TC06907

Appeal number: TC/2017/07632

Income Tax and National Insurance Contributions – whether payments from an office, a contract of service or a contract for services keywords – appeal dismissed

FIRST-TIER TRIBUNAL
TAX CHAMBER

PETROL SERVICES LIMITED **Appellant**

- and -

THE COMMISSIONERS FOR HER MAJESTY'S REVENUE & CUSTOMS **Respondents**

TRIBUNAL: JUDGE GETHING
Mr John Agboola

Sitting in public at Birmingham Employment Tribunal, Tax, Centre City Tower 5-7 Hill Street, Birmingham, West Midlands, B5 4UU on Monday 5 November 2018

Mr Dougal Powrie of Kibworth tax Services Limited, for the Appellant

Mr Martin Priestly Presenting Officer of HM Revenue and Customs, for the Respondents

DECISION

1. The issue in this case is whether Petrol Services Limited (**"the Appellant"**) is liable to pay income tax under the PAYE system and employee and employer national insurance contributions (Primary and Secondary Class 1 Contributions (**"the NICs)**) on payments made by the Appellant to a company and a partnership (which I refer to as the consultancy vehicles) in circumstances where:

(1) the Appellant had no staff, officers or employees other than the two directors, Mr Odedra and Mr Badiani ("the Directors").

(2) Each of the Directors was named as a consultant alongside his consultancy vehicle under a contract entered into with the Appellant in 1999.

(3) The directors actually carried out all the activities necessary to conduct the Appellant's business.

2. For the tax years ending 5 April 2012 to 2015 determinations were issued under Regulation 80 of The Income Tax (Pay as You Earn) Regulations SI 2003/2682 ("**the PAYE Regulations**") and for the tax years 2009 to 2015 decisions were made pursuant to section 8 of the Social Security Contributions (Transfer of Functions etc) Act 1999 ("**the SSCA 1999**") in the following amounts:

1	2	3	4	5
Tax Year	Director	Pay (£)	Tax (£)	NICs (£)
2009-10 (1 month only)	Mr Odedra	5,000		942
	Mr Badiani	5,000		942
2010-11	Mr Odedra	60,000		8,338
	Mr Badiani	60,000		6,948
2011-12	Mr Odedra	46,664	19,221	9,777
	Mr Badiani	46,664	16,081	5,463
2012-13	Mr Odedra	33,332	13,826	6,653
	Mr Badiani	33,332	9,494	3,566
2013-14	Mr Odedra	36,800	12,129	7,501

	Mr Badiani	36,800	10,805	4,016
2014-15	Mr Odedra	53,400	21,360	10,571
	Mr Badiani	53,400	13,855	6,271
Total			**116,771**	**70,625**

3. We heard evidence from Mr Odedra on behalf of both of the Directors (as Mr Badiani has hearing issues and as his first and best language is Guajarati and would need a translator) and Mr Odedra was cross examined by HMRC's presenting officer.

4. We also heard evidence from Mrs Jones, an officer of HMRC and the case worker in relation to the enquiry that led to this appeal. Mrs Jones had served third party notices requesting information from third party suppliers as to the capacity in which Mr Odedra and Mr Badiani acted in their dealings with the third parties.

The facts

5. In the periods under consideration we find the facts as follows:

(1) The Appellant carried on a business of running a petrol station business.

(2) The Directors were not paid any remuneration directly by the Appellant.

(3) The Directors and their spouses owned between them all of the shares in the Appellant in equal shares (25% each). (The shares had been acquired by their wives on 16 July 2007).

(4) There were no written contracts between the Appellant and the Directors other than the agreements (called "Consultancy Agreements") entered into in 1999, which we refer to as the "1999 contracts".

(5) The two contracts were as follows:

(a) One is between the Appellant on the one hand and Mr Odedra/ his consultancy vehicle on the other dated 15 June 1999. The consultancy vehicle specified in the contract is a limited company. (Mr Odedra said that this was a mistake, it is a general partnership of which he and his wife were 50/50 partners that had provided the consultancy services).

(b) The other is between the Appellant on the one hand and Mr Badiani/his consultancy vehicle on the other dated 20 June 1999. The consultancy vehicle in this case was a company called Jadeprime Limited. The shares in the company are owned by Mr Badiani and his wife in equal shares.

(c) The contracts are almost identical. Clause 1 entitled particulars defines a number of terms. It reads as follows in relation to the meaning of consultant: *"1.2 the consultant*"

Then in hand writing below the following appears: *"J&J Enterprises (Leicester) Ltd /OR B.ODEDRA"*

In the case of Mr Badiani's contracts it is identical save that the handwritten entry reads *"JADEPRIME LTD/MR N. BADIANI"*

We refer to Jadeprime Ltd (or the partnership that Mr Odedra says was intended to be the vehicle) and J&J Enterprises (Leicester) Ltd as "the Consultancy vehicles".

Clause 1.4 defines the term. Mr Odedra's contract has an initial term of 5 years terminable on two years notice. Mr Badiani's term was one year terminable on 6 months' notice*:*

"1.4 The term

"a period of 5 years from the commencement date and thereafter unless terminated by either party giving to the other not less than two years notice in writing."

"1.5 The initial fee

three thousand pounds per calendar month exclusive of VAT."

