistency in the delays before Mr Sandford's invoices were paid, and SPL's liability to pay was shown as 'debtors payable' in the accounts;

- the business was registered for VAT and made income tax returns as such, claiming for capital allowances, office furniture and equipment expenses annually of between £7,500 and £9,000, public liability insurance, accountancy fees and the cost of a bank overdraft; no office-type facilities were available to Mr Sandford on SPL's premises;

- SPL was in practice the business's only customer – some very minimal printing work on the menus for Burn's Suppers, worth about £60 a year, was the only other business undertaken and Mr Sandford's business stationery showed SPL's mobile phone number and an SPL email address;

- by means of a hand held computer supplied by SPL, jobs needing Mr Sandford's type of skill were offered to SPL's service providers, who were all treated as independent service providers; the offers of work were then either accepted or rejected by them;

- Mr Sandford accepted the offers of work within his area if it was possible to undertake the work, given the distance that might be involved in getting to the place where the work was to be done, and he would only reject jobs otherwise if they were out of his area – though on occasion he would do such jobs on special terms if no-one else could be found, or quote *ad hoc* for unusual types of work such as decommissioning old equipment;

- the process of offering jobs to service providers was computerised and involved ordinarily little or no human intervention on the part of SPL, so that if the nearest service provider rejected the offer of a job it would automatically be offered to another, and SPL could not oblige a supplier to take a job on;

- if a job was particularly urgent, the service supplier offered it would be told so and urged to give it priority but, if he could not do so, it would go elsewhere;

- there was no correlation between the number of jobs done each day by Mr Sandford and his daily rate, which was always the same and, while the expectation was that they would offer work, SPL undertook no specific obligation to do so;

- in practice, the relationship was driven by Mr Sandford having (i) for the five years after 2001, a share of the profits generated by the business sold to SPL by virtue of his being a continuing shareholder in CCC, (ii) an interest in keeping the distribution equipment operational, and also (iii) by his need for the income;

- on SPL's side, the relationship was driven by their having an interest in using Mr Sandford's services to keep their new distributorships running smoothly, since he was skilled and experienced at the work, knew the equipment and would ensure that it was kept in working order;

- but, although both parties hoped it would last, the relationship was essentially precarious, based on an oral contract and there was no prescribed period of notice to terminate it; when it suited Mr Sandford to terminate the agreement, he gave just a week's notice, though there is nothing to suggest that he was obliged to give even that much; by contrast, acknowledged employees of SPL, such as Mr Sandford's brother Peter on the sales side, were required to give, and did give, one month's notice;

- typically, a day would see three or four jobs done, or work performed at SPL's depot at Broxburn, with a working day of eight or more hours, and there was never a day – agreed holidays or sickness excepted - without some business for Mr Sandford from SPL;

- Mr Sandford was free, having accepted a job, to find someone else to do it, though in fact he did not take advantage of that opportunity – for their part, as long as the job was done and there were no complaints from SPL's distributor, SPL neither knew nor cared who had individually carried out the work, and any faults in the work reported by customers had to be remedied at Mr Sandford's own cost;

- although in principle Mr Sandford was free to undertake similar work for other customers, it was not practicable for him to do so in view of his actual commitment to SPL's jobs, and he did not do so; Mr Sandford did, however, help with his wife's catering business in the evenings and at weekends;

- a 'uniform', which usually consisted simply of a shirt or T-shirt with SPL's logo, was issued to and in principle worn by its service suppliers, especially when visiting customers such as schools where identification of the person visiting was important to the customer, and for similar reasons Mr Sandford - as all service providers - carried an SPL business card;

- supervision or control by SPL over Mr Sandford's work was restricted to ensuring compliance with public law obligations, such as the requirements of health and safety law, and his work would only be queried if an SPL customer had complained about it; there was no day to day supervision;

- initially a car, and later a van, was supplied by SPL for Mr Sandford's use, neither having SPL's logo; save when he went out of his area, or when covering for an employed engineer, Mr Sandford paid for fuel and insurance[1] and, on one occasion, the repair of the car; when Mr Sandford was given the van it was, however, serviced by SPL;

[1] The van was insured by SPL who then invoiced Mr Sandford.

