NATIONAL INSURANCE CONTRIBUTIONS - services provided through service company - if the arrangements had taken the form of a contract between the Appellant and the client whether the Appellant would be regarded as employed - yes - appeal dismissed - Social Security Contributions and Benefits Act 1992 Ss 2 and 4A; Social Security Contributions (Intermediaries) Regulations 2000 SI 2000 No. 72 7 Reg 6(1)

THE SPECIAL COMMISSIONERS
EDDIE BATTERSBY Appellant
and
STEPHEN DAVID CAMPBELL
(HM INSPECTOR OF TAXES) Respondent
SPECIAL COMMISSIONER: DR NUALA BRICE
Sitting in private in London on 3 August 2001
The Appellant in person
Barry Williams, Regional Advocacy Adviser, for the Respondent

The appeal

1. Mr Eddie Battersby (the Appellant) appeals against a decision made on 29 November 2000 relating to national insurance contributions. The decision was:
"That the circumstances of the arrangements between Mr E Battersby and Pennyright Bank for the performance of services from 31/05/2000 to 29/11/2000 are such that, had they taken the form of a contract between Mr E Battersby and Pennyright Bank, Mr E Battersby would be regarded for the purposes of Parts I to V of the Social Security (Contributions and Benefits) Act 1992 as employed in employed earner's employment by Pennyright Bank. That E.B.COM Limited is treated as liable to pay primary and secondary Class 1 contributions in respect of the worker's attributable earnings from this engagement."

The legislation

2. The legislation relevant to the issue in the appeal has become known colloquially as the IR35 legislation because that was the reference number of a Press Release which was issued by the Inland Revenue on 9 March 1999. The Press Release was entitled "Countering avoidance in the provision of personal services." The legislation proposed in the Press Release changes the treatment, for the purposes of income tax and national insurance contributions, of payments made to service companies. This appeal concerns only national insurance contributions.

3. The legislation about the payment of national insurance contributions is contained in The Social Security Contributions and Benefits Act 1992 (the 1992 Act) which contains separate provisions applicable to employed earners on the one hand and self-employed earners on the other. Section 75 of the Welfare Reform and Pensions Act 1999 inserted a new section 4A into the 1992 Act to take effect from 22 December 1999. New section 4A provided that Regulations might make provision for securing that, in stated circumstances, payments to service companies should be treated as earnings paid to a worker in respect of an employment. The Regulations made under the provisions of new section 4A are the Social Security Contributions (Intermediaries) Regulations 2000 SI 2000 No. 727 (the 2000 Regulations). These came into force on 6 April 2000. The relevant part of Regulation 6 provides:

"6(1) These Regulations apply where-
(a) an individual ("the worker") personally performs, or is under an obligation personally to perform, services for the purposes of a business carried on by another person ("the client"),
(b) the performance of those services by the worker is carried out, not under a contract directly between the client and the worker, but under arrangements involving an intermediary, and
(c) the circumstances are such that, had the arrangements taken the form of a contract between the worker and the client, the worker would be regarded for the purposes of Parts 1 to V of the Contributions and Benefits Act as employed in employed earner's employment by the client."

The issue

4. The Appellant is a computer consultant. In 1988 he established a limited company through which he supplied his services (the service company). In 1993 he started supplying services to Pennyright Bank through the service company. It was not disputed that the Appellant personally performed services for the purposes of the business carried on by Pennyright Bank and that the performance of those services was carried out not under a contract directly between the Appellant and Pennyright Bank but under arrangements involving an intermediary (namely the service company) within the meaning of subparagraphs (a) and (b) of Regulation 6(1).

5. Thus the issue for determination in the appeal was whether the circumstances were such that, had the arrangements taken the form of a contract between the Appellant and Pennyright Bank, the Appellant would be regarded for the purposes of the 1992 Act as employed in employed earner's employment by Pennyright Bank within the meaning of paragraph (c) of Regulation 6(1).

The evidence

6. Oral evidence was given by the Appellant on his own behalf. An agreed bundle of documents was produced. The Appellant produced three more documents in addition to those in the bundle.

The facts

7. The Appellant is a computer analyst and programmer. From 1982 he was employed by various companies. On 20 June 1988 he established a service company called E.B.Com Limited (E.B.COM) of which he and his wife were the directors. The Appellant then became self-employed. In the early 1990's there was an economic recession and the Appellant was out of work for nine months. This caused him hardship because, as a self-employed person, he did not receive unemployment benefits. The Appellant accepted work in Scotland but did not move his home there; he found the traveling between home and work to be inconvenient.

8. In 5 April 1994 the Appellant started working for Pennyright Bank whose premises were a half hour's drive from his home. He obtained the contract through an agency called Grinstead Associates (Grinstead). Pennyright Bank paid Grinstead who paid E.B.COM from whom the Appellant took his remuneration in the form of dividends. When the Appellant started to work for Pennyright Bank he was working on an old computer system that was to be replaced. Accordingly, he would not at that stage have been offered a permanent job with Pennyright Bank.

9. In 1996 E.B.COM bought out the contract with Grinstead for the sum of £5,460.00. Thereafter the Appellant continued to work for Pennyright Bank as a self-employed contractor directly through E.B.COM. In May 1999 Pennyright Bank wished to consolidate the procurement of all its self-employed contractors and did that through a company called Staff Agency Limited (Staff Agency). Thereafter the contracts were between E.B.COM and Staff Agency; Pennyright Bank paid Staff Agency who paid E.B.COM from whom the Appellant received his remuneration.

10. The Appellant's contracts with Pennyright Bank were initially for six months and later for twelve months at a time. The contract in force at the relevant time was a consultancy agreement between Staff Agency and E.B.COM. Under that agreement E.B.COM agreed to procure that the Appellant would devote his time, attention, skill and ability in accordance with the requirements of Pennyright Bank at such location as Pennyright Bank might reasonably require. The agreement contained a special provision in the following terms;

"This agreement does not create the relationship of employer/employee between the company [Staff Agency Limited] or client [Pennyright Bank] and the contractor [E.B.COM] or any of its personnel [the Appellant] ... ."

11. At the relevant time the arrangements under which the Appellant worked for Pennyright Bank had the following features:

- E.B.COM agreed to assign to Pennyright Bank all intellectual property or other rights created during the performance of the Appellant's services.
- E.B.COM remained responsible for the Appellant's sickness, disability and pension arrangements.
- E.B.COM was only to be paid for time worked by the Appellant and not for sickness and holidays. Any absence of the Appellant had to be agreed and approved in advance by Pennyright Bank.
- Staff Agency could end the agreement at any time on giving four weeks notice to E.B.COM or with immediate effect if there were technical incompetence, unprofessional performance, unsuitability or misconduct of the Appellant.
- Responsibility for the quality, quantity, and performance of the services rested with Pennyright Bank at all times.
- The normal hours of work were seven hours a day and payment was of an hourly rate with overtime paid pro rata; reasonable travelling and subsistence expenses were also payable.
- If Pennyright Bank complained about the Appellant, or if the Appellant withdrew, Staff Agency would provide Pennyright Bank with a replacement.
- The equipment used by the Appellant was a mainframe computer system which was owned by Pennyright Bank and which was situated at Pennyright Bank's premises.

12. At Pennyright Bank's premises the Appellant worked in a large open plan office which accommodated about 55 people. As a self-employed contractor the Appellant did not have a job title. The Appellant managed a small group of seven, of whom two were self-employed contractors and the rest were permanent employees. The self-employed contractors were mainly involved in project planning and the employees mainly supplied general production support. However, they all used the same equipment and the work was managed as a whole. The Appellant reported to a personal manager who was employed by Pennyright Bank. He had meetings with the

personal manager to discuss how projects were going, whether he would meet his deadlines, and any other problems. The Appellant was the technology manager for his team. However, as a self-employed contractor he was not able to undertake any personnel management of the permanent employees. This was done by another employed manager who reported to the same person as the Appellant. The Appellant could express views about the performance of the employees in his team but the permanent manager formally reviewed their performance. Although the Appellant attended project meetings he did not attend other meetings arranged for permanent employees.

13. In April 2001 Pennyright Bank offered the Appellant a permanent position as an employee and he accepted that offer. He considered that it had many advantages. He would not be troubled by the IR35 legislation; he would obtain the benefits of private health insurance, sick pay, holiday pay and pension provision; he would have job security; he could manage the permanent employees in his team; and he would become involved in internal management and company decisions.

The arguments of the Appellant

14. The Appellant argued that he was not employed by Pennyright Bank. He argued that it was common in the computer industry for enhancement work to be undertaken by selfemployed contractors and for support work to be undertaken by permanent staff. Employers preferred self-employed contractors because they could be laid off without severance pay. He took the risks of self-employment and he did not have any employment rights. Pennyright Bank could reduce his earnings without notice. He had had to renew his contract after each period of six months (or latterly each year) during the time he was self-employed. The Appellant emphasised that he ran his company properly and said that he paid an accountant £1,000 per year to perform the appropriate professional services to keep it in order. He distinguished his company from an "umbrella" company which was a single company out of which many contractors operated and where the contractors were not directors of the company. He argued that the IR35 legislation was more likely to apply to umbrella companies than to his own.

The arguments for the Respondent

15. For the Respondent M-r Williams argued that it was necessary to look at the substance of the arrangements rather than the form. The substance was that the Appellant was an employed earner. He had a personal obligation to Pennyright Bank and had been there for seven years. He supervised seven others, including employees, and in turn he was supervised by a personal manager. He was integrated into the structure of Pennyright Bank. Although in theory the Appellant could have been substituted by another employee, in practice that had never been done. The Appellant was not at risk of bad debts and he had not called a witness from Pennyright Bank to speak to the relationship. Mr Williams cited the authorities referred to later in this Decision and also Bank voor Handel en Scheepvaart N.V. v Administrator of Hungarian Property (1952) 35 TC 311; Morren v Swinton and Pendlebury Borough Council [1965]1 WLR 576; Massey v Crown Life Insurance Co [1978] 2 All E.R. 576; O'Kelly v Trust House Forte Plc [1984] QB 90; [1983] ICR 728; Carmichael and another v National Power plc [1999] 4 All ER 897; Express and Echo Publications Ltd v Tanton (1999) CA Transcript of 11 March 1999; MacFarlane and Skivington v Glasgow City Council EAT/1277/99 Transcript of 17 May 2000; O'Murphy v Hewlett-Packard Ltd Employment Tribunals Case 5300148/01 Transcript of 27 March 2001; and R (on the application of Professional Contractors Group Ltd and others) v Inland Revenue Commissioners [2001] STC 629.

Reasons for decision

16. Before considering the arguments of the parties it is convenient first to deal with a point made at the hearing by the Appellant with some force. The Appellant emphasized that people who supplied their services through service companies were not "tax fraudsters". He said that he had run E.B.COM for 14 years; all the money was accounted for in the books and he had paid all his income tax and value added tax. I have much sympathy with these comments. The Appellant, and his wife who assisted him, were honest, frank and open. There is no question in this appeal of any tax fraud. In this appeal the Inland Revenue do not dispute that the service company was run correctly, and that the right amounts of tax were paid, before the changes in the law which were effected by the 2000 Regulations. However, what has to be decided in this appeal is the effect of the changes made by the 2000 Regulations and, in particular, whether the Appellant now comes within the terms of Regulation 6(1)(c) of those Regulations.

The legislation

17. In considering the legislation I start with the 1992 Act. The definitions are in section 2 and the relevant parts provide:

"2(1) In this Part of this Act and Parts 11 to V below-
(a) "employed earner" means a person who is gainfully employed ... either under a contract of service, or in an office ... with emoluments chargeable to income tax under Schedule E; and

(b) "self-employed earner" means a person who is gainfully employed ... otherwise than in an employed earner's employment...."

18. The relevant parts of the new section 4A of the 1992 Act, as inserted by the Welfare Reform and Pensions Act 1999, provide:

"4A(1) Regulations may make provision for securing that where-
(a) an individual ("the worker") personally performs, or is under an obligation personally to perform, services for the purposes of a business carried on by another person (the client),
(b) the performance of those services by the worker is (within the meaning of the regulations) referable to arrangements involving a third person (and not referable to any contract between the client and the worker), and
(c) the circumstances are such that, were the services to be performed by the worker under a contract between him and the client, he would be regarded for the purposes of the applicable provision of the Act as employed in employed earner's employment by the client, relevant payments or benefits are, to the specified extent, to be treated for those purposes as earnings paid to the worker in respect of an employed earner's employment of his."

19. The relevant parts of the 2000 Regulations have already been referred to. To complete the legislative picture a reference should be made to the Social Security Contributions (Transfer of Functions, etc.) Act 1999, which transferred the exercise of certain functions under the 1992 Act to the Board of Inland Revenue, and to Regulation 6(4) of the 2000 Regulations which provides:

"(4) Any issue whether the circumstances are such as are mentioned in paragraph 1(c) is an issue relating to contributions that is prescribed for the purposes of section 8(1)(m) of the Social Security Contributions (Transfer of Functions, etc.) Act 1999 (decision by officer of the Board)."

The issue

20. The issue in the appeal is whether the circumstances were such that, had the arrangements taken the form of a contract between the Appellant and Pennyright Bank, the Appellant would be regarded for the purposes of the 1992 Act as employed in employed earner's employment by Pennyright Bank within the meaning of paragraph 6(1)(c) of the 2000 Regulations. The full text of Regulation 6(1)(c) is;

"(c) the circumstances are such that, had the arrangements taken the form of a contract between the worker and the client, the worker would be regarded for the purposes of Parts I to V of the Contributions and Benefits Act as employed in employed earner's employment by the client."

21. The 1992 Act defines an employed earner as a person who is gainfully employed either under a contract of service, or in an office ... with emoluments chargeable to income tax under Schedule E. As it was not argued that the Appellant was employed in an office, the issue is whether the Appellant would have been gainfully employed under a contract of service if his contract had been with Pennyright Bank and not with E.B.COM.
The authorities and the principles

22. The authorities establish the principle that the question as to whether a person is employed under a contract of service, or whether he is self-employed and provides a contract for services, is a question of fact in each case to be determined having regard to all the relevant circumstances.

23. In Ready Mixed Concrete (South East), Ltd v Minister of Pensions and National Insurance [1968] 2 QB 497 the issue was whether a worker was within the class of employed persons under the National Insurance Act 1965 as being an employed person under a contract of service. At page 515C MacKenna J said:

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

24. At page 515F MacKenna J added:
"Control includes the power of deciding the thing to be done, the way in which it shall be done, the means to be employed in doing it, the time when and the place where it shall be done."

25. MacKenna J then went on to identify a number of factors to be taken into account in deciding whether a contract was a contract of service. These included: whether the contractor hired his own employees; whether the contractor provided and maintained his own tools or equipment; whether the contractor was paid by reference to the volume of work done; whether the contractor had invested in the enterprise and bore the financial risk; whether the contractor had the opportunities of profit or the risk of loss; and whether the relationship was permanent.

26. In Market Investigations Ltd v Minister of Social Security [1968] 2 All E.R.732 Cooke J said that the fundamental test was whether a person performed services as a person in business on his own account. Although control was relevant it was not the sole determining factor; when one was dealing with a professional man, or a man of some particular skill and experience, there could be no question of the employer telling him how to do the work.

27. In Hall v Lorimer [1994] STC 23 the taxpayer was a vision mixer who undertook work for a number of different television production companies and whose engagements consisted of short term contracts lasting one to two days. In four years he worked on over 800 days. The Court of Appeal held that there was no single path to a correct decision. The question whether an individual was in business on his own account might be helpful but might be of little assistance in the case of one carrying on a profession or vocation. Factors which were critical in that appeal were the duration of the particular engagements and the number of people by whom the individual was engaged.

28. McManus v Griffiths (1997) 70 TC 218 established the principle that, in deciding whether a person was employed or self-employed, the task was to try to make legal sense of the arrangements made. Especially where the documents had not been drafted professionally, it was necessary to concentrate on the substance of the contractual arrangements rather then their form or the parties' labels.

29. Applying those principles to the facts of the present appeal I find that a number of factors point to the conclusion that, if the Appellant had been employed under a contract with Pennyright Bank, he would be regarded as gainfully employed under a contact of service. Such factors are:
- The Appellant did agree, in consideration of remuneration, to work a given number of hours a day and to provide his own work and skill to Pennyright Bank. Any absence of the Appellant had to be agreed and approved in advance by Pennyright Bank.
- The Appellant was a man of skill and experience and so it would not be expected that Pennyright Bank would tell him how to do his work; however, the Appellant was managed by a personal manager employed by Pennyright Bank.
- In the performance of his work the Appellant was subject to Pennyright Bank's control inasmuch as the contract provided that it could be ended for incompetence or misconduct and that responsibility for the quality, quantity and performance of the services rested with Pennyright Bank at all times.
- The Appellant did not hire his own employees; the members of his team were either self-employed contractors who had contracted directly with Pennyright Bank or permanent employees of Pennyright Bank.
- The Appellant did not provide and maintain his own tools and equipment; he used the mainframe computer owned by Pennyright Bank.
- The Appellant was not paid by reference to the volume of work done but by reference to the number of hours he worked.
- The Appellant did not invest in any enterprise and he did not bear any financial risk; he had no opportunity of profit and no risk of loss.
- The relationship between the Appellant and Pennyright Bank had an element of permanency as it lasted for seven years.
- The Appellant only provided work for Pennyright Bank and for no other client.
- The Appellant was integrated into the structure of Pennyright Bank to the extent that he worked closely with its employees.

30. On the other hand, some other factors point to the conclusion that, if the Appellant had been employed under a contract with Pennyright Bank, he would not be regarded as being gainfully employed under a contact of service but rather as providing services under a contract for services. Such factors are:

- After incorporating the service company, and before working for Pennyright Bank, the Appellant accepted the consequences of self-employment as he was unable to claim benefits when he was out of work. However, this was a consequence of the fact that his clients contracted with the service company. Under Regulation 6(1)(c) of the 2000 Regulations the assumption has to be made that the arrangements take the form of a contract between the Appellant and Pennyright Bank.

- The agreement between Staff Agency and E.B.COM provided specifically that it did not create the relationship of employer/employee between Pennyright Bank and the Appellant. However, such label given by the parties cannot be conclusive.

- Pennyright Bank was not obliged to pay the Appellant while he was sick or on holiday; the Appellant did not participate in Pennyright Bank's pension scheme nor did he receive private health insurance.

- In theory the Appellant did not enjoy job security as his contract could be terminated on four weeks' notice. However, in practice the Appellant worked for Pennyright Bank continuously for seven years.

- The Appellant did not participate in any management decisions at Pennyright Bank and could not manage permanent employees.

31. Having considered all the relevant factors I conclude that those which point towards there being a contract of service outweigh the factors which point towards there being a contract for services. Concentrating on the substance of the contractual arrangements rather than their form, I therefore conclude that, if the Appellant had been employed under a contract with Pennyright Bank, he would be regarded as being gainfully employed under a contact of service.

Decision

32. My decision on the issue for determination in the appeal is that, if the arrangements had taken the form of a contract between the Appellant and Pennyright Bank, the Appellant would be regarded for the purposes of the 1992 Act as employed in employed earner's employment by Pennyright Bank.

33. The appeal is, therefore, dismissed.

DR NUALA BRICE
SPECIAL COMMISSIONER

FS CONSULTING LTD v PATRICK MCCAUL (HMIT) (2002)

Sp Comm (Dr Nuala Brice) 22/1/2002

TAX - EMPLOYMENT

NATIONAL INSURANCE CONTRIBUTIONS : INDIVIDUAL WORKERS : SERVICE COMPANY : INTERMEDIARIES : ARRANGEMENTS : EMPLOYED EARNER'S EMPLOYMENT : PROVISION OF SERVICES TO CLIENT VIA AGENCY : SOCIAL SECURITY CONTRIBUTIONS AND BENEFITS ACT 1992 : SOCIAL SECURITY CONTRIBUTIONS (INTERMEDIARIES) REGULATIONS 2000 SI 2000/727 : SOCIAL SECURITY (CATEGORISATION OF EARNERS) REGULATIONS 1978 SI 1978/1689

There was nothing to indicate that Reg.6(1)(c) Social Security Contributions (Intermediaries) Regulations 2000 SI 2000/727 did not apply where the arrangements to employ the services of a consultant involved both an intermediary and a non-intermediary.

Anonymised decision on an appeal by the taxpayer ('the appellant') from decisions by the Inland Revenue ('the Revenue') that the circumstances of the arrangements between the appellant's sole employee ('S') and a third party ('Better') for the performance of services by S were such that, had they taken the form of a contract between S and Better, S would be regarded for the purposes of the Social Security Contributions and Benefits Act 1992 as employed in employed earner's employment by Better, with the consequence that the appellant was liable to pay primary and secondary Class I national insurance contributions in respect of S's attributable earnings from that engagement.

S was a computer consultant and the sole director and shareholder of the appellant.

During the relevant periods S supplied his services to the appellant, who supplied them to an agency ('Topper'), who supplied them to Better.

The Revenue contended that the circumstances of those arrangements fell within Reg.6(1)(c) Social Security Contributions (Intermediaries) Regulations 2000 SI 2000/727.

The appellant contended that: (i) "the arrangements" mentioned in Reg.6(1)(b) and (c) were those involving the intermediary (the appellant), but not those involving Topper, which was not an intermediary as defined; (ii) had those arrangements taken the form of a contract between S and Better, S would not be regarded as employed by Better, in particular because under those arrangements Better paid remuneration to Topper rather than to S; and (iii) the arrangements involving Topper were governed by the Social Security (Categorisation of Earners) Regulations 1978 SI 1978/1689, but that under those Regulations S was not treated as falling within the category of an employed earner because he was not subject to supervision, direction or control as to the manner of rendering his services.

HELD: (1) With regard to (i), the legislation was not entirely clear as to its application in relation to the position where the arrangements involved both an intermediary (the appellant) and a non-intermediary (Topper).

However, given that the legislation did not state that it did not apply in such a circumstance, the tribunal considered that the arrangements between the appellant, Topper and Better were within Reg.6(1)(c) of the 2000 Regulations.

(2) Having considered all the relevant factors the tribunal was satisfied that, if S had been employed by Better, he would have been regarded as being employed in employed earner's employment.

(3) It was inappropriate for the tribunal to entertain the appellant's argument as to (iii), since the decisions under appeal had not been made under the 1978 Regulations and that argument concerned both Topper and S, neither of whom was a party to the appeal. Appeal dismissed.

John Antell for the appellant. I B Mitchell (advocacy advisor) of the London Region Advocacy Unit for the respondent.

LTL 18/2/2002 (Unreported elsewhere)

Document No. AC0700386

NATIONAL INSURANCE CONTRIBUTIONS – services of individual provided to client through service company and agency – whether "the arrangements" included the contract with the agency – yes - whether, if the arrangements had taken the form of a contract between the individual and the client, the individual would be regarded as employed – yes – whether the individual fell within the category of employed earner under the 1978 Regulations – appeal dismissed - Social Security Contributions and Benefits Act 1992 Ss 2 and 4A; Social Security (Categorisation of Earners) Regulations 1978 SI 1978 No 1689 Reg 2(2) and Sch 1 Part I Col (A) Item 2(a); Social Security Contributions (Intermediaries) Regulations 2000 SI 2000 No. 727 Reg 6(1)

THE SPECIAL COMMISSIONERS

F.S. CONSULTING LIMITED

Appellant

- and -

PATRICK McCAUL
(HM INSPECTOR OF TAXES)

Respondent

SPECIAL COMMISSIONER : DR NUALA BRICE

Sitting in London on 3 December 2001

John Antell of Counsel for the Appellant

I B Mitchell, Advocacy Adviser of the London Region Advocacy Unit, for the Respondent

ANONYMISED DECISION

The appeal

1. F.S. Consulting Limited (the Appellant) appeals against four decisions made on 21 June 2001 relating to national insurance contributions. The first decision was in the following terms:

> "That the circumstances of the arrangements between Frank Simpson and Better Investments Plc for the performance of services from 6 April 2000 to 30 June 2000 are such that, had they taken the form of a contract between Frank Simpson and Better Investments Plc, Frank Simpson would be regarded for the purposes of Parts I to V of the Social Security (Contributions and Benefits) Act 1992 as employed in employed earner's employment by Better Investments Plc. That F.S. Consulting Limited is treated as liable to pay primary and secondary Class I contributions in respect of the worker's attributable earnings from that engagement."

2. The other three decisions were in the same terms save that the dates mentioned were:

In the second decision -	3 July 2000	to 1 September 2000
In the third decision -	4 September 2000	to 30 November 2000
In the fourth decision -	1 December 2000	to 29 June 2001

The legislation

3. The legislation about the payment of national insurance contributions is contained in The Social Security Contributions and Benefits Act 1992 (the 1992 Act) which contains separate provisions applicable to employed earners on the one hand and self-employed earners on the other. Section 75 of the Welfare Reform and Pensions Act 1999 inserted a new section 4A into the 1992 Act to take effect from 22 December 1999. The relevant parts of section 4A provide:

> **"4A(1) Regulations may make provision for securing that where-**
>
> **(a) an individual ("the worker") personally performs, or is under an obligation personally to perform, services for the purposes of a business carried on by another person (the client),**
>
> **(b) the performance of those services by the worker is (within the meaning of the regulations) referable to arrangements involving a third person (and not referable to any contract between the client and the worker), and**
>
> **(c) the circumstances are such that, were the services to be performed by the**

worker under a contract between him and the client, he would be regarded for the purposes of the applicable provision of the Act as employed in employed earner's employment by the client,

relevant payments or benefits are, to the specified extent, to be treated for those purposes as earnings paid to the worker in respect of an employed earner's employment of his."

4. The Regulations made under the provisions of new section 4A are the Social Security Contributions (Intermediaries) Regulations 2000 SI 2000 No. 727 (the 2000 Regulations) which came into force on 6 April 2000. The relevant parts of Regulation 6 provide:

"6(1) These Regulations apply where-

(a) an individual ("the worker") personally performs, or is under an obligation personally to perform, services for the purposes of a business carried on by another person ("the client"),

(b) the performance of those services by the worker is carried out, not under a contract directly between the client and the worker, but under arrangements involving an intermediary, and

(c) the circumstances are such that, had the arrangements taken the form of a contract between the worker and the client, the worker would be regarded for the purposes of Parts I to V of the Contributions and Benefits Act as employed in employed earner's employment by the client."

The issues

5. Mr Frank Simpson (Mr Simpson) is a computer consultant and the sole director and shareholder of the Appellant. During the relevant time Mr Simpson supplied his services to the Appellant who supplied them to an agency called Topper Recruitment Limited (Topper) who supplied them to Better Investments Plc (Better). It was not disputed that Mr Simpson personally performed services for the purposes of a business carried on by Better within the meaning of section 4A(1)(a) and Regulation 6(1)(a).

6. The Inland Revenue argued that Regulation 6(1)(c) applied. The Appellant argued: first, that "the arrangements" mentioned in Regulation 6(1)(c), and the arrangements mentioned in Regulation 6(1)(b), were those involving the intermediary (the Appellant) but not the arrangements involving Topper who was not an intermediary as defined; secondly that had those arrangements taken the form of a contract between Mr Simpson and Better, Mr Simpson would not be regarded as employed by Better, in particular because under those arrangements Better did not pay remuneration to Mr Simpson but to Topper; and, thirdly, that the arrangements involving Topper were governed by the Social Security (Categorisation of Earners) Regulations 1978 SI 1978 No. 1689 (the 1978 Regulations) but that under those Regulations Mr Simpson was not treated as falling within the category of an employed earner because Mr Simpson was not subject to supervision, direction or control as to the manner of the rendering of his services.

7. It seems to me it would not be proper for me to determine this appeal on the basis of the Appellant's third argument. The decision under appeal is not based on the 1978 Regulations but, more importantly, the third argument does not concern the Appellant in

this appeal (F.S. Consulting Limited) but does concern Topper and Mr Simpson, neither of whom are parties to this appeal. I have therefore identified the first two of the Appellant's arguments as being the issues in the appeal. However, as I heard arguments from the Appellant about the 1978 Regulations I will very briefly express my views.

8. Thus the issues for determination in the appeal are:

(1) whether "the arrangements" mentioned in Regulation 6(1)(c), and the arrangements mentioned in Regulation 6(1)(b), are those involving the intermediary (the Appellant) but not the arrangements involving Topper who was not an intermediary as defined; and

(2) whether, had the arrangements taken the form of a contract between Mr Simpson and Better, Mr Simpson would be regarded as employed in employed earner's employment by Better.

The evidence

9. Oral evidence was given by Mr Simpson on behalf of the Appellant. On 19 November 2001 Mr Simpson signed a written statement of his evidence. An agreed bundle of documents, which contained a copy of Mr Simpson's statement, was produced.

The facts

10. From the evidence before me I find the following facts.

11. The Appellant was incorporated on 21 July 1997 and commenced to trade on 31 August 1997. Its sole director and shareholder is Mr Simpson who is a computer consultant conversion specialist. Mr Simpson's skills are comparatively rare; in evidence which I accept Mr Simpson said that he knew of no more than forty other consultants with his expertise in conversion work.

12. Mr Simpson started working with a major bank in 1987 and trained as a computer programmer. He then became a senior programmer and later was promoted to team leader. In 1997 Mr Simpson left the bank. He personally sent his curriculum vitae to various companies seeking the position of analyst/programmer. Later in 1997 the Appellant was incorporated.

13. The Appellant then arranged through an agency for Mr Simpson to provide services to a building society for three months and then to an insurance company for six months. (Agencies make no initial charge for matching workers to clients but make a profit by entering into contracts with both the worker and the client under which the client pays an hourly rate to the agency and the agency pays a lower hourly rate to the worker). Mr Simpson continued to write personally to other companies seeking positions with them. He wrote from his home address giving the telephone numbers both of his home and of his current place of work.

14. After the initial six months the contract with the insurance company was extended but shortly thereafter the insurance company sold its business. Mr Simpson was given the

four weeks' notice provided for by his contract with the agency and, as a result of the recommendation of some colleagues with whom he had worked at the insurance company, was offered a contract with Better which commenced in December 1998. When that contract was complete Mr Simpson was offered another contract with Better. He continued to provide services to Better until and during the period the subject of the decisions under appeal.

15. The decisions under appeal relate to the period from 6 April 2000 to 29 June 2001. Throughout that time Mr Simpson provided his services to the Appellant, who in turn provided them to the agency Topper, who in turn provided them to Better. Better paid Topper; Topper paid a lesser sum to the Appellant; and the Appellant in turn paid Mr Simpson.

16. A contract was entered into between Topper and the Appellant in April 2000. The contract provided that, for the period mentioned in the schedule, the Appellant would provide an individual to perform consultancy services for a client of Topper; the services were to be performed by the individual named in the schedule but the Appellant might propose a replacement which had to be approved by the client. The services were to be performed at the location specified. The individual had to take all necessary instructions from the client and comply with all the client's rules, regulations and procedures. Travelling time and expenses were the responsibility of the Appellant. The individual had to record the hours worked on a Topper time sheet on a weekly basis and send it to Topper. The contract could be terminated immediately if the client terminated its agreement with Topper because of incompetence, unsuitability or unprofessional conduct by the individual. Otherwise the contract could be terminated by Topper with four weeks' notice. Clause 7 of the contract read:

> "7. It is clearly understood that in no circumstances can this contract be interpreted as a contract of employment and that it is a contract for the supply of services only, however no warranty is given or implied that the assignee is consider by Topper Recruitment to be self-employed."

17. The schedule to the contract of April 2000 was for the thirteen week period from 3 April 2000 to 30 June 2000. It provided that the specified consultant was Mr Simpson; that the client was Better; that the fee rate was £1,839 per week; that the hourly rate was £49.04 per hour (both exclusive of value added tax); that overtime rates were *pro rata*; and that the standard working week was 37.5 hours. The schedule was extended three times. The first extension was in June 2000 and ran for nine weeks from 3 July to 1 September 2000. The second extension was in September 2000 and ran for thirteen weeks from 4 September 2000 to 30 November 2000. And the third extension was in November 2000 and ran from 1 December 2000 to 29 June 2001. These are the periods in the decisions under appeal.

18. During the period under appeal Mr Simpson was working to a design co-written by himself and other consultants during a previous contract with Better. Mr Norman Brown, an employee of Better, was the project manager and the task was to develop systems to convert one information technology system to another. There were seven members in the team, of which five were employees of Better and two (including Mr Simpson) were consultants. Better identified its business requirements and the front end analysis work was done by the employees of Better. This analysis identified the code required and Mr Brown decided when

it was required. Mr Simpson and the other consultant designed the code and were free to design it as they thought fit. The work done by Mr Simpson and the other consultant included: breaking down the work into programs and sub-programs; providing design specifications; coding the programs and sub-programs; unit testing each program and sub-program; testing sections of the suite of programs and sub-programs if thought appropriate; testing the whole suite of programs and sub programs; providing operating instructions to Better on how to run each program and sub-program; and finally handing the suite of programs to Better with the operating instructions. The testing of the code was carried out by the employees of Better. Mr Simpson gave advice on all matters of coding and designing.

19. While working at Better Mr Simpson never acted as team leader and had no job title. He could not decide which employees of Better worked in the team and he could not "hire or fire" them; he could advise the employees but could not instruct them what to do. As project manager Mr Brown controlled what was to be done and when it was to be done but left it to Mr Simpson and the other consultant to determine how it was done. There was very little direction or control by Better over how Mr Simpson did his work. Although normally some quality control checks would be carried out by someone else within a team, I accept the evidence of Mr Simpson that, in practice, there were no quality control checks of his work at Better.

20. The equipment for the work was provided by Better at their site and involved access to a mainframe computer. Better also provided for Mr Simpson at their premises a desk in an open plan office, a telephone, a desk top personal computer and anything else that he needed for his work. Initially Mr Simpson worked at Better's premises, with occasional work at the premises of the Appellant. Later he worked at another of Better's sites as well. Ultimately the first site was closed down and all the work was done at the second site.

21. The actual hours worked by Mr Simpson were flexible. Mr Simpson recorded his time on a time sheet and billed Topper for the time he worked. The time sheet had to be signed by a representative of Better to verify the time worked. All Mr Simpson's work was paid for and none of his invoices remained unpaid. Prior notice of non-attendance was required and permission was also required before leave could be taken. When Mr Simpson wanted to take time off for holidays he told Better in advance and there were no difficulties.

22. The contract between the Appellant and Topper gave the Appellant the right to substitute Mr Simpson with another consultant who had previously provided consultancy of a high standard to Better. In fact, however, the right to substitute another consultant was never used. In evidence which I accept Mr Simpson said that he would only seek to substitute another consultant in certain circumstances, such as at the end of a contract if he had found something better and wanted to give notice or if he were ill for any length of time.

23. Mr Simpson left Better in June 2001 and now works for a building society. Although at the relevant time Mr Simpson was free, as a matter of contract, to undertake work for as many clients as he wished, in practice he only ever worked for one client at a time. The nature of the services he provided attracted large companies with mainframe computers and contracts of three months and over were normal for these clients.

The arguments for the Appellant

24. For the Appellant Mr Antell first argued that the effect of section 2(1)(a) with section 2(2)(b) of the 1992 Act was that it was necessary to find either a contract of service or a regulation which deemed Mr Simpson to be an employed earner. Mr Simpson had no contract of service with Better because: there had been a succession of contracts and there was no foregone conclusion that a contract would be renewed; Mr Simpson decided his own hours and took holidays when he wanted to; Mr Simpson took the risks of invoicing and of having late payments and debts; Mr Simpson received no holiday or sick pay; there was no obligation on Mr Simpson to provide his own personal services; he was not integrated into the team and was not part and parcel of the oganisation of Better; and he had no control over the employees of Better. Mr Antell relied upon *R (on the application of Professional Contractors Group Ltd and others) v Inland Revenue Commissioners* [2001] STC 631 at [48 (iv)] as authority for the view that it was necessary to consider the actual relationship and decide whether any obligation was owed by the client to the service provider. Also, Mr Simpson was not obliged to provide the work personally but could arrange for a substitute.

25. Mr Antell next argued that, in applying the 2000 Regulations, Topper had to be ignored because paragraph 5 provided that where an intermediary was a company the worker had to have a material interest in it; here Mr Simpson did not have a material interest in Topper. He then argued that in this appeal there was no obligation on Better to pay Mr Simpson. Better paid Topper who paid a reduced sum to Mr Simpson. He also relied upon *Montgomery v Johnson Underwood Ltd* [2001] EWCA Civ 318 where the Court of Appeal had applied the dicta of McKenna J in *Ready Mixed Concrete (South East) Limited v Minister of Pensions and National Insurance* [1968] 2 QB 497 at 5151 which dicta identified the need for both the payment of a wage and the provision of work. Here the wage was not paid to Mr Simpson (but to Topper) and Topper had to be ignored.

26. Mr Antell's third argument was that the 1978 Regulations applied to Topper. He argued that the 1978 Regulations could not be ignored as they had been saved by regulation 12 of the 2000 Regulations. He went on to argue that Mr Simpson did not come within the 1978 Regulations. He referred to item 2 in column (A) of Part I of Schedule I to the 1978 Regulations for the test of supervision and control and argued that, although Better had some control over what Mr Simpson did and when, it had no control over the manner of the rendering of his services. He cited *Staples v The Secretary of State for Social Services* (CO/1073/84 15 March 1985 Unreported) as authority for the view that the test of supervision and control in the 1978 Regulations was whether an employee could be told how to do a job and not merely what job to do and that a person with considerable skill was not subject to direction as to how he should do his job.

27. Finally Mr Antell cited *Pepper v Hart* 65 TC 421 and relied upon Inland Revenue Leaflet IR 56 "Employed or Self-employed"; Inland Revenue Press Release PR162/99 "Personal Services Provided through Intermediaries- Preventing Avoidance: Preserving Flexibility" which, he argued, was referred to in Parliament; and Hansard Debates 3 May 2000 Col. 214.