"1.6 The fee paid shall be reviewed every twelve months and increased having regard to the increase in turn-over and profit of the company pursuant to clause 4 hereof"

The 1999 contracts do not define the type of services to be provided. Clause 2 states

"2 The Company engages the consultant and the consultant agrees to serve for the term

2.1 During the term the consultant shall devote such time and attention and ability to the business of the company as may reasonably be necessary for the proper exercise of the consultant's duties provided that mothing herein contained shall require the consultant to devote more than 15 hours a week to the company's business."

2.2 The consultant shall advise and assist the company as required in all branches of its business and within the terms of this agreement the consultant shall comply with the reasonable directions of the company and use the consultant's reasonable endeavours to promote the interests of the company".

"3 In consideration of the consultant's services hereunder the company shall pay to the consultant the fee in arear on the last working day of each month.

The payments to be made to the Consultants under the consultancy contracts were made monthly by cheque into bank accounts. In the case of Mr Odedra the payment was paid into the bank account of the partnership maintained by him and in the case of Mr Badiani into the bank account of the company maintained by him.

"4 The fee paid to the consultant shall be reviewed every twelve months and increased having regard to the increase in turnover and profit of the company"

"5 In addition to the fee the company shall pay or reimburse the consultant all expenses reasonably and properly incurred in connection with the service provided by the consultant hereunder."

"8 On determination of this consultancy agreement for any reason (including effluxion of time) the consultant shall forthwith deliver to the company all records papers samples keys credit cards and goods belonging to the company in the possession or under the control of the consultant."

(6) The petrol station business currently comprises two petrol stations. They are run without any employees as a result of:

(a) the shop at the stations being sublet and the tenant of the shop pays rent and collects the payments for the petrol on behalf of the Appellant.

(b) the carwash on each site is let to another person who provides hand car wash services and pays rent to the Appellant.

The only functions that the Appellant is carrying out are purchasing of petrol and the determination of the prices, collecting and checking the takings from the petrol sales from the shop tenant and collecting rent and inspecting premises, insuring and where necessary arranging repairs. There are occasional rent and rate reviews and planning applications.

Pricing the petrol is important because there are petrol stations at large national food chains in the vicinity of both and getting the price right is crucial to stay competitive. A three pence price difference can result in loss of customers. Through Mr Badiani's contacts the Appellant secured a purchase agreement with Essar which allowed a reasonable period to pay.

(c) At first there were five petrol stations but this has been reduced to two.

(7) Mr Odedra and Mr Badiani usually work together. They visit the petrol stations together two or three times a week and usually make decisions together save if one is on holiday or ill. At the petrol stations one checks the takings and the other checks the site to ensure it is clean and there are no breaches of the

insurance conditions, fire hazards are a serious issue for petrol stations. They also check the volume of petrol sold (and order more) and they check the prices of fuel being offered by other petrol stations nearby and adjust the prices accordingly.

(8) Each of Mr Odedra and Mr Badiani usually work between 20 and 40 hours a week even though the 1999 contracts provide that the Consultant is not required to work more than 15 hours per week.

(9) Mr Odedra may take holiday whenever he wishes. He agrees his holidays with Mr Badiani and may not take more than two weeks at a time but there is no limit on the amount of holiday. If he is on holiday or ill Mr Badiani's son acts as substitute. The fees are unaffected by the amount of holiday taken.

(10) Mr Odedra has habitually provided services to other businesses in the past but now he is in his 60s he does not do that so much. The services he provides to the Appellant are recurring ones as described above at (6) and one-off services when for example planning permission is required on a reorganisation of a petrol station, negotiating rates with local authorities and finding tenants for the businesses. It was accepted that the modus operandi did not involve tendering for work for the Appellant, making pitches and preparing reports.

(11) Generally neither Mr Odedra nor Mr Badiani claimed expenses in their capacity as directors of the Appellant. There was an occasion when a claim for £480 appeared to have been made for petrol. It seems this was credited to the Directors' loan accounts of the Appellant. Mr Odedra explained this was to deal with a shortfall in takings owing to customers driving away without paying.

(12) Mr Odedra provided such equipment as is needed to perform his services although it was accepted that very little equipment was needed to do so.

6. In and around 1999 the position was as follows:

(1) Mr Odedra had carried on a business of manufacturing clothing but this was becoming increasingly difficult as margins were being squeezed. He had conducted the clothing business through the partnership that is said to be the party to the 1999 contract.

(2) Mr Badiani had carried on petrol service station business through the company that is party to the 1999 contract. Mr Badiani also conducts business through another company JJ Petroleum Limited.

(3) Mr Odedra and Mr Badiani were friends from their childhood and in 1999 Mr Badiani had invited Mr Odedra to join him in establishing the petrol business.

(4) Mr Odedra and Mr Badiani identified an investor who would provide the finance to fund the enterprise. The Appellant company was formed and the investor acquired 50% of the shares in the company. Mr Odedra and Mr Badiani owned the other 50% in equal shares. There was no connection between Mr Odedra and Mr Badiani on the one hand and the investor on the other.

(5) The 1999 contracts were entered into between the Appellant and the consultants. There was no clear explanation of what benefit the external investor acquired as a result of the arrangement being structured as it was.