- the vehicles were fitted with trackers to identify the service provider closest to the SPL customer needing help;

- holidays were unpaid, but the dates of them had to be cleared with SPL to avoid periods when their employed area operators or service engineers in Scotland were away; but, if he had insisted on it, Mr Sandford could have taken his holidays when he wished – albeit with the possibility of souring his relationship with SPL;

- service providers and employed engineers alike were asked to report unavailability due to sickness by 9 am on the day in question, so that alternative dispositions might be put in place for work that they had been expected to be able to do;

- Mr Sandford had no pension or health benefits, save of course for the "consultancy fee" designed to enable him to continue to pay for the benefits he had had with CCC; in contrast, SPL's corps of area operators and service engineers, who had overlapping but distinct r□les in the company and were formally employees, did enjoy these benefits;

- out of pocket expenses such as parking charges, phone calls, weekend availability or overnight hotel costs were reimbursed by SPL, often at a flat rate;

- in principle, Mr Sandford used his own tools and equipment, but equipment such as that for an installation which he did not have would be made available to him by SPL, or if more parts were needed for the job and were purchased by Mr Sandford, he would be reimbursed by SPL;

- where the use of SPL's equipment was concerned, service suppliers were invited to training sessions but, though in practical terms there might be little alternative to doing so, they were not obliged to attend them and they would simply not be offered jobs involving such equipment if they did not attend;

- Mr Sandford did attend the service meetings organised by SPL, but was not strictly obliged to do so, and he did on occasion provide *ad hoc* training to other service providers or SPL staff, and SPL disseminated technical information to service providers relevant to the various SPL machines they would encounter;

- SPL provided Mr Sandford, as other service providers, with a mobile phone for work purposes and asked them to keep it on at all times so that SPL could make contact whenever necessary; SPL sought to protect their customer base by retaining ownership and control of the phone.

12 All continued on that basis for five years until Mr Sandford announced to SPL in a letter dated 29 March 2007 that he would no longer be able to work for them, that he would be finishing on 6 April, and that he would leave his van at a nearby depot. The five years during which CCC derived a share of the profits of the business that they had sold to SPL had now expired, and it transpired that a company called Cambusnethan Slush Limited had been incorporated on 2 February 2007 with Mr Sandford as the company's secretary and a director.

13 The suggestion that Mr Sandford was in reality employed rather than self-employed emerged in a letter dated 26 June 2007 from Mr Sandford's tax agents to HMRC in which they noted that, although their client had stated that he was self-employed,[2] their opinion was to the contrary and they sought a refund of income tax he had accounted for under self-assessment, and suggested that SPL was liable to pay it instead. In response to this, HMRC interviewed Mr Sandford by telephone on 23 July 2007 addressing detailed questions to him, and a formal Opinion was issued by HMRC on 29 August 2007 in favour of employment status.

14 A meeting was then held with SPL on 19 & 20 February 2008 followed by detailed correspondence between SPL, HMRC and Mr Sandford, again attempting to resolve the issue. A further meeting was held on 7 October 2008 at which more detailed questioning was undertaken by HMRC. On 1 December 2008, an official at HMRC informed SPL -

> I have now concluded my enquiries into the employment status of Ross Sandford and based on the enquiries I have made I am unable to give an opinion at this time; it is therefore my intention not to disturb matters with regard to Mr Sandford's engagement by Slush Puppie Limited . . . I am now pleased to confirm my Compliance Check has now been concluded and I thank you for your co-operation throughout.

15 Mr Sandford's agents, to whom this had been copied, refused to accept this conclusion, and HMRC reluctantly accepted that the matter would have to be resolved "independently" and that formal assessments would have to be raised, allowing both parties to put their case to what they referred to as an "independent body".

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[2] Mr Sandford's witness statement dated 20 March 2012 presented to the tribunal begins "I was a self-employed engineer working solely for Slush Puppie Limited".

16 SPL expressed considerable surprise that HMRC, having given a final ruling in favour of self-employment after lengthy investigation, it should be possible for Mr Sandford to re-open the matter all over again. SPL also said that they were puzzled why Mr Sandford, having no doubt returned his income on the basis of self-employment, had now changed his mind and claimed that he was employed: HMRC replied that "because of confidentiality issues" they were unable to comment. Yet further work was then begun by HMRC officers to prepare for this appeal.

17 On 25 September 2009, Mr Sandford's agents formally applied for the income tax he had paid "in error" by reason of self-employment to be refunded, and stated that he would not agree to any offset of income tax he had paid against PAYE deductions that SPL should (they said) have made from his salary.

The case law

18 From the very extensive case law on this subject, we must extract the main principles which determine the nature of a relationship of the kind under appeal. In doing so, we start with the warning given by Nolan LJ in *Hall v Lorimer* [1994] 1 All ER 250, at 257, adopting the words of Mummery J in the court below, that:-

> In order to decide whether a person carries on business on his own account, it is necessary to consider many aspects of that person's work activity. This is not a mechanical exercise of running through items on a checklist to see whether they are present in or absent from a given situation. The object of the exercise is to paint a picture from the accumulation of detail. The overall effect can only be appreciated by standing back from the detailed picture which has been painted, by viewing it from a distance and by making an informed, considered, qualitative appreciation of the whole.