The arguments for the Respondent

28. For the Respondent Mr Mitchell argued that *Pepper v Hart* could only be relied upon if the legislation was ambiguous, obscure or absurd and Regulation 6(1)(c) was quite clear. Within the meaning of that regulation the worker was Mr Simpson and the client was Better. Further, even if *Pepper v Hart* did apply it only permitted reference to Parliamentary material and not to Inland Revenue leaflets or press releases. He cited *McManus v Griffiths* [1997] STC 1089 as authority for the view that it was necessary to concentrate on substance and not form. He distinguished *Professional Contractors Group* on the ground that it concerned European Law and he argued that the evidence supported the view that Better had the complete right of control over the work of Mr Simpson, although the right may not have been exercised in practice. He compared the work done by Mr Simpson with that of a surgeon in the National Health Service, or an electrician, or a pharmacist, or a chemist. Such professional persons were not supervised but were still employees. Further, although there might have been a right of substitution there was in fact no substitution; as the expertise of Mr Simpson was rare it might not be possible to find a suitable substitute. He argued that the 2000 Regulations were silent on the subject of agency workers and that it was necessary to apply the wording of Regulation 6(1)(c).

Reasons for decision

29. In considering the arguments of the parties I have found it convenient first to summarise the legislation and the 2000 Regulations; then to consider each of the issues in the appeal, and finally to look briefly at the 1978 Regulations.

A summary of the legislation

30. The relevant definitions are contained in section 2 of the 1992 Act of which the relevant parts provide:

> **"2(1) In this Part of this Act and Parts II to V below-**
>
> **"employed earner" means a person who is gainfully employed ... either under a contract of service, or in an office ... with emoluments chargeable to income tax under Schedule E; and**
>
> **"self-employed earner" means a person who is gainfully employed ... otherwise than in an employed earner's employment ... .**
>
> **(2) Regulations may provide:**
>
> **(a) for employment of any prescribed description to be disregarded in relation to liability for contributions otherwise arising from employment of that description;**
>
> **(b) for a person in employment of any prescribed description to be treated, for the purposes of this Act, as falling within one or other of the categories of earner defined in subsection (1) above, notwithstanding that he would not fall within that category apart from the regulations."**

31. The 1978 Regulations were made under the provisions of section 2(2) and, so far as relevant in this appeal, provide for some earners to fall within the category of employed earner notwithstanding that the employment is not under a contract of service. The

relevance of the 1978 Regulations is that background to this issue is that Mr Antell, for the Appellant, argued that the 2000 Regulations applied where there was a service company (an intermediary) and that the 1978 Regulations applied where there was an agency. In this appeal there was both a service company and an agency and so the 2000 Regulations applied only to the arrangements with the service company and the 1978 Regulations applied to the arrangements with the agency.

32. In 1999 section 75 of the Welfare Reform and Pensions Act inserted a new section 4A into the 1992 Act to take effect from 22 December 1999. Section 4A is relevant to this appeal and the relevant parts are set out in paragraph 3 of this Decision. The Regulations made under the provisions of new section 4A are the 2000 Regulations which came into force on 6 April 2000. Regulation 6 is relevant in this appeal and the relevant parts of Regulation 6 are set out in paragraph 4 of this Decision. The decision under appeal refers to the provisions of Regulation 6(1)(c) of the 2000 Regulations which defines the issues in this appeal.

Issue (1) – Do "the arrangements" include those with Topper?

33. The first issue is whether "the arrangements" mentioned in Regulation 6(1)(c), and the arrangements mentioned in Regulation 6(1)(b), are those involving an intermediary (the Appellant) but not the arrangements involving Topper who was not an intermediary as defined.

34. Regulation 6(1)(c) refers to "the arrangements" and "the arrangements" are mentioned in Regulation 6(1)(b) as "arrangements involving an intermediary". The meaning of intermediary is set out in Regulation 5 of the 2000 Regulations which provides:

> **"5(1) In these Regulations "intermediary" means any person ... -**
> **(a) whose relationship with the worker in any tax year satisfies the conditions specified in paragraph (2), (6), (7) or (8), and**
> **(b) from whom the worker ....**
> **(i) receives, directly or indirectly in that year a payment or benefit that is not chargeable to tax under Schedule E, or**
> **(ii) is entitled to receive ... directly or indirectly, in that year any such payment or benefit.**
>
> **(2) Where the intermediary is a company the conditions are that:**
> **(a) the intermediary is not an associated company of the client ...; and**
> **(b) either-**
> **(i) the worker has a material interest in the intermediary, or**
> **(ii) the payment or benefit is received or receivable by the worker directly from the intermediary and can reasonably be taken to represent remuneration for services provided by the worker to the client."**

35. Topper is a company but it is not an associated company of Better; Mr Simpson has no material interest in Topper; and the payments were not received by Mr Simpson directly from Topper, although they were so received indirectly through the Appellant. For this reason I conclude that Topper is not an intermediary as defined by Regulation 5. The Appellant did not dispute that it was an intermediary as defined in Regulation 5.

36. The question, therefore, is whether "the arrangements" mentioned in Regulation 6(1)(c), and the arrangements mentioned in Regulation 6(1)(b), are those involving the

worker (Mr Simpson), the client (Better) and the intermediary (the Appellant) only and not the arrangements involving the non-intermediary (Topper).

37. To answer that question I look again at the wording of Regulation 6(1)(b). Applying Regulation 6(1)(b) to the facts of the present appeal the performance of the services by the worker (Mr Simpson) was carried out, not under a contract directly between the client (Better) and the worker (Mr Simpson) but under arrangements which involved an intermediary (the Appellant). The arrangements also involved a non-intermediary (Topper) but it seems to me that that fact does not prevent Regulation 6(1)(b) from applying in this appeal. It seems to me that the phrase "arrangements involving an intermediary" is wide enough to include arrangements involving both an intermediary and a non-intermediary; the phrase is not "arrangements with an intermediary" which would exclude arrangements with a non-intermediary.

38. As I do not find this interpretation of Regulation 6(1)(b) to be free from ambiguity I have consulted the non-statutory material referred to by Mr Antell. Neither the leaflet or the press release is Parliamentary material and so they do not come within the rule in *Pepper v Hart*. The press release says that the purpose of the Regulations is to remove opportunities for the avoidance of Class 1 contributions by the use of intermediaries such as service companies in circumstances where an individual worker would otherwise be an employee of the client. The rules would apply in the same way as they apply to individuals who operate without intermediaries. The leaflet describes the rules applicable to employment and self-employment and summarises certain special rules including work arranged through an agency. There is, however, nothing in either which states that the arrangements in Regulation 6(1)(b) do not include arrangements with a non-intermediary if there is an intermediary.

39. The Hansard Debates for 3 May 2000 are Parliamentary material. In the passage at Col 214, relied upon by Mr Antell, Dawn Primarolo said:

> "We are not talking about all service companies or IT contractors. The new rules will apply to people in service companies who would be employees of their clients if the service company did not exist. The usual case law tests will be used to determine whether someone would be an employee."

40. I do not read that passage as a clear and unequivocal statement that the arrangements in Regulation 6(1)(b) do not include arrangements with a non-intermediary if there is an intermediary.

41. I do not find this particular point to be entirely clear. However, it seems to me that the primary purpose of the 2000 Regulations is to consider the contract between the individual and the client in cases where there is a service company (an intermediary). There is no indication in the Regulations that that primary purpose does not apply in cases where, as well as there being an intermediary, there is also a non-intermediary. Accordingly, I conclude that when applying Regulation 6(1)(c) I have to decide whether the circumstances were such that, had the arrangements (involving the intermediary (the Appellant) but also involving a non-intermediary (Topper)) taken the form of a contract between the worker (Mr Simpson) and the client (Better) the worker (Mr Simpson) would be regarded as employed in employed earner's employment by the client (Better). This means that although

Better paid Topper, and not the Appellant or Mr Simpson, the payment of the remuneration is still part of the arrangements which require to be considered.

42. I have reached this view on the wording of Regulation 6 of the 2000 Regulations but the view is confirmed by a reference to the provisions of section 4A (the enabling section under which the 2000 Regulations are made). Section 4A(1)(b) provides for the performance of the services by the worker to be referable to arrangements involving a third person and not referable to a contract between the client and the worker.

43. My conclusion on the first issue is that "the arrangements" mentioned in Regulation 6(1)(c), and the arrangements mentioned in Regulation 6(1)(b), are those involving both the intermediary (the Appellant) and the arrangements involving Topper who was not an intermediary as defined.

Issue (2) - Would Mr Simpson be regarded as employed by Better?

44. The second issue is whether, had the arrangements taken the form of a contract between Mr Simpson and Better, Mr Simpson would be regarded as employed in employed earner's employment by Better.

45. The authorities establish the principle that the question as to whether a person is employed under a contract of service, or whether he is self-employed and provides a contract for services, is a question of fact in each case to be determined having regard to all the relevant circumstances.

46. In *Ready Mixed Concrete (South East), Ltd v Minister of Pensions and National Insurance* [1968] 2 QB 497 the issue was whether a worker was within the class of employed persons under the National Insurance Act 1965 as being an employed person under a contract of service. At page 515C MacKenna J said:

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

47. At page 515F MacKenna J added:

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

48. MacKenna J then went on to identify a number of factors to be taken into account in deciding whether a contract was a contract of service. These included: whether the contractor hired his own employees; whether the contractor provided and maintained his own tools or equipment; whether the contractor was paid by reference to the volume of work done; whether the contractor had invested in the enterprise and bore the financial risk;

whether the contractor had the opportunities of profit or the risk of loss; and whether the relationship was permanent.

49. In *Market Investigations Ltd v Minister of Social Security* [1968] 2 All E.R.732 Cooke J said that the fundamental test was whether a person performed services as a person in business on his own account. Although control was relevant it was not the sole determining factor; when one was dealing with a professional man, or a man of some particular skill and experience, there could be no question of the employer telling him how to do the work.

50. In *Hall v Lorimer* [1994] STC 23 the taxpayer was a vision mixer who undertook work for a number of different television production companies and whose engagements consisted of short term contracts lasting one to two days. In four years he worked on over 800 days. The Court of Appeal held that there was no single path to a correct decision. The question whether an individual was in business on his own account might be helpful but might be of little assistance in the case of one carrying on a profession or vocation. Factors which were critical in that appeal were the duration of the particular engagements and the number of people by whom the individual was engaged.

51. *McManus v Griffiths* (1997) 70 TC 218 established the principle that, in deciding whether a person was employed or self-employed, the task was to try to make legal sense of the arrangements made. Especially where the documents had not been drafted professionally, it was necessary to concentrate on the substance of the contractual arrangements rather then their form or the parties' labels.

52. Applying those principles to the facts of the present appeal I find that a number of factors point to the conclusion that, if Mr Simpson had been employed under a contract with Better, he would be regarded as gainfully employed under a contact of service. Such factors are:

- Mr Simpson did agree, in consideration of remuneration, to provide his own work and skill to Better and it was also part of the arrangements that the standard working week was 37.5 hours. Any absence of Mr Simpson had to be agreed and approved in advance by Better (although in fact there were no difficulties).

- Mr Simpson was a man of skill and experience and so it would not be expected that Better would tell him how to do his work; however, Mr Simpson was part of a team made up mainly of employees of Better and of which the project manager was an employee of Better. The project manager controlled what was to be done and when it was to be done although he left it to Mr Simpson to decide how it should be done. Also, the contract between the Appellant and Topper provided that Mr Simpson had to take all necessary instructions from Better and comply with Better's rules, regulations and procedures.

- In the performance of his work Mr Simpson was also subject to Better's control to the extent that the contract between the Appellant and Topper provided that it could be terminated immediately if Better terminated its agreement with Topper because of the incompetence, unsuitability or unprofessional conduct of Mr Simpson.

- Mr Simpson did not hire his own employees; the members of his team were mainly permanent employees of Better and one other consultant who had entered into his own contract with Better.

- Mr Simpson did not provide and maintain his own tools and equipment; he used the mainframe computer and other equipment provided by Better.

- Mr Simpson was not paid by reference to the volume of work done but by reference to the number of hours he worked.

- Mr Simpson did not invest in any enterprise and he did not bear any financial risk; he had no opportunity of profit and no risk of loss. All his invoices were paid.

- The relationship between Mr Simpson and Better had some element of permanency as it lasted for two and a half years from December 1998 to June 2001.

- While working for Better Mr Simpson only provided work for Better and for no other client. Before working for Better he worked for two other clients and since leaving Better he has worked for one other client but has never worked for more than one client at a time.

- Mr Simpson was integrated into the structure of Better to the extent that he worked closely with its employees; also the project manager was an employee. .

53. On the other hand, some other factors point to the conclusion that, if Mr Simpson had been employed under a contract with Better he would not be regarded as being gainfully employed under a contact of service but rather as providing services under a contract for services. Such factors are:

- The agreement between the Appellant and Topper provided specifically that it was not a contract of employment and was a contract for the supply of services only. However, such label given by the parties cannot be conclusive. Also it is significant that that contract was between the Appellant and Topper whereas regulation 6(1)(c) of the 2000 Regulations provides that it is the notional contract between Mr Simpson (the worker) and Better (the client) which is relevant.

- Better was not obliged to pay Mr Simpson while he was sick or on holiday;

- In theory Mr Simpson did not enjoy job security as the Appellant's contract with Topper could be terminated on four weeks' notice. However, in practice Mr Simpson worked for Better continuously for two and a half years.

- Mr Simpson was not part of the management at Better and did not

manage permanent employees of Better.

- The Appellant had the right to propose a replacement to substitute for Mr Simpson which replacement had to be another consultant who had previously supplied consultancy services to Better and had to be approved by Better. However, the right of substitution was never used.

- There was very little direction or control by Better over how Mr Simpson did his work and there were no quality control checks. On the other hand Mr Simpson was a man of skill and experience and it would not be expected that Better would tell him how to do his work.

54. Having considered all the relevant factors I conclude that those which point towards there being a contract of service outweigh the factors which point towards there being a contract for services. Concentrating on the substance of the contractual arrangements rather than their form, I therefore conclude that, if Mr Simpson had been employed under a contract with Better he would be regarded as being employed in employed earner's employment by Better.

The 1978 Regulations

55. I finally express very brief views about the arguments put forward by the Appellant about the 1978 Regulations. The 1992 Act was a Consolidating Act and its predecessor was the Social Security Act 1975 (the 1975 Act). Under the provisions of the 1975 Act, which corresponded to section 2 of the 1992 Act, the 1978 Regulations were made. Regulation 2 provided for the treatment of earners in one category as falling within another category and for the disregard of certain employments. Regulation 2(2) was relied upon by the Appellant and the relevant part provides:

> **"(2) ...every earner shall, in respect of any employment described in any paragraph in column (A) of Part I of Schedule I to these regulations, be treated as falling within the category of an employed earner in so far as he is gainfully employed in such employment and is not a person specified in the corresponding paragraph in column (B) of that Part, notwithstanding that the employment is not under a contract of service, or in an office (including elective office) with emoluments chargeable to income tax under Schedule E."**

56. Thus the effect of regulation 2(2) is that every earner described in column (A) of Part I of Schedule I is treated as an employed earner notwithstanding that the employment is not under a contract of service.

57. Column (A) of Schedule 1 of the 1978 Regulations lists employments in respect of which earners are to be treated as falling within the category of employed earner. Item 2 of Column (A) reads:

> **"2. Employment ... in which the person employed renders, or is under obligation to render, personal service and is subject to supervision, direction or control, or to the right of supervision, direction or control, as to the manner of the rendering of such service and where the person employed is supplied by or through some third person ... and-**
>
> > **(a) where earnings for such service are paid by or through, or on the basis of accounts submitted by, that third person or in accordance with arrangements made with that third person ... ."**

58. The effect of paragraph 2 of Column (A) is that workers supplied through a third person, (normally agency workers) are treated as employed earners if they render personal services and are subject to supervision direction or control, or to the right of supervision, direction and control as to the manner of rendering the service.

59. If I had to express a view on whether Mr Simpson came within the terms of the 1978 Regulations I would be bound by the decision in *Staples*. That case concerned a head chef and Glidewell J held that he was not subject to supervision, direction or control as to the manner of rendering his services within the meaning of the 1978 Regulations as he was not a person who was subject to direction by management as to how he should do his job. In this appeal Better could specify to Mr Simpson what had to be done and the time in which it had to be done but could not specify how it was to be done. On the other hand Mr Simpson was part of a project team of which the leader was employed by Better. I would not find this matter to be without difficulty but on balance would conclude that Mr Simpson was not subject to supervision, direction or control as to the manner of rendering his services.

60. I agree with Mr Antell that the 1978 Regulations remain in existence as Regulation 12 of the 2000 Regulations provides that nothing in the 2000 Regulations affects the operation of regulation 2 of the 1978 Regulations as that regulation applies to employment listed in paragraph 2 in column (A) of Part I of Schedule I. However, in my view, as the 2000 Regulations save the 1978 Regulations, both Regulations are effective and a decision can be reached on either or both Regulations. The decision in issue in this appeal was reached under Regulation 6(1)(c) of the 2000 Regulations.

Decision

61. My decisions on the issues for determination in the appeal are:

(1) that "the arrangements" mentioned in Regulation 6(1)(c) and the arrangements mentioned in Regulation 6(1)(b) are those involving both the intermediary (the Appellant) and the non-intermediary (Topper); and

(2) that, had the arrangements taken the form of a contract between Mr Simpson and Better, Mr Simpson would be regarded as employed in employed earner's employment by Better.

62. The appeal is, therefore, dismissed.

Nuala Brice

DR NUALA BRICE

SPECIAL COMMISSIONER

22 JAN 2002

LIME-IT LTD v THE COMMISSIONERS OF INLAND REVENUE (2002)

Sp Comm (JF Avery Jones) 17/10/2002

TAX - AGENCY - INSURANCE

The appellant IT company was not liable to pay primary and secondary Class 1 national insurance contributions in respect of earnings by its director for a client under a contract between the appellant and an agent of the client. Had the worker contracted directly with the client, she would not have been employed under a contract of service.

Appeal from the respondent's decision that the appellant ('Lime') was liable to pay primary and secondary Class 1 national insurance contributions in respect of certain earnings by F, the sole shareholder and director of Lime.

Lime was an IT company that, among other things, provided computer support services.

Lime contracted with an agent that provided expert help and assistance to "end-users", to provide support services to an end-user ('Marconi').

It was common ground that: (i) reg.6(1)(a) Social Security Contributions (Intermediaries) Regulations 2000 SI 2000/727 was satisfied as F had personally provided those services; and (ii) reg.6(1)(b) was satisfied as Lime was an intermediary involved in arranging the performance of those services.

On appeal, the issue was whether reg.6(1)(c) was satisfied, that is, whether F would have been regarded as employed under a contract of employment if the arrangements had taken the form of a contract between F and Marconi.

HELD: (1) The pointers against the contract being a contract of service if the contract was between F and Marconi were that:

(a) Marconi contracted for particular projects and the end-date and number of hours were estimates of the time needed for completion of those projects;

(b) F did not work a regular pattern of hours, her hours were dictated by the requirements of the work;

(c) Lime could not be required to work outside the specification;

(d) although it was not obliged to do so, Lime purchased a laptop computer specially for use in the job;

(e) payment terms were 30 days after invoice and Lime suffered delays in payment;

(f) Lime had the right to substitute an alternative supplier;

(g) F did not work alongside any Marconi employees as part of the Marconi organisation; and

(h) during the Marconi contract, Lime operated as a normal small business with its own office working for four other clients.

(2) In essence, Marconi was contracting for a particular IT job from a small business in the way one would expect an IT consultant to be engaged.

On the hypothesis that F had contracted directly with Marconi, she would not have been employed under a contract of service, she would have been in business on her own account.

(3) (Obiter) In future cases on the legislation, Special Commissioners would wish to explore at a preliminary hearing whether it was possible to obtain evidence from the client. Appeal allowed.

David Smith of Accountax Consulting Ltd for Lime-IT. Barry Williams of London Regional Advocacy Unit for the respondents.

(2003) STC (SCD) 15

Document No. AC0302039

NATIONAL INSURANCE CONTRIBUTIONS – intermediary ("IR 35") – whether worker would be employee if there were a contract between the worker and the client – no

THE SPECIAL COMMISSIONERS

LIME-IT LIMITED - Appellant

- and -

THE COMMISSIONERS OF INLAND REVENUE - Respondents

Special Commissioner: DR JOHN F AVERY JONES CBE

Sitting in London on 2 October 2002

David Smith, Accountax Consulting Limited, for the Appellant

Barry Williams, London Region Advocacy Unit, for the Respondents

DECISION

1. This is an appeal against a Notice of Decision dated 11 February 2002 that the Appellant is liable to pay primary and secondary Class 1 National Insurance contributions in respect of Miss Lisa Fernley's earnings in respect of a particular contract under what has become known as the "IR35" legislation. The Appellant was represented by Mr David Smith of Accountax Consulting Limited, and the Commissioners of Inland Revenue by Mr Barry Williams.
2. In outline, Miss Lisa Fernley is the sole shareholder and director of the Appellant company, a new IT company formed on 4 April 2000 providing services and in connection therewith supplying both hardware and software. The Appellant's brochure describes the services it offers as: "IT solution design, implementation and support; IT support services; networking services; system tuning and optimisation; web design services; hardware and software sales." On 17 April 2000 (although the signature page indicates that it was executed by the parties on 2 and 8 May 2000 respectively) the Appellant contracted with Executive

Recruitment Services plc (ERS), an agent providing expert help and assistance to "End-users", the contract naming Alenia Marconi Systems (Marconi) as the End-user. The issue is whether, if the Appellant and ERS had not existed so that there was a direct relationship between Miss Fernley and Marconi, she would be an employee.

3. I heard evidence from Miss Fernley, and also from two officers of the Inland Revenue who had been concerned with the case, Mrs Wenn and Mr Justin. The Appellant, as appears from the correspondence, was unhappy with the Revenue's handling of the case and Mr Justin produced a lengthy note saying that he was not happy either with the way the case had been handled, and, with the guidance currently available, he would have tackled the situation differently, for which he apologised to the Appellant. In particular when he gave his initial opinion that IR 35 applied he was working on new unpopular legislation before Royal Assent finding himself swamped with work and operating under guidance that then concentrated on the documents without suggesting that he should have a meeting with, or obtain more information from, the Appellant and the End-user. Since the Appellant has been critical of the Revenue I should also record that when later the Revenue asked to meet Miss Fernley she refused the request. I appreciate Mr Justin's frankness in preparing this note, as I am sure the Appellant does, but his handling of the case is not ultimately relevant to the decision I have to make.
4. Schedule 1 to the contract between the Appellant and ERS describes the work as follows:

   "The project: to organise and manage PC desktop support within AMS Dynamics Division using a combination of permanent staff and contract resources to achieve measured improvements in quality of service and service level and report weekly to the end user on progress.

   Manage planning, implementation and migration to Microsoft Exchange email system

   Plan and implement remote access solution for mobile users.

   Produce research and plan for migration to Microsoft Windows 2000

   Site of Supply: Borehamwod/Stanmore or such other sites of the Client [not a defined expression but obviously referring to Marconi] or the Supplier [the Appellant] as may be agreed as expedient from time to time for performance of the Services."

   Schedule 2, headed "Term of Supply", is as follows:

   "Term of Supply from 10 April 2000 to 10 April 2001 (estimated date for completion of the project) or such alternate date as may be agreed from time to time by the parties as the date of completion of the project (end date) subject to the termination provisions in clause 4 [which should be clause 3, permitting termination on reasonable notice in various circumstances and on breach of the contract].

   1. The Agent [ERS] will pay the Supplier a fee at the rate of [the figures have been blanked out in my copy] per hour (plus VAT where applicable) [] per hour for overtime.

2. The Supplier shall provide the required services for 37 hours per week being the estimated number of hours per week for completion of the project within the contract term or such hours as are reasonably requested by the Client for the project.

3. Payment will be made against the Agent's timesheets which have been authorised by the Client, together with the Supplier's invoice."

5. Thus the work is for specific projects, such as organising and managing (rather than providing) a computer support function, introducing a new email system, organising remote access, and changing to Windows 2000. These projects were expected to take one year with the Appellant (meaning Miss Fernley as the only employee) working an estimated 37 hours per week at an hourly rate, but the contract would end on completion of the project.
6. Another relevant term of the contract is that there was a right of substitution that Miss Fernley negotiated and was not included as a standard condition, which is demonstrated by the reference to "Client" whereas the rest of the contract refers to the "End-user".

"In the event that the Supplier finds itself unable to provide the whole or any part of the Specified Services for whatever reason, the Supplier shall offer the Client a substitute ("the Substitute Supplier") of equivalent expertise to work in the Supplier's place. The Client has the right to refuse to accept the Substitute Supplier on any reasonable grounds. If the Client finds the Substitute Supplier acceptable, the Supplier shall provide an overlap period of up to (ten) working days during which time the Supplier shall ensure that the Substitute Supplier fully understands the requirements of the Client and progress made in providing the Specified Services. The Supplier shall not charge the Client any extra sum for this overlap period. Thereafter, the Supplier shall continue to invoice the Client and shall be responsible for the payments and expenses of the Substitute Supplier. In the event that the Supplier cannot provide an acceptable Substitute Supplier, the Client is entitled to terminate this Agreement forthwith."

The drafting shows that considerable thought went into this clause, for example the Appellant being obliged to provide free overlap time. This is a right for the Appellant to substitute another person in place of the Appellant rather than a right for Miss Fernley to substitute another employee of the Appellant for herself. That contract contemplates that various employees work on the contract and it contains provisions in clause 4 for ERS to specify in advance to the End-user the number, qualification and experience, and rate of payment of the personnel. I presume that Marconi fixed the hourly rate on the basis that Miss Fernley would do all the work herself. This would explain the reference to her name in the purchase order (see paragraph 7 below). I am therefore doubtful whether another employee of the Appellant could be used without Marconi's agreement, although the right to substitute another supplier of "equivalent expertise" for the Appellant existed, subject to Marconi's right to refuse to accept the substitute on reasonable grounds. In fact this right of substitution was never exercised and Miss Fernley did all the work personally. Another term of the contract is that the End-user was not entitled to direct the Appellant to perform any task other than that identified or implicit in the specification.

7. The only evidence of the contract between ERS and Marconi is a purchase order dated 8 May 2000 (the date on which ERS signed the agreement with the Appellant) which stated "To supply the services of Lisa Fernely (sic) for the period 10/4/00 until 6/4/01 [note that the other contract specifies 10 April 2001 as the expected termination date]." The hourly and overtime rate is then stated. Miss Fernley had not seen this document at the time. It was obtained by the Revenue from Marconi and a copy provided to her by ERS was only later seen by her. The contract between the Appellant and ERS contains the provision "The Agent [ERS] shall conclude an agreement with each End-user to whom Supplier's [the Appellant] details are sent which reflects the terms of this Agreement." In the absence of any evidence from Marconi I shall presume that this provision was carried out and that the ERS-Marconi contract was on the same terms as the Appellant-ERS contract. Accordingly, giving effect to both contracts, I shall assume that, although the ERS-Marconi contract required Miss Fernley's services in accordance with the wording on the purchase order as the hourly rate was based on her dong the work, Marconi were bound by the clause allowing substitution of another person of equivalent expertise with the benefit of the arrangements for a hand-over period, subject to their right to refuse to accept the substitute on reasonable grounds.
8. Marconi terminated the contract without notice on 3 April 2001, a few days before it was due to terminate, which, as I am assuming that the ERS-Marconi contract conforms to the Appellant-ERS contract, was on 10 April 2001. Miss Fernley said that there had been no disagreement with Marconi but she understood that they had outsourced the whole of their IT function and so the Appellant's services were no longer required. This came as a surprise as she had been in process of negotiating a further year's contract for a further specific project.
9. Regulation 6(1) of the Social Security Contributions (Intermediaries) Regulations 2000, made under sections 75 and 76 of the Welfare Reform and Pensions Act 1999 and the Social Security Contributions (Intermediaries) Regulations 2000, provides:

> "These Regulations apply where—
>
> a. an individual ("the worker") personally performs, or is under an obligation personally to perform, services for the purposes of a business carried on by another person ("the client"),
> b. the performance of those services by the worker is carried out, not under a contract directly between the client and the worker, but under arrangements involving an intermediary, and
> c. the circumstances are such that, had the arrangements taken the form of a contract between the worker and the client, the worker would be regarded for the purposes of Parts I to V of the Contributions and Benefits Act [the Social Security Contributions and Benefits Act 1992] as employed in employed earner's employment by the client."

"Intermediary" is defined in Regulation 5 and it is common ground that the Appellant is an intermediary for this purpose. "Employed earner's employment" is defined in section 2(1) of the Social Security Contributions

and Benefits Act 1992 to include a person who is gainfully employed under a contract of service (which is not further defined).

10. Paragraph (a) of Regulation 6(1) is satisfied; Miss Fernley did in fact personally perform services for the purposes of a business carried on by Marconi. Paragraph (b) is also satisfied; the intermediary is the Appellant. The real issue in the case is paragraph (c) which requires one to ask whether, had the arrangements taken the form of a contract between Miss Fernley and Marconi, she would be regarded as employed under a contract of service. In other words, one ignores for this purpose the existence of the Appellant (and ERS) and concentrates on what is actually done by Miss Fernley for Marconi in accordance with the arrangements made with the other parties. I heard evidence from Miss Fernley but no evidence was called from Marconi. Miss Fernley explained that as they had outsourced their entire IT work there was now nobody there who could speak to what was actually done while the Appellant was working for them. While I fully understand the difficulty the Appellant faced, it would have been very helpful if the former IT Manager could have been a witness so that I could have heard from both parties to the hypothetical contract. In future cases on this legislation (and its income tax equivalent) the Special Commissioners will wish to explore at a preliminary hearing whether it is possible to obtain evidence from the client.
11. Miss Fernley gave evidence, all of which I accepted, that the Appellant was then a new small business with no other employees. There is now one employee. It has its own web-site and markets its services to local businesses. During the Marconi contract the Appellant worked for 4 other clients. Miss Fernley worked at one of Marconi's offices, and partly from her office at her home where there is a room containing four computers dedicated to the Appellant's business. The Appellant paid for any travel between Marconi sites. She was left to do the Marconi job on her own, reporting weekly informally on progress to the IT manager. She did not work alongside Marconi employees; there were no Marconi employees doing her type of work and nobody with her type of expertise. Nobody told her how to do the job and nobody controlled her work, other than no doubt checking her time sheets. She did not work a regular 37 hour week as envisaged by the contract; her work varied from nothing to 52.5 hours in a week with considerable variations from week to week. For example, the number of hours worked in consecutive weeks in May and June 2000 were 49.5, 28, 44.5, 20.5, 52.5, 33.5, 0 hours. She worked the hours needed to get the job done. She described this variation of hourly figures as typical of the pattern during the contract. She was not treated as a member of Marconi's staff. She had a security pass but it named the Appellant and said "contractor" on it and it was a different colour from the employees' passes. The Appellant (not Miss Fernley) was listed in Marconi's internal telephone directory, and she had an email address there. She did not benefit from other usual employee benefits such as holiday pay, sickness pay or the use of sports facilities. The Appellant purchased a lap-top computer with the same specification as those used by Marconi costing £1,600 specially for the job, but there was no contractual obligation on it to do so. The Appellant invoiced monthly at the hourly rate with payment due in 30 days. On at least one occasion the Appellant had difficulty in being paid. Miss Fernley wrote to ERS on 24 April 2001 reminding them about two overdue invoices for a total of £6,563.84. On 24 May 2001 she wrote again threatening to sue for the debt plus interest, listing the two invoices as both being dated 6 April 2001 and stated to be due for payment on 16 April (I am not clear why as both contracts say 30 days, but this may have been varied). She wrote

again on 5 June, which was two months after the date of the invoice. The invoices were finally settled with interest.

12. The case law test of whether someone has a contract of service is difficult. It is even more difficult to apply the case law to a hypothetical contract. I am unclear about the extent of applying the hypothesis in relation to other work. On the face of it the hypothesis does not apply to other work performed by the intermediary, but in determining whether the hypothetical contract is an employment contract one needs to take into account other work done by the worker, which will actually be performed by the intermediary perhaps partly by other workers. I understood Mr Williams to contend that other work should not be taken into account. Fortunately in view of my findings in relation to the contract in isolation I do not need to pursue this aspect in this case. Mr Williams made clear that the Revenue accepted the genuineness of the Appellant's business, and that the Appellant was not avoiding National Insurance contributions by rewarding Miss Fernley by dividends; this case was purely concerned with applying the legislation to a hypothetical contract. The basic test of whether someone is employed or self-employed is to ask whether a person is "in business on his own account" (*Market Investigations v Minister of Social Security* [1968] 3 All ER 732). In *Ready Mixed Concrete (South East) Ltd v Minister of Pensions and National Insurance* [1968] 2 QB 497, 498 D MacKenna J listed three conditions for a contract of service to exist:

    "(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 a sufficient degree to make that other master, (iii) the other provisions of the contract are consistent with its being a contract of service."

13. A number of different factors for helping to determine this have been developed by the courts to determine whether a contract of service exists, as follows (I have not stated the authority for each one as they are well-known and were accepted by both parties):

    Control. Mr Smith contended that there was no control by Marconi as to the manner in which Miss Fernley carried out her activities. Mr Williams contended that control was not an important test where experts are concerned. The way the work was performed was that Miss Fernley planned the projects herself and then communicated the plan to Marconi. In addition if their server broke down she would need to go immediately to the premises where it was and fix it. She reported on progress informally to the IT Manager weekly. He was the person who checked that Marconi was getting value from the contract. She managed to fit in work for the Appellant's other clients when her presence was not required at Marconi by the nature of the project, informing the IT manager of her movements so that she could be contacted if necessary. The contract provides that the Appellant could not be required to perform any task other than those identified or implicit in the specification. I accept Miss Fernley's evidence that Marconi did not exercise any significant control as to the manner in which she carried out her activities, but, as Mr Williams contended, control may not be particularly important when one is dealing with an expert.

    Financial risk and ability to profit. Mr Smith pointed to the contractual limit of liability of £1m in the contract between the Appellant and ERS as showing that there was significant financial risk. Mr Williams pointed to the

fact that the work was charged at an hourly rate with overtime at a higher rate, as one expects for an employee. The only way for the Appellant to make more profit would be for more hours to be worked, which is exactly the same for an employee doing overtime. An hourly rate is indicative of employment, much more so than a fixed price contract, but there are self-employed who charge at an hourly rate. Mr Williams accepted the existence of the bad debt risk but said that employees also had to accept the risk of the employer's insolvency. There were some serious delays in payment of invoices, over two months delay on one occasion. The fact of invoicing and the 30 day (or even 10 day, if that is what was subsequently agreed) terms for payment, even ignoring the actual delays in payment, seem to me to point to self-employment. I presume that Marconi (assuming that they were responsible for the delays) did not keep its employees waiting for their salary. I do not think that the limit of liability in the contract is particularly important; employees, such as employed doctors, can incur liability too and are required to carry insurance.

Provision of equipment. Mr Smith points to the lap-top computer which the Appellant purchased for the Marconi job. Mr Williams said that there was no contractual obligation to provide this, and pointed to the desk and telephone she had at Marconi as slight indicators of employment. Miss Fernley said that it was more convenient to use her own computer equipment. It would be normal for her to down-load files from the lap-top to computers at Marconi. This factor does seem to me to point to self-employment. An employee does not normally provide a lap-top but a self-employed person may do so if it makes the work easier to do, regardless of any contractual requirement. I do not regard the provision of a desk and telephone at Marconi as particularly significant. The Appellant has an office including four computers at Miss Fernley's home.

Right to substitute. Mr Smith relied heavily on this provision. Although the right was never exercised it is not a provision which can be described as a sham. It was negotiated specifically at the Appellant's request. Although I did not have any evidence from Marconi there is no reason to suppose that they would not have been willing to pay the same rate for a substitute of "equivalent expertise" as the contract requires. Indeed it was very much in their interest that the Appellant would provide a free overlap period to inform the substitute about the state of the work. It seems to me that in the hypothetical contract with Miss Fernley, Marconi must be taken to have the benefit and burden of this provision. It is a strong indicator of self-employment. Indeed in *Express and Echo Publications Ltd v Tanton* (unreported 11 March 1999) the Court of Appeal held that where a person is not required to perform the work personally, as a matter of law the relationship could not be one of employment:

"…it is, in my judgment, established on the authorities that where, as here, a person who works for another is not required to perform his services personally, then as a matter of law the relationship between the worker and the person for whom he works is not that of employee and employer."

Mutuality of obligation. Mr Williams pointed to the difficulty of applying this test to a hypothetical contract. It seems to me that Marconi could require Miss Fernley to work 37 hours per week or for such hours as are reasonably requested and she could require payment for such work.

Personal factors. This test takes into account the number of separate engagements the person holds. *Hall v Lorimer* 66 TC 349 was concerned with numerous short-term engagements. Mr Williams contended that a series of short-term engagements which individually might have the appearance of employment might amount in total to self-employment He suggested that the longer the contract the less relevant are personal factors in determining status, and this was a one-year contract. But he recognised that an astute businessman may work for one favoured client because it was commercially advantageous to do so. It seems to me that the length of the contract is a slight pointer to employment.

Basis of payment, holiday and sick pay. Mr Williams contended that the obligation to work 37 hours a week pointed to an employment relationship. This is the normal working week for Marconi employees. There is no right to holiday or sick pay. Travel between Marconi's different locations was paid for by the Appellant and not reimbursed, as one would expect it to be for an employee. In practice Miss Fernley did not work a 37 hour week. The variations in the number of hours actually worked is more indicative of self-employment.

Termination of contract. The contract terminates when the work is complete; 10 April 2001 is described as the "estimated date for completion of the project." This would be an unusual feature of an employment contract and is a pointer to self-empoyment. The contract was in fact prematurely terminated by Marconi.