(6) The finance provided by the investor was by way of loan and when the loan was repaid, the external investor sold his shares in July 2005 leaving Mr Odedra and Mr Badiani, owning all the shares equally. The spouses acquired shares in the appellant in July 2007.

(7) The amount of the payments made by the Appellant in each year is not disputed. The payments were reported in full as income of the consultancy vehicles in each of the periods concerned. HMRC had enquired into the returns of the Appellant in 2000 and 2007but no adjustments were made to the returns. The Appellant did not assert that HMRC were estopped from enquiring into the arrangements as income tax is an annual tax.

7. The Appellant sought to deduct the payments as expenses of its trade.

8. The Respondents claimed that the payments are remuneration of Mr Odedra and Mr Badiani either as a matter of fact or that the 1999 contracts should be re-characterised as contracts of service rather than contracts for services and that the arrangements were motivated by the saving of tax.

9. The Respondents enquired into the returns and in the course of the enquiry the case officer asked a series of questions of third parties using third party notices which included a requirement to, *"identify the party to the negotiations and in what capacity the person was acting."* The notices were sent to the following;

(1) Chevron Global marketing

(2) Lambert Smith Hampton

(3) Leicestershire County Council

(4) Natrass Giles, and

(5) Property Briefing Limited.

Not every recipient provided information in response but none of the responses showed that the Directors were operating in their capacity as consultant to the Appellant.

The legislation in question

The Income Tax (Employment and Pensions) Act 2003 ("ITEPA")

Section 6

"(1) The charge to tax on employment income under this part [Part 2] is a charge to tax on-

(a) general earnings, and

(b) specific employment income.

The meaning of general earnings and specific employment income is given in section 7."

Section 7

*"(1) This section gives the meaning for the purposes of the Tax Acts of "**employment income**", "**general earnings**" and "**specific employment income**".*

(2) Employment Income means –

(a) earnings within Chapter 1 of part 3,[which comprises only section 62 ITEPA],

(b) any amount treated as earning (see subsection 5), or

(c) any amount which counts as employment income (see subsection 6)."

"(5) Subsection 2(b) …… refers to any amount treated as earnings under

(a) Chapters 7 to 10 of this Part (agency workers, workers under arrangements made by intermediaries) and workers providing services through managed service companies)

Section 62

"(2) In those parts, 'earnings', in relation to an employment, means –

"(a) any salary, wages or fee,

"(b) any gratuity or other profit or incidental benefit of any kind obtained by the employee if it is money or money's worth, or

"(c) anything else that constitutes an emolument of the employment."

Section 5

"*(1) The provisions of the employment income Parts that are expressed to apply to employments apply equally to offices unless otherwise indicated.*

"(2) In those provisions as they apply to an office-

(a) references to being employed are to being the holder of an office,

(b) employee means the office-holder

(c) employer means the person under whom the office holder holds office."

The Social Security Contributions and Benefits Act 1992 , (SSCBA 1992)

Section defines "employed earner" as "a person who is gainfully employed in Great Britain either under a contract of service of in an office (including elective office) with earnings"

Section 3(1) SSCBA 1992 defines earnings to include: "any remunerations of profit derived therefrom.

Section 6, Section 7 and Para 3 of Schedule 1 SSCBA 19992 impose primary and secondary national insurance contributions as follows:

Section 6(1)

"Where in any tax week earnings are paid to or for the benefit of an earner over the age of 16 in respect of any one employment of his which is employed earner's employment-

(a) a Primary Class 1 contribution shall be payable in accordance with this section…if the amount paid exceeds the current primary threshold …."

(b) A Secondary Class 1 contribution shall be payable in accordance with this section… if the amount paid exceeds the current secondary threshold…."

Section (1)

*"For the purposes of this Act, the '**secondary contributior**' in relation to any payment of earnngs to or for the benefit of an employed earner, is*

(c) In the case of an earner employed under a contract of service, his employer

(d) In the case of an earner employed in an office with earnings, either-

(i) such person as may be prescribed in relation to that office: or

(ii) if no such person is prescribed, the government department …."

Para 3(1) Schedule 1

"Where earnings are [paid to an employed earner and in respect of that payment liability arises for primary and secondary Class 1 contributions, the secondary contributor shall(except in prescribed circumstances, as well as bing liable for any secondary contribution of his own, be liable in the first instance to pay also the earners primary contribution, on behalf of and to the exclusion of the earner: … "

The Appellant's case

10. The Appellant argues that:

(1) There are no contracts of service in existence. Accepting the role of director does not automatically give rise to a contract of service. An executive director is required to have an actual written contract but the same is not true of a non-executive director. No contract of service has been proved to exist.

(2) HMRC's contention that payments to a person in respect of an office are taxed as if they were earnings from employment and that a contract of service will automatically take precedence over a contract for services is incorrect. Section 5(1) ITEPA 2003 which says that the Parts of the Act dealing with employment income apply equally to offices is not sufficient to bring payments under a consultancy agreement into the charge to income tax as employment income.

(3) There is in existence a contract for services in the form of the 1999 contract.

(4) That the standard of performance of the duties under the 1999 contract is comparable to the standards expected of directors under various provisions in the Companies Acts is irrelevant. There is no contract of service. The burden of proof is on the Appellants but it is impossible to prove a negative.

(5) Mr Odedra and Mr Badiani were non-executive directors of the Appellant. The services required under the 1999 contract are not those that one would expect a non-executive director to perform.