> It is a matter of evaluation of the overall effect of the detail, which is not necessarily the same as the sum total of the individual details. Not all details are of equal weight or importance in any given situation. The details may also vary in importance from one situation to another.

19 The correct approach to employment status was spelt out by Peter Gibson LJ in the case of *Express & Echo Publications Ltd v Tanton* [1999] IRLR 367, at [21]-[23], as follows:

> (1) The tribunal should establish what were the terms of the agreement between the parties. That is a question of fact.
>
> (2) The tribunal should then consider whether any of the terms of the contract are inherently inconsistent with the existence of a contract of employment. That is plainly a question of law, and although this court, as indeed the Employment Appeal Tribunal before us, has no power to interfere with findings of fact (an appeal only lies on a point of law), if there were a term of the contract inherently inconsistent with a contract of employment and that has not been recognised by the tribunal's chairman, that would be a point of law on which this court, like the Employment Appeal Tribunal before us, would be entitled to interfere with the conclusion of the chairman.
>
> (3) If there are no such inherently inconsistent terms, the tribunal should determine whether the contract is a contract of service or a contract for services, having regard to all the terms. That is a mixed question of law and fact.

20 We turn to the various criteria which the authorities have treated as significant or determinative.

Personal service

21 The requirement that services must be performed personally has been seen as a characteristic of the employment relationship, and if it is not present the relationship will not be one of employer/employee: per Peter Gibson LJ in *Express Echo* at [31]; and the right to send a substitute to perform services, whether or not it is exercised, is inconsistent with employment: per Peter Gibson LJ in *Express Echo* at [25]. While freedom to perform work for another during the period of the engagement is not inconsistent with employee status (per Cooke J in *Market Investigations Ltd v. Minister of Social Security* [1968] 3 All ER 732, at 739), a personal service requirement is one of the three fundamentals of employment recognised in *Ready Mixed Concrete (South East) Limited v. Minister of Pensions and National Insurance* [1968] 1 All ER 433: by MacKenna J at 439-440:

> A contract of service exists if the following three conditions are fulfilled: (i) The servant agrees that in consideration of a wage or other remuneration he will provide his own work and skill in the performance of some services for his master. (ii) He agrees, expressly or impliedly, that in the performance of that service he will be subject to the other's control in a sufficient degree to make that other master. (iii) The other provisions of the contract are consistent with its being a contract of service.

Mutuality of obligation & Control

22 Mutuality does not require the employer to provide the employee with work <u>in addition</u> to wages: per Stephenson LJ in *Nethermere (St Neots) v. Taverna* [1984] IRLR 240, at 246, but an obligation on the employer to provide work, or in the absence of available work to pay, is a touchstone or feature one would expect to find in an employment contract and whose absence would call into question the existence of such a relationship.

23 In *Propertycare Limited v Gower*[2004] All ER (D) 16 Jan, the Employment Appeal Tribunal observed, at 9(3):-

> The cases, starting with *Ready Mixed Concrete*, show that mutuality of obligation means more than a simple obligation on the employer to pay for work done; there must generally be an obligation on the employer to provide work and the employee to do the work.

24 And in *Montgomery v Johnson Underwood* [2001] IRLR 269, Longmore LJ noted, at [46], that:-

> Whatever other developments this branch of the law may have seen over the years, mutuality of obligation and the requirement of control on the part of the potential employer are the irreducible minimum for the existence of a contract of employment.

25 The right of control is a necessary though not always a sufficient condition of a contract of service, and in classifying the contract other matters besides control may be taken into account and it is not the sole determining factor: per MacKenna J in *Ready Mixed Concrete*, at 516. Indeed, where a professional worker is concerned, the lack of control over the manner in which the work is done may be neutral in determining employment status: per Lord Parker CJ in *Morren v Swinton & Pendlebury Borough Council* [1965] 2 All ER 349, at 351.

Business on own account

26 Among the factors relevant here are whether the service provider provides his own equipment or hires his own helpers, what degree of financial risk he takes, what degree of responsibility for investment and management he has, whether and how far he has an opportunity of

profiting from sound management in the performance of his task and whether the business he has is already established: per Cooke J in *Market Investigations*, at 738. But the risk of bad debts and outstanding invoices is not normally associated with employment: per Nolan LJ in *Hall v. Lorimer,* at 258.