Part and parcel of the organisation. Mr Williams contended that Miss Fernley was integrated into the Marconi organisation, so that anyone meeting her would be unlikely to distinguish her from an employee. This does not seem to me to be the case. She had her own business cards; her security pass was different from an employee's, saying "contractor" and having the Appellant's name; she had a telephone extension under the Appellant's name in Marconi's internal directory, and an email address within the organisation; she could not use Marconi sports facilities.

Intention of the parties. Mr Williams submitted that this test was relevant only where the case was borderline or where the status is ambiguous. It is in any event difficult to see how to apply intention to a hypothetical relationship between two parties who never actually contracted with each other and consequently had no intentions. Even trying to infer intentions is difficult. As a minor example, the fact that the parties contract to allow VAT to be added to payments might indicate that they did not intend an employment relationship. Here the Appellant-ERS contract provides for VAT but since that is a contract between two companies it does not say anything about how different parties would view the hypothetical contract.

14. The pointers against the hypothetical contract being a contract of service are that Marconi contracted for particular projects. The end-date and the number of hours were both estimates of the time needed to complete those projects. Miss Fernley did not work a regular pattern of hours; the hours were dictated by the requirements of the work. The Appellant could not be required to do work outside the specification. The Appellant purchased a lap-top with a particular specification specially for use in the job, although there was no obligation on them to do so. The payment terms were 30 days after invoice and they suffered delays in being paid in the way that businesses do. There was a right for the Appellant to

substitute another supplier. Miss Fernley did not work alongside any other Marconi employees as part and parcel of the Marconi organisation. During the Marconi contract the Appellant operated as a normal small business with its own office working for four other clients.

15. The pointers towards the hypothetical contract being a contract of service are that the contract provides for a fixed number of hours weekly at an hourly rate for a one year contract. No doubt this is the aspect that Mr Justin primarily focussed on. The reality of the hours worked is very different from the contract, demonstrating the necessity of looking beyond the terms of the contract. The element of financial risk is low when payment is made on this basis, but the risk of delay in payment and bad debts is there. The Marconi purchase order refers to Miss Fernley doing the work personally but this is explained by the fact that the hourly rate was fixed with her expertise in mind, and in my view is not contrary to the right of substitution.
16. In assessing this evidence I bear in mind that I have heard no evidence from Marconi and it is always possible that the Appellant may be emphasising factors favourable to them. But even allowing for this possibility, and standing back and looking at all the factors there is very little to suggest an employment relationship. In essence Marconi was contracting for a particular IT job from a small business in the way one would expect an IT consultant to be engaged. In my view on the hypothesis that Miss Fernley had contracted directly with Marconi she would not have been employed under a contract of service; she would have been in business on her own account.
17. Accordingly I allow the appeal. Mr Smith said that he reserved the right to apply for costs, while recognising the limited jurisdiction of the Special Commissioners to award costs. If he wishes to pursue this he should apply to the Clerk to the Special Commissioners within 21 days of the date of release of this decision for a further hearing limited to the issue of costs.

DR JOHN F. AVERY JONES
SPECIAL COMMISSIONER

SC 3027/02
Authorities referred to in skeletons but not in the decision
Montgomery v Johnson Underwood 2001 EWCA Civ 318
Carmichael v National Power [1999] 4 All ER 879
WHPT Housing Association v Secretary of State for Social Services [1981] ICR 737
Battersby v Campbell [2001] STC (SCD) 189
FS Consulting v McCaul [2002] STC (SCD) 138
Morren v Swinton and Pendlebury Borough Council [1965] 1 WLR 576
Nethermere (St Neots) Ltd v Gardiner [1984] ICR 612
Bank voor Handel en Scheepvaart v The administrator of Hungarian Property 35 TC 311
Massey v Crown Life Insurance [1978] 2 All ER 576

SYNAPTEK LTD v GRAEME YOUNG (HMIT) (2003)

Ch D (Hart J) 27/2/2003

TAX - CIVIL PROCEDURE - COMMERCIAL LAW - EMPLOYMENT

APPLICATIONS FOR CASE TO REMITTED TO GENERAL COMMISSIONERS : DISCRETION : FURTHER FINDINGS OF FACT : APPEALS BY WAY OF CASE STATED : S.56 TAXES MANAGEMENT ACT 1970 : INADEQUATE STATEMENT OF CASE : INADEQUATE FINDINGS OF FACT : IR35 LEGISLATION : FINANCE ACT 2000 : PERSONAL SERVICE COMPANIES : INCOME TAX AND NATIONAL INSURANCE CONTRIBUTIONS CHARGED ON FEES PAID BY CLIENT : ARRANGEMENTS EQUIVALENT TO EMPLOYER/EMPLOYEE RELATIONSHIP : REG.6(1) SOCIAL SECURITY CONTRIBUTIONS (INTERMEDIARIES) REGULATIONS 2000 : S.4A SOCIAL SECURITY CONTRIBUTIONS AND BENEFITS ACT 1992 : S.75 WELFARE REFORM AND PENSIONS ACT 1999

In an appeal by way of case stated from a decision of the General Commissioners dismissing the appellant's appeal from the Inland Revenue that the circumstances of arrangements between an individual providing services to a company through a personal services company were such that had they taken the form of a contract between the individual and the company then the individual would be regarded as employed by the company, the court stood over the appellant's application to remit the case for further findings of fact pending determination of the appeal.

Synaptek's ('S') application for its case to be remitted to the General Commissioners ('the commissioners') for the commissioners further findings.

If successful, S's appeal by way of case stated from a decision of the commissioners dismissing S's appeal from a decision of the Inland Revenue ('the revenue') of 30 April 2001 would have to be adjourned.

Gordon Stutchbury ('G') was a software engineer employed by S, which provided G's services to clients, including the Government's IT Services Agency ('ITSA') and a company known as EDS.

The revenue decided that the circumstances of the arrangement between G and EDS for the performance of services from 1 May 2000 to 29 October 2000 were such that they had taken the form of a contract between G and EDS, so that G would be regarded as employed by EDS.

S's appeal to the commissioners was dismissed.

S's grounds for remission were: (i) the decision that was under appeal was to the effect that G was to be regarded as employed by EDS from 1 May 2000 to 29 October 2000.

The commissioners entirely overlooked the undisputed evidence before them that the relationship between S and EDS commenced only on 1 September 2000, prior to which ITSA had fulfilled EDS' role; and (ii) the case stated contained inadequate findings of fact concerning arguments to be adduced on appeal on the substantive issues, such that it would be difficult for a court properly to consider the issues of law.

HELD: (1) The respondent, ('HMIT') accepted that G's services were provided to ITSA under relevant arrangements from 1 May to 30 September 2000 when ITSA's work was transferred to EDS and therefore there was a seamless transition as to the work carried out by G.

Accordingly, it was unnecessary to remit the case to the commissioners in order to enable them to make a finding to that effect.

The argument on appeal could proceed on the basis that the relevant transfer of transactions did take place on 30 October.

The consequences of that were a matter for argument.

(2) The authorities indicated that the nub of the matter was the question whether a particular contract was a contract of service or for services, which question warranted careful analysis and fine distinctions, Hall v Lorimer (1994) STC 23 considered.

S's criticisms of the commissioners' findings of fact could be grouped into three categories: (i) facts that one could see from the case stated were alleged before the commissioners and where it was possible to interpret their decision as having accepted the correctness of the fact alleged.

It was possible to interpret the commissioners' decision as having broadly accepted the factual allegations.

The commissioners only found it necessary to distil from those allegations broad conclusions as found in the findings of fact; (ii) allegations of fact where it was not clear whether the commissioners accepted the factual allegations and such was not reflected in their findings.

Here, the court could not decide whether S's points were good or not and therefore the question of remission had to be decided once the court had decided the questions of constructions raised by S; (iii) matters on which there was evidence before the commissioners but was not expressed or recorded as contentions and no explicit findings of fact had been made.

It was not appropriate to remit the case to the commissioners for specific findings as to whether or not they had accepted such evidence and if so what significance was attached to it.

Such points amounted to "nit-picking" as per Scott J in Consolidated Goldfields plc v IRC (1990) STC 356.

(3) The court could understand S's dissatisfaction with the way in which the commissioners had expressed their findings.

It was difficult, simply reading the findings and the conclusion to understand on a first reading without looking at the underlying legal materials entirely, to follow their reasoning.

Such difficulty was exacerbated by the relatively exiguous nature of the findings made.

It might be that a court would reach the conclusion that the commissioners' findings were to slender to permit any rational conclusion.

However, this court had not reached that stage yet.

The application to remit would not be dismissed as it depended on the conclusion the court might reach on the question of construction. Application stood over pending determination of appeal.

Conrad McDonnell instructed by Bond Pearce for S. Clive Sheldon instructed by the Treasury Solicitor for HMIT.
LTL 27/2/2003 EXTEMPORE (Unreported elsewhere)

Document No. AC9200496

Case No: CH/2002/APP/0777

Neutral Citation No: [2003] EWHC 645 (Ch)
IN THE HIGH COURT OF JUSTICE
CHANCERY DIVISION

Royal Courts of Justice
Strand, London, WC2A 2LL

Date: 28th March 2003

Before :

THE HONOURABLE MR JUSTICE HART

Between :

SYNAPTEK LIMITED **Claimant**

− and −

MR GRAEME YOUNG (HM IN$PECTOR OF TAXES) **Defendant**

Mr Conrad McDonnell (instructed by Bond Pearce) for the Claimant
Mr Clive Sheldon (instructed by Solicitor of Inland Revenue) for the Defendant

Hearing dates 27th and 28th February 2003
Handdown Judgment 28th March 2003

Approved Judgment

I direct that pursuant to CPR PD 39A para 6 1 no official shorthand note shall be taken of this Judgment and that copies of this version as handed down may be treated as authentic

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The Honourable Mr Justice Hart

Mr Justice Hart:

1. This is an appeal by way of case stated against the decision of the General Commissioners for the South Shields Division of Tyne and Wear dated 4th September 2002 dismissing an appeal by Synaptek Limited ("Synaptek") against a Notice of Decision of the Inland Revenue dated 30th April 2001 in the following terms:

> That the circumstances of the arrangements between Gordon Stutchbury and EDS for the performance of services from 1 May 2000 to 29 October 2000 are such that, had they taken the form of a contract between Gordon Stutchbury and EDS, Gordon Stutchbury would be regarded for the purposes of Parts I to V of the Social Security (Contributions and Benefits) Act 1992 as employed in employed earner's employment by EDS.
>
> That Synaptek Limited is treated as liable to pay primary and secondary Class 1 Contributions in respect of the worker's attributable earnings from that engagement."

2. The case concerns the application of what is popularly known as the IR35 legislation, the background to which is explained in the judgments of Burton J at first instance and Robert Walker LJ on appeal in *On the application of Professional Contractors Group Limited, R v IRC [2001] STC 659, [2002] STC 165.* That legislation (for income tax purposes contained in Finance Act 2000, and for social security purposes contained in the Social Security Contributions (Intermediaries) Regulations 2000) applies typically to small "service" companies which provide the services of a particular individual to a client who requires those services. This case concerns the latter regulations ("the Regulations"). In the present case Synaptek was the service company, Gordon Stutchbury ("Mr Stutchbury"), a software engineer, the individual whose services were supplied, and (subject to a wrinkle which I mention below) EDS the client to whom the services were supplied. The position is additionally complicated by the fact that there was no contractual relationship between Synaptek and EDS Synaptek's agreement to provide the services was made with NES Computer Services Limited ("NESCO"). EDS was itself providing services (as successor to the government IT Services Agency ("ITSA")) the Benefits Agency at the Inland Revenue site at Longbenton.

3. Regulation 6(1) provides as follows:

> (1) These Regulations apply where:−
>
> (a) an individual (‘the worker') personally performs, or is under an obligation personally to perform services for the purposes of a business carried on by another person (‘the client'),
>
> (b) the performance of those services by the worker is carried out, not under a contract directly between the client and the worker, but under

arrangements involving an intermediary, and

(c) the circumstances are such that, had the arrangements taken the form of a contract between the worker and the client, the worker would be regarded for the purposes of Part 1 to V of the Contributions and Benefits Act as employed in employed earner's employment by the client"

4. It was common ground that Synaptek was an "intermediary" for the purposes of the Regulation, that Mr Stutchbury personally performed services, and that (subject to the wrinkle) those services were provided for the purposes of a business carried on by EDS. It was accepted by Synaptek that "the arrangements" included the terms of the contract between Synaptek and EDS and the terms of the contract between EDS and NESCO, and that "the circumstances" referred to in Regulation 6(l)(c) include the arrangements and the detail of the day to day performance of those contracts, including any matters not expressly stipulated in those contracts.

5. The General Commissioners, after reciting that Mr Stutchbury had given oral evidence to them and listing documentary material which had been placed before them, expressed their findings of fact as follows:

5.1 Mr Stutchbury is a consultant in software engineering and is in business on his own account. Following a number of employments, including a technical apprenticeship at NEI Reyrolle (switchgear manufacturers) and a period in the Police Force, he sought a career in computing. He qualified in 1987 and worked initially for a nuclear medicines company in Surrey.

5.2 In 1990 Mr Stutchbury purchased an off−the−shelf company Sisterfield Ltd, whose name he subsequently changed to Synaptek Ltd, the Appellant in this case. Mr Stutchbury and his wife are the only shareholders and directors. Mrs Stutchbury is also the Secretary of the Company and is responsible for the administration. This has involved visits from the Contributions Agency and from the VAT Inspector and contact with the company's accountants. Mr Stutchbury has made substantial investment in his company and the Accounts to 30.04.01 show the accumulated cost of Computer Equipment to be £29,835. The Appellant had in the past engaged a total of four employees and had undertaken work for many customers in its twelve year history.

5.3 EDS is an American Company which has a number of Government contracts including one to supply computer software and services to the Benefits Agency at Longbenton, Newcastle upon Tyne. EDS do not have sufficient permanent staff for this work and so recruit additional help. EDS do not deal directly with suppliers of consultancy services, particularly smaller businesses such as the

Appellant. When engaging suppliers, EDS use the services of agencies, for, example NESCO. The agency is responsible for payment to the Appellant and, if the agency goes into liquidation, the Appellant will not be paid.

5.4 On 15 December 1999 the Appellant entered into an agreement with NESCO under which Mr Stutchbury was to undertake work for ITSA - DSS at Longbenton, Newcastle upon Tyne. The role of ITSA was subsequently taken over by EDS through the terms of the agreement of 15 December 1999 continued to be observed without any material difference to the Appellant or to Mr Stutchbury. For the period referred to in the Notice of Decision, therefore, the work was to be undertaken for EDS.

5.5 The Agreement of 15 December 1999, applied to the relevant period, contained the following features:

(i) The Appellant would secure that Mr Stutchbury carried out the services required by EDS

(ii) The services were to be carried out at the DSS building at Longbenton though that location could be changed by agreement between the Appellant and NESCO at any time.

(iii) It was open to any of the three parties, NESCO, the Appellant or EDS, to terminate the agreement by four weeks written notice to other two parties. Further, it was open to EDS or NESCO to terminate the Agreement with immediate effect if Mr Stutchbury failed to carry out the services to the satisfaction of EDS.

(iv) Mr Stutchbury was to work for at least 37.5 hours per week and payment would be at the hourly rate of £42. There would be no sick pay or holiday pay. The cost of travelling to work was provided for in the hourly rate. Each week Mr Stutchbury was to complete a timesheet which had to be authorised by EDS and submitted to NESCO. Payment would only be made by NESCO on production of a duly completed timesheet and an appropriate invoice.

(v) In the interest of continuity, the Appellant was to procure that the work was undertaken by Mr Stutchbury personally. The Appellant could substitute alternative personnel but only with the approval of EDS.

(vi) The Appellant would remain the employer of Mr Stutchbury.

(vii) The intellectual property in the software developed by Mr Stutchbury was to belong to EDS.

5.6 Mr Stutchbury was an expert in his field. He worked on two projects at Longbenton. Subject to problems arising on either project, it was up to Mr Stutchbury how he did the work and when he did it. He did not take his own staff with him. For the most part he worked alongside employees of EDS. From time to time, when requested, he would go to the aid of employees of other firms on the site. He did not seek permission, though usually informed a co−worker or the job manager as a matter of courtesy. The time involved was included in his normal timesheet to NESCO, Mr Stutchbury did not work any fixed hours. He was inclined to work longer hours at the beginning of the week. Mrs H Docherty, an employee of EDS, was his Line Manager and she managed the projects

5.7 Site security was controlled by the Inland Revenue who had the ultimate say on who could enter, and this extended to everyone. Mr Stutchbury was issued with a Pass.

5.8 Mr Stutchbury did not use his own equipment on the site but he did take his own books for reference.

5.9 At various times during the course of his involvement with EDS, Mr Stutchbury undertook other work for unconnected parties including PTS Services and Ainleys This was in his own time, largely in the evenings and at weekends.

5.10 Although there was a right of substitution in the event, for example, of Mr Stutchbury's illness, consent was never sought. Any substitute would have had to be suitably qualified and meet with the approval of EDS. Mr Stutchbury would have been a good judge of suitable qualification since he had successfully introduced three individuals to EDS. Mrs Stutchbury could not have acted as a substitute for her husband.

5.11 The facts of this case bear a close similarity to the facts in F.S. Consulting Limited v Patrick McCaul. The principles set out by the Special Commissioners in that case would, therefore, be a useful guide."

6. They then set out (in paragraph 6) what Synaptek's contentions had been. These included a number of assertions of fact which were not the subject of express findings.

Then, after setting out the Inland Revenue's contentions, and listing some 23 authorities to which they had been referred, they proceeded to their conclusion in

the following terms:

> We the Commissioners who heard the appeals decided:−
>
> 1. Having considered all the elements of this case, and the recent decisions to which we have been referred, we have decided on balance that, if there had been a contract between Mr Stutchbury and EDS for the period 1 May to 29 October 2000, it would have been a contract of service with Mr Stutchbury as employee.
>
> 2. We have therefore decided that the circumstances fall within Regulation 6(1), Social Security Contributions (Intermediaries) Regulations, 2000, and that the Notice of Decision by the Inland Revenue dated 30.04.2001 should stand."

7. Mr McDonnell, on behalf of Synaptek, observed that there is very little in the way of reasoning in the Case Stated. Such reasoning as there is has to be inferred from their reference to the cases to which they were referred. I agree with the comment but do not think that it is a legitimate criticism. The General Commissioners' duty is to find the facts and state their conclusions see the General Commissioners (Jurisdiction and Procedure) Regulations 1994, regulations 13 and 20(2). The extent to which they may be under a duty, in a case where their findings depend on resolving issues of pure fact, to explain why they have arrived at particular findings is not a matter which I need to consider. In the present case their particular findings of fact are not (save as mentioned below) challenged as not being open to them on the evidence which was before them.

8. Deciding, in a borderline case, whether a particular contract is a contract of service or a contract for services is notoriously difficult. It arises in a number of contexts, most commonly today in an income tax or social security context or in the application of employment protection legislation. In general the question is regarded as one of fact, or as it is sometimes put, a question of mixed fact and law, the evaluation and determination of which is a matter for the fact−finding tribunal (see, e.g. *Cooke v Blacklaws* [1985] STC 1, *Sidey v Phillips* [1987] STC 87, *O' Kelly v Trust House* Forte [1983] IRLR 369, at 381−383, *Clark v Oxfordshire Health Authority* [1998] 1RLR 125). If, however, the question falls to be resolved solely by reference to the contents of a written contract, the question is regarded by the court as a question of law.

9. The distinction is illuminated by a passage from the speech of Lord Hoffmann in *Carmichael v National Power plc* [1999] 1 WLR 2042, where he said at pp. 2048D− 2049C):

> I add a few words only on the troublesome distinction between questions of fact and questions of law.
>
> The difficulties which have arisen in this area are, I think,

attributable to the historical origin of the distinction in trial by jury and the pragmatic way in which the courts have applied it. In his Hamlyn Lectures on *Trial by Jury* (1956), Lord Devlin said (at p.61):

The questions of law which are for the judge fall into two categories: first, there are questions which cannot be correctly answered except by someone who is skilled in the law; secondly, there are questions of fact which lawyers have decided that judges can answer better than juries."

Included in the second category is the construction of documents in their natural and ordinary meaning. An uninitiated person might have thought that, for example, the interpretation of a letter written by a layman stating the terms upon which he offered work to someone else, should be a question of fact, best decided by an employment tribunal (formerly an industrial tribunal: see the Employment Rights (Dispute Resolution) Act 1998), which was likely to be more familiar with the relevant background than a judge. But the opposite is the case: see *Davies v Presbyterian Church of* Wales [1986] 1 WLR 323. This rule may be part of the explanation for the otherwise remarkable fact that the Employment Appeal Tribunal has a majority of lay members although it has jurisdiction to hear appeals only on questions of law. As Lord Devlin explains (at pp. 97−98) the rule was adopted in trials by jury for purely pragmatic reasons. In mediaeval times juries were illiterate and most of the documents which came before a jury were deeds drafted by lawyers. In the eighteenth and nineteenth centuries the rule was maintained because it was essential to the development of English commercial law. There could have been no precedent and no certainty in the construction of standard commercial documents if questions of construction had been left in each case to a jury which gave no reasons for its decision. Thus the rule that the construction of documents is a question of law was well established when industrial tribunals were created and has been carried over into employment law.

It was this rule upon which the majority in the Court of Appeal relied as entitling them to say that the construction of the exchange of letters between the C.E.G.B and the respondents, together with any terms which could be implied be law into the contract which they created, was a question of law. I agree with my noble and learned friend the Lord Chancellor that even if this was the case, I would prefer the construction adopted by the industrial tribunal to that of the majority in the Court of Appeal. But I think that the Court of Appeal pushed the rule about the

> construction of documents too far. It applies in cases in which the parties intend all the terms of their contract (apart from any implied by law) to be contained in a document or documents. On the other hand, it does not apply when the intention of the parties, objectively ascertained, has to be gathered partly from documents but also from oral exchanges and conduct. In the latter case, the terms of the contract are a question of fact. And of course the question of whether the parties intended a document or documents to be the exclusive record of the terms of their agreement is also a question of fact."

10. It was submitted by Mr McDonnell that the question under Regulation 6(1) necessarily involved a question of law, since the Commissioners were not being invited to make findings of fact as to what were the actual contractual arrangements, but had rather to consider whether the rendering of services under the terms of a hypothetical contract should be regarded as employment in employed earner's employment by the client. In order to answer that question, the Commissioners had first to hypothesise, or construct, the terms of the relevant contract. Once that exercise had been done, the determination of the question whether the contract was one of service or for services was, he submitted, necessarily a question of law.

11. I do not accept that submission. The inquiry which Regulation 6(1) directs is in the first instance an essentially factual one. It involves identifying, first, what are the "arrangements involving an intermediary" under which the services are performed, and, secondly, what are the "circumstances" in the context of which the arrangements have been made and the services performed. The legal hypothesis which then has to be made is that the arrangements had taken the form of a contract between the worker and the client. To the extent that "the arrangements" are in the particular case to be found only in contractual documentation, it may be true to say that the interpretation of that documentation is a question of law. Even in that case, however, the findings of the fact−finding tribunal will be determinative of the factual matrix in which the interpretative process has to take place, and influential to a greater or lesser degree in enabling the essential character of the arrangements to be identified. Where, on the other hand, the arrangements cannot be located solely in contractual documentation, their identification and characterisation is properly to be described as a matter of fact for the fact−finding tribunal. The fact that the tribunal is then asked to hypothesise a contract comprising those arrangements directly between the worker and the client does not, by itself, convert the latter question from being a question of mixed fact and law into a pure question of law.

12. The significance of the point is, of course, that if the question is characterised as one of fact, or of mixed fact and law, this court can only interfere if it concludes that the decision reached by the Commissioners is an impossible one on the facts found by them or that they have misdirected themselves. If, on the other hand, it is

a question of law this court is free to substitute its own opinion. In a context where the answer to be given depends on the relative weight to be given to a number of potentially conflicting indicia, the distinction may be of critical importance: in the one case the decision of the Commissioners is conclusive and in the other it is not. As I understood his submissions, Mr McDonnell's argument that the question here was one of law was founded solely on the proposition that the hypothesis required to be made by Regulation 6(3) necessarily involved a point of law. Subject to that proposition his submissions appeared to me to assume that the task of the Commissioners was to make appropriate findings of fact and to evaluate their weight in the traditional manner in relation to the fundamental issue of service or services. Indeed the main thrust of his submissions was, not that the Commissioner's had been wrong so to approach the matter, but that insufficient weight had been given by the Commissioners to certain matters of pure fact (in particular the way in which Mr Stutchbury in fact conducted himself in providing the services). He did not, as I understood him, submit that the question before the Commissioners could be determined solely by reference to the Contractual documentation to which they were referred.

13. It is not clear from the stated case how the Commissioners approached the task of identifying the relevant "arrangements". As already indicated, in his written submissions Mr McDonnell argued that the "arrangements" encompassed the terms of the contract between ‘Synaptek' and NESCO (which were before the Commissioners) and the terms of the contract between NESCO and EDS (which were not). He further argued that the "circumstances" referred to in Regulation 6(1)(c) included the arrangements and also the detail of the day to day performance of those contracts, including any matters not expressly stipulated in those contracts. Although the case stated is not explicit, it appears to me that this analysis was adopted by the Commissioners.

14. On that analysis the starting point of the inquiry lay in the provisions of the contract between Synaptek and NESCO ("the NESCO agreement"). Its principal features are summarised in paragraph 5.5 of the stated case but for ease of exposition it is desirable to set out in extenso its provisions. In that agreement Synaptek is referred to as "the Company", Mr Stutchbury as "the Company Employee". The particulars annexed to the agreement were in the following form:

The Particulars (L9793)
15 December 1999

1.	**Client**	ITSA - DSS
2.	**The Subcontractor**	
2A	**Company**	Synaptek Limited
	Company Number	2475448
2B	**Company Employee**	Gordon Stutchbury
3.	**Reporting to:** .	David Cummings

4.	**Location:**		Longbenton
5.		**Services:**	Support Technician - Futures
6.	**Start Date:**	1 May 2000	
7.	**Finish Date:**	29 October 2000	
8.	**Notice Period:**	4 weeks	
9.	**Rate:**	42.00 per hour	
10.	**Hours per week:**	37.5	
11.	**Additional Services Rate:**	Pro rata	
12.	**Additional Info:**		

15. So far as material the provisions of the agreement itself included the following:

2 COMMENCEMENT

2.1 The Contract will commence on the Start Date and will expire automatically without notice being required from either party on the Finish Date (Particulars Sections 6 and 7) or earlier termination in accordance with Clause 8 below.

×.

3. CONTRACT

3.1 No variation of these terms shall be binding unless agreed in writing and signed by a Director of NESCO and of the Company and by the Company Employee.

3.2 Except as amended in accordance with sub−clause 3.1 these terms constitute the entire agreement between the parties and supersede all previous written and oral negotiations and representations.

3.3 In the event of conflict between these terms and any terms of business of the Company these terms shall prevail.

3.4 Should any of these terms be or become unenforceable the validity of the remaining terms will not be affected.

3.5. The Company will ensure that the Company Employee performs the obligations of the Company and of the Company Employee under this agreement.

4. THE COMPANY AND THE COMPANY EMPLOYEE

4.1 It is the client's responsibility to provide the Company and the Company's responsibility to provide the Company Employee with detailed and accurate description of the Services.

4.2 The Company shall supply to NESCO an up−to−date and accurate curriculum vitae and any supporting documents for the Company Employee.

4.3 The Client will allocate work to the Company and the Company will allocate work to the Company Employee. NESCO has no responsibility for supervising, directing or controlling the Company Employee.

4.4 The Company shall procure that the Company Employee carries out the services in a diligent and professional manner and in compliance with all instructions, rules, procedures, regulations, codes, laws and policy guidelines of the Client relating to conduct, health and safety at work, security, confidentiality and secrecy, fire and accident risk and all other matters which may affect the Company Employee at the Location.

×.

4. 11 The Company Employee agrees with each of NESCO and the Client that he will be bound by and comply in all respects with these terms.

5. LOCATION AND HOURS

5.1 The Location may be changed by agreement between the Company and NESCO at any time.

5.2 The normal working week for the company Employee is specified in the Particulars Section 10.

5.3 If at any request of the Client the Company Employee agrees to provide additional services outside the normal working week, details shall be included in the Company Employee's weekly time sheet and NESCO will pay for such services at the Additional Services Rate specified in the Particulars.

5.4 The Company will ensure that the Company Employee gives such notice as the Client may require to the Client and NESCO of proposed holiday leave.

6. TIMESHEETS/INVOICING/PAYMENT/VAT

6.1 The Company Employee must submit to NESCO a timesheet for each week worked signed by or on behalf of the Client to whom the Company Employee shall give one copy.

6.2 No payment will be made unless and until properly completed and counter−signed timesheet and appropriate invoice from the Company have been received by NESCO.

6.3 The Company will submit to NESCO such written information as NESCO requests in support of such invoices including but not limited to copies of its certificate of incorporation of the Company and VAT registration document where appropriate.

6.4 In any event no payment will be made by NESCO to the Company in respect of any contractual period not actually worked including notice periods.

×.

8. TERMINATION

8.1 NESCO, the Company or the Client may terminate this Contract at any time for any cause by giving written notice to the other two parties of the period set out in the Particulars Section 8 expiring at any time.

8.2 If the Company Employee

8.2.1 fails to supply the Services to the satisfaction of the Client or does anything detrimental to the interests of the Client or NESCO; or

8.2.2 shall be guilty of any criminal act;

then the Client or NESCO may given written notice to the Company terminating this contract and to the Company Employee terminating the provision of the Services with immediate effect and in either case this contract shall thereupon terminate.

8.3 If the Client cancels its requirement for the Company Employee on or before the Start Date NESCO may terminate this contract by notice in writing with immediate effect and without liability for compensation.

8.4 In the event of termination of this contract by the Client NESCO and the Company shall forthwith provide to each other full written particulars of the reason for the termination so far as the same are known.

8.5 If the Company or the Company Employee fails to observe these terms to (in the reasonable opinion of NESCO) a material and significant extent and fails to remedy the same within seven days of notice from NESCO requiring it to do so then NESCO has the right to terminate this contract forthwith and without any liability to the Company.

8.6. If NESCO fails to observe these terms to (in the reasonable opinion of the Company) a material and significant extent and fails to remedy this same within seven days of notice from the Company requiring it to do so then the Company has the right to terminate this Contract forthwith and without liability to NESCO of any kind.

8.7 Termination of this Contract shall take effect without prejudice to any accrued rights, and liabilities of either party.

9. SUBSTITUTION

9.1 In the interests of continuity the Company shall use its best endeavours to procure that the Services are provided by the Company Employee personally but may with the consent of the Client substitute alternative personnel subject to procuring that such alternative personnel are bound by the terms of this agreement.

9.2 The Company shall procure that the Company Employee shall not for a period of six months following the termination of this agreement for any reason without the prior written approval of a Director of NESCO be engaged directly or indirectly in the provision of services similar to those supplied by the Company hereunder to the Client or any associated or subsidiary personal company firm or organisation.

10 OFF−SITE FACILITIES AND TRAINING

10.1 The Company shall procure that the Company Employee has adequate computer facilities at its premises or the Company Employee's home or office and that the Company Employee spends such time there at no cost to NESCO as may be necessary for the provision of the Services to a proper and professional standard including preparation, testing and revision of any aspect of the Services provided at the Location.

10.2 The Company shall be responsible for ensuring that the Company Employee, and any other person provided pursuant to these terms, has the necessary qualifications and competence for the proper performance of the Services and the Company shall be responsible for the costs of all training which may from time to time be necessary to comply with the provisions of this clause.

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15. EXCLUSIONS AND INDEMNITY

15.1 Save as herein provided NESCO shall not be liable to the Company or the Company Employee in any event in contract, tort (including negligence and breach of statutory duty) or otherwise howsoever and whatever the cause thereof.

15.1.1 for any increased costs or expenses;

15.1.2 for any loss of profit, business, contracts, revenues, or anticipated savings; or

15.1.3 for any special indirect or consequential damage of any nature whatsoever.

15.2 The Company will indemnify NESCO against all action proceedings claims or demands in any way connected with this contract brought or threatened as a result of any act or omission by the Company or the Company Employee and shall effect professional identify insurance for not less than £1 million in respect of any such act or omission."

16. For the purposes of Regulation 6(1) the respective obligations of Mr Stutchbury and EDS have to be identified and, on the hypothesis that there was a contract between them, a conclusion formed as to whether that contract is a contract of service or a contract for services. In *Ready Mixed Concrete (South East) Ltd v Minister of Pensions and National Insurance* [1968] 2 Q.B. Mackenna J. expressed that test in the following terms at p.515:

> A contract of services 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 a sufficient degree to make that other master.
>
> (iii) The other provisions of the Contract are consistent with its being a contract of service."

17. The authorities show that there is no one test which is conclusive for determining into which category a particular contract falls. As Nolan L.J. put it in *Hall v. Lorimer* [1994] S.T.C. 23 at p.28: "In cases of this sort there is no single path to a correct decision. An approach which suits the facts and arguments of one case may

be unhelpful in another."

18. Mr McDonnell submitted that in the present case every relevant aspect of the circumstances and the arrangements was incompatible with employment and was indicative of the provision of services. He put at the forefront of his case the circumstances that Mr Stutchbury (through Synaptek) was, as found by the Commissioners, in business on his own account (see paragraphs 5.1 and 5.2 of the case stated) and continued to work for other clients during the period of his engagement with EDS (see paragraph 5.9*)* . In *Market Investigations Ltd v. Minister of Social Security* [1969] 2 Q.B. 173, Cooke J. said at pp 184−5.

> the fundamental test to be applied is this: "Is the person who has engaged himself to perform these services performing them as a person in business on his own account?" If the answer to that question is "yes," then the contract is a contract for services. If the answer is "no," then the contract is a contract of service. No exhaustive list has been. compiled and perhaps no exhaustive list can be compiled of the considerations which are relevant in determining that question, nor can strict rules be laid down as to the relative weight which the various considerations should carry in particular cases. The most that can be said is that control will no doubt always have to be considered, although it can no longer be regarded as the sole determining factor, and that factors which may be of importance are such matters as whether the man performing the services provides his own equipment, whether he hires his own helpers, what degree of financial risk he takes, what degree of responsibility for investment and management he has, and whether and how far he has an opportunity of profiting from sound management in the performance of his task"

19. Mr McDonnell submitted that once it is estab1ished that a person was in business on his account that is an extremely powerful pointer to the fact that the particular engagement by the individual is one for services rather than of service. For that proposition he relied on the decision of Rowlatt J in *Davis v Braithwaite* (1933) 18 T.C. 198. That case raised the question whether the earnings of an actress from a variety of engagements over three years of assessment were assessable as profits of her profession or vocation under Schedule D or as profits from her employment as an actress under Schedule E. The real point at issue was her liability to tax in respect of her American earnings, and on that question it was in her interest to argue that each separate engagement represented a separate contract of employment to which Schedule E applied. Rowlatt J. held on the particular facts that the argument could not succeed. In my view, nothing in his judgment can be read as authority for the proposition that there is anything like a presumption that any engagement entered into by a person who is in business on his account is a contract for services rather than a contract of service (and indeed Mr McDonnell did not suggest that the evidential burden shifted). As Pennicuik V−C said in *Fall v Hitchen* [1973] 1 WLR 66 at 74 (in a passage approved of by the Court of Appeal

in *Hall v. Lorimer* [1994] S.T.C. 23 at 31):

> [Rowlatt J in *Braithwaite]* nowhere says that if an actor enters into a contract in such terms as to amount to what he calls a post, then that actor, is not chargeable under Schedule E but under Schedule D. On the contrary, it is implicit in the whole of his judgment, it seems to me, that if a professional person, whether an actor or anybody else, enters into a contract involving what the learned judge calls a post, then that person will be chargeable in respect of the income arising from the post under Schedule E notwithstanding that he is at the same time carrying on his profession, the income of which will be chargeable under Schedule D."

20. The fact that Synaptek (and notionally Mr Stutchbury) was in business on its (notionally his) own account is no doubt an important contextual circumstance to be taken into account in determining whether the particular notional contract under which Mr Stutchbury was engaged by the client was one for services or of service. But it is no more than that. The weight to be given to it was, in my judgment, a matter for the General Commissioners. That they took it into account is clear from their reference to the point in paragraphs 5.1 and 5.2 of the stated case.

Mutuality of Obligation

21. The main point on which Mr McDonnell relied as showing that the Commissioners had misdirected themselves as a matter of law was their treatment of the question whether there was sufficient mutuality of obligation in the notional contract for it to be recognisable as a contract of service. In paragraph 6.7 of the stated case the Commissioners had recorded Synaptek's contention on this point in the following terms:

> 6.7 EDS were not obliged to provide work for Synaptek and Synaptek were not obliged to work EDS. A mutuality of obligation normally essential to a contract of service, was accordingly absent."

22. This passage appears to have been a reflection of written submissions made by Mr Stutchbury where similar words occur in the context of the comment that "At the end of this contract I will leave for another company, as I came to EDS from another company. When the job is complete I will move on as I have done for the past 10 years for something more interesting and/or more money;" and, following a reference to *O'Kelly v Trust House Forte* that "EDS will dispose of Synaptek's services once the contract with BA [Benefits Agency] expires. There is no obligation for Synaptek to continue working for EDS and EDS are not obliged to provide work. There is also a 4 week termination clause so EDS can terminate the contract early."

23. These passages suggest that the argument being advanced before the Commissioners related to the existence of any obligation on EDS to enter into the contract in the first place rather than to the question whether there was any obligation on EDS to provide work during the currency of the contract. The only way in which the Commissioners dealt with the argument was in the first sentence of paragraph 5.5 (iv) of the stated case, implicitly rejecting the submission.