(6) There is no requirement under the Companies Act 2006 that provides that a non – executive director should be remunerated. Palmer on Company Law at para 8.901 states:

> "*A director does not have the right to be remunerated for any services performed for the company except as provided by its constitution or approved by the company's members.*[1] *This rule is an aspect of the general principle that a director is not allowed to make a profit unless expressly permitted.*[2]"

The Companies articles include Table A which at regulation 82 indicates that a director is entitled to remuneration as provided by ordinary resolution of the shareholders in general meeting. There was no such resolution. It would have been unlawful for the Appellant to pay any remuneration.

(7) There is no warrant to treat the payments as distributions or anything other than payments for consultancy services under the 1999 contracts.

(8) The arrangements are not artificial:

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[1] Dunstan v Imperial Gas Light Co 110 E.R. 47

[2] Hutton v West Cork Railway Company (1883) 23 Ch D 654

(a) They were established in 1999 when there was an independent 50% shareholder whose interests had to be protected.

(b) This is manifestly so, as in 2007 HMRC investigated the affairs of the Appellant but no Regulation 80 determination was made in consequence.

(c) The categories of duties that the Consultants perform are not those commonly undertaken by non-executive directors.

(d) There was no requirement to carry out the activities at a particular time or place. In fact the consultancy services were often performed from home which in the period under consideration was not typical employee behaviour.

(e) Services were also performed outside the ambit of the 1999 contract by the consultancy vehicles.

(f) Each of Mr Odedra and Mr Badiani held an office but that was held in parallel with the 1999 contract and the tasks performed under the 1999 contract were not those commonly performed by directors such as counting cash takings, ordering petrol although the negotiation of the contract with Essar would be the sort of duty a director but not an employee might perform.

(g) There was no pre-existing employment relationship before the consultancy arrangement was put in place.

(h) That the fees were paid in fixed monthly instalments is not inconsistent with the 1999 contract being a contract for services.

(i) The fact that the note to Appellant's accounts describes Mr Odedra's consultancy vehicle as a company and not a partnership is not material. In any case the term company can be used to describe a partnership, the use of "& Co" after the name of a partnership is very common.

(j) If the consultancy vehicles are intermediaries then the fact that the directors had a non-executive directorship is irrelevant.

(9) The quality of the written document may be poor and it may contain errors but the two directors are business people whose first language is not English and they relied on their advisers.

(10) The documentation HMRC had obtained from third parties to try and discern the capacity in which the directors were acting was insubstantial. Further third parties simply want to know the negotiators have the capacity to conclude a binding contract.

(11) Further as NICS apply only to "earnings" from an office and earnings is a technical term. NICS do not apply to fees from a consultancy. HMRC

Manual EIM00730 indicates that it is possible for a director of a company to provide consultancy services to the company of which he/she is a director.

11. Turning to the authorities Mr Powrie for the Appellant argued:

(1) The Supreme Court decision in ***RFC 2012 Plc (In Liquidation)(formerly The Rangers Football Club Plc)(Appellant) v Advocate General for Scotland (Respondent)(Scotland) ("Rangers")*** [2017] UKSC 45, which involved payments to an EBT and then by the EBT to a sub-trust for each player, which then made loans to the players that were repayable on death, does not apply to treat the payments in this case as remuneration of an office or employment for the following reasons:

(a) The arrangements in this case did not have a tax avoidance motive. They were put in place with the acquiescence of an independent third party shareholder for commercial reasons. The consultancy vehicles existed before the Appellant was incorporated.

(b) The decision in Rangers was on the basis that the payments to the EBT in that case were a reward for work carried out as employees:

"*But the bonuses were paid as a reward for the work which the employees had carried out in their capacity as employees."* [31]

"*Both sums involve the payment of remuneration for the employee's work as an employee*." [39]

In this case there never was a prior employment so Rangers is inapplicable.

The decision of McKenna J in ***Ready Mixed Concrete (South East) Limited v Minister of Pensions and National Insurance*** [1968] 2 QB 497 specifically provides for a three point test, all three parts of which must be satisfied to be an employee. The test is cited with approval in in the 2018 decision of *Sprint Electric Limited v Buyer's Dream Ltd* [2018] EWHC 1924 (Ch)

"[the decision] *has been accepted as setting out essential and necessary conditions for a contract of service:*

'A contract of service exists if these 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 service 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 sufficient degree to make that other master. (iii) The other provisions of the contract are consistent with its being a contract of service.'"

Mr Powrie argued that (i) there are payments in this case (but not by the Appellant to the directors), but (ii) even if that were satisfied it is clear there

is insufficient control by the Appellant of the performance of the services to make the Appellant the master of Mr Odedra and Mr Badiani.

(2) In ***Lorimer (Inspector of Taxes) v Hall*** Mummery J cited Vinelott J in the case of ***Walls v Sinnett*** where Vinelott J cautioned against using analogies on the facts when he said:

'*It is, in my judgment, impossible in a field where a very large number of factors have to be weighed to gain any real assistance by looking at the facts in another case and comparing them one by one to see what facts are common, what are different and what particular weight was given by another tribunal to the common facts. The facts as a whole must be looked at, and a factor which might be compelling in one case in light of the facts of that case may not be compelling in the context of another case.*'

Mr Powrie said looking at the facts in the round in this case there was no contract of service. Nonetheless he went through the list of factors considered by HMRC to be pertinent:

> *(a) That the alleged contract for services does not sufficiently define the duties using as it does general expression to act in the best interests of the company.*

HMRC considered the omission of a precise description of the services to be provided was indicative that the contract was one of service. The words are consistent with the duties of a director. Commercial consultancy contracts would specify the tasks to be performed by a consultant.