Intention of the parties

27 A statement of the parties' disavowing any intention to create a relationship of employment cannot prevail over the true legal effect of the agreement between them, but in a borderline case a statement of the parties' intention may be taken into account and may tip the balance one way or the other. In *Massey v Crown Life Insurance Co* [1978] 2 All ER 576, Lord Denning MR, at 580, observed:

> It seems to me on the authorities that, when it is a situation which is in doubt or which is ambiguous, so that it can be brought under one relationship or the other, it is open to the parties by agreement to stipulate what the legal situation between them shall be. That was said in *Ready Mixed Concrete* in 1968 by MacKenna J. He said:
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> > If it were doubtful what rights and duties the parties wished to provide for, a declaration of this kind might help in resolving the doubt and fixing them in the sense required to give effect to that intention.
>
> So the way in which they draw up their agreement and express it may be a very important factor in defining what the true relation was between them. If they declare that he was self-employed that may be decisive.

Conclusions

28 Overall, the relationship between Mr Sandford and SPL, which was the subject of an oral contract of which we have determined the essential features, seems to us to have been essentially flexible and pragmatic. The picture is that of Mr Sandford wanting the work, and wanting his share of the profits of SPL's running of the business it had bought to flow through to him *via* his continued shareholding in CCC; of SPL not wanting to waste Mr Sandford's technical and managerial skill, and local knowledge, derived from CCC's previous distributorship, and wanting to treat the members of the Sandford family well in view of the long family connection. That neither side insisted on having a written contract is a further pointer to the essentially *ad hoc* nature of the relationship. **

29 In this context, both Mr Sandford and SPL intended that, in his particular case, the transition would take the form of self-employment as a service provider to SPL, on terms as to payment and benefits which were very much more favourable to Mr Sandford than they were to the other service providers. Mr Sandford was well accomplished in his work, and he was trusted to ensure that jobs were carried out, whether by him or by another, and asked to offer *ad hoc* training to engineers; matters could safely be left in his hands, and he neither needed nor received supervision.

30 Naturally, Mr Sandford worked closely with SPL's systems and routines, and it would hardly have served his purpose to do otherwise. And the fact of attending service meetings, or working generally in close cooperation with SPL, does not show that Mr Sandford was an integral part of that organisation in the sense in which employees were.

31 The circumstances of his financial and organisational independence of SPL point strongly away from employment. That Mr Sandford chose not to undertake any other business during the five years from the sale by CCC is clearly attributable to his financial interest in profiting from the sale being a success; immediately when that ceased to be the case, he was quick enough to move into the same type of activity through the setting up of Cambusnethan Slush Limited. The relationship lasted exactly as long as it was profitable for Mr Sandford for it to last, and no longer.

32 In terms of mutuality, the evidence indicates that there was no obligation on either side beyond the day on which work was undertaken, and no pay and no work went together. A daily rate, together with the system for acceptance or rejection of work, is a strong indicator that matters were based on daily contract.

33 That this continued for five years together in the same pattern, and the practical convenience of monthly invoicing, are factors which do not detract from the conclusion that flexible self-employment was the relationship that both parties intended to create when the initial negotiations reached a conclusion. There is no contemporary hint of any contrary intention on Mr Sandford's part while the relationship lasted; when it ended, it is significant that the issue was only raised on the advice of tax agents seeking, in an area of the law well-known for its openness to argument, their client's financial benefit.[3]

[3] This is no criticism of the agents in putting forward an arguable case on behalf of their client, which is their professional obligation if so instructed.

34 Did Mr Sandford's business involve any significant financial risk? Clearly, the risk that SPL might for their own reasons dispense with his services without any of the protections of employment law, insolvency law or redundancy rights being available to him, was one that Mr Sandford was vulnerable to throughout. The risk that his invoices might not be paid promptly, or at all, is reflected in the overdraft facility which Mr Sandford had with his bank and the irregularity with which they were in fact paid.

35 That no substantial risks materialised in the course of five years is no indication that they did not exist potentially. There was no evidence that the sale to SPL of CCC's business contained any non-competition clauses: both parties knew that, and without any formal contract Mr Sandford took his chance that SPL would take the initiative - which he himself in the event took in 2007 - to part company, and leave him with no alternative but to ply his trade elsewhere. SPL took the corresponding risk that Mr Sandford would, as in due course he did, set up in competition with them.

36 It is true that the outward appearances of Mr Sandford's business made it seem to SPL's customers as though they were dealing with SPL itself. The wearing of a 'uniform', the type of business card used and the telephone numbers and email address on the stationery used by Keyakin Mhor Consulting, all combined to reassure customers that Mr Sandford was 'an SPL man', and that SPL vouched for him. That SPL held Mr Sandford out as one of theirs was the important thing for customer confidence, but it is not decisive of Mr Sandford's status.

37 For these reasons, we find that Mr Sandford was not an employed earner and was self-employed. We accordingly allow the First Respondents' appeals against the section 8 notices and the regulation 80 determination.

Further appeal rights

38 This document contains the 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 no 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.

Malachy Cornwell-Kelly
Tribunal Judge

RELEASE DATE: 25 May 2012