24. Before me Mr McDonnell directed his fire at the question of EDS' obligations to provide work during the currency of the contract. He submitted that, on the true construction of the NESCO agreement (assuming equivalent provisions to be found in the notional contract between EDS and Mr Stutchbury) there was no such obligation on EDS. He submitted that the effect of the contractual provisions, properly construed, was that EDS was perfectly free during the currency of the contract not to provide Mr Stutchbury with any work.

25. There is now a considerably body of authority on the question whether an obligation on the employer to provide work is necessarily and in all cases an indispensable attribute of a contract of employment: see *Nethermere (St Neots) Ltd v Gardiner* [1984] 1RLR 240, *McLeod v Hellyer Brothers Ltd* [1987] 1RLR 232, *Clark v Oxfordshire Health Authority* [1998] 1RLR 125 and *Montgomery v Johnson Underwood Ltd* [2001] 1RLR 269. It is unnecessary in the present case to examine these since Mr Sheldon on behalf of the Inspector accepted that if, taking the period of the notional contract as a whole EDS was under no obligation to provide work, the necessary element of mutuality was indeed lacking for that period.

26. The argument that EDS was under no such obligation was founded entirely on the provision in Clause 6.4 of the NESCO contract that:

> In any event no payment will be made by NESCO to the Company in respect of any contractual period not actually worked including notice periods."

Mr McDonnell submitted that this provision had effect irrespective any contractual period had not been worked: it might be simply because EDS had been unable or unwilling to provide work.

27. In my judgment that is not the correct way to read this provision. Its purpose is to emphasise that payment is dependent not only on the completion of proper timesheets and invoices, but also on actual work having been done. It does not, in my judgment, detract from the obligation on the client reflected in Clause 4.3 to "allocate work to the Company." Moreover, if the contract is read as containing no obligation on the client to provide work, it is quite impossible to see what purpose is served by the termination provisions in Clause 8.

<u>The Right of Substitution</u>

28. In *Express and Echo Publications v Tanton* [1999] 1RLR 367, CA, it was held that a clause in a driver's contract providing that "[i]n the event that the contractor is unable or unwilling to perform the services personally, he shall arrange at his own expense entirely for another suitable person to perform the services" was incompatible with the contract having been one of employment. The E.A.T has subsequently held (see *MacFarlane v Glasgow City Council* [2001] 1RLR 7) that a more limited power of delegation is not necessarily inconsistent with a contract of employment. In the present case the provision in question (Clause 9.1 of the NESCO agreement) does not give Synaptek any *right* to perform the services by anyone other than Mr Stutchbury. The effect of the contract is that, unless and until agreed otherwise, the services do have to be performed personally by Mr Stutchbury. In addressing the question whether that provision pointed to the contract being one for services rather than of employment, the Commissioners were entitled in my judgment to regard it as simply one fact among others, and, in assessing the weight to be given to it**,** to take into account the extent to which the provision was utilised in practice.

Misplaced reliance on *FS Consulting Ltd v McCaul*

29. Mr McDonnell submitted that the Commissioners could be shown to have misdirected themselves by their invocation, in paragraph 5.11 of the stated case, of this decision of Special Commissioner Dr. Brice reported at [2002] SIC (SCD). The contractual arrangements in that case bore some similarity to those in the present case, but there were several distinguishing features. In particular the working hours of the "employee" in that case were less flexible than Mr Stutchbury's, there was a greater degree of control by the client over the services performed by the "employee," there was no obligation on the "employee" to maintain his own tools and equipment or undertake his own training, there was no provision for the "employee" to have professional indemnity insurance, and the "employee" had never worked for more than one "client" at a time.

30. Had there been anything ‘in the case stated to suggest that the Commissioners thought that the facts in *F.S. Consulting* were indistinguishable from those in the present case, there would have been a powerful argument for saying that they must have misdirected themselves. However, all that they say is that the facts "bear a close similarity" and that the principles set out by the Special Commissioner therefore provide "a useful guide." The relevant principles identified by Dr Brice are set out in paragraph 44 to 51 of her Decision. She there began by stating the principle that the question is one of fact to be determined having regard to all the relevant circumstances. She then went on to summarise the effect of *Ready Mixed Concrete, Market Investigations, Hall v. Lorimer* and *McManus v. Griffiths.*

31. In the present case no less than 23 authorities were cited to the Commissioners. Their reference to the principles set out in *F.S. Consulting* seems to me to have been no more than an efficient and economical way of encapsulating the relevant principles, and one which was justified by the close contextual similarity of the facts in that case to the present one. It does not in my judgment demonstrate that

they misdirected themselves.

Conclusions

32. If (as I have held) the Commissioners did not misdirect themselves in law, there plainly was evidence before them which made the conclusion which they reached a possible one. In support of the contention that the contract was one for services, reliance could be placed (1) on the fact that Synaptek (and notionally Mr Stutchbury) was in business on its (notionally his) own account, (2) the limited control by EDS of time at which and the manner in which Mr Stutchbury performed the services, (3) the right of substitution, (4) the fact that Synaptek was responsible for Mr Stutchbury's training and the provision of computer facilities at its own premises, (5) the express provisions in Clause 12 of the NESCO agreement in relation to intellectual property rights, (6) the requirement in Clause 15.2 of the contract for professional indemnity insurance, (7) the flexibility of the hours worked by Mr Stutchbury and (8) the use by him of his own reference books (as to which Mr McDonnell submitted that insufficient weight had been given to potential character as tools of his trade). On the other side of the coin, however, were the facts (1) that the minimum hours to be worked were broadly equivalent to a normal working week, (2) that the only risk borne by Mr Stutchbury was the insolvency of NESCO/EDS, (3) that the duration of the contract was for a fixed period (of 6 months) rather than in relation to the completion of a particular project, (4) that Mr Stutchbury worked alongside EDS employees and was sufficiently integrated with its workforce to have a line manager and (5) the requirement in Clause 4.4 of the NESCO agreement (not in fact expressly adverted to by the Commissioners) that he comply with all EDS instructions. The relative weight to be given to the various factors (all of which are either mentioned or alluded to in the case stated) was a matter for the Commissioners. It is not possible, in my judgment, to say that they were wrong in law in the conclusion at which they arrived.

Error in the Notice of Decision

33. There was one respect in which the Notice of Decision was erroneous, and the error was not corrected, by the Commissioners. This is the wrinkle to which I referred in paragraph 2 above. The Notice of Decision was directed to the arrangements between Mr Stutchbury and EDS during the period from 1st May 2000 to 29th October 2000. In fact, for the period from 1st May 2000 to 31st August 2000 the arrangements were not with EDS but with ITSA.

34. The error, such as it was, appears to have arisen from the way in which Synaptek described the arrangements in initial correspondence with the Inspector. Although the fact of the transfer of undertaking by ITSA to EDS as from 1st September 2000 was in evidence before the Commissioners no significance was attached to it by the parties, and no relevant finding made by the Commissioners. The facts are, however, not in dispute. The point has only come to be taken as an afterthought by Synaptek's present advisors in the course of the appeal process.

35. Had the point been taken before the Commissioners it is impossible to see what difference it would have made to the result save that they would almost certainly have thought it right to amend the Notice of Decision by the insertion of appropriate wording in relation to the period from 1st May 2000 to 31st August 2000. The only factual difference between the earlier (ITSA) period and the later (EDS) period is that in the former case the "right" of substitution was deleted from the NESCO agreement as from 6th May 2000. It is a fair inference that this was done at the prompting of ITSA which, as a government agency, did not wish to be associated with a contractual provision which lent colour to an argument that the arrangements should, for IR35 purposes, be interpreted as providing for services rather than for employment. However that may be, it is plain that Synaptek's separate arguments in relation to the earlier period would, if anything, have been weaker than in relation to the later period.

36. Had the point been taken before the Commissioners they would have had the power to amend the Notice of Decision in an appropriate manner and otherwise to confirm it: see Section 10 of the Social Security Contributions (Trustor of Functions,) Act 1999. Since the facts were not in dispute there is no point in remitting the case to them to consider the point. The Court has power to make the necessary amendments to the Commissioners' determination (see Section 56(6) of the Taxes Management Act 1970) and I propose to exercise that power.

SYNAPTEK LTD V GRAEME YOUNG (HMIT) (2003)

[2003] EWHC 645 (Ch)

Ch D (Hart J) 28/3/2003

TAX - COMMERCIAL LAW - EMPLOYMENT

NATIONAL INSURANCE CONTRIBUTIONS : EMPLOYED EARNER'S EMPLOYMENT : CLASS I : WORKER'S ATTRIBUTABLE EARNINGS : SERVICE COMPANIES : HYPOTHETICAL CONTRACTS : INDIRECT CONTRACTS : DURATION : INTERMEDIARY : IR35 LEGISLATION : PERSONAL SERVICE COMPANIES : BUSINESS ON OWN ACCOUNT : CONTROL OF WORKERS : RIGHT OF SUBSTITUTION : INTELLECTUAL PROPERTY RIGHTS : PROFESSIONAL INDEMNITY INSURANCE : FLEXIBILITY OF HOURS : MUTUALITY OF OBLIGATIONS : QUESTIONS OF FACT : QUESTIONS OF LAW : MIXED FACT AND LAW : FINANCE ACT 2000 : REG.6(1) SOCIAL SECURITY CONTRIBUTIONS (INTERMEDIARIES) REGULATIONS 2000 : PARTS I-V SOCIAL SECURITY CONTRIBUTIONS AND BENEFITS ACT 1992

The General Commissioners were entitled to find, as a question of mixed fact and law and applying reg.6(1) Social Security Contributions (Intermediaries) Regulations 2000 SI 2000/727, that arrangements between a software engineer and his client for the performance of services were such that, had they taken the form of a contract between the engineer and client, it would have been a contract of service with the engineer as employee. The engineer's service company was therefore treated as liable to pay primary and secondary Class I contributions in respect of his attributable earnings from that engagement.

Appeal by way of case stated from the decision of the General Commissioners dismissing an appeal by a service company ('Synaptek') from a decision of the Inland Revenue that Synaptek was liable to pay primary and secondary Class I contributions in respect of the attributable earnings of a software engineer ('GS').

Synaptek had entered into an agreement with a company ('EDS') for the performance of services by GS.

The Inland Revenue concluded under reg.6(1) Social Security Contributions (Intermediaries) Regulations 2000 SI 2000/727 that the circumstances of the arrangements were such that, had they taken the form of a contract between GS and EDS, GS would be regarded for the purposes of Parts I-V Social Security Contributions and Benefit Act 1992 as employed in employed earner's employment by EDS.

On appeal Synaptek contended that the contract was one for services and relied on the following aspects: (i) it was in business on its own account (as was GS, notionally); (ii) the limited control by EDS of GS' performance of the services; (iii) the right to substitute alternative personnel; (iv) the fact that Synaptek was responsible for GS's training and the provision of computer facilities at its own premises; (v) the express provisions in relation to intellectual property rights; (vi) the requirement for professional indemnity insurance; (vii) the flexibility of the hours worked by GS; and (viii) the use by him of his own reference books.

Synaptek also contended that the question under reg.6(1) of the Regulations was a question of law so that the Court of Appeal was free to substitute its own opinion.

In support of the contention that the contract was one of service, the Revenue relied on the following facts: (a) the minimum hours to be worked were broadly equivalent to a normal working week; (b) the only risk borne by GS was the insolvency of EDS; (c) the duration of the contract was for a fixed period rather than in relation to the completion of a particular project; (d) GS worked alongside EDS employees and was sufficiently integrated with its workforce to have a line manager; and (e) the requirement that GS complied with all EDS instructions.

HELD: (1) The fact that the tribunal was asked by reg.6(1) of the Regulations to hypothesise a contract comprising the arrangements directly between the worker and the client did not by itself convert the question of what those arrangements were from being a question of mixed fact and law into a pure question of law.

(2) For the purposes of reg.6(1) of the Regulations, the respective obligations of GS and EDS had to be identified and, on the hypothesis that there was a contract between them, a conclusion formed as to whether that contract was a contract of service or a contract for services.

The authorities showed that there was no one test that was conclusive for determining into which category a particular contract fell.

(3) The fact that Synaptek was in business on its own account was no doubt an important contextual circumstance to be taken into account in determining whether the particular notional contract under which GS was engaged by the client was one for services or of service, but it was no more than that, and the weight to be given to it was a matter for the commissioners.

(4) The commissioners were right to conclude that there was mutuality of obligation between EDS and Synaptek in the hypothetical contract.

(5) The commissioners were entitled to regard the substitution clause in the contract as one fact among others, and, in assessing the weight to be given to it, to take into account the extent to which the provision was utilised in practice.

(6) The commissioners' reference to the principles set out in FS Consulting Ltd v Patrick McCaul (HMIT) (2002) LTL 18/2/2002 was no more than an efficient and economical way of encapsulating the relevant principles and one that was justified by the close contextual similarity of the facts in that case to the present one.

It did not demonstrate that they misdirected themselves.

(7) The commissioners had not misdirected themselves in law and there was evidence before them that made the conclusion that they reached a possible one.

The relative weight to be given to the various factors was a matter for the commissioners and it was not possible to say that they were wrong in law in their conclusion. Appeal dismissed.

Conrad McDonnell instructed by Bond Pearce for the claimant. Clive Sheldon instructed by Solicitor of Inland Revenue for the defendant.

LTL 25/4/2003 : (2003) STC 543 : (2003) ICR 1149 :
Times, April 7, 2003

Document No. AC0104811

TILBURY CONSULTING LTD v MARGARET GITTINS (HMIT) (SPC NO.0579) (2003)

Sp Comm (AN Brice) 15/8/2003

TAX - CIVIL PROCEDURE

DIRECTIONS : WITNESSES : SUMMONS : INTERESTS OF JUSTICE : CLIENTS : REAL COMMERCIAL RISK : EMPLOYED EARNERS : CONTRACTS OF SERVICE : NOTIONAL CONTRACT

The interests of justice were best served by the grant of a witness summons even though the summons posed a real commercial risk to the appellant taxpayer.

Preliminary hearing on directions in an appeal from a decision of the respondent.

The appellant's director ('R') contracted with the appellant ('TCL') who contracted, through another company, with Ford Motor Company ('Ford').

The issue on the appeal was whether R would have been regarded as employed in employed earner's employment by Ford if he had contracted directly with Ford.

The respondent wrote to a Ford employee ('B') to establish the nature of R's engagements with Ford via a list of questions.

B answered the list and when questioned again voiced his displeasure at having been troubled by the matter again.

The respondent sought a witness summons to be issued requiring B to give oral evidence at the appeal as it was necessary to hear from both parties to the notional contract.

TCL objected that there was a real commercial risk that B or Ford might conclude that the arrangements with TCL were more effort than they were worth if they were summoned to the appeal and argued for B's evidence to be in writing according to the letters he had already answered.

HELD: The witness summons was to be issued.

The interests of justice were the overriding objective and they were best served by the grant of the summons.

The presumption was that an application for such a summons would normally be granted.

The desirability of producing evidence from both the worker and the client was emphasised in the explanatory leaflet on IR35 appeals and the decision in Lime-IT Ltd v Justin (2003) STC (SCD) 15.

It was clear that B had relevant evidence to give that might be expanded or clarified by oral evidence.
Judgment accordingly.

Theresa Naylor of Accountax Consulting Ltd (chartered tax advisers) for TCL. Barry Williams of the Inland Revenue Appeals Unit London for the respondent.
LTL 11/9/2003 : (2004) STC (SCD) 1

Document No. AC0105730

0379

WITNESS SUMMONS - application for - objected to - whether commercial risk to taxpayer ever-rides the interests of justice - no -application allowed - The Special Commissioners (Jurisdiction and Procedure) Regulations1994 SI 1994 No. 1811 Reg 5(1)

THE SPECIAL COMMISSIONERS

TILBURY CONSULTING LIMITED — **Appellant**

- and -

MARGARET GITTINS (HM INSPECTOR OF TAXES) — **Respondent**

Special Commissioner: DR A N BRICE

Sitting in public in London on 18 July 2003

Miss Theresa Naylor, of Accountax Consulting Limited, Chartered Tax Advisers, for the Appellant

Mr Barry Williams, of the Inland Revenue Appeals Unit London, for the Respondent

REASONS FOR DIRECTION

Background

1. On 12 June 2003 the Special Commissioners gave notice of a preliminary hearing in this appeal which is an appeal by Tilbury Consulting Limited (the Appellant) against a decision of Mrs Margaret Gittins (the Respondent). Thereafter the parties corresponded and agreed a number of directions. However, the Respondent wanted a witness summons to be issued to Mr Ian Baker of Ford Motor Company (Ford) requiring his attendance at the hearing of the appeal to give oral evidence but the Appellant objected. The preliminary hearing was held on 18 July 2003 and a number of Directions were given at that hearing. Direction (2) was that, on the application of the Respondent, the witness summons would be issued. Direction (2) stated that reasons for the Direction would be given separately. These are the reasons referred to.

The Regulations

2. The procedure before the Special Commissioners is governed by the Special Commissioners (Jurisdiction and Procedure) Regulations 1994 SI 1994 No. 1811. Regulation 5 contains the provisions about the summoning of witnesses and the relevant part provides:

> **"5(1) Where a party to any proceedings requires the attendance of a person at the hearing of those proceedings to give evidence or to produce any document in his possession, custody or power relevant to the subject matter of the proceedings, a Special Commissioner may, on the application of that party, issue a summons (in this regulation referred to as a "witness summons") requiring the attendance of that person at the hearing, or the production of the document, wherever that person may be in the United Kingdom".**

The facts relevant to the application

3. Mr Roger Tilbury, a director of the Appellant, contracts with the Appellant who contracts with Compuware who contracts with Ford. The issue in the appeal is whether, had the arrangements taken the form of a contract between Mr Tilbury and Ford, Mr Tilbury would be regarded as employed in employed earner's employment by Ford (see *F S Consulting Limited v McCaul* [2002] STC (SCD) 138 at paragraph 8(2)).

4. On 7 September 2001 the representatives of Mr Tilbury contacted the Inland Revenue and asked for an opinion about his status. With the consent of Mr Tilbury, the Respondent wrote on 19 February 2002 to Mr Ian Baker of Ford. The Respondent said that she had received an enquiry in respect of Mr Tilbury who supplied consultancy services through his own limited company to Ford. She said that she needed to establish the exact nature of the terms and conditions which existed in respect of the engagements and asked Mr Baker to provide information in reply to twenty-two detailed questions.

5. On 18 July 2002 Mr Baker sent a reply by facsimile transmission to the Respondent's twenty-two questions. On 6 August 2002 the Respondent wrote to the Appellant's representatives to say that she had considered the information supplied by

Ford and was of the opinion that, if there had there been a contract between Ford and Mr Tilbury, it would be considered to be a contract of service. Further correspondence between the parties followed and, on 4 December 2002, the Respondent wrote again to the Appellant's representatives to say that she had not changed her view. The last paragraph of that letter stated that the opinion in it did not create a decision subject to appeal but the Appellant could request a section 8 decision against which there was a right of appeal.

6. Without informing the Appellant of her intention so to do the Respondent wrote again to Mr Baker on 6 January 2003 and asked for some further information about the use of a substitute if Mr Tilbury were not available. Mr Baker replied on 14 January 2003 to give the information requested. The tone of his reply gave the impression that he had not been too pleased to have been troubled again about the matter.

The arguments of the Inland Revenue

7. For the Inland Revenue Mr Williams applied for the witness summons. He argued that, in order to decide the issue in the appeal, it was necessary for the Special Commissioners to have evidence from both parties to the notional contract and he referred to the supplement to the Explanatory Leaflet about appeals and other proceedings before the Special Commissioners entitled ""IR35" Appeals" published by the Presiding Special Commissioner on 21 March 2002. He also relied upon paragraph 10 in *Lime-IT Limited v Justin* [2003] STC (SCD) 15. If a witness summons were not issued it would mean that the appeal would be decided without oral evidence from one of the parties to the notional contract and the Special Commissioners would be unable to see and hear a witness give that evidence and ask questions of their own. It would not be adequate for further information to be obtained in writing or through the Appellant's representatives. Mr Williams argued that the interests of justice over-rode the arguments put forward on behalf of the Appellant.

The arguments of the Appellant

8. For the Appellant Miss Naylor argued that there was a real commercial risk to the Appellant if the witness summons were issued. One of Mr Tilbury's contracts had already been terminated and there was a real risk that Mr Baker or Ford might conclude that the arrangements with Mr Tilbury were more trouble than they were worth. The tone of Mr Baker's second letter of 14 January 2003 indicated that he might be losing his patience. Further, Mr Baker had already written twice to the Inland Revenue and so his evidence was in writing. The Appellant did not challenge the written evidence and the oral evidence would only duplicate it. Ms Naylor distinguished *Lime-IT* where there was no evidence from the client but in this appeal there was evidence in writing from Ford. Ms Naylor relied upon regulation 17(6) which provided that the Tribunal could not refuse to admit evidence which would be admissible in proceedings before a court of law. She argued that, under regulation 5(4)(b), Mr Baker could not be cross-examined by the Inland Revenue and it was, therefore, difficult to see what his presence would add.

Reasons for directions

9. Before considering the arguments of the parties I set out the relevant provisions of the supplement to the Explanatory Leaflet referred to by Mr Williams. The relevant paragraphs state:

> "1. **What is an IR35 appeal?**
> An IR35 appeal is an appeal against a decision of the Inland Revenue that payments made to intermediaries such as service companies should be treated as earnings of the worker for the purposes of income tax and/or national insurance contributions.
>
> In IR35 appeals the worker is called "the worker", the service company (or other intermediary) is called "the intermediary", and the person, firm or company to whom the worker supplies work is called "the client".
>
> 5. **Why is an IR35 income tax appeal unusual?**
> An IR35 income tax appeal is unusual because it is the intermediary which receives the decision from the Inland Revenue and so it is the intermediary which is the appellant in the appeal. However, the two persons most affected by the decision of the Inland Revenue are the worker and the client and neither of these are the appellant in the appeal
>
> 8. **What oral evidence is likely to be needed?**
> Since the question to be decided is whether the worker should be regarded as an employee of the client it would be helpful for both the worker and someone from the client to give oral evidence about the factors mentioned in 6 above. Oral evidence would also be useful about: the extent to which the terms of the written contracts have been carried out; whether there has been any unwritten variation in the contracts; and whether any additional terms have been implied in the contracts.
>
> 9. **How should I get evidence from the client?**
> You can ask someone from the client to attend at the hearing of your appeal and to give evidence on your behalf.
>
> If you wish to make sure that someone comes then you can apply in writing for a witness summons. Please read paragraph 6 of the Explanatory Memorandum which tells you how to do this."

10. These paragraphs explain the desirability of producing evidence from both the worker and the client. In *Lime-IT* there was no witness to give evidence on behalf of the client and the Special Commissioner said, in paragraph 10:

> "In future cases on this legislation (and its income tax equivalent) the Special Commissioners will wish to explore at a preliminary hearing whether it is possible to obtain evidence from the client."

11. Once again this emphasises the desirability of producing evidence from both the worker and the client.

12. With those matters in mind I turn to consider the arguments of the parties and here I have to balance the interests of justice on the one hand and the commercial risk to Mr Tilbury on the other.

13. Dealing first with the interests of justice this is, of course, the over-riding objective. Although regulation 5 gives the Special Commissioners a discretion as to whether to issue a witness summons the presumption must be that an application for such a summons will normally be granted. Regulation 5(11) provides that a person on whom a witness summons has been served may apply to have it set aside and no doubt that would be done if a summons were not applied for in good faith, or if the witness was unable to give relevant evidence, or if the application were irrelevant, speculative or oppressive. In this appeal I am satisfied that the application is none of those things and it is clear that Mr Baker has relevant evidence to give. The document published by the Presiding Special Commissioner, and the decision in *Lime-IT*, emphasise the desirability of his giving it. It is also relevant that, although the Appellant in this appeal is Tilbury Consulting Limited, there will be no difficulty in Mr Tilbury personally giving oral evidence about his notional contract with Ford. It is, therefore, desirable for the other party to the notional contract (Ford) to give oral evidence about it as well.

14. The Appellant argues that Mr Baker's evidence is already in documentary form and that the oral evidence will only repeat this. However, that is not inevitable and the documentary evidence may well be expanded and/or clarified by oral evidence.

15. The Appellant's main argument is the commercial risk faced by Mr Tilbury. Whilst fully appreciating this I have nevertheless concluded that the interests of justice are best served by granting the application for the issue of the witness summons.

Direction

16. For the above reasons a Direction has been given that a witness summons be issued to Mr Ian Baker of Ford requiring his attendance at the hearing of the appeal to give oral evidence. When the date of the hearing has been fixed the summons will be issued.

Nuala Brice

DR NUALA BRICE

SPECIAL COMMISSIONER

RELEASE DATE

15 AUG 2003

SC 3020/03
12.08.03

SPC00425

National insurance - earnings of workers supplied by service companies etc. - provision of services through intermediary - worker establishing information technology company - company contracting with agency for provision of information technology services to client of agency - whether company liable for national insurance contributions on earnings of worker - whether, if arrangements had taken the form of a contract between worker and client, worker would have been regarded as gainfully employed by the client - Social Security Contributions (Intermediaries) Regulations 2000 SI 2000/727, Reg 6(1)(c) - Social Security Contributions and Benefits Act 1992, section 4A

THE SPECIAL COMMISSIONERS

ANSELL COMPUTER SERVICES LIMITED **Appellant**

- and -

DAVID RICHARDSON
(HM INSPECTOR OF TAXES) **Respondent**

Special Commissioner: G AARONSON QC

Sitting in London on 23 March and 16 April 2004

David Smith, Accountax Consulting Limited, on behalf of the Appellant

Kevin Gleig, HMIT, Regional Appeals Unit on behalf of the Respondents

DECISION

The nature of these appeals

1. These appeals are brought by Ansell Computer Services Limited ("ACSL") which has its registered office in St Albans, Hertfordshire. ACSL has been in business since 1986.

2. From that time until the present Mr Michael Ansell has been a director and shareholder in ACSL and, quite clearly, is its key asset.

3. Mr Ansell is a very experienced, and very highly regarded, computer software engineer, with particular expertise in the defence sector. For several years he has been working on the software elements of weapons and other defence systems, acting as part of a large team of specialists given the overall task of designing, developing and testing the relevant electronic systems.

4. In the periods in question Mr Ansell worked at the premises of two different companies working in the defence sector. The first was Alenia Marconi Systems Limited ("Marconi") and the second was BAe Systems Avionics Limited ("BAe"). Mr Ansell's work for both of the companies was at the same premises (BAe had taken over some of the work previously carried out by Marconi following the acquisition in 1999 of the defence electronics business of GEC and the Marconi group by British Aerospace PLC).

5. As a matter of form ACSL's appeal is against Decision Notices given by Mr M Justin, an officer of the Board of Inland Revenue, under section 8 Social Security Contributions (Transfer of Functions, etc.) Act 1999. The Decision Notices in question relate to the officer's opinion as to whether ACSL is liable to pay National Insurance Contributions in respect of the payments made by Marconi and BAe for the work performed by Mr Ansell. This potential liability arises from what is commonly referred to as the "IR35" legislation - i.e. the Schedule E and NIC rules first announced in the Inland Revenue Press Release No 35 following the Spring Budget of 2000. In brief, these rules apply where a person (described as "the worker") is made available to work for some other person (described as "the client") by a third party (usually the worker's own limited company and referred to as "the intermediary"). Applying those terms to the present case, Mr Ansell is "the worker", his company ACSL is "the intermediary", and Marconi and BAe were "the clients".

6. I will in due course refer to the legislation, the contractual arrangements (so far as they can be ascertained or inferred), the nature of Mr Ansell's work and the way in which he provided it. I will also summarise the guidance given in the case law. I have used the word "summarise" advisedly, as the alternative would be to write

7. a decision of inordinate length, given the fact that the parties' skeleton arguments together run to about 90 pages and cite well over 30 authorities. I mention this not to criticise the parties, whose arguments were very helpful and well presented. The point I am making is simply that cases of this sort have to be decided upon an overall view of the facts in the light of the guidance given by earlier cases.

8. At the heart of the dispute is the question whether Mr Ansell would have been employed under a contract of service if (contrary to the actual contractual arrangements) he worked for the clients under a direct contract. To put it another way, supposing that Mr Ansell had worked for Marconi and BAe under a direct contract between him and them, would he have been their employee?

9. Both parties agree that what might be referred to as the onus of proof (i.e. satisfying me that the supposed relationship would have been a contract for the provision of services (i.e. as an independent contractor and not as an employee)) rests upon the Appellant, ACSL.

10. For the reasons which I shall explain, I have formed the view that Mr Ansell would, on the supposed direct contractual relationship with Marconi and BAe, have worked for them in the periods in question as an independent contractor, and not as an employee.

The Decision Notices

The appeals against the Decision Notices

11. In January 2001 Mr Ansell asked the Inland Revenue for formal decisions on two periods of work which he performed. The first was from 1 July 2000 until 30 September 2000, when he worked for Marconi. The other was from 2 October 2000 to 30 March 2001, when he worked for BAe. The Inspector gave his opinion on 27 December 2002. This was disputed by the Appellant whose representatives asked for formal Decision Notices to be issued. These were made on 16 May 2003.

The relevant legislation

12. Section 75 of the Welfare Reform and Pensions Act 1999 inserted, with effect from 22 December 1999, a new section 4A into the Social Security Contributions and Benefits Act 1992.

13. That new section enabled the Treasury to make Regulations which would give effect to the IR35 proposals for NIC purposes. The key provisions of section 4A are as follows –

> "(1) Regulations may make provision for securing that where –

(a) an individual ("the worker") personally performs, or is under an obligation personally to perform, services for the purposes of a business carried on by another person ("the client"),

(b) the performance of those services by the worker is (within the meaning of the regulations) referable to arrangements involving a third person (and not referable to any contract between the client and the worker), and

(c) the circumstances are such that, were the services to be performed by the worker under a contract between him and the client, he would be regarded for the purposes of the applicable provisions of this Act as employed in employed earner's employment by the client,

relevant payments or benefits are, to the specified extent, to be treated for those purposes as earnings paid to the worker in respect of employed earner's employment of his.

(2) For the purposes of this section –

(a) "the intermediary" means –

(i) where the third person mentioned in subsection (1)(b) above has such a contractual or other relationship with the worker as may be specified, that third person, or

(ii) where that third person does not have such a relationship with the worker, any other person who has both such a relationship with the worker and such a direct or indirect contractual or other relationship with the third person as may be specified; and

(b) a person may be the intermediary despite being –

(i) a person with whom the worker holds any office or employment, or

(ii) a body corporate, unincorporated body or partnership of which the worker is a member;

and subsection (1) above applies whether or not the client is a person with whom the worker holds any office or employment.

(3) Regulations under this section may in particular, make provision –

(a) for the worker to be treated for the purposes of the applicable provisions of this Act, in relation to the specified amount of relevant payments or benefits (the worker's "attributable earnings"), as employed in employed earner's employment by the intermediary;

(b) for the intermediary (whether or not he fulfils the conditions prescribed under section 1(6)(a) above for secondary contributors) to be treated for those purposes as the secondary contributor in respect of the worker's attributable earnings."

14. The expression "employed earner's employment" in subsection 4A(1)(c) is explained in section 2 of that Act as meaning employment either under a contract of service or in an office with emoluments chargeable to income tax under Schedule E.

15. The Regulations empowered by section 4A of the 1992 Act are the Social Security Contributions (Intermediaries) Regulations 2000. The key passage in the Regulations is to be found in paragraph (1) of Regulation 6 which is in very similar (but not identical) terms to the provisions of subsection 4A(1) of the 1992 Act. The differences are accounted for by the fact that some of the expressions are terms defined elsewhere in the Regulations. Regulation 6(1) reads as follows –

"(1) These Regulations apply where –

(a) an individual ("the worker") personally performs, or is under an obligation personally to perform, services for the purposes of a business carried on by another person ("the client"),

(b) the performance of those services by the worker is carried out, not under a contract directly between the client and the worker, but under arrangements involving an intermediary, and

(c) the circumstances are such that, had the arrangements taken the form of a contract between the worker and the client, the worker would be regarded for the purposes of Parts I to V of the Contributions and Benefits Act as employed in employed earner's employment by the client.

(2) Paragraph (1)(b) has effect irrespective of whether or not –

(a) there exists a contract between the client and the worker, or

(b) the worker is the holder of an office with the client.

(3) Where these Regulations apply –

(a) the worker is treated, for the purposes of Parts I to V of the Contributions and Benefits Act, and in relation to the amount deriving from relevant payments and relevant benefits that is calculated in accordance with Regulation 7 ("the worker's attributable earnings"), as employed in employed earner's employment by the intermediary, and

(b) the intermediary, whether or not he fulfils the conditions prescribed under section 1(6)(a) of the Contributions and Benefits Act for secondary contributors, is treated for those purposes as the secondary contributor in respect of the worker's attributable earnings,

and Parts I to V of that Act have effect accordingly.

(4) Any issue whether the circumstances are such as are mentioned in paragraph (1)(c) is an issue relating to contributions that is prescribed for the purposes of section 8(1)(m) of the Social Security Contributions (Transfer of Functions, etc.) Act 1999 (Decision by Officer of the Board)."

16. There is no dispute that Mr Ansell is "the worker" for the purposes of Regulation 6 (and also section 4A of the 1992 Act). Likewise there is no question that Marconi (and, subsequently, BAe) is "the client" for the purposes of Regulation 6 (and the "third person" referred to in section 4A).

17. The dispute turns solely upon the question whether the circumstances are those described in sub-paragraph 6(1)(c) of the Regulations (corresponding to subsection 4A(1)(c) of the 1992 Act), which I have italicised for ease of reference.

The Evidence

18. Three witnesses gave evidence. The first was Mr Michael Ansell, "the worker" in relation to each of the two contracts under dispute.

19. The second was Mr Paul McIntosh, who was an employee of BAe, and was the Project Software Manager for the particular project on which Mr Ansell worked. This project involved the development of certain radar systems. Evidence as to the nature of the systems, and the particular elements of it on which Mr Ansell and others worked was given in sufficient detail for me to form a broad understanding of it. Given that the work relates to elements of defence systems I do not think it appropriate to go into any more detail than is necessary in this written Decision. Accordingly, for present purposes I shall simply describe this project as "the D Project".

20. The final witness was Mr David Coulbeck. At the material time he was employed by Marconi as Software Project Manager on the earlier of the two defence projects on which Mr Ansell worked. For the same reason as applies to the D Project I think it sufficient to note that the Marconi project involved the software for part of a guidance system, and I shall refer to it simply as "the B Project".

21. Each of these witnesses produced a witness statement, upon which they were examined and cross-examined. Mr Ansell was called as witness for the Appellant, represented by Mr David Smith. He was cross-examined by Mr Kevin Gleig for the Inland Revenue. Mr McIntosh and Mr Coulbeck were witnesses for the Inland Revenue, and were called by Mr Gleig and cross-examined by Mr Smith.

22. I consider that each of the witnesses gave evidence to the best of their recollection. For the most part the evidence of each of them was consistent with the evidence given by the others, and also with the (fairly scant) relevant documentation. There was, however, one significant point on which the evidence of Mr Ansell was inconsistent with that of Mr Coulbeck (while, on the same point, Mr Ansell's evidence was consistent with the evidence given by Mr McIntosh). This related to the question whether Mr Ansell could be required to work on any given occasion during the period of his contract (as Mr Coulbeck thought was the case) or whether, on the other hand, Mr Ansell was free to take time off to suit his own convenience without seeking the permission of Mr Coulbeck in his capacity as Project Manager. I shall discuss this in a little more detail later on, but on this point I have formed the view that Mr Ansell's evidence is to be preferred as representing the true contractual state of affairs. Mr Coulbeck, I believe, assumed that he had the power to require Mr Ansell to work on any specified occasion. But since he was not involved in making the contractual arrangements and the issue had not come up in practice he probably did not know what the true position was.

The Contractual Chain between Mr Ansell and Marconi

23. From the evidence before me the contractual chain linking Mr Ansell with Marconi was as follows. On 30th June 2000 ACSL ("the intermediary" for the purposes of the IR35 rules, and "the supplier" as described in the contract) entered into a contract with a company called Centre Dynamics Limited ("CDL") (described in the contract as "the agent"). Under this agreement CDL would find an "End-user" for the services supplied by ACSL. The contract was expressed to be for an unlimited period, until terminated by breach or mutual consent. It included terms entitling CDL to terminate the agreement if the supplier fails to perform the tasks required for any End-user with reasonable skill.

24. The agreement also contained a detailed provision enabling ACSL to withdraw from part of the work placed by CDL with the End-user, provided (i) that the End-user was given reasonable notice, (ii) that the absence would not interfere with the

overall achievement of the work programme or its agreed timetable, and (iii) if appropriate ACSL would offer a suitably qualified substitute to continue the work for the End-user.

25. One other significant term needs mentioning. The contract included a provision which required CDL to conclude an agreement with each End-user which itself reflects the terms of the agreement between ACSL and CDL. It was specifically provided that such an agreement would include, inter alia, a substitution clause in the form contained in the ACSL-CDL agreement, the effect of which is summarised above.

26. So far as payment is concerned, the agreement provided that CDL would pay ACSL £40.20 per hour for the work performed by ACSL, subject to a maximum number of hours set out in a schedule (which specified the services to be rendered to the End-user). That schedule stated that the total number of hours would not be expected to exceed 550.

27. Applying the provisions of that agreement to the known facts in the present case, the agreement was as follows. ACSL would provide the services of Mr Ansell to Marconi for the purpose of carrying out work of a particular nature, for what was expected to be a maximum of 550 hours; CDL would pay ACSL at the rate of £40.20 per hour. The agreement does not control the amount of money which CDL would charge Marconi, which would be a matter for negotiation between CDL and Marconi. The difference between the price paid by Marconi to CDL and the price paid by CDL to ACSL would represent CDL's profit margin.