Mr Powrie said that the contracts exist (and are not alleged) and it is not for the company to specify how the consultant should carry out the duties.

> *(b) The degree of control over the consultants providing the services. The higher the degree of control the more likely the person is an employee.*

HMRC say that as the contractors are directors they are under the complete control of the company. Further the number of hours actually worked is in fact indicative that they were actually engaged as directors.

Mr Powrie said that the consultants could decline to work and take breaks of their choosing which is completely incompatible with the master and servant relationship.

> *(c) Whether the person doing the work provides his own equipment. The greater the amount of equipment required to do the job and supplied by the person providing the services the more likely that the person is self-employed.*

Mr Powrie stated that very little equipment was needed in this case and it was provided by the consultants themselves. Provision of equipment has little bearing in a case such as this.

> (d) *Whether the person doing the work hires anyone to assist him.*

HMRC argued that the directors carried out all the activities of the company as is common in closely held companies.

Mr Powrie said they subcontracted the work to be done. There were employees but they were employed by the subcontractors.

(e) The degree of financial risk taken

HMRC said that the Directors were exposed to the risk and reward by virtue of being shareholders not by virtue of being consultants.

Mr Powrie indicated the contractors did take financial risk. If they failed the company would become insolvent, the consultants would not be paid. If they were successful the company would be successful, their fees would be paid, as was the case.

(f) The degree of responsibility for investment and management.

HMRC contend the Consultants would be expected to put forward proposals to be approved by the Appellant. There were no proposals. This is because all of the decisions were taken by the directors in their capacity as directors.

Mr Powrie said there were no such decisions.

(g) How far the person providing the services has an opportunity to profit from sound management in the performance of his task.

HMRC said the directors were able to benefit through their shareholdings which indicates the services were rendered as directors of a close company.

Mr Powrie stated that the consultants were not able to benefit from the increased profit in the Appellant although they could charge higher fees.

(h) The understanding of the intentions of the parties.

HMRC said that as the parties were controlled by the same parties the intentions of the parties should have no weight and the correct treatment should be determined by the underlying facts.

Mr Powrie said that the fact that they had common shareholders is not true of the period when the arrangement was first brought into existence and the contracts entered into because of the outside investor.

(i) Whether the person providing the services has set up a business like organisation of his own.

HMRC assert the contractors existed only to provide services to the Appellant.

Mr Powrie argues that was not the case the consultancy vehicles did carry on other activities.

(j) The degree of continuity in the relationship between the person performing the services and the person to whom they are provided.

HMRC says that the fact that the contracts have been rolled over for over a decade is evidence of a contract of service.

Mr Powrie thought this was irrelevant.

> *(k) How many engagements did he perform and whether they are performed mainly for one person or for a number of people.*

HMRC say the consultants claim to provide services to the Appellant and one other person JJ Petroleum.

Mr Powrie said they did have other customers.

> *(l) Whether the person providing the services is accessory to the business of the person to whom the services are provided or is part and parcel of the latter's organisation.*

HMRC assert that as Mr Odedra and Mr Badiani were directors of the Appellant they were part and parcel of the Appellant's organisation which is consistent with Mr Odedra and Mr Badiani being held out as directors in communications with third parties. Further following ***Future On-Line Ltd v Foulds (HM Inspector of Taxes)*** 2004 EWHC 2597 Ch, all of Mr Odedra's and Mr Badiani's services were provided in that capacity. Further HMRC contend that the existence of a right of substitution although indicative of self-employment was not found to be determinative in ***Usetech Ltc v Young*** [2004] 76 TC 811. However in this case there was no express right of substitution.

Mr Powrie said that neither Mr Odedra nor Mr Badiani were part and parcel of the Appellant's organisation. ***Future On-Line Ltd v Foulds*** requires the wider context to be considered from which it is clear that they are not part and parcel of the Appellant's business. There is a total absence of control by the Appellant. Mr Odedra and Mr Badiani did not have to work any particular number of hours, they had no fixed entitlement to holiday, there was no mutuality of obligation. On the contrary, the individuals through their consultancy vehicles altered the structure of the Appellant's business so that through the leasing of the shop and carwash at the petrol stations, the business was effectively conducted by contractors. For this service the consultants received fees.

Further in **Usetech v Young** Mr Young failed the test because his duties and those of the staff were identical. Specifically he had to ask for holiday, he had no ability to substitute a person to perform his duties and there was mutuality of obligation. In this case none of these factors is satisfied: there is an ability to substitute, a lack of mutuality of obligation and an ability to take holiday without permission.

Mr Powrie argued that in this case the whole art of the business is to be able to set the retail sales price of petrol so that the price remained competitive in the area. This can be done remotely, from a person's death bed, if necessary. There is no requirement for the setters of the margin to be part and parcel of the Appellant's organisation.

(3) Mr Powrie argued that if HMRC are correct in saying Mr Odedra and Mr Badiani have a personal obligation to provide services to the Appellant and the services are not provided directly to the Appellant but are provided through the consultancy vehicles, the Intermediaries legislation in Section 49 ITEPA 2003 ought to apply. In such a case it would be the consultancy vehicles that ought to be accounting for income tax and national insurance contributions and not the Appellant. The case of ***MDCM Limited v Commissioners of Her Majesty's Revenue & Customs*** 2018 UKFTT 147 concerned the application of that legislation to a nightshift manager and the Tribunal found in favour of the Appellant. In that case HMRC argued that control was the most important factor [44]. The Appellant argued that the only control the manager was subject to was the sort of control manifest in a large scale construction project. The Tribunal found the terms of the hypothetical contract contained the following terms:

(a) Mr Daniels was subject to no greater control than over any other contractor.

(b) He could not provide a substitute

(c) He could refuse to work on any site,

(d) He was paid a daily rate and had to pay his own hotel, travel and other expenses

(e) He took no financial risk

(f) There was no provision of notice on termination or payment in lieu of notice

(g) He was provided safety equipment

(h) He was not integrated into the business of STL the operator of the construction site.

The Tribunal did not accept HMRC's arguments about control. It recognised that the lack of financial risk and inability to substitute pointed to employment but the lack of notice, the flat rate of pay, and no entitlement to employee benefits were not consistent with employment.

(4) Mr Powrie also took us to ***Jensal Software Limited v Commissioners of Her Majesty's Revenue & Customs*** [2018] UKFTT 271 paras [120] to [122] where the following extracts from various decisions are cited:

(a) McKenna J's decision in ***Weightwatchers (UK) Ltd v HMRC*** 2012 STC 265:

"*Control includes the power of deciding the thing to be done., the way in which it is to be done, the means to be employed in doing it, the time when and the place where it shall be done."*[120]

(b) The Court of appeal in ***Montgommery v Johnson Underwood Limited*** [2001] EWCA Civ 318:

"*Society has provided many examples from masters of vessels and surgeons to research scientists and technology experts, where such direct control is absent. In many cases the employer …may have no more than a very general idea of how the work is done and no inclination to directly interfere with it. However some sufficient framework of control must surely exist. A contractual relationship concerning work to be carried out in which one party has no control over the other could not sensibly be called a contract of employment.*" [121]

(c) Lord Phillips in the ***Catholic Child Welfare Society*** case [2012] UKSC 56 in a case concerning a highly skilled person:

"*Today it is not realistic to look for a right to direct how an employee should perform his duties as a necessary element in the relationship between employer and employee. Many employees deploy a skill that is not susceptible to direction by anyone else in the company that employs them. Thus the significance of control today is that the employer can direct what the employee does, not how he does it."* [122]

Mr Powrie concluded that there was:

(i)No contract of service as there was no control by any of the three benchmarks.

(ii)No justification for ignoring the 1999 contracts that had come into place in 1999 and no justification to re-characterise them. The arrangements were not tax motivated. There were no prior pre-existing contracts of service which the arrangements replaced.

HMRC's Case

12. HMRC argued that:

(1) As Mr Odedra and Mr Badiani were directors of the Appellant they have a contract of service with the Appellant.

(2) Section 5 ITEPA applies to tax the earnings of a director as if they were the earnings of the employee.

(3) The contract of service trumps all other contracts.

(4) The Tribunal need only ask if the payment made by the Apellant related to the directorships of Mr Odedra and Badiani.

(5) The burden is on the Appellant to show the payments are entirely divorced from the office of director.

(6) Alternatively to the extent that the Tribunal has to determine which of the two contracts the payments made by the Appellants relate HMRC assert that the facts support the allocation to the contract of service in respect of

the directorships, and again the burden of proof is on the Appellant to show the Determinations and Decisions made are incorrect.

(7) The 1999 contracts made between the consultancy vehicles (owned by the directors and their spouses) and the Appellant are entirely artificial. They do not identify any specific duties and the obligations are framed in a manner which resonates with the duties of care owed by a director to a company. The lack of specificity in relation to the duties means that the motivation to perform comes primarily from interest of the individuals as directors and shareholders of the Appellant.

(8) The activities performed by the individuals amount to the day to day running of the business as well as long term strategic decisions and none is beyond what might reasonably be expected of the directors of a close company.

(9) The payments are regular monthly amounts and bear no direct relationship between the amount and timing of the work done which is indicative of salary.

(10) The 1999 contracts also name the individuals as well as the consultancies as the consultant a party which indicates that it is the services of the individuals that were being sought.

(11) The replies to the Notices issued under Schedule 36 Finance Act 2008, suggest that Mr Odedra and Mr Badiani were acting in their capacity as directors because in their dealings with third parties they did not make it clear they were acting in their capacity as Consultants to the Appellant,

(12) The accounts of the Appellant does not accurately describe Mr Odedra's consultancy vehicle as a partnership

(13) It was accepted that the payments were made to the consultancy vehicles but the *Rangers* decision indicates that the charge to income tax may arise irrespective of whether the employee receives the payment.

(14) As in the *Rangers* case the directors had acquiesced to the payments being made to the third parties.

HMRC's contentions as to the application of the case law is set out above in paragraph 11(2) above and we not repeat the arguments again in this section.