28. To continue the contractual chain, it is clear that some arrangement was entered into by CDL with Marconi, under which Mr Ansell would be provided as a contractor to work on the B Project. There is, however, no signed contract to this effect, nor was any evidence on this given by CDL which, I was told, is no longer in business. Regrettably there is also no clear evidence as to this contractual link from Marconi itself, as Mr Coulbeck made it clear that he was not responsible for the contractual terms governing the engagement of contractors. The problems that can arise by imposing the tax or NIC liability under the IR35 legislation upon an intermediary (ACSL), while providing no means of enabling the intermediary to require "the client" (Marconi in this case) to explain its contractual arrangements with another party (CDL in this case) has been commented on by the Special Commissioner Dr Avery Jones in *Lime-IT Limited -v- Justin* [2003] STC (SCD) 15 at page 20a; and, more extensively, by the Special Commissioner Dr Brice in *Tilbury Consulting Limited -v- Gittins* No 1 [2004] STC (SCD) 1. I share their concern; but in the present case I consider that the material before me is sufficient to enable me to form a view as to the nature of this particular link in the contractual chain.

29. The relevant documents, much relied on by Mr Gleig, take the form of amendments to purchase orders raised by Marconi on CDL. They are barely

legible, and are cryptically expressed. For instance, one of them refers to extending the "L of L". From the witness evidence it is tolerably clear that "L of L" stood for the "limit of liability" of Marconi, and the amount of the LoL represented the maximum number of hours at an agreed hourly rate (£42 in the case of one of the documents) for which Marconi would engage the services of Mr Ansell. Following extensive discussion and questioning the witnesses on this, it seems that this really did represent the *maximum*, and was not a fixed number of hours for which Marconi was agreeing to engage Mr Ansell's services.

30. On the evidence which I have heard it seems that the parties were, in practice, able to get on with the arrangement in a practical way and without difficulty. I conclude that the practical arrangement agreed between CDL and Marconi was that Mr Ansell would work at Marconi on the specified project for a number of hours which was not expected to exceed 550. Because of the absence of clear evidence on the point, I have not been able to conclude whether or not Marconi had been made aware by CDL of the key terms of the agreement between ACSL and CDL. Specifically I do not know whether Marconi had been made aware of, and agreed to, the substitution provisions in the ACSL-CDL contract. However, I infer from the evidence of the witnesses that the practice of substitution was recognised by Marconi (and also BAe), even though it would rarely arise in practice.

The framework in which Mr Ansell worked in practice at Marconi

31. I have already described the written contractual links, so far as they can be found. I shall now flesh out the relationship between Mr Ansell and Marconi from the witness evidence given before me.

32. Mr Ansell, together with a few other individuals, was engaged as a contractor to work on the B Project. There were in fact four teams, each comprising approximately six individuals, with each team devoting itself to a particular element of the software package involved in the B Project. Although his engagement (as the personnel provided by CDL to Marconi) was for the 3 months beginning July 2000, this was in fact a renewal of similar arrangements which had started 2 years earlier. It was explained to me that the B Project had a number of stages, with different elements being involved in each stage. The policy of Marconi was to use permanent employees for the majority of the work, with specialist contractors being added to the teams where necessary to ensure that the teams could accomplish their respective tasks as each stage of the B Project came to be worked upon. The non-employee contractors were, in a sense, "buffer stock", being personnel who would supplement the teams with the necessary expertise, but on the basis that they could be dispensed with without the complications which employment law imposes in respect of employees. Indeed, Mr Coulbeck was of the view that he could dispense with the services of Mr Ansell, and other contractors in his position, on as little as one day's notice if, for

whatever reason, he did not consider that their contribution was needed to complete any given stage of the project.

33. So far as working hours were concerned, Mr Ansell was adamant that he was not obliged to work any particular number of hours in any given day or week, that he could turn up when he liked (subject only to safety considerations, which I shall expand upon in a moment). He was also adamant that he could take time off at his own choosing, say to play golf if he wished; and in such case he did not have to seek permission from Mr Coulbeck or anyone else, and would merely inform them as a matter of courtesy. While Mr Coulbeck did not share this view I have, as noted earlier, concluded that Mr Ansell's evidence is to be preferred on this point, particularly since it coincided with the views of Mr McIntosh (who was Mr Coulbeck's opposite number in the BAe contract).

34. As it happens, Mr Ansell was as diligent as he was skilled, and he did in fact work fairly conventional hours, so that his perceived freedom to turn up or not as he wished was a matter of principle rather than practice. There were also a number of significant factors which encouraged Mr Ansell to work at conventional times. First, he was part of a team which worked on particular elements of a particular phase of a weapon development programme. If his work lagged behind that of his colleagues, or raced too far ahead of them, there would be problems in co-ordinating their output. Secondly, as his computer programming work was wholly involved in secret defence projects it was inevitably the case that it had to be carried out on a secure computer system housed in a secure building. This meant that he had to use a particular computer at a particular workstation, and therefore could not do any of the actual work at home or elsewhere using a laptop etc. Thirdly, some of the non-computer equipment which he had to use from time to time was extremely expensive (certain items costing over £1 million) and therefore obviously having to be located in secure premises; but some of it could also be quite dangerous to use. Mr Ansell's evidence on this was graphic: when asked why he would not be permitted to work late at night in the secure premises, he explained that this was for "safety reasons. The company did not want people getting electrocuted whilst using expensive equipment". It seems that the chances of catastrophic events of that sort occurring would considerably increase if he, or any other contractor or employee, was permitted to work alone long before or long after normal working hours.

35. Although, for the reasons described, Mr Ansell was not permitted to carry out his work anywhere outside the designated secure premises, and using the designated secure computer system, he did in fact spend a few hours each week at home keeping himself abreast of new thinking and developments in his field. His evidence was that he would spend up to 5 hours a week doing this without any remuneration from Marconi and, insofar as it involved books or journals etc., at his own expense. This contrasted with the position of an employee, who would ordinarily expect to do this work during paid time, and with any out of pocket expenses borne by the employer.

36. As regards the number of days or hours worked on each particular phase of the project, Mr Ansell agreed that he did in fact work consistently throughout the 3 month period of the contract; but explained that this was so for the reasons described above - essentially to ensure that his work dovetailed with the work of colleagues in his team, and also with the work of the other teams working on the same phase of the development. He was clear in his own mind, however, that he was providing his services to achieve a particular task in the allotted timeframe, and that he had no right to expect that he would be offered the opportunity to work on the next phase. As it happened, however, he was re-engaged at the end of each phase until completion of the B Project.

37. So far as supervision and control was concerned, the evidence was that Mr Ansell had considerable expertise and therefore did not need instruction or control, in the traditional sense, as to how he carried out his responsibilities. However, he was working as part of a team which was working in conjunction with other teams, and consequently his work, like that of everyone else, had to be overseen by the project manager. Mr Ansell was also expected to take part in peer discussions, and did so regularly and diligently.

38. Finally, in a number of practical respects Mr Ansell, like other contractors, was treated differently by Marconi from its employees. For example he was not entitled to join the employee social club, or to use employee on-site parking facilities. He did not have any entitlement to a company pension plan, or share options, or company-related bonus payments, or healthcare or a company car. So far as pay was concerned, he did not receive sick pay or holiday pay, was not entitled to statutory paternity pay or redundancy payments if his particular work was curtailed. These were some of the practical consequences of being (as a matter of general law) a contractor, and not an employee, and hence falling outside the legislation and the non-statutory practices which benefited and protected employees. Indeed, avoiding the need to make these protections and benefits available to contractors was one of the commercial reasons that led Marconi to engage people like Mr Ansell as contractors and not as employees. This was a genuine commercial advantage sought by Marconi, and the corresponding disadvantage was something which Mr Ansell was genuinely prepared to accept in order to attain the greater element of flexibility and independence which contractor status conferred.

The contract with BAe in practice

39. Mr Ansell explained that by the end of September 2000 the B Project was just about complete and, so far as he was concerned, "my packages of work were complete".

40. Shortly beforehand he had a chance meeting with Mr McIntosh in the car park of the building where Mr Ansell was working on the B Project. At that time Mr McIntosh was the project software manager for the D Project (relating to certain radar systems). He was responsible for building the team to run the project, and had already engaged four BAe employees, some of whom had extensive experience. However, he considered that there was a need for the particular expertise which someone like Mr Ansell could bring, and wanted him to join the team.

41. The contractual arrangements involving Mr Ansell and BAe were very similar to those which I have described earlier in relation to Marconi. On 30th September 2000 ACSL entered into an agreement with CDL, in terms which are not materially different from the 30th June agreement described above. The services to be provided would be for a total number of hours not expected to exceed 1,000, and the rate of payment (as in the earlier agreement) was to be £40.20 per hour.

42. Again, as with the Marconi agreement, there is no evidence as to the arrangements entered into by CDL with BAe. Given that the arrangement seemed to work perfectly well in practice, I infer that BAe were broadly aware of CDL's agreement with ACSL (or, at least, with Mr Ansell). I also conclude that BAe were generally aware of the possibility of substitution if Mr Ansell would for some reason be unable to complete his work.

43. As to the practical aspects of the BAe arrangement, the evidence of Mr McIntosh (who, as noted above, was called as a witness by the Inland Revenue) was wholly consistent with that given by Mr Ansell. So far as concerned Mr Ansell's hours of work, holiday arrangements, notification of prospective absence etc., Mr McIntosh was quite clear that the arrangements concerning Mr Ansell were significantly different from those which applied to employees. For example, so far as holiday arrangements were concerned, the cross-examination was as follows -

> Question: "I am more concerned with the process of him [Mr Ansell] having to get permission or not."
> Answer: "There is no defined process in our company that I am aware of that requires contractors to ask for permission to take holiday."
> Question: "Is it fair to say that, in that regard, he would be different from an employee -"
> Answer: "He was different, definitely, in that area."

44. On another significant point Mr McIntosh echoed the evidence of Mr Coulbeck. So far as BAe was concerned, the only problems that would arise with the payment to Mr Ansell would be if his work *exceeded* the estimated and budgeted time. The time in this context was the six month period beginning 1st October, during which Mr Ansell was expected to work for no more than the specified number of hours for a total cost (to BAe) of approximately £51,480. If, for

whatever reason, there was insufficient work for Mr Ansell to do to justify that cost, then he would simply do less and the money would be saved. As Mr McIntosh put it "That is not a problem if I do not need his services, if we underspend; the only problem would occur if we exceeded that time." This was consistent with the general policy relating to contractors. When asked why he did not hire Mr Ansell for 18 or 24 months (being the estimated length of time to complete the D Project) he replied:

> "Because the policy in the company would be that contractors are hired for the shortest period of time and then when their services are no longer required, you get rid of them. But of course you would look at the end of a period if you still have tasks to carry out, you would resubmit the form, resubmit the justification, explain why you need someone and effectively start the process of recruitment again. But the company does not really encourage project managers to keep contractors longer than they need to be kept."

45. At this point (which has relevance to Mr Smith's argument based on mutuality of obligation) it is worth recalling the comments of Mr Coulbeck. In re-examination Mr Gleig asked Mr Coulbeck the following:

Question:	"Mr Smith asked if you had an obligation to provide work for Mr Ansell. In the period that is under review, which is the three month period, did you have an obligation to provide work throughout that period?"
Answer:	We had taken him on because we wanted him to do something, so if we suddenly found we no longer had any work, the project was cancelled or some such, then we would have closed the contract. He would have left us."
Question:	"How would you have given him notice?"
Answer:	"I believe, it was very short, like a day, I could give; whereas with a permanent member of staff I could not do that. It would be a much bigger issue because it was then redundancy."

46. As to the question of substitution, Mr McIntosh stated that the contracts manager of BAe informed him that he was in principle prepared to allow a substitution, providing of course that a suitable candidate could be found. On that aspect the evidence was that it would be hard but not impossible to find suitable candidates, and that Mr Ansell might know some suitable individuals with the requisite level of security clearance.

47. As with the Marconi arrangement, BAe did not give Mr Ansell rights relating to parking, car, pensions, share options, healthcare etc. There was no material difference between this aspect of his engagement with BAe and his engagement with Marconi.

48. As with the Marconi arrangements, Mr Ansell was in fact re-engaged on the D Project by BAe at the end of the six months, and has subsequently been further re-engaged so that he was still working on the project shortly before the hearing.

Overall impression as to bona fides

49. Standing back and taking the evidence of all three witnesses together, I am satisfied that the contractor relationship was seen by the respective parties (i.e., Mr Ansell on the one hand and Marconi and BAe on the other) as being significantly different from employment, and as having commercial advantages which were perceived by each of them to outweigh the disadvantages. I am satisfied that the arrangements were entirely bona fide, and were not designed to disguise or re-label what in reality would be thought of as employment.

Guidance from the cases

50. Having reached my conclusions on the evidence, I now turn to consider the guidance given by previous decisions in this and related areas.

51. As I mentioned at the outset, each of the written skeleton arguments given to me by Mr Smith and Mr Gleig referred very extensively to cases which have considered the difference, in various contexts, between employment and independent contractor status. I appreciate their diligence, and I have in reaching my conclusion taken account of the comments which they have made in relation to those cases.

52. However, the path which needs to be followed, while occasionally presenting new and unexpected vistas, is by now fairly well trodden, and I do not mean to belittle the effort of Mr Smith and Mr Gleig by confining myself to a handful of cases that seem to me to raise the relevant points.

53. I shall start with a very recent decision on the IR35 legislation, and the first (so far as I am aware) that has reached the High Court. This is the case of *Synaptek -v- Young* [2003] EWHC 645 (Chancery), a decision of Hart J. The case concerned the provision of computer software services through an intermediary company. The General Commissioners had decided that, on balance, under the hypothetical contract between the worker and the client the worker would have been an employee. Hart J held that the Commissioners' conclusion was clearly a possible one, and that they had not misdirected themselves in law, and accordingly he dismissed the appeal against their decision.

54. Hart J's judgment is a convenient place to recall the basic principles that have been developed over the years by the courts to differentiate between a contract of employment and a contract for the provision of services. At paragraph 16 he referred to the test propounded by MacKenna J in *Readymixed Concrete (South East) Limited -v- Minister of Pensions and National Insurance* [1968] 2 QB 497

at 515. This test has been cited on countless occasions. MacKenna J expressed the test in the following terms:-

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

55. This is clearly an important authority, although I would respectfully comment that I do not find this test to be invariably helpful. Expressions such as "for his master" and "control in a sufficient degree" can in some situations raise questions as to how one can tell whether those words are applicable to the case in hand; and the third requirement, to the effect that the other provisions of the contract have to be consistent with its being a contract of service, involves, as it seems to me, an element of circularity.

56. In paragraph 17 of his judgment Hart J refers to the judgment of Nolan LJ in *Hall -v- Lorimer* [1994] STC 23 at 28-29, where he said -

> "In cases of this sort there is no single path to a correct decision. An approach which suits the facts and arguments of one case may be unhelpful in another."

57. At paragraph 18 of his judgment Hart J referred to the judgment of Cooke J in *Market Investigations Limited -v- Minister of Social Security* [1969] 2 QB 173 at 184-185. Cooke J said that -

> "… The fundamental test to be applied is this: 'Is the person who has engaged himself to perform these services performing them as a person in business on his own account?' If the answer to that question is 'Yes', then the contract is a contract for services. If the answer is 'No', then the contract is a contract of service. No exhaustive list has been compiled and perhaps no exhaustive list can be compiled of the considerations which are relevant in determining that question, nor can strict rules be laid down as to the relative weight which the various considerations should carry in particular cases. The most that can be said is that control will no doubt always have to be considered, although it can no longer be regarded as the sole determining factor; and that factors which may be of importance are such matters as whether the man performing the service provides his own equipment, whether he hires his own helpers, what degree of financial risk

he takes, what degree of responsibility for investment and management he has, and whether and how far he has an opportunity of profiting from sound management in the performance of his task."

58. I accept that, on the facts of the present case, Mr Ansell did little of the particular things which Cooke J enumerated as factors which may be of importance. Mr Ansell did not hire his own helpers; he provided his own equipment only for a few hours a week at home; he did not take on any great financial risk (although he was dependent for his remuneration upon payment by CDL to ADSL); and he did not have any significant opportunity to profit from sound management in the performance of his task, whether with Marconi or with BAe. Indeed, Mr Gleig emphasised these very points in urging me to conclude that Mr Ansell should be regarded, on the hypothetical contractual arrangement between himself and Marconi/BAe, as an employee.

59. However, as Cooke J made clear, those particular factors *may* be of importance; but, on the facts of any particular case, they may not. In the present case I consider that they are not of sufficient importance. This is because the very nature of Mr Ansell's work, shrouded as it has to be in secrecy and performed in isolation from anyone apart from other individuals with similar levels of security clearance, does not permit him to exercise his profession in the entrepreneurial way that would be available to someone working in less sensitive areas of activity (whether in the I.T. field or elsewhere).

60. In this situation it seems to me appropriate to look more to other factors to help decide on which side of the line the hypothetical contractual arrangement would fall. The factors which appear to me to be of greater significance in the present case are:-

(i) the absence of any obligation on Marconi or BAe to keep Mr Ansell in work throughout the 3 months/6 months period of his respective engagements;

(ii) the absence of any obligation by Mr Ansell to put in a particular amount of work, whether each day or each week or in aggregate during his period of engagement;

(iii) the ability which Mr Ansell had to take time off at his own choosing, without seeking permission from the team leaders at Marconi or BAe; and

(iv) the ability to withdraw and suggest a substitute individual (which both Mr Ansell and Marconi/BAe regarded as genuine, even though it was very unlikely that the situation would in fact arise); and

(v) the various other practical matters (no company car, sick pay, holiday pay, social club etc.) which differentiated contractors from employees at a daily practical level.

61. I should mention one additional point which Mr Smith put forward very forcefully. He urged that Mr Ansell could not as a matter of law be regarded as an employee, because there was no obligation on Marconi or BAe to continue to use his services, and hence no "mutuality of obligations". He referred me to the case of *Montgomery -v- Johnson Underwood Limited* [2001] WCA Civ 318. This case concerned a claim for unfair dismissal by a telephonist who worked at a local company, but was given that job by an employment agency. The question arose as to whether she should be regarded as an employee of the local company or of the employment agency. The Court of Appeal held that the employment tribunal had erred in holding that the applicant was employed by the employment agency, notwithstanding that there was little or no control, direction or supervision of the applicant by the agency. The tribunal also considered that the absence of mutuality of obligation appeared to them to be largely irrelevant to the specific engagement. Longmore LJ said this:-

> "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: see *Nethermere (St Neots) Limited -v- Gardiner* [1984] IRLR 240, 245 per Stephenson LJ approved in *Carmichael -v- National Power PLC* [2000] IRLR 43, 45 per Lord Irvine of Lairg LC."

62. Given this clear statement by Longmore LJ, I see considerable force in Mr Smith's submission. Certainly the evidence given by Mr Ansell and Mr Coulbeck suggests that Marconi could have been entitled to terminate Mr Ansell's activities at virtually no notice; and Mr McIntosh's evidence likewise indicated that BAe might have considered itself able to terminate Mr Ansell's work at a time of its choosing.

63. I also note that Hart J in *Synaptek* referred to a number of cases which consider the issue as to whether mutuality of obligation is, as a matter of law, an irreducible requirement of a contract of employment. At paragraph 25 he said this -

> "There is now a considerable body of authority on the question whether an obligation on the employer to provide work is necessary and in all cases an indispensable attribute of a contract of employment: see *Nethermere (St Neots) Limited -v- Taverna and Gardiner* [1984] IRLR 240, *McLeod -v- Hellyer Bros Limited* [1987] 1 WLR 728, *Clark -v- Oxfordshire Health Authority* [1998] IRLR 125 and *Johnson Underwood Limited -v- Montgomery* [2001] EWCA Civ 318."

64. However, for myself I find that the question as to what elements of an arrangement are themselves critical to the existence of that mutuality is not always straightforward. I have reached the clear conclusion on all the evidence that Mr Ansell would not have been an employee in the hypothetical contract which the IR35 legislation requires us to construct. Accordingly, it is unnecessary for me to decide whether, as a matter of law, there would be insufficient mutuality of obligation to support an employee relationship.

Conclusion

65. In his Notice of Decision given on 16th May 2001 Mr Justin on behalf of the Board of Inland Revenue stated -

> "1. That the circumstances of the arrangements between Mr M J Ansell and Aliena Marconi Systems Limited for the performance of services from 1 July 2000 to 30 September 2000 are such that, had they taken the form of a contract between Mr M J Ansell and Aliena Marconi Systems Limited, Mr M J Ansell would be regarded for the purposes of Parts I to V of the Social Security Contributions and Benefits Act 1992 as employed in employed earner's employment by Aliena Marconi Systems Limited.
>
> 2. That Ansell Computer Services Limited is treated as liable to pay primary and secondary Class I Contributions in respect of the worker's attributable earnings from that engagement."

A similar decision was given in respect of the arrangements between Mr Ansell and BAe from 2nd October 2000 to 30th March 2001.

66. I disagree. Having considered the evidence I have concluded that the circumstances of the arrangements between Mr Ansell and Marconi/BAe are such that, had they taken the form of a contract between Mr Ansell and those companies, that contract would have been one for the provision of services and not of employment.

67. Accordingly the appeals succeed.

GRAHAM AARONSON QC
SPECIAL COMMISSIONER

Release Date: 29 July 2004

SC 3061/03

CASES REFERRED TO IN SKELETON ARGUMENTS

Bank voor Handel en Scheepvart NV v The Administrator of Hungarian Property 35 TC 311

Barnett v Brabyn [1996] STC 71

Battersby v Campbell [2001] STC 189

Carmichael v National Power [1999]1 WLR 2042

Clark v Oxfordshire Health Authority [1998] IRLR 125

Davis v Braithwaite (1933) 18 TC 198

Express and Echo Publications Limited v Tanton [1999] IRLR 367

F S Consulting Limited v McCaul [2002] STC (SCD) 138

Global Plant Limited v Secretary of State of Social Security [1971] 1 QB 139

Hall (HM Inspector of Taxes) v Lorimer CA [1994] STC 23

Lee Ting Sang v Chung Chi-Keung [1990] IRLR 236

Lime-IT Limited v Justin [2003] STC (SCD) 15

Market Investigations Limited v Minister of Social Security [1968] 3 AER 732

Massey v Crown Life Insurance [1978] 1 WLR 676

McLeod v Hellyer Brothers Limited [1987] IRLR 232

McManus v Griffiths (1997) 70 TC 218

McMeechan v Secretary of State for Employment [1997] IRLR 353

Montgomery v Johnson Underwood [2001] EWCA Civ 318

Morren v Swinton and Pendlebury Borough Council (1965) 1 WLR 576

Mrs MacFarlane & Mrs Skivington v Glasgow City Council [2001] IRLR 7 EAT

Narich Property Limited v Commissioner of Payroll Tax [1984] ICR 286

Nethermere (St Neots) Limited v Gardiner [1984] ICR 240

O'Kelly v THF [1983] 3 All ER 456

Professional Contractors Group v CIR [2001] STC 629

Propertycare Limited v Gower 2003 EAT/547

Ready Mixed Concrete (South East) Limited v Minister of Pensions and National Insurance [1968] 2 QB 497

Stevedoring & Haulage Services Limited v Fuller [2001] EWCA Civ 651

Stoddart v Cawder Gold Club [2001] EAT/87300

Stuncroft Limited v Havelock 2001 EAT (unreported)

Swan Hellenic Limited v Secretary of State for Social Services 1983 QBD (unreported)

Synaptek Limited v Young [2003] EWHC 645 (Ch)

Tilbury Consulting Limited v Gittins (No 2) [2004] STC (SCD) 72

WHPT Housing Association Limited v Secretary of State 1981 ICR 737

ANSELL COMPUTER SERVICES LTD v DAVID RICHARDSON (HMIT) (SpC 425) (2004)

Sp Comm (G Aaronson QC) 29/7/2004

TAX

CONTRACTORS : CONTRACTS FOR SERVICES : EMPLOYMENT STATUS : MUTUALITY : NATIONAL INSURANCE CONTRIBUTIONS : CONTRACT FOR SERVICES : LIABILITY OF SERVICE COMPANY FOR NI : IR35 LEGISLATION : HYPOTHETICAL CONTRACTS : MUTUALITY OF OBLIGATIONS : reg.6 SOCIAL SECURITY CONTRIBUTIONS (INTERMEDIARIES) REGULATIONS 2000

The arrangements between a worker, supplied by a service company providing services to client companies through an intermediary, and the client, had they taken the form of a direct contract between the worker and the client, would have been one for the provision of services and not one of employment, therefore the service company was not liable for national insurance contributions in respect of the payments made by the client for work performed by the worker under the Social Security Contributions (Intermediaries) Regulations 2000 reg.6(1)(c).

The appellant (X) appealed against a decision on its liability to national insurance under the Social Security Contributions (Intermediaries) Regulations 2000 reg.6(1)(c)

. X entered into a contract with a company C under which C would find an 'end-user' for the services supplied by X.

X agreed to provide the services of Y, its director to two clients, Z for the purpose of carrying out work of a particular nature, for an expected maximum number of hours, and C agreed to pay the agreed hourly rate to X.

The contract was expressed to be for an unlimited period until terminated by breach or consent.

It also provided that, if appropriate, X would offer a suitably qualified substitute to continue the work for Z.

The potential liability for national insurance contributions arose from what is commonly referred to as the IR 35 legislation.

The relevant question was whether the circumstances of the arrangements between X and Z were such that, had they taken the form of a direct contract between Y and Z, that contract would have been one for the provision of services or alternatively a contract of employment.

If the former, the IR35 legislation would not apply while if the latter X would have been liable for national insurance contributions in respect of the payments made by Z for the work performed by Y.

X's case was that Y could not be regarded as an employee because he was not obliged to work any particular number of hours in any given day or week; he could turn up when he liked and could take time off at his own choosing without seeking permission; he was treated differently by Z from its employees in that he did not have access to benefits such as sick pay a company car or to the employee social club; there had been no mutuality of obligations required for the existence of a contract of employment.

HELD: The significant factors were the absence of any obligation on Z to keep Y in work throughout the period of his engagements; the absence of any obligation on Y to put in a particular amount of work; Y's ability to take time off at his own choosing without seeking permission; the ability to withdraw and suggest a substitute individual; the various other practical matters which differentiated contractors from employees; and the absence of mutuality of obligations in the fact that Z believed that they could have terminated Y's activities at virtually no notice, all of which led to the conclusion that Y would not have been an employee in the hypothetical contract which the IR35 legislation required to be constructed, Montgomery v Johnson Underwood Ltd (2001) EWCA Civ 318, (2001) ICR 819 applied.

Accordingly, the circumstances were not those described in reg.6(1)(c) and X was not liable for national insurance contributions in respect of the payments made by Z for the work performed by Y. Appeals allowed.

Counsel: For the appellant: Non-counsel representative For the respondents: Non-counsel representative

LTL 14/9/2004 : (2004) STC (SCD) 472

CH/2004/APP/0271, Neutral Citation Number: [2004] EWHC 2248 (Ch)
IN THE HIGH COURT OF JUSTICE
IN THE CHANCERY DIVISION

Royal Courts of Justice
Strand, London, WC2A 2LL

Friday 8th October, 2004

B e f o r e:

THE HONOURABLE MR JUSTICE PARK

– – – – – – –

USETECH LIMITED

Appellant

− v −

GRAEME YOUNG (HM INSPECTOR OF TAXES)

Respondent

– – – – – – – – –

Simon Devonshire (instructed by Nelsons) for the Appellant
Akash Nawbatt (instructed by the Solicitor of Inland Revenue) for the Respondent

J U D G M E N T

I direct that pursuant to CPR PD 39A para 6.1 no official shorthand note shall be taken of this Judgment and that copies of this version as handed down may be treated as authentic.

Abbreviations, dramatis personae, etc

1. These are as follows.

ABB	ABB Vetco Gray (UK) Limited, the ‘end user' of the services of Mr Hood; a company which provided a range of equipment to the oil and gas industry.
Mr Devonshire	Simon Devonshire, counsel for Usetech.
EAT	Employment Appeal Tribunal.
Hood, Mr	William Hood, specialist in a software system used by ABB, called Pro−Engineer; shareholder in and director of Usetech.
IR35	The reference number of an Inland Revenue Press Release of 2000, which led to the enactment of the legislative provisions which are in point in this case.
Nawbatt, Mr	Akash Nawbatt, counsel for the Inspector of Taxes, the respondent to this appeal.
NES	NES International Limited, a company described as an agency company which provided technical recruitment services.
NICs	National Insurance Contributions
Usetech	Usetech Limited, the appellant on this appeal; ‘one man company' owned by Mr Hood, which provided his services to end users.

Overview

2. This is a tax and NICs appeal by the taxpayer, Usetech, against a decision of a Special Commissioner, Mr Colin Bishopp, dated 12 March 2004. The decision determined a question of principle concerning the liability to tax and NICs of Usetech and its principal shareholder and director, Mr Hood. Usetech was a ‘one man company' whose business consisted of making the services of Mr Hood available to third party users. By transactions entered into in May 2000 Mr Hood's services were

made available to ABB, and he worked in the business of ABB for about 17 months from 1 June 2000. The transactions involved not only Mr Hood, Usetech and ABB, but also, in a manner which I will describe later, another company, NES. Mr Hood had no beneficial interest in NES. The question of principle is whether the transactions attracted the operation of provisions introduced, both for tax and for NICs, in 2000 and commonly referred to as the IR35 legislation. IR35 was the reference number of an Inland Revenue Press Release which had foreshadowed the legislation.

3. If the IR35 legislation applied its effect would be to treat payments received by Usetech for the provision by it of Mr Hood's services (the payments being received, not from ABB directly, but from NES) as if they had been personal income of Mr Hood from an employment with ABB. For income tax they would be treated as emoluments taxable under Schedule E, rather than as receipts of Usetech's trade which would be taken into account in computing its profits liable to corporation tax. For NICs they would be treated in a similar way as employment income of Mr Hood. The liabilities both to income tax and to NICs would fall to be met by Usetech, not by Mr Hood. Thus it is Usetech which is the appellant taxpayer.

4. The Inland Revenue issued formal decisions that the IR35 provisions applied, and Usetech appealed to the Special Commissioners. In form there were two decisions and two appeals, one for tax and one for NICs, but they turned on two sets of almost identical legislation and stood or fell together. The appeals were heard by Mr Bishopp on 22 January 2004, and by a reserved decision dated 12 March 2004 he dismissed the appeals, thus affirming the decisions which the Inland Revenue had issued. Usetech now appeals to me. It is clear that an appeal can only succeed if the decision was wrong in law. There is no appeal on a question of fact: see s.56A(1) and (4) of the Taxes Management Act 1970.

5. Mr Devonshire, who appears for Usetech, has helpfully limited his submissions to two specific respects in which he says that the Special Commissioner erred in law. I will describe them fully later in this judgment. The first respect involves an argument that the IR35 legislation cannot apply because of a contractual provision between Usetech and NES (not between Usetech and ABB or between NES and ABB), which Mr Devonshire submits must be taken into account, entitling Usetech to provide the services of a substitute in place of Mr Hood. I will refer to this as the right of substitution argument. The second respect in which Mr Devonshire says that the Special Commissioner erred involves an argument that ABB was not obliged to provide work for Mr Hood to do (although in fact it did do so). Therefore, it is argued that, even after applying the hypotheses required by the IR35 provisions, there was insufficient mutuality of obligation for an employer/employee relationship to exist, with the result that the provisions did not apply. I will refer to this as the want of mutuality argument.

6. I have considered Mr Devonshire's arguments carefully, but my conclusion is that I cannot accept either of them. The issues are too complex for me to encapsulate the essence of my reasoning in this overview at the beginning of my judgment. I shall explain it as the judgment progresses. The result is that I respectfully agree with the decision of the Special Commissioner. Therefore I shall dismiss the appeal.

The IR35 legislation

7. For income tax and corporation tax (income tax so far as concerns Mr Hood and corporation tax so far as concerns Usetech) the legislation is contained in section 60 of and Schedule 12 to the Finance Act 2000. The critical provisions are those which identify the cases to which Schedule 12 applies. If the Schedule applies there is not, if I understand correctly, any dispute as the consequences. The dispute is whether it applies at all. The case revolves around provisions in paragraph 1 of the Schedule. I will now set out the relevant parts of the paragraph, interpolating in italicised square brackets the actual identities in this case of the parties referred to in general terms in the paragraph.

> 1 (1) This Schedule applies where -
>
> (a) an individual (‘the worker') *[Mr Hood]* personally performs, or is under an obligation personally to perform, services for the purposes of a business carried on by another person (‘the client') *[ABB]*,
>
> (b) the services are provided not under a contract directly between the client *[ABB]* and the worker *[Mr Hood]* but under arrangements involving a third party (‘the intermediary') *[Usetech]* , and
>
> (c) the circumstances are such that, if the services were provided under a contract directly between the client *[ABB]* and the worker *[Mr Hood]* , the worker would be regarded for income tax purposes as an employee of the client *[ABB]*.
>
> (2), (3) ×
>
> (4) The circumstances referred to in sub−paragraph (1)(c) include the terms on which the services are provided, having regard to the terms of the contracts forming part of the arrangements under which the services are provided.

8. In the quotation of sub−paragraph (1)(b) above I have identified ‘the intermediary' in this case as being Usetech. As I will explain later, on the facts NES might also be regarded as an intermediary in the general sense of the word, but it is clear from paragraph 3 of Schedule 12, which I need not set out verbatim, that only Usetech counts as an intermediary for the purposes of paragraph 1. However, the ‘arrangements involving × the intermediary' (referred to in sub−paragraph (1)(b)) may involve other persons as well as the intermediary. If they do the respects in which the other persons are also involved may affect the application or non−application of paragraph 1. In the present case this could be relevant to the participation of NES in the entire transaction: NES was neither ‘the worker' nor ‘the client' nor ‘the intermediary', but it was involved in the arrangements in which ‘the intermediary' (Usetech) was involved, so its part in those arrangements falls to be taken into account as well as Usetech's part in them.

9. A more general point of construction is worth spelling out at this stage. The conditions of sub−paragraphs (a) and (b) involve an analysis of the actual facts and

legal relationships, but when that analysis shows that those two sub−paragraphs are satisfied sub−paragraph (c) involves an exercise of constructing a hypothetical contract which did not in fact exist, and then enquiring what the consequences would have been if it had existed. There may be room in some cases for dispute about what the hypothetical contract would contain, and in the present case there is. The dispute arises in connection with the right of substitution argument which is advanced by Mr Devonshire on behalf of Usetech. I will explain how precisely the issue arises at a later stage in this judgment.

10. The comparable provisions for NICs are contained in regulation 6 of the Social Security Contributions (Intermediaries) Regulations 2000. They are not quite identical to the provisions in the Finance Act 2000, but they are similar in all relevant respects. For completeness I will set out the specific wording.

> 6 (1) These Regulations apply where -
>
> (a) an individual (the worker) *[Mr Hood]* personally performs, or is under an obligation personally to perform, services for the purposes of a business carried on by another person (the client) *[ABB]*,
>
> (b) the performance of those services by the worker *[Mr Hood]* is carried out, not under a contract directly between the worker *[Mr Hood]* and the client *[ABB]* , but under arrangements involving an intermediary *[Usetech]* , and
>
> (c) the circumstances are such that, had the arrangements taken the form of a contract between the worker *[Mr Hood]* and the client *[ABB]* the worker *[Mr Hood]* would be regarded for the purposes of Parts I to V of the Contributions and Benefits Act as employed in employed earner's employment by the client *[ABB]*.

As in the Finance Act 2000 there is a provision (regulation 5) under which ‘the intermediary' is, so far as this case is concerned, Usetech (and not NES). However, the same point applies in that, to the extent that NES was involved in the arrangements, its participation may have to be taken into account in determining whether regulation 6 applies notwithstanding that it was none of the parties (‘the worker', ‘the client', or ‘the intermediary') specifically identified in the regulation. Curiously regulation 6 does not contain a provision like paragraph 1(4) of Schedule 12 to the Finance Act 2000, expanding on what is covered by ‘the circumstances' referred to in sub−paragraph (c) of regulation 6(1). However, no−one has suggested to me, nor do I consider, that that or the other minor differences between the two statutory provisions affects this case or opens a possibility of the case being decided one way for NICs and another way for income tax and corporation tax.

The facts

11. Mr Hood has now retired but at the time when this case arose he worked in connection with the production of design drawings of oil wells, rigs and similar equipment. He was a specialist in the use of a software product called Pro−Engineer, which produced 3−D models of such equipment. He started to operate through his one man company, Usetech, in May 1996. There was no evidence before the Special Commissioner about his arrangements before then, so the Commissioner inevitably decided the case on the basis of the Usetech arrangements alone, uninfluenced by what Mr Hood's tax and national insurance status may have been in earlier years.

12. Usetech had several engagements for the provision of Mr Hood's services to ‘end users' over its trading life from 1996 to May 2003 (when Mr Hood was obliged to retire by reason of ill health). Some of the engagements were pursuant to direct contracts between Usetech and the end users, but engagements with ABB were not, since, as I explain in more detail in the next paragraph, NES was interposed between Usetech and ABB (the end user). There were three different periods when Mr Hood was working in the business of ABB at its premises in Aberdeen. The present case is specifically about the period of 17 months beginning in June 2000. (In fact the Special Commissioner was only strictly concerned with the period from 1 June 2000 to 31 March 2001, but I assume that that was for some procedural reason to do with tax years or companies' accounting periods or something of that nature. The Commissioner's decision would undoubtedly govern the whole period of the engagement for Mr Hood to work in the business of ABB.)