Discussion

13. It is not in dispute that Mr Odedra and Mr Badiani held the office of director under the Appellant at all material times.

14. What is in dispute is the amount of the earnings from that office. The Appellant says that none of the payments described in column (2) of the Table in [2] above (and which, it is common ground, were made by the Appellant, ("the Column (2) Payments") are payments of "earnings" within ITEPA section 62.

15. The Appellant says that the Column (2) Payments are not earnings but are payments for consultancy services rendered by the consultants to the Appellant through the

activities Mr Odedra and Mr Badiani. The Respondents say that the Column (2) Payments are earnings from Mr Odedra's and Mr Badiani's respective offices as directors of the Appellant.

16. No authority was cited to us by either side to indicate whether the quantum of emoluments/earnings from an admitted office is a question of law or a question of fact. We note that in *Billows v Robinson (Inspector of Taxes)* [1991] STC 127 a unanimous Court of Appeal treated the question as one of fact, as would have been our own inclination apart from authority. Treating it as a question of fact, we are of the firm opinion that the Column (2) Payments are payments of earnings.

17. The Appellant argues that as non-executive directors Mr Odedra and Mr Badiani did not have and were not required to have written contracts which provided for remuneration and as they had never been voted remuneration by the Appellant in general meeting, the payments could not be attributed to the office held by them.

18. We do not find the above compelling.

19. First, the Appellant accepts that Mr Odedra and Mr Badiani are directors, whether they are executive or non-executive, they hold an office the remuneration for which would be taxable as earnings.

20. Second, the fact that there has been no resolution passed voting them remuneration would not necessarily cause any payment of remuneration in respect of the office to be unlawful. As Mr Odedra and Mr Badiani are old friends and as they and their wives own all of the shares in the Appellant, a formal resolution to approve remuneration is not required following Buckley LJ in *re Duomatic* which was endorsed by Lord Neuberger in *EIC Services Limited v Phipps* [2003] EWHC 1507 where he said that if all the members of the company, being aware of the relevant facts, either give their approval to the course of action or they conduct themselves as to make it inequitable for them to deny that they have given their approval, a resolution is not required. It is inconceivable that the spouses were not aware of the arrangements given that they acquired 25% of the shares in the Appellant in 2007, and have held them ever since, and are joint owners of their spouse's Consultancy vehicle.

21. The Appellant argued that unless there was an avoidance motive the fact that payments were made to the Consultancy vehicle and not to Mr Odedra and Mr Badiani, the sums cannot be taxed as earnings. That is incorrect. An individual is liable to income tax on earnings on payments even if paid to a third person and this is so irrespective of whether there is a tax avoidance motive. The legislative provision imposing tax on earnings "*is silent as to the identity of the recipient*", per Lord Hodge in the *Rangers* case, at end of [38].

22. The Appellant argued that 1999 contracts were contracts for services and not contracts of service. Having reviewed the contracts we consider that they should properly be regarded as contracts of service.

23. The appellant also argued that the services provided under the 1999 contract were not of the sort provided by non-executive directors. We found this a particularly

unattractive argument. Firstly it is normal in the case of closely held companies for the directors to perform all tasks however lofty or lowly they may be. Secondly whereas we fully accept that it is legally possible for an individual to have his own independent business (for example as an accountant or solicitor) while also having the office of director of a company, and that in such a case the person's professional fees are not earnings from his office as director, though we observe in passing that in our experience this does not normally occur where the individual is a competitor of, or in the same line of business as, the company as appears to have been the case here. In relation to the Appellant, Mr Odedra and Mr Badiani conducted all of the activities that were conducted by the Appellant. We have concluded, looking at all the evidence, that Mr Odedra and Mr Badiani did not have any independent business of the kind to which we have referred and which constituted the source of the Column (2) Payments, with the result that those payments arose from those gentlemen's respective offices or employments with the Appellant.

24. Following the House of Lords decision in *BMBF v Mawson* 2005 STC 1 the purposive rule of construction of taxing statutes has been required. It is necessary to construe the law purposively and where appropriate apply it to the transaction viewed realistically. Lord Nicholls at [36] cited an extract from *Collector of Stamp Revenue v Arrowtown Assets Limited* [2003] HKCFA 46 at [35] where Ribeiro PJ said :

"[T]he driving principle in the Ramsay line of cases continues to involve a general rule of statutory construction and an un-blinkered approach to the analysis of the facts. The ultimate question is whether the relevant statutory provisions, construed purposively, were intended to apply to the transaction, viewed realistically."

The provisions of ITEPA and SSCBA 1992 are intended to impose a liability to income tax and NICs on earnings from an office or employment and to provide for the collection of that income tax and NICs by the employer. The obligation ought not to be side stepped by the Appellant putting in place contracts that purport to be consultancy contracts pursuant to which the directors of the Appellant (contracting alongside a vehicle owned by the director) exclusively conduct the entire business of the Appellant.

When viewed realistically, as no services were provided by the Consultants other than those provided by the directors of the Appellants, the payments should be regarded as having been an award for the services as director of the Appellant.