13. ABB is a United Kingdom subsidiary of a world−wide group which provides a range of equipment to the oil and gas industry. It has a core staff of 750 to 850 permanent employees, but it supplements them when demand requires by taking on what its Human Resources Manager described as ‘sub−contract employees'. This was done by means of companies described as ‘agencies', of which NES was one. There was no evidence from NES, but on its letter heading it describes itself as ‘Europe's largest technical recruitment agency'. As will appear, NES sometimes acted contractually as a principal rather than as an agent in the strict legal sense.

14. The way in which Mr Hood was engaged to work in the business of ABB, which I assume was typical of how ABB and NES operated, was as follows. Management within ABB identified that ABB had a need for another specialist in Pro−Engineer, but did not wish to have another permanent employee recruited. The Human Resources manager contacted agencies, including NES. NES knew about Mr Hood, and contacted him, or more strictly contacted his personal company, Usetech. Mr Hood was obviously willing to go and work in Aberdeen in ABB's business, because the matter proceeded. If ABB had not already known Mr Hood it would have required to interview him first, and had in fact done so for the earlier occasion when he had been provided to it through NES. However, since it already knew him it did not require an interview on this occasion. Two contracts were entered into, one between Usetech and NES and one between NES and ABB. Each contract appears to have been made on 22 May 2000, to commence on 1 June 2000, although the documents which were before the Special Commissioner are a little confusing about this. The system of having two contracts is quite common (or so I understand), and

contracts of these kinds are sometimes referred to as ‘the lower level contract' and ‘the upper level contract'. However, I will refer to them in this judgment as ‘the Usetech/NES contract' (the lower level) and ‘the NES/ABB contract' (the upper level). There must also have been a contractual relationship (at the lowest level) between Mr Hood and Usetech, but it appears that there was no written contract of service. At least no such written contract was produced in evidence.

15. As regards the Usetech/NES contract (the lower level contract) there appear to have been two contractual documents: a one page letter of offer by NES signed by way of acceptance by Mr Hood on behalf of Usetech, and a longer set of ‘Terms and Conditions' in standard form. A complication here is that the documents before the Special Commissioner appear to have included three versions of the first document and three of the second. This may have had something to do with variations in the anticipated duration of the engagement, but there are aspects of the duplication or triplication of documents which puzzle me. However, I do not think that they are fundamental to the issues in the case.

16. The first of the three offer letters is dated 22 May 2000. It is from NES and is addressed to Usetech at Mr Hood's home address. It includes the following: ‘*We are pleased to offer you a contract to supply contract staff in a position as Pro−Engineer Designer in accordance with the following: NAME(S) OF CONTRACT STAFF: WILLIAM HOOD. CLIENT: ABB VECTO GRAY.'* Certain brief other details follow, covering such matters as the hourly rate of payment, the commencement date, and the notice period. Mr Hood signed to indicate acceptance. For completeness I mention that the other two offer letters have slightly different periods of service, do not mention Mr Hood personally and are not signed by him by way of acceptance. I do not follow what their relevance to the appeal is or what their function was, and I have concentrated on the letter dated 22 May 2000.

17. I turn to the longer form document, the standard form headed ‘*Terms and Conditions for the supply of services to NES International Ltd (performed by a limited company sub−contractor'.* There are three versions of this document in the documents which were before the Special Commissioner and which are now before me. None of them mentions Usetech (or any other specific sub−contractor for that matter), and none of them is signed by or on behalf of either NES or Usetech (or any other person). The evidential status of the three documents in the bundle is not clear to me, but I will assume that at least one of them was supplied by NES to Usetech (in common, I assume, with all other subcontractor companies which had similar relationships with NES), and that it did in general regulate the contractual relationship between the two companies. The Special Commissioner said, and I agree, that although the three versions of the Terms and Conditions are not quite identical, the differences between them do not appear to be material to this case.

18. The Terms and Conditions are quite long documents. They are in no sense tailor−made for the particular relationship being entered into between Mr Hood, Usetech, NES and ABB. They are standard form documents plainly intended to be used by NES across the spread of arrangements which it makes with companies like Usetech to enable the services of employees of such companies to be provided to outside clients like ABB. It would be disproportionate for me to set out one of the

documents in this judgment or to attempt a full summary of it. In the broadest of terms it provides for 'the sub−contractor' (in this case Usetech) to agree with NES that it will provide 'the Services' to the reasonable satisfaction of 'the client', that is the end user, being ABB in this case. The agreement which the sub−contractor has, however, is between it and NES, not between it and the end user. 'The Services' (which Usetech agreed with NES to provide to the reasonable satisfaction of ABB) are defined as *'the work or project identified in the contract letter and/or notified to the sub−contractor by the Client'*. I assume that the contract letter referred to is the letter of 22 May 2000 (or possibly all three letters) by which NES offered the engagement to Usetech and Usetech accepted it. On that basis it appears that (in so far as the matter is affected by the 22 May 2000 letter, which was the only document which appears to have signed on behalf of Usetech by way of acceptance) 'the Services' were the services of Mr Hood as Pro−Engineer Designer.

19. The Terms and Conditions cover a range of matters which I need not describe in this judgment. They include matters such as payments of fees (to be made to Usetech by NES, not by ABB), use of motor vehicles, trade secrets, and non−competition by the sub−contractor with the end user (NES's 'client'). There is, however, one provision which I should set out in full, since it provides the basis for Mr Devonshire's right of substitution argument. The final clause is headed 'General', and contains a number of different provisions. One of them reads as follows:

> The Sub−Contractor shall be entitled to substitute the named Personnel for an alternative, with the prior written consent of the Company - such consent not to be withheld if the proposed replacement has the appropriate skills, qualifications and abilities in the reasonable opinion of the Client.

I specifically point out that 'the Company', which can give prior written consent to a substitution, is NES, and is not 'the Client': in this case it is not ABB. Further, the only parties to this agreement are the sub−contractor (Usetech in this case) and NES. The client (e.g. ABB) is not a party. I will examine the argument which Mr Devonshire bases on this provision at a later stage in this judgment.

20. So much for the contractual relationship between Usetech and NES. There was also a contractual relationship between NES and ABB. I should state at the outset that Usetech and Mr Hood did not know the detailed content of that relationship. If they thought about the matter they must obviously and correctly have assumed that there would be a contract of some sort between NES and ABB, that it would provide for NES in some way to cause Usetech to provide the services of Mr Hood to ABB, and that ABB would make payments to NES for the services. But I doubt that Usetech and Mr Hood would have known or assumed anything more detailed about the NES/ABB contractual relationship.

21. There was indeed an NES/ABB contract (an upper level contract), and it was placed before the Special Commissioner. I understand that the copy of it was obtained from ABB. It takes the form of a letter agreement, signed on behalf of both parties, dated 22 May 2000, which was also the date of the offer letter made by NES to Usetech and signed by way of acceptance by Mr Hood. The letter which constitutes the NES/ABB contract is from NES to ABB. It is headed: *'Sub−Contractor - Usetech Ltd. Contract Staff - Mr William Hood.'* It begins: *'We confirm that the above Contract*

Staff supplied by the above sub−contractor will be available to commence work on 30th May 2000 to perform the services of Pro−Engineer Designer.' A number of other detailed matters were covered, including the hourly rate payable by ABB to NES for the services (a little higher, as one would expect, than the hourly rate payable onward by NES to Usetech), a seven days notice period, and a minimum number of weekly hours (37.5 hours). Two pages of detailed Terms and Conditions are attached, but they do not appear to me to add anything relevant (except for condition 3.2, to which I refer in paragraph 63 below).

22. There is nothing in the NES/ABB contract about the provision of a substitute for Mr Hood, and in my view that contract is solely one for the provision of his services, not one for the provision of the services of him or a substitute who is reasonably acceptable to ABB.

23. Moving on from the contracts as such, there are some other factual points which might have a bearing on the right of substitution argument and which I ought therefore to mention. The question of a substitute for Mr Hood never arose. For the 17 months of the engagement which began on 30 May (or 1 June) 2000 the services were provided entirely by Mr Hood himself. Mr Hood did, however, say in his witness statement that there were other Pro−Engineer specialists whom he knew and whom he could have sent. I should also quote the following findings from paragraph 25 of the Special Commissioner's decision.

> [T]he reality × is that ABB required Mr Hood's services. It was not contracting, indirectly, with [Usetech] for the supply of a person competent in Pro−Engineer; it required Mr Hood. It would not have accepted a substitute, if Mr Hood had sent one, without interview and certainly not on the basis that Mr Hood or the substitute might attend as [Usetech] elected from day to day. Mr Hunter's evidence, which I accept, can lead to no other conclusion than that the arrangement was personal to Mr Hood. I do not go so far as to say that the right to substitute was a sham - Mr Hunter agreed that, if Mr Hood had become unavailable and suggested someone to continue in his place, that suggestion would be given some weight - but Mr Hood and [Usetech] could not dictate, at will, who would perform the work: it had to be Mr Hood. In my view, the ‘right' of substitution was largely illusory.

24. So far as the right of substitution argument is concerned I do not think that there are any other specific aspects of the facts which I need to describe. However Mr Devonshire also advances the want of mutuality argument, and there are some other factual points which I ought to mention, since they could be of some relevance to that argument. The Special Commissioner, having heard evidence from Mr Hood and from two witnesses from ABB, found that any temporary member of staff (like Mr Hood) was treated, on a day to day basis, in a manner barely distinguishable from an employee. One of the ABB witnesses said that as a general rule temporary staff were expected to work 50 hours a week, and Mr Hood did so. Mr Hood's own evidence was that he typically worked for 58 hours per week. He also said that, if there was no work for him to do, he could be sent home. He could recall at least three or four occasions when the computer crashed and he was sent home without payment. The Special Commissioner recorded this aspect of Mr Hood's evidence, but did not make a specific finding of his own on it. I confess that I have some reservations about it, and I will return to this later when I discuss the want of mutuality argument.

The Special Commissioner's decision

25. In a careful and comprehensive reserved decision the Special Commissioner, Mr Bishopp, set out the statutory provisions and reviewed the facts. He noted that the IR35 provisions (both for tax and for NICs) require a notional contract between Mr Hood and ABB to be assumed, and that the critical question was whether that contract would have been a contract of employment. He considered a number of factors which might bear on the question, and in the course of doing so he quoted a well−known passage from the judgment of McKenna J in *Ready Mixed Concrete (South East) Ltd v Minister of Pensions and National Insurance* [1968] 2 QB 497 at 515:

> 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 to a sufficient degree to make that other master. (iii) The other provisions of the contract are consistent with its being a contract of service.

The Special Commissioner considered condition (iii) first, and concluded that there was nothing in the notional contract which was 'incompatible with the relationship between them [ABB and Mr Hood] of employer and employee' (paragraph 24 of the decision). It was at this point that he considered the issue of substitution, doing so in the terms which I quoted in paragraph 23 above and concluding that in his view 'the right of substitution was largely illusory'. (As will appear later I would put the matter rather differently, but I would not change the 'bottom line' conclusion that the provision for substitution in the Usetech/NES contract does not lead to a decision in favour of Usetech.)

26. Moving on, the Special Commissioner compared Mr Hood with normal employees of ABB who had similar skills to his own, and saw little outward difference. I quote a few extracts from paragraph 27 of the decision:

> Mr Hood was expected to undertake the work allocated to him by ABB and to do so in accordance with its directions and at times of its choosing. × In that, too, he was in materially the same position as an employee. × [O]verall it seems to me that there is no difference between the measure of control exercised over his work by ABB and that it would have exercised over an employee of his status.

27. The Special Commissioner considered that, in so far as there was a requirement for mutuality of obligation to exist for a relationship to be a contract of employment, the requirement was in any event satisfied by the obligation on the one hand to work and on the other to remunerate. (In my view there may be rather more to be said on this point, but as I will explain I do not disagree with the Commissioner's conclusion.)

28. The Commissioner also considered whether Mr Hood or Usetech could realistically be seen to have been in business on their own account, and was of the opinion that they could not. For that and the other reasons which I have summarised and which he

examined more fully he decided: *'The conclusion must be that the notional contract between ABB and Mr Hood was one of service. I can find no factor in the case which is inconsistent with that conclusion.'*

The appeal to this court

29. In the overview at the beginning of this judgment I observed that Mr Devonshire has limited the grounds of appeal to two issues, which I am calling the right of substitution argument and the want of mutuality argument. Points about the right of substitution and points about the alleged want of mutuality were made on behalf of Usetech before the Special Commissioner, but, as it seems to me, they were made not so much as self−contained arguments either of which would be sufficient entirely by itself to conclude the appeal in favour of Usetech, but rather as items in a comprehensive view of the interconnecting relationships between Mr Hood, Usetech, NES and ABB. I think that the Special Commissioner perceived the main case advanced on behalf of Usetech as being one which looked at all aspects of the case together and in the round. Those aspects included the provision in the Usetech/NES contract about substitution and also what was contended to be a want of mutuality between Usetech and ABB. But they also included points made about the degree of control exercised by ABB over the work done by Mr Hood, about alleged differences in practice between Mr Hood's position in the operations of ABB and the positions of full time employees, about other activities altogether carried on by Mr Hood through Usetech, and so on.

30. In the thorough skeleton argument which Usetech's advocate placed before the Special Commissioner he wrote: *'On the evidence it is submitted that the hypothetical contract in this case would show a genuine substitution right, a lack of control over Mr Hood, project based work on an hourly basis, a clear lack of mutuality of obligations, flexibility of hours, no significant integration of Mr Hood into the ABB organisation and several practical differences between Mr Hood and regular ABB employees'.* That was in the nature of a global synopsis. It should be apparent from the previous section of this judgment that the Special Commissioner did not accept several of the elements in the synopsis. In the result he was not persuaded that, looking at everything in a global way, the overall picture which emerged was that, if Mr Hood had been engaged by a direct contract between himself and ABB, he would have been an independent contractor and not an employee.

31. It may be worth adding that there appears to have been no significant argument advanced to the Commissioner that, before Mr Hood established Usetech and provided his services to end users through Usetech (with or without the interposition of an agency company like NES), he carried on some sort of self−employed profession which involved him having a series of engagements with a succession of clients. (Compare, for example, the observations of Rowlatt J about theatrical actors and actresses in *Davies v Braithwaite* [1931] 2 KB 628 at 635 to 636.) Certainly there was no argument before me that the present case could be affected by an established tax treatment or NICs treatment which had been applied to Mr Hood in the earlier years of his working career. I can, however, imagine other cases in which arguments of that sort could be material.

32. Mr Devonshire, realistically in my opinion, has not invited me to approach the appeal on the basis that I should take all the circumstances into account and conclude that Mr Hood would indeed have been an independent contractor, not an employee. An argument of that sort was entirely appropriate for the first instance hearing before the Special Commissioner, but in the High Court the decision of the Commissioner can only be effectively challenged on grounds that it was wrong in law. In *Synaptek Ltd v Young* [2003] STC 543, [2003] EWHC 645 (Ch), at page 553 Hart J said (in a case which arose under the same IR35 statutory provisions as the present one): *'Deciding, in a borderline case, whether a particular contract is a contract of service or a contract for services is notoriously difficult. × In general the question is regarded as one of fact, or as it is sometimes put, a question of mixed fact and law, the evaluation and determination of which is a matter for the fact−finding tribunal.'* The judge had been invited to reverse a decision of General Commissioners that, if there had been a direct contract between the individual involved in that case and the end user of his services, it would have been a contract of employment. He declined to do so, essentially on the ground that the Commissioners' decision had been one of fact which it was not open to him (the judge) to alter on an appeal limited to questions of law.

33. It is against that background that Mr Devonshire has restricted his challenge to the Special Commissioner's decision in this case to the right of substitution argument and the want of mutuality argument. Each argument is to the effect that, because of the item focused on (the alleged right of substitution in the first case and the alleged want of mutuality in the second), the postulated relationship between Mr Hood and ABB was legally incapable of being the relationship of employee and employer. Therefore in this judgment I consider only those two arguments. In a sense the starting point for me is that, but for the alleged right of substitution and the alleged want of mutuality, it is common ground in this court that, if Mr Hood had been engaged directly by ABB, he would have been an employee. That is not to say that the Special Commissioner could not possibly have taken a different view. I have not been asked to consider whether he could have done that, and I have not done so. I say a little more about this at the end of this judgment.

The right of substitution argument

34. In paragraph 25 above I said that I agreed with the Special Commissioner's conclusion that the inclusion of a substitution provision in the Usetech/NES contract did not mean that the appeal should be allowed, but I also said that I would myself put the matter rather differently from how he put it. He said in paragraph 25 of his decision that 'the "right" of substitution was largely illusory'. I follow what led him to say that, but in my view there is a logically prior question which ought to be considered. Would there have been any right of substitution at all in the notional contract between Mr Hood and ABB which the IR35 provisions require to be assumed? In my view, for reasons which I will explain, there would not, and that is in itself sufficient to exclude Mr Devonshire's right of substitution argument.

35. As regards income tax and corporation tax FA 2000 Schedule 12 paragraph 1(1)(c) poses a hypothesis expressed as: *'had the arrangements taken the form of a contract between the worker [Mr Hood] and the client [ABB]'*. As regards NICs the

hypothesis under the Social Security Contributions (Intermediaries) Regulations 2000 regulation 6(1)(c) is expressed as: '*if the services were provided under a contract directly between the client [ABB] and the worker [Mr Hood].'* The two wordings are not identical, but the meanings are. There was not in fact a direct contract between Mr Hood and ABB, but the provisions require it to be assumed that there was. What would it have contained? Mr Devonshire's argument assumes that it would have contained a provision permitting Mr Hood to substitute himself by an alternative Pro−Engineer specialist, subject only to ABB's consent which could not be withheld if the substitute had the appropriate skills. If that assumption is wrong the right of substitution argument falls away altogether.

36. The factor which complicates the issue in this case is that in the chain of contracts NES is interposed between Usetech and ABB. The structure primarily contemplated by the legislation seems to me to be one where there are two contracts: the first is a contract of service, written or oral, between the worker and his one−man service company (the equivalent of Usetech), and the second is a contract between the service company and the end user (the equivalent of ABB) for the service company to furnish the personal services of the worker to the end user. In a case which is as straightforward as that I think that the contents of the notional contract between the worker and the end user will be fairly obvious: they will be based on the contents of the second contract between the service company and the end user, but with the worker himself agreeing that he will provide his services to the end user on, as near as may be, whatever terms are agreed between the service company and the end user.

37. In the actual case with which I am concerned there were three contracts, not two, which have to be subsumed into one notional contract:

a) First there was the actual contract between Mr Hood and Usetech. It appears that this did not take the form of a written service agreement: at least none was produced in evidence before the Special Commissioner. But there must have been a contractual relationship of some sort, however informal. It is not suggested, and could not realistically be suggested, that that relationship contained any term whereby, while Mr Hood agreed generally to work as an employee of Usetech (or as a working director of Usetech), he was entitled to provide a substitute for himself.

b) Second, there was the actual contract between Usetech and NES. That contract did contain the substitution provision which I have quoted in paragraph 19 above. Even so the provision was a standard form provision which, I assume, was always (or at least usually) part of the agreements which NES entered into with all one−man companies with which it did business. The provision appeared in a clause headed 'General' at the end of the contract, and was obviously not specially negotiated for Mr Hood and Usetech. It was, no doubt, binding between Usetech and NES, but it would not be binding upon a third party, like ABB, to which NES agreed to provide the services of Usetech's employee and director, Mr Hood, unless it or an equivalent

substitution provision was expressly included in the onward contract between NES and the third party.

c) Third, there was the actual contract between NES and ABB. As I described in paragraphs 21 above it took the form of a letter agreement for NES to provide the services of Mr Hood to ABB, with some standard terms and conditions attached. There was no provision for substitution included in the NES/ABB contract. In my definite opinion the NES/ABB contract was simply one for the services of Mr Hood, not for the services of Mr Hood or of a suitably skilled substitute.

38. In those circumstances, should the hypothetical direct contract between Mr Hood and ABB include the substitution provision or not? The Special Commissioner did not specifically decide that question, but I think that I should decide it myself. I believe that I can do that: it is not a question of fact such that I ought to remit it to the Commissioner to decide. Alternatively, if it is to any extent a question of fact, it is one of what inference should be drawn from the primary materials before the Commissioner. In my judgment there is only one tenable inference which can be drawn, and I see no point in remitting the case to the Commissioner for him to draw it.

39. In my judgment the hypothetical contract between Mr Hood and ABB would not have contained a substitution provision. That is, as it seems to me, the common sense of the matter; it is in accordance with the Special Commissioner's findings of fact; and it is also supported by the absence of evidence which one might have expected if there was a substantial case that the hypothetical contract would have contained a substitution provision. Suppose that there had been no interposition of NES, but that Usetech had itself contracted with ABB to provide the services of Mr Hood. I do not believe that a Usetech/ABB contract would have included a substitution provision, and there was no evidence from Mr Hood (the director of Usetech) that it would. The actual terms on which Mr Hood's services were provided to ABB (by NES under the NES/ABB contract) did not contain a substitution provision, and there would be no justification for assuming that, if he had contracted directly with ABB, he would have provided his services on any different basis. If, given the actual contracts between Usetech and NES and (separately) between NES and ABB, someone had turned up at ABB one day and said that he was being provided by NES as a well−qualified substitute for Mr Hood (already a far−fetched and unrealistic assumption), and ABB had sent the man away, Usetech might have had a contractual complaint against NES, but it would certainly have had no contractual complaint against ABB. Let me take the hypothetical assumptions a stage further. Suppose again that Usetech contracted directly with ABB but that (improbably) Usetech tried to have inserted in the contract a provision that it could from time to time provide a substitute for Mr Hood. Would ABB have agreed? There was no specific evidence on the point, but I believe that the strong probability, which Usetech needed to adduce strong evidence to refute, is that ABB would not have agreed. I assert that the only realistic form which the hypothetical direct contract between Mr Hood and ABB could have taken would have been one without a substitution provision.

40. My assertion is in accordance with the Special Commissioner's findings, and a contrary assertion would be inconsistent with them. He found that 'the reality × is that ABB required Mr Hood's services.' He went on to observe that *'ABB was not contracting indirectly with [Usetech] for the supply of a person competent in Pro−Engineer: it required Mr Hood'* . I have taken those particular findings from paragraph 25 of the decision. I have quoted much of that paragraph in full in paragraph 23 above, and the whole of it is consistent only with a conclusion that a hypothetical contract between ABB and Mr Hood would have been one for the specific services of Mr Hood and no−one else. There are also points to be made about evidence which is absent from the case. Mr Hood's witness statement does touch on the substitution provision in the Usetech/NES contract, but he does not suggest that it was of practical importance to him. There was no evidence that, in years before he started to operate through Usetech and may have had one or more direct contracts with end users of his services, he insisted on having substitution provisions in his contracts. It is inherently improbable that he would have done that, and, if he had, I can, I think, realistically assume that he would have said so.

41. At the risk of labouring the point I repeat that the substitution provision in the Usetech/NES contract was a standard form provision at the end of NES's standard form contract. I cannot imagine that it was a provision which Usetech asked to be included, and I doubt that any particular notice was taken of it when the contract was entered into. At any rate there was no evidence that particular notice was taken of it. In contrast, the main clause of the contract, on which Mr Hood might realistically have focused his attention, was clause 3, headed 'Provision of the Services'. By clause 3.1 Usetech agreed with NES that it would carry out 'the Services', and by clause 3.3 it agreed (still with NES) that it would 'provide the Services to the reasonable satisfaction of the client [ABB]'. As I have pointed out earlier (see paragraph 18 above) 'Services' was a defined term. It meant 'the work or project identified in the contract offer letter'. In the contract offer letter from NES to Usetech dated 22 May 2000 the work identified was the supply of Mr Hood as Pro−Engineer Designer to ABB; it was not the supply of Mr Hood or of a qualified substitute.

42. In all the circumstances I consider that, if there had been a real direct contract between Mr Hood personally and ABB for him to provide his skilled services to ABB, the contract would not have included a substitution provision. If, contrary to what I believe likely, Mr Hood had raised in negotiation the possibility of such a provision, ABB would in my view not have agreed to it, and I do not believe that Mr Hood would have pressed the point. Rather he would have proceeded to agree to provide his services without any provision for him to be entitled to provide a substitute. Of course if, in the events that happened, he became unable to provide his services under the assumed direct contract between himself and ABB (for example because of illness), he might have drawn on his contacts to suggest to ABB a possible replacement for himself. Mr Hunter of ABB said that the company would have given some weight to Mr Hood's suggestion. That, however, is a far cry from the direct contract between Mr Hood and ABB containing an express provision which conferred on him an entitlement to substitute someone else for himself, subject only to the substitute having the required skills.

43. There is one other point which I should consider before I move on. Mr Devonshire makes the point that, although Mr Hood and Usetech knew the detailed provisions of

the Usetech/NES contract, or at least had full access to those detailed provisions if they wanted, they did not know the terms of the NES/ABB contract. So, while they knew, or could have known, that there was a substitution clause in the first of those contracts, they did not know and had no means of knowing that there was no corresponding substitution clause in the second of those contracts. From this it is said to follow that the hypothetical contract must have been one which did contain a substitution clause, because that was a feature of the contract of which Mr Hood and Usetech had personal knowledge. It is further argued that the conclusion is reinforced by the self−assessment nature of the tax system. How, Mr Devonshire asks, could Usetech be expected to make a self−assessment of its liability to corporation tax under the IR35 provisions of FA 2000 on the footing that there was no substitution clause in the NES/ABB contract, when it did not know the contents of that contract?

44. I do not accept that argument, which to me has an air of unreality and formalism about it. I take it for granted that Usetech did not submit a self−assessment return which showed itself as liable to corporation tax under the IR35 provisions, but I do not suppose for a moment that, if it had known the detailed contents of the NES/ABB contract, it would have assessed its own liability on the basis that those provisions applied. In any case the self−assessment provisions are a matter of tax machinery and were not intended to affect substantive principles of tax liability. If, as the Special Commissioner held and as I believe, Usetech would have been liable to corporation tax under the IR35 provisions had there been no self−assessment system in operation, then it was still liable to corporation tax under those provisions notwithstanding that there was a self−assessment system in operation.

45. Usetech did not know the detailed content of the NES/ABB contract, but it did know that there must have been an NES/ABB contract, and it had itself entered into the Usetech/NES contract in order to enable NES to conclude its contract with ABB. Usetech had no reason to suppose that the NES/ABB contract would contain a substitution clause. If it had speculated about it the likely speculation would have been that there would have been no such clause. Usetech took no steps to request or require NES to include such a clause in the onward contract between itself and ABB. I do not think that Usetech and Mr Hood can successfully argue that, because they did not have specific knowledge that the NES/ABB contract did not contain a highly improbable provision, therefore they escape the operation of the IR35 provisions.

46. I also draw attention to certain observations of Burton J in *R (on the application of the Professional Contractors Group Ltd and others) v IRC* [2001] EWHC Admin 236, [2001] STC 629 at page 651. The case involved an unsuccessful challenge under human rights law and Community law to the whole concept of the IR35 provisions. In the course of the judge's discussion of certain guidance material which had been prepared by the Revenue he touched on arrangements which, like the one in this case, involved a lower level contract and an upper level contract: the lower level contract being between the worker's personal service company (like Usetech) and an agency (like NES), and the upper level contract being between the agency and an end user (like ABB). He said this:

> Equally, in so far as the inspector has access to something not available to the service contractor [the worker, the equivalent of Mr Hood], such as the contract between the agency [the equivalent of NES], which recruited him,

> and the client [the equivalent of ABB], which is or may be relevant, then it should clearly be supplied by the agency or the client or by the inspector. × It appears to me clear that the Revenue must bear in mind that under IR35 they are *not* considering an actual contract between the service company [the equivalent of Usetech] and the client [ABB], but imagining or constructing a notional contract which does not in fact exist. In those circumstances, of course the terms of any contract between the agency and the client as a result of which the service contractor will be present at the site are important, as would be the terms of any contract between the service contractor and the agency. But, particularly given the fact that, at any rate at present, a contract on standard terms may or may not be imposed by an agency, or may be applicable not by reference to a particular assignment, but on an ongoing basis, and may actually bear no relationship to the (non−contractual) interface between the client and the service contractor, such documents can only form a part, albeit an important part, of the picture.

47. It seems plain that Burton J was of the opinion that all relevant circumstances would fall to be taken into account in determining the contents of the hypothetical contract between the worker and the end user, including the provisions (or the absence of particular provisions) of a contract between an agency like NES and an end user like ABB. And he took that view whether or not the worker and his personal service company knew what the detailed provisions of the contract between the agency and the end user were. I would respectfully agree, and I would only add that it is by no means unknown for a person's liability to tax to be affected by a transaction which he knew was going to happen between other parties even if he did not know the details of it. For an example see *Emery v IRC* (1980) 54 TC 607.

48. For all of the foregoing reasons I do not accept the starting point of Mr Devonshire's right of substitution argument: I do not accept that the hypothetical direct contract between Mr Hood and ABB would have contained a substitution clause under which it would have been open to Mr Hood not to provide his services personally but instead to provide a suitably skilled substitute. That being so, I do not strictly need to consider whether I agree with the next step in Mr Devonshire's argument, which is that, if the contract had contained such a provision, it would as a matter of law have been incapable of being a contract of employment. That matter was, however, fully argued, and I think that I ought to say something about it, although I hope that I will be forgiven if I do not go into the arguments as comprehensively as I would otherwise have done.

49. The right of substitution argument is based largely on the decision of the Court of Appeal in *Express and Echo Publications Ltd v Tanton* [1999] IRLR 367. The underlying issue was whether Mr Tanton was an employee entitled to the various protections provided by the Employment Rights Act 1996 and associated legislation. He was a driver who agreed to provide his services to the company. The contract included this provision:

> 3.3 In the event that the contractor is unable or unwilling to perform the services personally he shall arrange at his own expense entirely for another suitable person to perform the services.

The Court of Appeal held that, because of that sub−clause, the relationship was incapable of being an employment. I accept that there are sentences in the judgment

of Peter Gibson LJ which, taken by themselves, suggest that any contract for services which contained any right for the worker to provide a substitute can never be a contract of employment. However, the *Tanton* case needs to be evaluated together with other cases, including two later decisions of the EAT (the Employment Appeal Tribunal) which considered the ambit of it.

50. An earlier case which the court cited in *Tanton* is *Ready Mixed Concrete (South East) Ltd v Minister of Pensions and National Insurance* [1968] 2 QB 497. I have already quoted one passage from the judgment of McKenna J in paragraph 25 above. Shortly after that passage His Lordship said this (with my italics identifying wording to which significance has been attached in the recent cases before the EAT):

> Freedom to do a job either by one's own hands or by another's is inconsistent with a contract of service, *though a limited or occasional power of delegation may not be* : see Atiyah's Vicarious Liability in the Law of Torts (1967) pp. 59 to 61 and the cases cited by him.

I move on to the two recent EAT cases. *MacFarlane v Glasgow City Council* [2001] IRLR 7 (in which the President of the Tribunal was Lindsay J) concerned gym instructors who worked for the Council. If for any reason they were unable to take a class they were to arrange replacements from a register of coaches maintained by the Council. The EAT reversed a decision of the tribunal below that that provision, read in the light of *Tanton* , meant that the instructors could not be employees of the Council. Lindsay J referred to *Tanton* and to the passage in the *Ready Mixed Concrete* case which I quoted above. In paragraph 13 of the judgment he went on to say:

> The relevant clause in *Tanton* was extreme. The individual there, at his own choice, need never turn up for work. He could, moreover, profit from his absence if he could find a cheaper substitute. He could choose the substitute and then in effect he would be the master. Properly regarded, *Tanton* does not oblige the tribunal to conclude that under a contract of service the individual has, always and in every event, however exceptional, personally to provide his services.

The actual decision in *MacFarlane* was that the case should be remitted to the first instance tribunal for it to decide by reference to all of the circumstances whether the gym instructors were employed or self−employed, but not to proceed on the basis that, because there was a substitution provision in the terms of service, that conclusively established that there could not have been an employment relationship.

51. The second EAT case to which I refer is *Byrne Brothers (Formwork) Ltd v Baird* [2002] IRLR 96, in which both *Tanton* and *MacFarlane* were considered by a tribunal presided over by Mr Recorder Underhill QC. The applicants were building workers who were engaged under contracts which plainly set out not to be contracts of employment. The applicants nevertheless argued that on a proper understanding they were entitled to holiday pay under the Working Time Regulations 1998. The matter did not turn solely on whether in truth they were employees, but the observations of the EAT on that issue are instructive. The agreements included the following provision:

> 13. Where the subcontractor is unable to provide the services, the subcontractor may provide an alternative worker to undertake the services but only having first obtained the express approval of the contractor.

I quote some extracts from the Tribunal's judgment:

> In our view it is plain that the contracts do require the applicants personally to perform work or services for Byrne Brothers. As a matter of common sense and common experience, when an individual carpenter or labourer is offered work on a building site, the understanding of both parties is that it is he personally who will be attending to do the work. In our view that consideration is admissible as part of the factual matrix. × But even if that were not so × clause 13, which concerns the use of additional or substitute labour, only makes sense against the background of an understanding that, subject to its provisions, the services are to be provided by the subcontractor personally. It is of course true that the effect of the provisions of clause 13 is that in certain circumstances the services may be provided by someone other than the subcontractor himself. But the clause falls far short of giving the subcontractor a blanket licence to supply the contractual services through a substitute.

The Tribunal then reviewed the authorities which I have mentioned. One thing which it did was to cite the passage in Professor Atiyah's book on Vicarious Liability which was alluded to but not specifically cited by McKenna J in the *Ready Mixed Concrete* case (see the extract quoted in the previous paragraph of this judgment). The passage is to the effect that an employment requires the performance of 'at least part' of the work by the employee himself. That does not suggest that, if the person concerned can provide a substitute for any part of the work, the relationship is legally incapable of being an employment. The EAT in *Byrne Brothers* concluded by agreeing with the tribunal below that the essential facts brought the case within the ratio of *MacFarlane* rather than *Tanton.* So despite the existence of the substitution clause the workers were employees.

52. I have one other case to mention. My attention has been drawn to it by Mr Nawbatt. *Narich Pty Ltd v Commissioner of Pay−Roll Tax* [1984] ICR 286, was an Australian appeal to the Judicial Committee of the Privy Council. It concerned lecturers for Weight Watchers classes. Their contracts included a clause for substitution of other lecturers approved by the company. The lecturers who were the parties to the contracts were held to be employees. It is true that, as Mr Devonshire pointed out, there was no discussion of whether the existence of that clause affected the status of the lecturers as employed or self−employed. However, the Privy Council was undoubtedly aware of the clause. Indeed Lord Brandon, delivering the advice of the Board, listed it among clauses which required particular consideration. The conclusion was: '*The effect of the contract as a whole is to create between Narich and the lecturer the relationship of employer and employee.'* The *Narich* case was not cited to the Court of Appeal in *Tanton* : it may be relevant to note that Mr Tanton had appeared in person on the appeal and that the judgment was, I believe, an unreserved one. If the case had been cited I do not suppose for a moment that the decision in *Tanton* would have been any different, but perhaps the court might have expressed itself somewhat differently when considering the effect of substitution clauses.

53. As it seems to me the present state of the law is that whether a relationship is an employment or not requires an evaluation of all of the circumstances. In the words of Hart J in *Synaptek Ltd v Young* [2003] STC 543 at 554−555, the context is one *'where the answer to be given depends on the relative weight to be given to a number of potentially conflicting indicia'*. The presence of a substitution clause is an indicium which points towards self−employment, and if the clause is as far−reaching as the one in *Tanton* it may be determinative by itself. In this case, however, if, contrary to my view, the hypothetical direct contract between Mr Hood and ABB has to be assumed to have contained a substitution clause similar to that in the Usetech/NES contract, in my opinion (agreeing with the Special Commissioner) it would not be sufficient to override the effect of all the other considerations which led the Commissioner to decide that the relationship would have been that of employee and employer.

54. For all of the foregoing reasons I do not accept Mr Devonshire's right of substitution argument.

The want of mutuality argument

55. I am unable to accept the want of mutuality argument either. The argument is that a contract cannot be a contract of employment unless there is mutuality of obligation: an obligation of the employee to provide his service to the employer, and conversely an obligation or obligations of the employer - certainly an obligation to remunerate the employee for work done, and (a less clear cut matter) an obligation to provide work for the employee to do, or at least an obligation to pay the employee for times when he is available for work but no work is provided. It is argued in this case that, if a direct contract had been in force between Mr Hood and ABB, it would not have obliged ABB to provide work for Mr Hood, and therefore it would have lacked the element of mutuality which would have been essential for it to be a contract of employment. Mr Devonshire relies in that connection on evidence from Mr Hood that he was at times sent home (or back to his lodgings) by ABB at short notice (e.g. when the computer crashed or when work was not available). Mr Hood recalled 'at least three or four occasions when the computer crashed and I was sent home without payment'. He also said that Usetech 'did not receive any payment whatever for the down time'. However, as I read his witness statement, that last sentence relates to occasions when he had been planning to work over weekends but it turned out that there was no weekend work available.

56. The Special Commissioner addressed the want of mutuality argument briefly in paragraph 28 of his decision. He did not accept it, principally because he considered that the requirement of mutuality might 'be satisfied by the obligation, on the one hand, to work and, on the other, to remunerate'.

57. For myself, while I agree with the result which the Special Commissioner reached on this issue, and certainly I consider that it was a result which it was open to him to reach, I would be inclined to put the matter in a more detailed way. If there is a relationship between a putative employer and employee, but it is one under which the 'employer' can offer work from time to time on a casual basis, without any obligation

to offer the work and without payment for periods when no work is being done, the cases appear to me to establish that there cannot be one continuing contract of employment over the whole period of the relationship, including periods when no work was being done. There may be an ‘umbrella contract' in force throughout the whole period, but the umbrella contract is not a single continuing contract of employment. See *Clark v Oxfordshire Health Authority* [1998] IRLR 125 (Court of Appeal); *Carmichael v National Power PLC* [1999] 1 WLR 2042 (House of Lords); *Stevedoring & Haulage Services Ltd v Fuller* [2001] EWCA Civ 651, [2001] IRLR 627 (Court of Appeal).

58. That leaves open the possibility that each separate engagement within such an umbrella contract might itself be a free−standing contract of employment, and it was, I believe, that concept which the Special Commissioner had in mind as covering this case. That is consistent with his referring in the same paragraph of his decision to the decision in *Market Investigations Ltd v Minister of Social Security* [1969] 2 QB 173, in which part time interviewers for a market research company were held to be engaged under a series of separate contracts of employment. The judgment of Cooke J in that case contains a valuable and much cited discussion of principles which are relevant to distinguishing between contracts of employment and contracts for services rendered in a self−employed capacity (see especially pages 184G to 185E). I confess that I have doubts about the factual conclusion which the learned judge reached when he applied the principles to the facts of the case. For myself, I see considerable force in the alternative analysis, namely that the interviewers provided their services on a free lance or casual basis and not as employees. See for an example of an analysis of that nature *O'Kelly v Trust House Forte Plc* [1984] QB 90.

59. However that may be for a case where the argument is that there has been a succession of separate contracts of employment, this case is not really of that nature. In contrast to a case like *Market Investigations* (or so it seems to me), the facts lend themselves readily to the conclusion that, if Mr Hood had been working for ABB under a direct contract, it would have been a contract of employment. The engagement lasted for 17 months. Viewed realistically there was nothing casual about it. On Mr Hood's own evidence he worked for an average of 58 hours a week. The Special Commissioner found that ‘he was, as a rule, expected to work the "core" hours from 8am to 5pm'.

60. I would accept that it is an over−simplification to say that the obligation of the putative employer to remunerate the worker for services actually performed in itself always provides the kind of mutuality which is a touchstone of an employment relationship. Mutuality of some kind exists in every situation where someone provides a personal service for payment, but that cannot by itself automatically mean that the relationship is a contract of employment: it could perfectly well be a contract for free lance services. However, in this case it was at the lowest open to the Special Commissioner to form the view that, if there had been a direct contract between Mr Hood and ABB for him to provide his services to ABB, it would have fallen to be regarded as a contract of employment, not as contract for free lance services. Mr Devonshire argues that that was not the case because ABB was not obliged to provide work for Mr Hood to do. The argument is unconvincing on the facts. At the cost of repeating myself I say again that ABB provided work for Mr Hood over a continuous period of 17 months, and provided enough work for him to be working for 58 hours

in a typical week. As to the occasions mentioned in Mr Hood's witness statement when he says that he was sent home because there was nothing for him to do, the occasions must have been highly exceptional. The evidence of the engineering manager from ABB was that ‘as a general rule, temporary staff were expected to work 50 hours a week, and Mr Hood did so' (decision paragraph 13). Neither witness from ABB recalled an occasion on which Mr Hood was sent home without pay, though they did accept that that could have been possible.

61. However, I have some reservations (as I said in paragraph 24 above) about the evidence from Mr Hood that he was sent home without payment. There are two points which make me cautious about the evidence in that respect, and I remain cautious notwithstanding that the ABB witnesses accepted that for Mr Hood to be sent home without pay was a possibility. The first point is: how could Mr Hood know whether, if he was sent home because there was no work, there would be no payment for his unused time? Whether ABB would pay for any time when Mr Hood was available for work but his services were not needed was a matter between ABB and NES. In connection with the right of substitution argument Mr Devonshire said that Mr Hood and Usetech did not know what the contents of the NES/ABB contract were. So how could Mr Hood say that, on the occasions when he was sent home, there was no payment made by ABB for his availability?

62. The second point is that, if Mr Hood's evidence is that ABB only paid for hours of actual work, that is inconsistent with a provision in the NES/ABB contract. As I have said in paragraph 21 above, the letter agreement of 22 May 2000 between NES and ABB specified an hourly rate of payment, and also specified ‘Minimum Hours: 37.5 hours'. If ABB sent Mr Hood home in a week when he worked for fewer than 37.5 hours, ABB was liable to pay for unworked time up to a total number of 37.5 paid hours for the week. The minimum hours provision in the NES/ABB contract was underpinned by a provision that seven days notice had to be given by either party to terminate the contract. I cannot be sure, but I think it unlikely that these provisions were present to the minds of the ABB witnesses when they accepted that it would have been possible for Mr Hood to be sent home without payment.

63. The minimum hours provision in the contract is important in another respect, because it presents a fundamental objection to the whole of the want of mutuality argument. The starting point for that argument is that, under the hypothetical contract between ABB and Mr Hood, ABB would have had no obligation to provide work. But I believe that ABB would have had an obligation to provide work. The letter agreement of 22 May 2000 between NES and ABB (see paragraph 21 above) incorporated a set of printed Terms and Conditions. One of them was condition 3.2:

> The Client [ABB] shall provide the Minimum Hours of work to each member of the Contract Staff.

Mr Hood was the only member of the Contract Staff, so the effect of the letter and the Terms and Conditions in combination was that ABB agreed with NES that it would provide a minimum of 37.5 hours of work a week for Mr Hood. Even if it failed to do that, it would plainly have to pay NES for 37.5 hours.

64. The cases indicate, and (as I recall) Mr Devonshire accepted, that the mutuality requirement for a contract of employment to exist would be satisfied by a contract which provided for payment (in the nature of a retainer) for hours not actually worked. It is only where there is both no obligation to provide work and no obligation to pay the worker for time in which work is not provided that the want of mutuality precludes the existence of a continuing contract of employment. See especially the *Clark* and *Stevedoring & Haulage* cases referred to in paragraph 57 above.

65. For the reasons which I explained in connection with the right of substitution argument I believe that the hypothetical contract between ABB and Mr Hood would contain provisions reflecting those in the actual NES/ABB contract. It would therefore provide that ABB was to provide a minimum of 37.5 hours of work a week, and to pay for the hours actually worked (with payment for a full 37.5 hours if the hours actually worked fell short of the required 37.5). There would have been both an obligation to provide work and an obligation to pay for a minimum of 37.5 hours a week. On that basis the mutuality requirement would in any event be satisfied. This particular point is not, I think, made by the Special Commissioner, but it is, as it seems to me, a further and decisive refutation of the want of mutuality argument.

Conclusion

66. For the foregoing reasons I conclude that this appeal falls to be dismissed. I would like to repeat the point, implicit if not explicit in earlier parts of this judgment (especially paragraphs 32 and 33), that my decision does not necessarily mean that the Special Commissioner was bound to reach the decision which he did. He looked at the entire circumstances in the round (as I believe that both the Inspector and the advocate for Usetech invited him to do), and he came to the conclusion that, if there had been no Usetech, a direct contract between Mr Hood and ABB would have been a contract of employment. Suppose that he had looked at the case in a similar way (perhaps also taking account of Mr Hood's earlier history of being a specialist in his particular field), and had reached the opposite conclusion: that a contract between Mr Hood and ABB would not have been a contract of employment but rather would have been an ingredient in a self−employed profession. My present decision should not be understood as meaning that such a decision by the Special Commissioner would have been wrong in law. It might or might not have been, and I have heard no argument on the question. However, given that decisions of Commissioners in tax appeals are generally final on questions of fact rather than law, the grounds on which I could now reach a decision in favour of Usetech are much narrower than those on which the Special Commissioner could have reached such a decision.

67. Mr Devonshire has appropriately limited his submissions to me to grounds on which it can be said that the Commissioner made a clear error of law, rather than that he came to one conclusion rather than another on a question of fact and degree which arguably might have gone either way. I have, I hope, examined carefully and comprehensively the two grounds which Mr Devonshire has advanced. I am unable to agree with either of them. The result therefore can only be that I dismiss the appeal.

USETECH LTD V GRAEME YOUNG (HMIT) (2004)

[2004] EWHC 2248 (Ch)

Ch D (Park J) 8/10/2004

TAX

CONTRACT OF EMPLOYMENT : CONTRACTS FOR SERVICES : INCOME TAX : INTERMEDIARIES : NATIONAL INSURANCE CONTRIBUTIONS : PROVISION OF SERVICES THROUGH INTERMEDIARIES : MUTUALITY OF OBLIGATION : RELATIONSHIP OF EMPLOYEE AND EMPLOYER : NOTIONAL CONTRACTS : HYPOTHETICAL CONTRACTS : RIGHT OF SUBSTITUTION : IR35 LEGISLATION : Sch.12 FINANCE ACT 2000 : reg.6 SOCIAL SECURITY CONTRIBUTIONS (INTERMEDIARIES) REGULATIONS 2000

The taxpayer company was liable to account for income tax under the Finance Act 2000 Sch.12 and national insurance contributions under the Social Security Contributions (Intermediaries) Regulations 2000 reg.6, where there was a notional contract of employment, which the provisions required to be assumed, between an engineer, who was the director of the taxpayer company, and a client for the provision of his services.

The appellant taxpayer company (U) appealed against a decision that it was liable to account for income tax under the Finance Act 2000 Sch.12 and national insurance contributions under the Social Security Contributions (Intermediaries) Regulations 2000 reg.6 .

U's business consisted of providing the services of its principal shareholder and director (H) to third party users.

U contracted with an agency (N) which in turn contracted with a company (B) for the provision of H's services.

U's agreement with N required U to provide the services to the reasonable satisfaction of B, and contained a provision for the substitution of H.

The contract between N and B was solely for the provision of H's services, and there was no provision for the supply of a substitute.

The issue was whether the transactions attracted the operation of the provisions in the 2000 Act and 2000 Regulations (the IR35 legislation).

The tribunal held that the IR35 legislation applied and a notional contract between B and H, which was a contract of service had to be assumed.

U argued that (1) there had been a right of substitution in the notional contract between H and B, the effect of which was that the relationship between them was legally incapable of being the relationship of employee and employer; (2) the contract could not be a contract of employment unless there was mutuality of obligation.

HELD: (1) Whether a relationship was one of employment or not required an evaluation of all of the circumstances, Synaptek Ltd v Young (HMIT) (2003) EWHC 645 (Ch), (2003) STC 543 considered.

There would not have been any right of substitution in the notional contract between H and B, which the IR35 legislation required to be assumed.

A hypothetical contract between H and B would not have contained a substitution provision.

The actual terms on which H's services were provided to B did not contain a substitution provision, and there would be no justification for assuming that if he had contracted directly with B, he would have provided his services on a different basis.

Furthermore, it could not be argued that because U and H did not have specific knowledge that the contract between N and B did not contain a highly improbable provision, they escaped the operation of the IR35 legislation.

(2) It was open to the tribunal to form the view that, if there had been a direct contract between H and B, for the provision of his services to B, it would have fallen to be regarded as a contract of employment.

B provided work for H over a continuous period of 17 months, and provided enough work for him to work 58 hours in a typical week.

Further, the contract between N and B specified a minimum of 37.5 hours per week.

If B sent H home in a week when he worked less than 37.5 hours, B was liable to pay for unworked time up to a total of 37.5 hours for the week.

The minimum hours provision presented a fundamental objection to the want of mutuality argument.

It was only where there was both no obligation to provide work and no obligation to pay the worker for time in which work was not provided that want of mutuality precluded the existence of a continuing contract of employment, Clark v Oxfordshire Health Authority (1998) IRLR 125 , applied. Appeal dismissed.

Counsel: For the claimant: Simon Devonshire For the respondent: Akash Nawbatt Solicitors: For the claimant: Nelsons For the respondent: Solicitor for Inland Revenue

LTL 18/10/2004 : (2004) STC 1671 : Times, October 22, 2004

Document No. AC0107003

IN THE HIGH COURT OF JUSTICE APP/317/2004

CHANCERY DIVISION

[2004] EWHC 2597 (Ch)

Royal Courts of Justice

Friday, 22nd October 2004

Before:
SIR DONALD RATTEE
(Sitting as a Judge of the High Court)

B E T W E E N:

FUTURE ON-LINE LIMITED
(A Firm) Appellant

- and -

S K FOULDS Respondent
(H.M. INSPECTOR OF TAXES)

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MR. J. ANTELL (instructed by Messrs. Druitts of Bournemouth) appeared on behalf of the Appellant.

MR. A. NAWBATT (instructed by the Solicitor for the Inland Revenue) appeared on behalf of the Respondent.

JUDGMENT
(As approved by the Judge)

SIR DONALD RATTEE:

1 This is an appeal against a decision dated 31st March 2004 of a Special Commissioner, Mr. Stephen Oliver Q.C. It concerns the application of what is commonly called the "IR35" legislation relating to liability for income tax under Schedule E, and National Insurance contributions of an individual who provides services to a client through the medium of a service company owned by the individual, in circumstances in which, had the individual provided these services under a direct contract with the client, he would have been regarded as an employee of the client. The effect of the legislation in such circumstances is to treat fees paid by the client to the service company, not as income of that company, but as earnings of the individual subject to income tax under Schedule E and National Insurance contributions.

2 The IR35 legislation is contained in the Finance Act 2000 so far as concerns income tax and the Social Security Contributions (Intermediaries) Regulations 2000 so far as concerns National Insurance contributions. I must read some of the relevant provisions. Income Tax: The material provisions applicable at the time relevant to this appeal are in Schedule 12 to the Finance Act 2000. Paragraph 1 of Schedule 12 provides:

> "1-(1) This Schedule applies where:
>
> (a) an individual ("the worker") personally performs, or is under an obligation personally to perform, services for the purpose of a business carried on by another person ("the client").
>
> (b) the services are provided, not under a contract directly between the client and the worker but under arrangements involving a third party ("the intermediary"), and
>
> (c) the circumstances are such that, if the services were provided under a contract directly between the client and the worker, the worker would be regarded for income tax purposes as an employee of the client.
>
> "(2) In sub-paragraph (1)(a) "business" includes any activity carried on –
>
> (a) by a government or public or local authority (in the United Kingdom or elsewhere), or

(b) by a body corporate, unincorporated body or partnership.

" (3) The reference in sub-paragraph (1)(b) to a "third party" includes a partnership or unincorporated body of which the worker is a member.

"(4) The circumstances referred to in sub-paragraph (1)(c) include the terms on which the services are provided, having regard to the terms of the contracts forming part of the arrangements under which the services are provided.

"(5) The fact that the worker holds an office with the client does not affect the application of this Schedule."

3 Paragraph 2 provides as follows:

"(1) If, in the case of an engagement to which this Schedule applies in any tax year –

(a) the conditions specified in paragraph 3, 4 or 5 are met in relation to the intermediary, and

(b) the worker, or an associate of the worker –

(i) receives from the intermediary directly or indirectly, a payment or other benefit that is not chargeable to tax under Schedule E; or

(ii) has rights entitling him, or which in any circumstances would entitle him, to receive from the intermediary, directly or indirectly, any such payment or other benefit,

the intermediary is treated as making to the worker in that year, and the worker is treated as receiving in that year, a payment chargeable to income tax under Schedule E ("the deemed Schedule E payment").

"(2) The deemed Schedule E payment is treated as made at the end of the tax year, unless paragraph 12 applies, (earlier date of deemed payment in certain cases).

"(3) A single payment is treated as made in respect of all engagements in relation to which the intermediary is treated as making a payment to the worker in the tax year.

"These are referred to in this Schedule as the relevant engagements in relation to a deemed Schedule E payment."

4 In the present case the relevant conditions for the purposes of para.2(1)(a) are those set out in para. 3, since the relevant intermediary is a company. I need not read those provisions. It is sufficient for present purposes to say that the conditions are satisfied with certain exceptions if the individual providing the services concerned has the beneficial ownership of more than 5 per cent. of the ordinary share capital of the company intermediary.

5 It is common ground in this case that the relevant conditions are satisfied in relation to the intermediary service company concerned. Part 2 of Schedule 12 sets out the process to be adopted in computing the amount of the Schedule E payment deemed to be received by the individual where para.1 applies. Their detail is not relevant for present purposes.

National Insurance Contributions

6 The equivalent provisions relating to National Insurance contributions applicable at the time relevant to this appeal are in the Social Security Contributions (Intermediaries) Regulations 2000, Statutory Instrument 2000 No.727, Regulation 6. These are in similar but not identical terms to the income tax provisions, which I have read, but it is common ground between the parties to this appeal that the effect of the two sets of provisions is the same, and that nothing turns on the differences in drafting, so I need not read the National Insurance provisions.

The Facts

7 The basic relevant facts are very simple. One Shane Roberts ("Mr. Roberts") is an information technology ("IT") specialist with a particular expertise in testing computer systems. From 1997 he has been employed as a consultant by the appellant which was, at all material times, a company whose issued shares were owned equally between Mr. Roberts and his wife. The appellant provided services under contract with persons within the IT industry. From 1st July 2000 until 30th May 2003 Mr. Roberts worked with a company called Electronic Data Systems Ltd ("EDS") pursuant to two contracts.

8 One was a contract between the appellant and a computer services agency company called Elan Computing Ltd ("Elan"). Under that contract the appellant undertook to provide the services of Mr. Roberts, or such other consultant as the appellant and EDS might agree to EDS at one or other of two specified locations. The other contract was between Elan and EDS and by it Elan undertook to supply the services of various contractors to EDS on submission by EDS to Elan of "a purchase order" in respect of the contractor EDS required. EDS submitted a series of such purchase orders to Elan for the "professional services" of Mr. Roberts. Mr. Roberts provided his services as required by EDS pursuant to the two contracts and purchase orders. In fact, the work he did was in relation to the installation of a computer system referred to as the Child Support Reform Programme pursuant to a contract between EDS and the Department of Work and Pensions.

9 The Inland Revenue determined that by virtue of the IR35 legislation the appellant was accountable to the Inland Revenue for tax under PAYE and Class 1 National Insurance contributions on the footing that both were payable in respect of the amounts received by the appellant for Mr. Roberts's services for EDS as though those amounts were salary paid by the appellant to Mr. Roberts. It is against those determinations by the Inland Revenue that the appellant appealed to the Special Commissioner. The Special Commissioner upheld the Revenue's determinations on the basis that they represented proper applications of the IR35 legislation to which I have referred. I will explain the Special Commissioner's decision and the argument before me by reference to the income tax provisions of Schedule 12 and not also the National Insurance contributions provisions of the Social Security Contributions (Intermediaries) Regulations 2000 because, as I have said, the parties are agreed that the effect of both sets of provisions is, for present purposes, the same.

10 The Special Commissioner upheld the Revenue's determinations on the basis that in the terms of para.1(1) of Schedule 12:

(a) Mr. Roberts (the worker) personally performed services for the purpose of a business carried on by EDS (the client).

(b) The services were provided not under a contract directly between the client (EDS) and the worker (Mr. Roberts) but under arrangements involving an intermediary (the appellant); and

(c) The circumstances were such that, if the services had been provided under a contract directly between the client (EDS) and the worker (Mr.Roberts) Mr. Roberts would have been regarded for income tax purposes as the employee of the client (EDS).

In reaching his conclusion that condition (c) was satisfied, the learned Special Commissioner made a very detailed and comprehensive analysis of the terms of the actual contractual arrangements under which Mr. Roberts's services were provided to EDS and the manner in which Mr. Roberts performed those services.

11 The appellant now makes two lines of attack on the Special Commissioner's decision. The first line of attack is based on a new argument not canvassed before the Special Commissioner, but one which I allowed counsel for the appellant to put without objection from counsel for the Inland Revenue. The new argument is that it is wrong to regard EDS as the client for the purposes of the conditions in para. 1(1) of Schedule 12. The client for that purpose is Elan and not EDS. It is clear that the reason the appellant makes this submission, albeit at this late stage, is that it would clearly be impossible on the facts found by the Special Commissioner to find that condition (c) of para.1(1) of Schedule 12 was satisfied, if the relevant client were the agency company Elan rather than EDS.

12 Mr. Antell, for the appellant, submitted that in the circumstances of this case the proper construction of para.1 of Schedule 12 was clearly to the effect that Elan is the relevant client, because all one is directed by the paragraph to ignore for the para.1(1)(c) test is the contract between the worker (Mr. Roberts) and the intermediary (the appellant). This means that the hypothetical contract for the purpose of para.1(1)(c) is one between Mr. Roberts and Elan. Elan can properly said to be a client because Mr. Roberts provided his services for the purposes of Elan's agency business.

13 Alternatively, Mr. Antell submitted that, if such construction of para 1(1) was not clear then the provisions are ambiguous and under the doctrine in Pepper v Hart [1993] A.C. 593 I should look at reports of Parliamentary proceedings in Hansard to ascertain the true intent of the legislature. Counsel took me to various passages in Hansard which he submitted made clear that the legislative intention was to give para.1 of Schedule 12 the effect for which he contends. I reject both these submissions. In my view it is clear that it was EDS who required the services of an IT specialist for the purposes of its business of supplying computer systems to its customers. I do not think it can sensibly be said that Mr. Roberts performed those services for the purposes of the business of Elan, which appears to have been the business of a recruitment agency.

14 As appears from the Special Commissioner's findings of fact to which I have referred, the contract entered into between the appellant and Elan was for the provision of the services of Mr. Roberts to EDS specifically. In my judgment the only person for the purposes of whose business it can realistically be said that Mr. Roberts was performing services was EDS. However, even if I am wrong in this view, and it can be said that Mr. Roberts also provided his services for the

purpose of the business of Elan, which business consisted of making such services available to its client, EDS, this in my judgment is immaterial for the purposes of the application of para.1 of Schedule 12 in the circumstances of the present case. On this basis there would be two clients within the meaning of the paragraph, Elan and EDS. One would then have to see whether the para.1(1)(c) test was met in respect of either of them.

15 On the Special Commissioner's findings of fact that test was met in respect of EDS. I accept Mr. Antell's submission that it is not met in relation to Elan. Therefore, the Revenue would still have been correct to apply para.1 in the way in which they have done. Mr. Antell submitted that to construe para.1 of Schedule 12 in a way which would allow the possibility of there being more than one client for the purposes of the paragraph would be objectionable, because it would enable the Revenue to choose which of the two or more it should treat as the relevant client, with possibly different tax results depending on which they chose. The identity of the notional employer may be material to the process of determining what deductions are allowed in computing the amount of the workers deemed receipt under the process set out in Part 2 of Schedule 12.

16 In this context, Mr. Antell relied on a dictum in the case of Vestey v Inland Revenue Commissioners [1980] A.C. 1148 in which, at p.1172 E of the report, Lord Wilberforce said this:

> "Taxes are imposed upon subjects by Parliament. A citizen cannot be taxed unless he is designated in clear terms by a taxing Act as a taxpayer and the amount of his liability is clearly defined. A proposition that whether a subject is to be taxed or not or, if he is, the amount of his liability, is to be decided even though within a limit by an administrative body represents a radical departure from constitutional principle. It may be that the Revenue could persuade Parliament to enact such a proposition in such terms that the courts would have to give effect to it. But unless it has done so, the courts acting on constitutional principles not only should not, but cannot validate it."

17 I accept the submissions of Mr. Nawbatt for the Inland Revenue that the principle there expressed by Lord Wilberforce has no relevance to the present argument. To construe para.1 of Schedule 12 in a manner which could produce two different persons as clients within the meaning of the Schedule would not give the Revenue any such unconstitutional discretion as that referred to by Lord Wilberforce. For on such a construction the Revenue can only treat as the relevant client a person as to whom the test in para. 1(1)(c) of Schedule 12 can be said to be satisfied. In the present case, even if either of Elan or EDS can be said

to be the client, the test in para.1(1)(c) is clearly satisfied only in relation to EDS. On the facts as found by the Special Commissioner it cannot be said that, if the services provided by Mr. Roberts were provided under a contract directly between Mr. Roberts and Elan, Mr. Roberts would be regarded for income tax purposes as an employee of Elan as opposed to an employee of EDS. This is rightly accepted by the Revenue.

18 Thus, even on the basis, which I do not think is the correct one, that Elan can be treated as a client within the meaning of para.1(1)(a) of Schedule 12, as well as EDS, the Revenue has no discretion as to which client to choose for the application of Schedule 12. It can only be EDS because that is the only client in respect of whom the para.1(1)(c) test is satisfied.

19 Despite Mr. Antell's submission to the contrary it seems to me highly unlikely that there could be circumstances in which, even if there can be more than one client within para.1(1)(a) of Schedule 12, there could be more than one in respect of which the para 1(1)(c) test is satisfied. However, whether or not in other circumstances it might be possible to find more than one client within the meaning of para.1(1)(a) of Schedule 12 as I have said, in my judgment, this is not such a case. On the facts of this case EDS is the only person of whom it can be said with any sense of reality that Mr. Roberts performed services for the purposes of its business.

20 Before leaving the appellant's first line of attack on the Special Commissioner's decision, I should say that in his submissions Mr. Nawbatt referred me to a recent unreported decision dated 8th October 2004 of Park J. on the application of the IR35 legislation in Usetech Ltd. v. Young (Inspector of Taxes) 2004 EWHC 2248 Chancery. That, like this, was a case in which the relevant worker's services were provided to a client, not only through an intermediary within para. 1(1)(b) of Schedule 12, but also through another company (the equivalent of Elan) acting as agent for the end user client. Park J. saw no difficulty in applying Schedule 12 on the footing that the end user of the worker's services was the relevant client, despite the position of its agent.

21 However, as Mr. Nawbatt accepted Mr. Antell's new point in this case was not argued in Park J's case, so that his decision cannot be said to be any authority on the point. On the other hand Park J's decision is authority against the further objection made by Mr. Antell for treating EDS as the client for the purposes of para.1 of Schedule 12, and that was that it would mean that the appellant's liability to the Revenue would depend on facts relating to the contractual arrangements between Elan and EDS not within the knowledge of the appellant. A similar argument was considered by Park J. in paras 43 to 47 of his Judgment.

I reject Mr. Antell's submission for the same reasons as those given by Park J. for rejecting the argument in his case.

22 I also reject Mr. Antell's Pepper v Hart argument, because I am not satisfied that there is any ambiguity or obscurity in the meaning of the provisions of Schedule 12 which would justify looking at Hansard, or any other Parliamentary material as an aid to construction. Thus, in my judgment, the appellant's first line of attack on the Special Commissioner's decision fails and I must turn to the second, which is that the Special Commissioner misdirected himself as to the law in considering whether the employment test in para. 1(1)(c) of Schedule 12 would be satisfied by the hypothetical contract between Mr. Roberts and EDS required to be assumed for the purposes of that test. I accept the Revenue's submissions that the question whether, had there been such a contact directly between Mr. Roberts and EDS, Mr. Roberts would have been properly regarded for income tax purposes as an employee of the client, must be determined in the light of the current common law test of employment explained in Ready Mixed Concrete (South East) Ltd. v Minister of Pensions and National Insurance [1968] 2Q.B. 497. That case was an appeal against the decision of the Minister of Pensions and National Insurance that an individual ("L") was, for the purposes of the National Insurance Act, 1965 an "employed person" under a contract of service to the appellant company.

23 At p.512H to 513B of the report in the case, MacKenna J. held that:

> "Whether the relation between the parties to the contract is that of master and servant or otherwise is a conclusion of law dependent on the rights conferred and the duties imposed by the contract."

At p.515A the learned Judge said:

> "…it is the right of control that matters, not its exercise."

Then at p.515C to H he said this:

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

"I need say little about (i) and (ii).

"As to (i). There must be a wage or other remuneration. Otherwise there will be no consideration, and without consideration no contract of any kind. The servant must be obliged to provide his own work and skill. Freedom to do a job either by one's own hands or by another's is inconsistent with a contract of service, though a limited or occasional power of delegation my not be: (See Atiyah's Vicarious Liability in the Law of Torts (1967) pp.59 to 61 and the cases cited by him).

"As to (ii). Control includes the power of deciding a thing to be done, the way in which it shall be done, the means to be employed in doing it, the time when and the place where it shall be done. All these aspects of control must be considered in deciding whether the right exists in a sufficient degree to make one party the master and the other his servant. The right need not be unrestricted.

> 'What matters is lawful authority to command as long there is scope for it. And there must always be some room for it, if only in incidental or collateral matters – see Zuijs v Wirth Brothers Proprietary, Ltd [1955] 93 C. L. R. 561 (p.571).'"

24 The appellant's first complaint about the way in which the Special Commissioner applied the test under para.1(1)(c) of Schedule 12 is that he wrongly accepted a submission of the Revenue to the effect that in applying the employment test, it is the right of control of the worker by the client and not whether such control was actually exercised that is significant. This submission of the Revenue before the Special Commissioner is clearly supported by the dicta of MacKenna J. in the Ready Mixed Concrete case which I have quoted earlier. However, the question before the court in that case was whether the worker was to be regarded as employed under an actual contract of service. In other words, was the actual contract between him and his "employer" one of service. The question to be answered in applying the test in para.1(1)(c) of Schedule 12 is not the same question. Here the question is whether: "The circumstances are such that if the services were provided under a contract directly between the client and the worker" the worker would be regarded as an employee of the client. Thus the relevant contract concerned is not an actual contract but a notional one to be assumed in the context of all the other actual circumstances of the case.

25 This point was adverted to by Burton J. in a case in which the court had to consider whether the IR35 legislation conflicted with the European Convention on Human Rights and European Community Law. At para.48 of his Judgment in

R (On the Application of Professional Contractors Group Ltd and Others) v Inland Revenue Commissioners [2001] Simon's Tax cases 629 at p.651 Burton J. said this:

> "It appears to me clear that the Revenue must bear in mind that under IR35 they are *not* considering an actual contract between the service company and the client, but imagining or constructing a notional contract which does not in fact exist. In those circumstances, of course the terms of the contract between the agency and the client as a result of which the service contractor will be present at the site are important, as would be the terms of any contract between the service contractor and the agency. But, particularly given the fact that, at any rate at present, a contract on standard terms may or may not be imposed by an agency, or may be applicable not by reference to a particular assignment, but on an ongoing basis and may actually bear no relationship to the (non-contractual) interface between the client and the service contractor, such documents can only form a part, albeit obviously an important part of the picture."

25 In my view it is necessary to take account not only of the terms of the actual contractual arrangements between the appellant and Elan and Elan and EDS, but of all the other circumstances in which Mr. Roberts performed his services for the purposes of EDS's business in order to test whether, had those circumstances been different only to the extent that the services were provided pursuant to a contract directly between Mr. Roberts and EDS, Mr. Roberts could properly be regarded as employed by EDS. In my judgment this is precisely what the Special Commissioners did. He did not restrict his consideration to the terms of the actual contractual arrangements between the appellant and Elan and Elan and EDS. He did also consider the actual way in which Mr. Roberts performed his services for EDS. He made a very full and careful analysis of both the contractual arrangements and the actual manner and circumstances in which Mr. Roberts's services were performed. He rightly regarded the actual contractual arrangements as an important but not exclusive element in the test to be applied under s.1(1)(c) of Schedule 12. I consider this criticism of the appellants quite unfounded.

26 The appellant's second criticism under this head is that the Special Commissioner, and I quote from the appellant's grounds of appeal:

> "…placed too much emphasis on the part and parcel of the organisation test and when applying that test failed to distinguish between part and parcel of EDS team who was assembled to carry out the CSR [Child Support Review] Project and being part and parcel of EDS itself."

In this context Mr. Antell relied on a dictum of Mummery J. (as he then was) in Hall (Inspector of Taxes) v Lorimer [1992] Simon's Tax cases 599 in which case the court heard an appeal from a decision of a Special Commissioner that a tax payer was not employed under a contract of service but carried on business on his own account for the purchase of an assessment of income tax. At p.612 of the report Mummery J. said:

> "The decided cases give clear guidance in identifying the detailed elements or aspects of a person's work which should be examined for this purpose. There is no complete exhaustive list of relevant elements. The list includes the express or implied rights and duties of the parties; the degree of control exercised over the person doing the work, whether the person doing the work provides his own equipment and the nature of the equipment involved in the work, whether the person doing the work hires any staff to help him; the degree of financial risk that he takes, for example as result of delays in the performance of the services agreed; a degree of responsibility for investment and management and how far the person providing the service has had an opportunity to profit from sound management in the performance of his task. It may be relevant to consider the understanding or intentions of the parties; whether the person performing the services has set up a business-like organisation of his own; the degree of continuity and the relationship between the person performing the services and the person for whom he performs them; how many engagements he performs and whether they are performed mainly for one person or for a number of different people. It may also be relevant to ask whether the person performing 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."

27 In the present case Mr. Antell submitted that Mummery J. made it clear that the "part and parcel of the organisation test" (as Mr. Antell called it) was only one factor that in some cases might be relevant, whereas in this case he submitted the Special Commissioner placed far more significance upon it and used it as an overall test to determine whether Mr. Roberts could be said to be employed by EDS. I do not accept this submission. The Special Commissioner dealt with the point in para.31 of his decision:

> "Finally, I am satisfied that Mr. Roberts throughout the time he worked for EDS, was part and parcel of the organisation. In the particular circumstances of the present arrangements Mr. Roberts was well integrated into EDS's structure assembled to carry through the CSR project. He had a manager to whom he was accountable. Mr. Roberts in turn worked as part of a team managing other people. He was involved in

> discussions as to work allocation with EDS's project line manager. He was expected to be available to advise and assist other members of the team. He attended meetings with interested parties alongside other EDS managers. Although Mr. Roberts's role in the organisation will not necessarily be determinative, it is clear that in the present circumstances he was an integral part of the EDS organisation dedicated to the CSR project. This feature is in line with the conclusions I have reached based on the control over Mr. Roberts's work in the presence of mutual obligations of an employer/employee nature existing between EDS and Mr. Roberts."

28 It is, in my judgment, clear from this that the Special Commissioner was not treating the part and parcel of the organisation feature of the circumstances of the present case as a test of employment in its own right, or as anything other than one of the features of all the circumstances he was properly considering under para. 1(1)(c) of Schedule 12. He regarded it only as confirming the conclusion which he had reached on the other factors of the case. (See the last sentence of para.31 of his decision that I have just quoted). This he was perfectly entitled to do.

29 The second part of this ground of appeal is that in considering the part and parcel of the organisation factor, the Special Commissioner fell into error in that he failed to distinguish between being part and parcel of EDS's team working on the CSR project and being part and parcel of EDS itself. In support of this submission Mr. Antell relied on a distinction drawn by the Special Commissioner in the decision under appeal in Hall v Lorimer in which the Special Commissioner said this:

> "Being one of a team to produce a programme does not in my view lead to the conclusion that in the taxpayer's case he is part and parcel of the organisation... A violinist in an orchestra may be part and parcel of the orchestra for the performance being given but it does not follow that he is part and parcel of the organisation which runs or manages the orchestra."

I do not consider this criticism of the Special Commissioner in the present case is justified. It is clear from what he said in para. 31 of his decision (which I have already quoted) that he found that Mr. Roberts:

> "…was an integral part of the EDS organisation dedicated to the CSR project. This feature is in line with the conclusions I have reached based on the control over Mr. Roberts's work and the presence of the mutual obligations of an employer/employee nature existing between EDS and Mr. Roberts."

30 I consider that on the facts that he found and set out in his decision the Special Commissioner was well entitled to reach the conclusion that Mr. Roberts was part and parcel of the organisation of EDS's business and that that fact was consistent with the Special Commissioner's view based on all the other circumstances of the case, that the relationship between EDS and Mr. Roberts was such that had it existed under a contract between them it would have been one of employer and employee.

31 Thus, in my judgment, the appellant has failed to make good any of its criticisms of the Special Commissioner's decision and I shall dismiss this appeal.

MR. NAWBATT: My Lord, you should have a costs' schedule, but I have another copy in case you have not.

SIR DONALD RATTEE: I have it here.

MR. NAWBATT: There is just one addition, that is today's costs. It is £80 for my attendance today plus £14 VAT, so the total will be £3481.

SIR DONALD RATTEE: So you are asking me to dismiss the appeal with costs in that sum?

MR. NAWBATT: My Lord, yes.

SIR DONALD RATTEE: Any objection to that, Mr. Antell?

MR. ANTELL: My Lord, I cannot object in principle, but I would query one particular item on the schedule of costs and that is the attendances by solicitors on documents which amounts to over six hours. It is not clear what was involved in that since the skeleton argument was drafted by counsel.

SIR DONALD RATTEE: Well what is the answer?

MR. NAWBATT: My Lord, I believe the answer is this, it is that if one looks at the appellant's cost schedule you will see that my learned friend's brief fee ----

SIR DONALD RATTEE: Well I have not seen one of those, I do not have one. Anyway, just tell me what it says.

MR. NAWBATT: Well he will correct me if I am wrong. The fees put in by my learned friend exceed mine by some distance, and so if you added my learned friend's and his solicitor's fees, and then you compared them to my instructing solicitors and my fees the appellant's costs far outweigh the respondent's, and

that I think is the explanation for the difference in costs. Those instructing me have spent more time on this case than my learned friend's instructing solicitors and that is reflected in my reduced brief fee. You have seen Mr. Antell's skeleton argument ----

SIR DONALD RATTEE: It is quite difficult to see how you spend six hours on them, there are very few documents, what do you with them for six hours?

MR. NAWBATT: My Lord, I think the answer is this. You will see Mr. Antell's skeleton argument; it is quite a weighty document.

SIR DONALD RATTEE: Yes.

MR. NAWBATT: So even before instructing me that was received, so they would have to go through the Special Commissioner's decision and then go through my learned friend's skeleton argument, and then there is the preparation of the brief, and then also you have seen the authorities and the statutory material as well.

SIR DONALD RATTEE: Yes. Yes, thank you. Do you want to say anything else, Mr. Antell?

MR. ANTELL: My Lord, only that it would normally be counsel who would go through the appellant's skeleton argument when drafting the skeleton argument in response.

SIR DONALD RATTEE: No. I think the costs are reasonable. I shall dismiss the appeal, order that the appellant pay the respondent's costs in the sum of £3,481. Anything else?