The Appellant asserted that the arrangements were not established for the avoidance of tax but to protect the original investor that provided initial capital to start the business. How the arrangement protected that investor was not explained and it is difficult to understand how they would do so. The arrangement involving Mr Odedra was very tax efficient. He and his wife were partners in the partnership with equal shares. Inevitably the tax collected from two partners on the fees paid with two personal allowances and lower rate bands would have been less than the tax that would have been paid by Mr Odedra as a director. It is inconceivable that tax was not a motivating factor in establishing the partnership structure. This is particularly so given that Mrs Odedra took no part in performing services under the 1999 contract. Mr Badiani did not give evidence and as his witness statement is silent on this point we do not know the tax

position of him and his wife and his consultancy vehicle. It would be inconceivable that the consultancy structure involved the payment of more tax than would have been due on the payment of the fees to Mr Badiani. It is inconceivable that the arrangement would be allowed to run for so many years if it were less tax efficient.

There was a dispute as to whether the consultancies provided services to third parties. It seems to us immaterial. The arrangement involving the Appellant is the only arrangement we are concerned about.

It follows that the appeal must be dismissed and that it is unnecessary to consider whether or not (as the Appellant claims) the agreements between the Appellant on the one hand and Mr Odedra and his partnership on the other hand and between the Appellant and Mr Badiani and his company on the other did not give rise to contracts of service. However, in case it is relevant, we have also concluded, on a review of the 1999 contracts that such contracts of service existed and that the Column (2) Payments were made under them, and were "earnings" for this additional reason ad set out below

25. The Appellant argued that as there was no written contract of service and only a written contract for services in each case, in the form of the 1999 contacts, the terms of which were such that the three factors necessary to establish employment set out by McKenna J in *Ready Mix Concrete* are not satisfied. Most importantly the Appellant says that there was no control over the performance of services.

26. The three factors are that:

(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 service for his master.

The 1999 contracts required performance of services by each of Mr Odedra and Mr Badiani for which remuneration was to be paid. They are each named as a Consultant. Both signed the contracts. Mr Badiani signed in his own capacity and as a director of his consultancy vehicle. Mr Odedra signed in his capacity as a director a company which he said was not intended to be a party to the agreement.

The 1999 contracts provided for the services to be performed for the Appellant for which there is an express right to be remunerated. This test is satisfied.

(ii) *He agrees, expressly or impliedly, that in the performance of that service he will be subject to the other's control in sufficient degree to make that other master.*

The terms of the 1999 contracts implicitly provide for the services supplied to be subject to scrutiny by the Appellant because the Appellant had to determine:

(1) Whether to extend the term of the contract at the expiry of the first [5][1] years [1.4]

(2) Whether to terminate the contract by giving notice [1.4]

(3) Whether the Consultant had performed the services to the required standard [2.1]

(4) Whether any assistance was required in the branches of its business [2.2]

(5) Whether the Consultant had performed services for the required 15 hours per week [2.1]

(6) Whether to give directions to the Consultant [2.2]

(7) Whether the consultant had complied with directions given

(8) Whether to increase the fee payable which had to be undertaken annually [4].

That the contract was extended not terminated at the expiration of the initial five year term in the case of Mr Odedra and one year in the case of Mr Badiani, has been ongoing since 1999 and that the remuneration was increased over the years is indicative that the Appellant did consider the quality of the services. The fact that the Appellant could only operate through the two directors whose services were being scrutinised does not mean that the performance of each one was not scrutinised by the other. To allow the contract to run the directors had to be satisfied that the services were being performed to the required standard. This would seem to suggest that Mr Odedra as director scrutinised the activities of Mr Badiani and Mr Badiani as director scrutinised the services of Mr Odedra. The standard of each was scrutinised and controlled by the Appellant.

This test is satisfied.

(iii) *The other provisions of the contract are consistent with its being a contract of service.*

Although the Contractor in the 1999 contracts is in each case Mr Badiani and Mr Odedra and their consultancy vehicle, there is no express right to substitute another individual in the performance of the services. Further that the individual is named is indicative that substitution is not permitted.

We find this test satisfied.

27. Other factors which are indicative of employment as discussed in paras [11(2), (3) and (4)] of which we note the following:

(1) Whether considering the facts as a whole are indicative of employment, following *Lorrimer v Hall* and *Walls v Sinnett*

(2) Whether the individuals are part and parcel of the organisation *Future On Line Limited v Foulds*

(3) Whether there is sufficient framework to control the activities of the individual rather than whether the manner of performance was subject to oversight, Montgomery v Johnson

(4) In the case of highly skilled individuals, an employment relationship will exists if what the individual does is subject to control and not how it is done, Catholic Welfare

Taking all the factors into account we consider the relationship to be that of employer and employee. We also consider that Mr Badiani and Mr Odedra were part and parcel of the Appellant's business. No one else performed any activities of the business apart from the two Directors. The 1999 contracts required oversight by the Appellant. There was a framework to control the activities of each of the Directors. The Directors were under the control of the Appellant.

The respondents asked the Tribunal to confirm the validity of the Directions and Decisions. As the appellant did not contest their validity other than on the substantive grounds we accept that they were validly made.

We dismiss the appeals in full.

We understand that some tax has been paid by the consultancy vehicles, Mrs Odedra and Mrs Badiani and would hope and expect HMRC to avoid any double taxation that might arise if there are no extant enquiries into any relevant returns for the periods in question.

28. 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.

HEATHER GETHING
TRIBUNAL JUDGE

RELEASE DATE: 27 DECEMBER 2018