MR. ANTELL: No, my Lord.

SIR DONALD RATTEE: Thank you both for your help.

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FUTURE ON-LINE LTD v S K FOULDS (HMIT) (2004)

[2004] EWHC 2597 (Ch)

Ch D (Sir Donald Rattee) 22/10/2004

TAX - SOCIAL SECURITY

COMPANIES : INCOME TAX : INTERMEDIARIES : NATIONAL INSURANCE : SERVICES : NOTIONAL CONTRACT OF SERVICE : CONSTRUCTION OF "CLIENT" UNDER S.1(1) OF SCHEDULE 12 OF THE FINANCE ACT 2000 AND SOCIAL SECURITY CONTRIBUTIONS (INTERMEDIARIES) REGULATIONS 2000 : IR35 LEGISLATION : SERVICE COMPANIES : SCHEDULE E : Sch.12 para.1(1) FINANCE ACT 2000 : reg.6 SOCIAL SECURITY CONTRIBUTIONS (INTERMEDIARIES) REGULATIONS 2000

In the circumstances there had been a direct contract between an individual and an end company and therefore a contract of service existed between them to the extent that, pursuant to the IR35 legislation, that individual's company was required to account for national insurance contributions and income tax during the relevant period.

The appellant company (F) appealed against a determination of the special commissioner.

X had provided specialist IT services through F, his service company, and an agency (E), to an end company (Y).

The special commissioner concluded that if there had been a direct contract between X and Y during the period of engagement it would have been a contract of service and therefore, pursuant to the IR35 legislation, F would have been required to account for national insurance contributions and income tax for the relevant period.

F argued that the special commissioner had erred in his construction of "client" under the Finance Act 2000 Sch.12 para.1(1) and the Social Security Contributions (Intermediaries) Regulations 2000 reg.6 and that by way of the proper construction of para 1 of schedule 12, E was the relevant client.

HMIT contended that the special commissioner had been right to identify the client as Y, had applied the correct test in determining whether the notional contract was one of service, and had been correct to find that it had been.

HELD: It was clear that Y required the services of an IT specialist and it could not be said that X had performed those services for the purpose of E's business.

Y was the only party with whom it could be said that X performed services for business purposes.

The special commissioner had been entitled to find that X had been part and parcel of Y's organisation and that the relationship between Y and X was such that the notional contract between them had been one of service. Appeal dismissed.

Counsel: For the respondent: Akash Nawbatt For the appellant: J Antell
LTL 22/10/2004 : (2005) STC 198

Document No. AC9100131

SPC00457

NATIONAL INSURANCE CONTRIBUTIONS – IR35 – computer services heading a team supporting and maintaining a computer system under a series of six monthly contracts – whether hypothetical contract would be an employment contract – yes – appeal dismissed

THE SPECIAL COMMISSIONERS

NETHERLANE LIMITED **Appellant**

- and -

SIMON YORK **Respondent**

Special Commissioner: DR JOHN F. AVERY JONES CBE

Sitting in public in London on 15 and 16 December 2004

A D Robertson FCA CTA for the Appellant

Mike Faulkner, HM Inspector of Taxes, Inland Revenue Southern England Regional Appeals Unit, for the Respondent

DECISION

1. This is an appeal by Netherlane Limited against a decision letter dated 9 September 2003 that the circumstances of the arrangements between Mr M J Renshaw and AMP UK (formerly NPI) for the performance of services from 6 April 2000 to 23 February 2001 were such that the "IR35" legislation applied to National Insurance contributions. The parties have agreed that the decision will be applied to the period to 28 September 2001. The Appellant was represented by Mr A D Robertson FCA ATII; and the officer by Mr Mike Faulkner.

2. Both Mr Robertson and Mr Faulkner had put in a tremendous amount of work in preparing the case for which I am grateful. Mr Robertson's written case ran to 74 pages; and Mr Faulkner's skeleton to 25 pages very helpfully cross-referenced to the documents. The bundle of documents ran to 364 pages and the witness statements to 32 pages. In spite of all this I regret to say that I thought that much of the efforts on the Appellant's side were misdirected and at the end of this decision I shall make some observations which I hope will be of assistance to others in the preparation of IR35 cases.

Findings of fact

3. There was the following statement of facts not in dispute

(1) Mr Martin J Renshaw left University in 1979 and became employed by Hambro Life (which later became Allied Dunbar) as a trainee computer programmer. He remained employed by Allied Dunbar until 1997 at which time he had attained the status of IT Project Manager.

(2) The Appellant company was incorporated on 10 June 1997. Throughout its existence Mr Renshaw has been the sole director and has held 60% of the shares. Mr Renshaw's wife holds the remaining 40% of the shares.

(3) For the purposes of this appeal, and subject to any amendment to returns necessitated by the Commissioner's decision, it is agreed that, with the assistance of a chartered accountant, the Appellant has complied with its obligations under company, business and taxation law. In particular it has done the following:

(a) Prepared annual accounts in compliance with company law and accounting standards;

(b) Submitted its accounts to Companies House and to the Inland Revenue;

(c) Prepared and submitted corporation tax returns each year;

(d) Written up payroll records, prepared payslips and submitted PAYE/NI returns to the Inland Revenue;

(e) Maintained a register of its fixed assets;

(f) Registered for VAT and submitted VAT returns;

(g) Required MJR to submit formal expense claims in respect of company business expenses incurred by him on NL's behalf;

(h) Prepared and submitted to the Revenue forms P11D and P11D(b);

(i) Invoiced its services to clients such as RML on credit terms using formal VAT invoices;

(j) Maintained a sales ledger to control the collection of customer debts;

(k) Maintained insurance cover for employer's liability, public liability, products liability and professional indemnity risks.

(4) The Appellant was offered a contract by a company called Resource Matters Ltd (RML) which required NL to provide IT services at the Cardiff premises of their client NPI Limited (NPI) (which later became AMP).

(a) The first contract commenced around 1 September 1997 and was for a period of 26 weeks.

(b) Shortly before the end of this term, a fresh 26 week contract was agreed and this pattern continued until June 2001.

(c) AMP notified Mr Renshaw in June 2001 that they would not have any further use for his services after 28 September 2001 and would not be prepared to offer a further 26 week contract as in the past but offered a 4 week contract instead. The reason given was that it was the policy of AMP (having taken over NPI) to use company employees to perform these services.

(5) AMP worldwide restructured in 2003. The UK operations are now part of HHG plc.

(6) The contract between Mr Renshaw and the Appellant for the 26 week period to 25 August 2000 and signed by Mr Renshaw on 9 February 2000 consisted of a double sided sheet of A4 paper. One side is headed "Resource Matters Ltd Contract for Services by I.T. Consultant". The other side is headed "Contract Assignment Schedule" and contained details of the actual assignment.

(7) Subsequent contracts consisted of a seven page "Contract Supply Agreement" that, other than the date and signatories, did not change from contract to contract plus a single page "Assignment Schedule" similar, but not identical, to the "Contract Assignment Schedule" of the old contract. The first new contract between Mr Renshaw and the Appellant also covers the 26 week period to 25 August 2000. It is dated 3 April 2000 but signed by the Appellant on 3 May 2000 and by RML on 8 May 2000.

(8) RML made a corresponding series of 26 week contracts with NPI to supply Mr Renshaw's services to NPI. Each contract consisted of 2 pages

that, other than the date, did not change from contract to contract together with a single page schedule that contained the details of the assignment.

(9) Summaries of the information on the Mr Renshaw/the Appellant and NPI/RML schedules for the relevant period are attached [not included as these are summarised below].

(a) Although the schedule to the 20 July 2000 NPI/RML agreement shows the rate per working day inclusive of VAT paid RML to be £664.53, the rate actually paid was £650.95.

(10) A decision under S8 of the Social Security Contributions (Transfer of Functions, etc) Act 1999 for the period 6 April 2000 to 23 February 2001 was made on 9 September 2003 and appealed, with an election for the appeal to be heard by the Special Commissioners, on 25 September 2003.

4. I heard oral evidence from Mr Renshaw, Mr Jonathan Summers (RML), Mrs Quinn (RML) by telephone conference call arranged on the second day's hearing, and from the officer who made the decision, Mrs Sue Gibb. I also had a witness statement from Mr Michael Clark (formerly of NPI) and I have read some correspondence with HHG plc, and Mr J W Turner formerly of NPI. I find the following facts:

(1) In 1997 Mr Renshaw decided to seek higher potential rewards by setting up as a freelance IT consultant finding work through recruitment agencies who expected him to operate through a company. He formed the Appellant of which he is the sole director and owner of 60 % of the shares, the other 40% being owned by his wife. At its peak he would earn two or three times what he would earn as an employee (although I imagine that this figure did not take fringe benefits into account).

(2) The recruitment agency the Appellant used in the relevant period was RML who from the beginning in 1997 found work with NPI. During the period in question the Appellant entered into the following contracts with RML (the lower level contracts): (a) 26 February 2000 to 25 August 2000, (b) from 26 August to 23 February 2001, (c) 24 February 2001 to 24 August 2001, and (d) a final one month contract 27 August 2001 to 28 September 2001. Strictly, only contracts (a) and (b) are in issue but as the parties have agreed that the decision will apply up to 28 September 2001 I have included information about the whole of the period.

(3) As stated above, there are two versions of contract (a) covering the identical period, one signed on 9 and 17 February 2000 but undated at the start, and the other signed on 3 and 8 May 2000, and dated 3 April 2000 at the start. The second version seems to have arisen from changes, which are set out in a letter to Mr Renshaw, made to the standard form on account of the IR35 legislation. The changes include that the Appellant will not engage in any conduct detrimental to the RML or the client, instead of that it will give priority to the Services over all other business activities; that the Appellant may (rather than shall) provide services at the location of the client; changing references to time sheets to work sheets; deletion of a clause requiring the Appellant to obey all lawful and

reasonable directions of RML or the client; addition of a new provision that the Appellant will provide at its own expense any training that Mr Renshaw may require in order to perform the consultancy, that that it will provide all necessary equipment as is reasonable for the adequate performance by Mr Renshaw (subject to any agreement to the contrary specified in the Assignment Schedule) [which there is not]; the restriction of the Appellant's limitation of liability to £1m rather than its being unlimited; the addition of the type of insurance cover required; addition of a disclaimer that RML makes no representation and takes no responsibility for ensuring that the terms of the contract are an accurate reflection of the relationship between the client and the Appellant, and also that RML accepts no liability for any liabilities "whether by reason of tax or other statutory or contractual liability to any third party arising from the Assignment." In the Assignment Schedule, 35 hours per week is replaced by 5 professional working days; under payment terms on invoice is changed to 7 days/weekly; references to a notice period of 4 weeks (which does seem to relate to anything in the contract) and to overtime are deleted. No changes were made to the upper level contract (see paragraph 4(5)) at the same time. In what follows, references to contract (a) are to the later version, although the earlier version was in force until the amendment. Mr Summers said (and I accept) the amendment was agreed in principle in March 2000 but he did not say that it was agreed by the Appellant, and Mr Renshaw merely said that that it was varied with effect from 3 April 2000 although signed later. Since the amended version was sent to him with a covering letter of 17 April 2000 explaining the changes I find that the amendment was made at the date of signature on 3 and 8 May 2000.

(4) The lower level contracts were in standard form with an "Assignment Schedule" specific to the particular work. Each contract provides for the Appellant to start on a specified date and continue to provide the services for the duration of the assignment with the contract automatically terminating on completion of the assignment. In other words it envisages a specific assignment. However the Assignment Schedule does not refer to a particular assignment but describes the assignment as "consultant" (contract (a)) or "software consultant" (the other contracts) and also specifies an end date. The Schedule therefore seems to me to change the nature of the contract from carrying out an assignment to a fixed term contract for the provision of consultancy services. The contracts contain the following terms:

> (a) The Appellant is to provide the services set out in the Assignment Schedule, but the schedule does not refer to any services other than the assignment. The services are to be provided on the terms of the agreement and the terms of the upper level contract are incorporated "where applicable."
>
> (b) The Appellant is named as "consultant"; and Mr Renshaw is named as "Personnel". No changes are to be made to the personnel without RML's consent, which shall not be

unreasonably withheld. All personnel must be employees of the Appellant.

(c) They provide for "5 professional working days" (contract (a)) or 35 hours per week (the other contracts).

(d) NPI or AMP is named as the client. In each contract he is described as "reporting to" Mike Clark (contracts (a) and (b)) or Matthew Brown (contracts (c) and (d)).

(e) The Appellant is required to make good at its expense any services not carried out to the client's satisfaction. There is no evidence that this ever occurred and this provision is not reproduced in the upper level contract. It would mean that no payment would be made for the time spent on correcting work and it is not suggested that this occurred.

(f) The contracts can be terminated immediately by RML if the client no longer requires the Appellant to provide the services.

(5) During the period in question RML entered into the following contracts with National Provident Institution (NPI) (the upper level contracts): (a) 26 February 2000 to 31 August 2000, (b) 1 September 2000 to 23 February 2001, (c) 24 February 2001 to 31 August 2001, and (d) a final one month oral contract 27 August 2001 to 28 September 2001. Except for a few days difference in the dates there are therefore equivalent lower and upper tier contracts every six months, with a final month. They include the following terms:

(a) Mr Renshaw is named as the consultant.

(b) RML confirms that Mr Renshaw will obey any lawful instructions given by NPI.

(c) The supervising manager is named as Mike Clark (contracts (a) and (b)), or Matthew Brown (contract (c)) who were not based in Cardiff. Mr Clark provided a witness statement but did not give oral evidence. I accept his evidence but bear in mind that he was not cross-examined. He sets out a table of the differences between an employee who was IT Project Manager as an employee, and a Contract IT Project Manager such as Mr Renshaw adding "The roles themselves were essentially the same, requiring the same skills and experience and focused on the same objectives and deliverables." The differences in his table were that the employee had flexible start and finish times with the ability to build up credit and take off up to one day per month; was paid monthly; was paid holiday and sick leave; was a member of the company's non-contributory pensions scheme; had private medical insurance, performance related annual bonus and share option scheme; was employed under a permanent contract until resignation, redundancy, dismissal etc; and was subject to annual performance and competency review,

a personal development plan including company-financed training. In contrast Mr Renshaw worked a minimum 7 hours per day (I accept Mr Renshaw's evidence that there was some flexibility here in reality) and could not build up credit; was paid at a daily rate monthly against timesheets; had no paid holiday or sick leave; was not in the pension scheme; had no private medical insurance, bonus or share options; was engaged on typically a 6 months short-term contract, with the offer of a subsequent contract being dependant on business need, satisfactory performance and agreement of rates, contracted via an intermediary who put forward suitable candidates, assisted with rate negotiations and managed the time sheets and invoicing; there were no formal performance reviews, no personal development or training other than on-the-job training of company specifics to enable completion of agreed tasks.

(d) The assignment is described as team leader (contract (a)), or project management/leader (contract (c))

(e) The place of work is in NPI's office in Cardiff. The nature of his work on the computer system necessitated his being on site during normal working hours but occasionally it was necessary for him to visit other sites, for example to talk to accounts staff if action needed to be taken to computer systems affecting them. Some work such as writing reports would be done on the train or at home, and he would also make phone calls away from the office using his own mobile phone. He also used his own laptop computer to work on the train.

(f) A rate of pay per working day is given. Working day is defined as "A working day is normally 7 hours, but the Consultant may be required to work beyond 7 hours on any particular day to ensure the completion of an agreed task." Overtime was not in fact paid although the contract provides for this if requested by NPI, and contract (a) states after "term leader" "(including hours of work and reference to overtime, if applicable)". In practice he normally worked more than 7 hours, particularly when changes were needed, for example on the introduction of stakeholder pensions, or when severe problems needed fixing. There was some flexibility; for example, there was no problem about leaving early if the work was complete, and hours might be varied by agreement with Mr Clark. In practice he would be paid for a half-day of 3.5 hours; there are three examples of this in the summary of time sheets from 9 April 2000 to 6 April 2001. Weekly time sheets (later work sheets, which are virtually identical) were completed with 7 hours even if more were worked and certified by someone at NPI. There was a separate record of the true time spent of each job for planning purposes but I was not shown an example.

The only occasion when a separate additional payment was negotiated was over the Millennium when he had to cover New Year's eve.

(g) Payment was made against time sheets (the change to describing these as work sheets made in the lower level contract was not made in the upper level contract). Invoicing was monthly with payment within 30 days.

(h) The contract was terminable immediately by NPI during the first six weeks and thereafter on four weeks notice. I accept Mr Summers' evidence that this provision was something that RML negotiated for, which they did not need so far as the lower level contract was concerned as this was terminable immediately on termination of the upper level contract. Contact (c) was also terminable on four weeks' notice by RML.

(i) Although there is no provision for holidays, in practice during the period from 9 April 2000 to 6 April 2001 he did not work for five weeks plus a few additional days which were presumably holidays, as he said that he did not have any absence for sickness. He would give NPI notice if he were away and some of his work would be covered by a member of the team.

(j) Contract (c) envisages that NPI may novate the contract with AMP (UK) Services Limited.

(k) The final month, contract (d), was a hand-over period after NPI or AMP had decided and informed him in June 2001 that the function would in future be dealt with by permanent employees and run from another location. Mr Renshaw was offered the job but declined it as he did not want to be an employee.

(6) Mr Renshaw's work consisted of leading a team that supported and maintained (including updating to deal with legislative changes) two NPI mainframe computer systems dealing with group pensions, originally the West system and then the Alice system. The work was primarily "fix on fail." Users would report faults to a help desk which logged calls and initially categorised them into four levels of severity based on company guidelines, depending for example on whether the problem affected the whole system or only one person. Such reports might happen 20 times in a day. Mr Renshaw received the log, worked out what needed to be done and he might change the priority categorisation before passing it to a member of his team of six or seven technical programmers to take action (the team was smaller at the end of the period as more of the work was outsourced). The six monthly contracts did not coincide with any particular aspect of the work; there would be computer problems to fix at the beginning and end of each contract. He would give a statistical report every fortnight to Mr Clark, who would also be informed immediately of

problems falling into the most urgent category. Mr Clark might sometimes suggest that he copy reports to others who might be affected. Poor performance by a member of the team would in the last resort be discussed with Mr Clark. He discussed salary reviews of members of the team with management. He was not otherwise concerned with career development of members of the team which would be dealt with by a manager. He described as typical day as including considering a print-out of outstanding problems on the train; having an early morning meeting with representatives of the various departments to pick-up on problems; talk to his team to arrange priorities; attend meetings and deal with phone calls; progress problems to a result; negotiate with managers for a suitable time to fix software problems if this meant that the system would be unavailable; he would deal with paper work and phone calls on the train on the way home using his own mobile phone.

(7) Mr Renshaw had never seen the upper level contracts the terms of which are incorporated by reference into the lower level contracts until the papers were prepared for this appeal. He did not ask to see these at the time they were entered into. While I expect that RML might not want to show him the figures which would show their mark-up they could hardly have refused to show him the terms that were incorporated into the lower level contracts if he had asked. While accepting that he was unaware of them, as the Appellant entered into the lower level contract incorporating its terms I shall take it and Mr Renshaw as having agreed to these terms.

5. Mr Renshaw was an impressive witness and I accept all his evidence. He had been employed by Allied Dunbar for 18 years and he had decided to work in a freelance capacity, but through the medium of the Appellant company. He is a man dedicated to his work and serving his clients, being intent on achieving results for the client, if necessary by working long hours although without additional remuneration. He knew what it was like to be an employee in the past, and now did not have an employee mentality. He was prepared to take the risk of having a series of six-month assignments which might not be renewed in order to receive a higher rate of remuneration than he would receive as an employee, although he lost all fringe benefits. The additional risks he was taking were real. He is understandably indignant that the Revenue should treat him indirectly as an employee by the IR35 legislation.

6. Mr Summers gave evidence that he was employed by Resource Control and Management Limited (RCaM) until April 2002 (although his witness statement had originally said 2001) when he joined RML. RCaM monitored and controlled subcontractors and agencies providing them, such as RML, on behalf of, originally, Pearl Assurance and also AMP which took over both Pearl and NPI. RCaM lost that contract to RML in March or April 2001 following which RML wore two hats, their original agency hat, and the new supervisory role that was formerly carried out by RCaM. He said, and I accept, that during the period in question changes were being made to the contractual arrangements. I was shown a contract dated 9 May 2001 between AMP and RML having effect from 1 March 2001 which is the contract under which RML took over RCaM's role, although the copy I saw did not have signatures.

That contract provides in an Appendix for a draft agreement between AMP and an IT Services Agency. I also saw a contract dated 15 September 2002 between AMP and RML but without any signatures and with schedules uncompleted. Mr Summers said that there was an earlier similar verion which could not be traced. It seems that this contract was intended to be used rather than the actual upper level contracts entered into from about 1 March 2001 when RML took over RCaM's role. It is possible but I am unable to make any finding that a similar contract was in use when RCaM were carrying out the supervising function before that date. This evidence is insufficient, particularly as I heard nothing from AMP, for me to find that the 15 September 2002 contract better reflects the terms of the upper level contract from 1 March 2001 and so I am bound to take the contracts that were actually entered into. However, because Mr Robertson placed reliance on its terms I note that it differed from the upper level contracts in the following respects: RML may propose a substitute who needs to be approved in writing by AMP; RML must comply with any timetable or other targets or project requirements as is reasonably required by AMP; RML may exercise a degree of control as to the method of performance of the services and undertakes to use reasonable endeavours to ensure that industry standards are complied with; subcontractors may take leave only with the agreement of RML and AMP; if the contractor is unable to work both RML and AMP must be informed; AMP may terminate the contract on one week's notice during the first six weeks; all clauses are to be represented in the contract between RML and the contractor; the uncompleted schedule provides for an eight hour day and overtime when authorised in advance. I record that the differences would have made no difference to my decision.

7. Before Mr Summers' evidence and in particular before he changed the date mentioned at the beginning of paragraph 6 above I thought that I was being given evidence from RML about the contracts entered into with NPI. I realised that Mr Summers was not concerned with RML except in RCaM's supervisory capacity before 1 March 2001 and then not at all until April 2002 when he joined RML. Bearing in mind that Mr Renshaw was unaware of the terms of the upper level contracts I gave Mr Robertson the option of calling further evidence and in the circumstances I agreed to Mrs Quinn of RML giving evidence by conference call. Mrs Quinn confirmed the existence of the changes to the arrangements mentioned by Mr Summers but could not recall the contractual position.

Legislation

8. Regulation 6(1) of the Social Security Contributions (Intermediaries) Regulations 2000 provides:

> "These Regulations apply where—
>
> (a) an individual ("the worker") personally performs, or is under an obligation personally to perform, services for the purposes of a business carried on by another person ("the client"),
>
> (b) the performance of those services by the worker is carried out, not under a contract directly between the client and the worker, but under arrangements involving an intermediary, and

(c) the circumstances are such that, had the arrangements taken the form of a contract between the worker and the client, the worker would be regarded for the purposes of Parts I to V of the Contributions and Benefits Act [the Social Security Contributions and Benefits Act 1992] as employed in employed earner's employment by the client."

"Intermediary" is defined in Regulation 5 and it is common ground that the Appellant is an intermediary for this purpose.

Preliminary points

9. Mr Robertson raised four preliminary points. First that as the notice that the Regulations applied has not been sent to NPI, it was invalid. Secondly, that the client was RML and not NPI and the notice was invalid for naming the wrong client. Thirdly, it was the Revenue's duty to obtain evidence before making a decision on status. Fourthly, that the delay had prevented him from obtaining evidence from those at NPI.

10. Regulation 3 of the Social Security Contributions (Decisions and Appeals) Regulations 1999 requires that a decision "must state the name of every person in respect of whom it is made," who is the person who can appeal it. Regulation 4 states that notice of a decision referred to in regulation 3 must be given "to every person named in the decision." No notice was given to NPI which Mr Robertson contended invalidated the notice since NPI are named in the decision. Mr Faulkner contended that NPI were not affected by the decision and so it was not made in respect of NPI who were not required to be given notice. I agree with Mr Faulkner. The decision was made in respect of the Appellant and Mr Renshaw because it affected their national insurance contributions. Although NPI are named so as to make clear to what relationship the notice applied the decision is not made in respect of NPI and so there can be no purpose in requiring them to be given notice. The reference to persons named must be construed as persons affected by the notice who are named in it. Commercially the relationship with NPI may have been affected because if the Regulations applied the Appellant has to pay national insurance contributions that it was not expecting to pay. But legally NPI was in the same position whether or not it applied. It would continue to pay RML the same amount, although they might seek to renegotiate the amount in the next contract. I consider that the notice was valid.

11. On the question of who is the client, Mr Robertson contended that as RML acted as a principal they were the client. Before RML took over RCaM's supervisory role on 1 March 2001, by which time contract (c) was already in force, RML's role was only that of introducer. The lower level contracts name the client as NPI (or AMP in contracts (b) and (c)) as the "Client," defined as "the person, firm or company requiring [RML's] services." Mr Renshaw was working at NPI's premises managing a team dealing with their computer. His services were performed, in the words of Regulation 6(1)(a), for the purpose of NPI's business. It is therefore unarguable that the client can be anyone other than NPI (or AMP). While during the one month's duration of contract (d), RML had a far greater role in managing the agents introducing contractors to NPI (or AMP) the reality was that there was an oral continuation of the contracts naming NPI (or AMP) as the client and Mr Renshaw

continued to work on their premises. In my view it is clear that throughout NPI (or AMP) was the client referred to in the legislation.

12. On the third point, Mrs Gibb gave an informal ruling that IR35 applied after receiving the following information: the contracts between RML and the Appellant and Mr Renshaw's "explanation of contract terms." Although a return had been made on the basis that IR35 did not apply she was willing to give an informal opinion as to whether it applied to assist the making of future returns. Before making the decision appealed against she had in addition some further explanations by Mr Renshaw, written answers from Mr Clark and correspondence with Mr Robinson. Mr Robertson cross-examined her at length on the effect of the Inland Revenue manual which states:

> "The officer dealing with the case should establish all the facts necessary to form an opinion of the status. This fact finding exercise is likely to take a variety of forms and may include field visits, interview(s), and examination of documents and contracts."

Mr Robertson interpreted this as requiring the Revenue to obtain all the facts themselves. It seems to me that his contention is based on a misunderstanding of the law. If the taxpayer wants an opinion it is up to the taxpayer to provide all the information so that the Revenue can form an opinion. In the words of Bingham LJ in *R v IRC ex p. MFK Underwriting Agencies Ltd* [1989] STC 879, 892f, he must "put all his cards face upwards on the table." If Mrs Gibb did not have enough information to form an opinion she would merely have said that. She was given enough information that, in her view, she could give an opinion, and she was willing to receive more information. In doing so she was acting absolutely correctly. The situation is that the taxpayer knows everything, and the Revenue knows nothing, of the facts. The manual envisages that the Revenue will help by interviewing people but that is where the taxpayer requests the interviews. It is not for the Revenue to go looking for facts that are in the taxpayer's knowledge, particularly so in this case when Mr Renshaw declined to attend an interview (as he is perfectly entitled to do). Any other system would be unworkable.

13. Mr Robertson's point on the delay is really a continuation of his point about the Revenue being obliged to search for information. He says that because the Revenue did not approach RML or NPI in 2001 the information is no longer available because NPI's and AMP's UK operations were demerged and are now administered by HHG plc. It follows from my decision on who has the responsibility to obtain evidence that there is nothing in this point. If the Appellant wanted evidence it could have obtained it at the time.

Reasons for my decision on whether IR35 applies

14. The IR35 legislation requires one to establish the terms of a hypothetical contract between Mr Renshaw and NPI. Mr Robertson made detailed suggestions as to what the hypothetical contract would contain. Mr Renshaw controls the Appellant and, as is to be expected, there are no express terms setting out their relationship. Treating Mr Renshaw as being party to the Appellant's contracts is therefore straightforward. The lower level contract expressly incorporates the terms of the upper level contract (so far as applicable) and so there is limited scope for conflict between them, and it is

relatively straightforward to cut out RML. Doing this results in the following terms for the hypothetical contract between Mr Renshaw and NPI:

(1) A series of three six months' contracts and a final one month contract.

(2) Description of the work as team leader, or project management/leader in charge of managing a team, but with no stated assignment.

(3) Working at NPI's office in Cardiff.

(4) Reporting to a named supervising manager.

(5) Working on continuing computer support and maintenance rather than on a specific assignment with a finite life.

(6) Obliged to obey any lawful instructions of NPI.

(7) Paid a daily rate for days worked (in practice applied to half a day).

(8) Working at least 7 hours per day but may be required to work longer to ensure the completion of an agreed task.

(9) Paid against time sheets or work sheets monthly within seven days (the time limit in the lower level contract).

(10) Terminable by NPI on four weeks' notice after the first six weeks of each contract, and immediately during the six weeks. Although I have accepted that this was included at the insistence of RML who are not a party to the notional contract, I consider that it should be included in the notional contact as NPI had conceded it and commercially it is of benefit to Mr Renshaw. Since the lower level contracts provide for immediate termination if the client (NPI) does not require the services, the upper level contract must take priority because if NPI no longer required the services of the Appellant it would have to give RML the contractual notice in the upper level contract.

(11) Not containing any of the usual features of contracts with employees listed by Mr Clark (see paragraph 4(5)(c)).

15. A number of different tests have been developed by the courts to determine whether an employment relationship exists. I list below those relied upon by the parties and I shall briefly set out the contentions of the parties and my findings on how each of them applies to the hypothetical contract:

Mutuality of obligation. Mr Robertson contends that there was no obligation on the parties to renew the contracts at the end of each six months' term, which is common ground. Mr Faulkner contended that there was full mutuality here. It does not seem to me to be relevant that there was no obligation to enter into another contract on termination of each one. This factor may be relevant to determine whether someone is employed under a single contract where there is an umbrella contract but there are breaks in work when the employer is free not to offer work and not to pay, as in *Carmichael v National Power* [1999] 1 WLR 2042. In this case mutuality is satisfied by NPI's obligation to pay a rate for a working day throughout each of the upper level contracts subject to their being able to terminate it on four weeks' notice after the first

six weeks of each contract. The reality was that there was plenty of work requiring Mr Renshaw's continuing services in managing the team supporting and maintaining the computer system, and this factor points towards an employment relationship.

Personal service and right of substitution. Mr Robertson contends that there was a right of substitution in the lower level contact which should be treated as incorporated into the hypothetical contract. Mr Faulkner said that this fell short of being a right. Mr Renshaw was the only employee of the Appellant and is the named consultant in both the lower and the upper level contracts. Any change would require (a) the Appellant taking on another employee, (b) obtaining RML's consent (not to be unreasonably withheld) as envisaged by the lower level contract, and (c) renegotiation of the upper level contract. I do not consider that I should imply that the lower level contract term be included in the hypothetical contract because RML did not agree such a term with NPI, although it meant that the two contracts were different, and so there is no evidence that NPI would have agreed if the question had been put to them. More importantly, however, even if the same provision had been in the hypothetical contract it would not have amounted to a *right* of substitution; it was no more than a possibility envisaged by the contract to which NPI might or might not have agreed, although their consent was not to be unreasonably withheld, and if the Appellant had taken on another employee. The reality was that only Mr Renshaw would do the work. I have accepted Mr Summers' evidence was that even if the Appellant had proposed a substitute, RML would have tried to bring in its own substitute. Mr Robertson also made the point that the contracts did not provide for holidays but in practice these were taken and some of Mr Renshaw's work had to wait for his return, so this cannot be used as an argument in support of substitution. This factor points to an employment relationship.

Control. Mr Robertson contended that control could cover what, where, when and how the work was done. He contended that NPI merely set the objectives; the nature of he work required most of it to be done in Cardiff; there was no control over the days worked, or how the work was done. Mr Faulkner drew attention to the control clause in the upper level contract. The upper level contract provided that Mr Renshaw must obey any lawful instructions given by NPI and work a seven hour day at NPI's office in Cardiff. Mr Renshaw was left to arrange how his and his team's work would be done but he reported to Mr Clark fortnightly and Mr Clark was kept informed about serious computer problems. In this respect Mr Renshaw was similar to a senior employee who was not told how to do his work but made regular reports of the state of the work. Clearly some control over Mr Renshaw was necessary as he was in charge of a team of NPI's employees.

In business on own account. Mr Robertson contended that the Appellant was certainly carrying on business and had other letting activities. Mr Faulkner said that the Appellant's other activities would not be relevant to the hypothetical contract. I agree. Mr Renshaw did not do other work at the same time. His only work from 1997 to September 2001 was for NPI. This factor points to an employment relationship.

Business risk. Mr Robertson pointed to the need to renegotiate the rate of payment in each six monthly contract, Mr Renshaw might have been required to work additional hours without extra payment, there was a risk attached to 7 days credit, he took risks as a director of the Appellant, the contract might have been terminated, and he took out his own insurance. Mr Faulkner contended that these were minor risks. In my view as he could not earn more by working longer hours because the Appellant was effectively paid a daily rate, this is more like an employment relationship. The other factors are unusual for an employee (although an employee paid in arrears takes some risk of non-payment) and point towards self-employment.

Provision of equipment. This is not a factor that is relevant to this type of work as he was working on NPI's mainframe computer. However, he provided his own laptop and mobile phone, which is more indicative of self-employment.

Length and number of engagements, and exclusivity. Mr Faulkner contends that the contracts in question are continuous and follow other contracts between the same parties starting in 1997. Mr Robertson contends that lengthy engagements are neutral as long relationships are regularly found in self-employment. I accept that there are genuinely a series of separate contracts with no obligation to renew them. In this case, however, no work was done for other clients and the work does not consist of a series of finite assignments. This factor points towards an employment relationship under a series of separate contracts.

Payment terms. Mr Robertson contended that the rate of remuneration was higher than for an employee. Although there is no evidence of what an employee would have earned for the same work and one would need to know the cost to the employer of the fringe benefits that an employee would receive, I can accept that NPI paid more under the actual contract that it would have paid an employee because it had the flexibility of taking on the Appellant on a six-month basis as opposed to taking on a permanent employee. But I do not think that helps to categorise the hypothetical contract. Mr Renshaw was paid a daily rate when working and not paid for holidays and sickness which is indicative of self-employment. On the other hand, the daily rate was more similar to an employee in that he could not earn more by working longer hours, which a self-employed person would normally be able to do.

Provision of benefits. He did not receive any of the fringe benefits listed by Mr Clark. This is indicative of self-employment.

Rights of termination. I have explained above why I consider that the upper level contract notice period should apply to the hypothetical contract, which is accordingly terminable on four weeks notice after the first six weeks of each contract. This is a slight pointer towards an employment relationship because termination on notice is less usual in self-employment.

Intention of the parties. It is not possible for the parties to have any intention over a hypothetical contract. However, the actual contracts were necessarily not employment contracts.

Part and parcel of the orgainsation. Mr Robertson contended that working with NPI's staff was dictated by the nature of the work and so this factor was neutral. Mr Faulkner contended that Mr Renshaw was fully integrated in the NPI organisation working with a team and in reporting to a manager. It seems to me that Mr Renshaw was very much part and parcel of NPI's organisation being the in-house person in charge of a team of people, not only in carrying out the work but being involved with salary reviews and poor performance of members of the team, although not with their career development more generally. He was working on a continuous process of computer support and maintenance rather than being engaged for a particular assignment. The six monthly contracts did not coincide with any particular assignment. This factor is a strong pointer towards an employment relationship. The work was identical to that of an employee; as Mr Clark put it: "The roles themselves were essentially the same, requiring the same skills and experience and focused on the same objectives and deliverables." He was eventually replaced by an employee.

16. Standing back and asking myself would Mr Renshaw be an employee under such a hypothetical contract, the factors that I consider are important in the present case are that he was the person in charge of a team in the sense of having management responsibility for the team, and in turn he was regularly reporting to a manager; that he was carrying out continuous support and maintenance work rather than a specific assignment; that he was paid a daily rate and could not therefore earn more by working longer hours; that he did not work for other clients; and that the arrangement would be terminable on four weeks' notice, all of which point towards an employment relationship. Other factors point away from employment, such as the absence of any usual employee fringe benefits (although in practice he had a normal holiday entitlement), and the method of payment against invoices and work sheets. Some other factors do not seem to me to be important to this question, such as the provision of equipment, and the lack of control over how he did his work. Weighing these all up I consider that clearly he would be an employee. In coming to this conclusion I am fully aware of the different risks involved. Mr Renshaw had absolutely no security at the end of each six months term and the reason that his contract was renewed was no doubt because he was good at his job. But in return he was paid more although against this he received no fringe benefits. To him, the difference in risk of not being able to renew the contract was no doubt very important and made him completely unlike an employee. But IR35 does not seem to pay attention to this as it starts from the actual contractual position and asks one to assume that it is replaced by a hypothetical contract. One therefore looks at each separate six-month contract separately. But the fact that there was actually a continuous series of six monthly contracts unrelated to any particular assignment merely makes the case for looking at this as an employment relationship stronger.

Concluding remarks

17. I said earlier that I would make some final comments about the preparation of IR35 cases. As Sir Donald Rattee said in *Future-on-Line Limited v Foulds* [2004] EWHC 2597 (Ch) at [25]: "In my view it is necessary to take account not only of the terms of the actual contractual arrangements between the appellant and [the other parties], but of all the other circumstances in which [the consultant] performed his services for the purposes of [the client's] business in order to test whether, had those

circumstances been different only to the extent that the services were provided pursuant to a contract directly between [the consultant] and [the client], [the consultant] could properly be regarded as employed by [the client]." I found myself extremely short of real evidence particularly about the other circumstances in which Mr Renshaw performed his services. Mr Renshaw's witness statement devotes a mere nine lines to "nature of services." The rest of the witness statement is really argument or a description of the contractual position. When, having read all the papers, I started hearing the case all I had about the nature of the work were the two statements which Mrs Gibb had. After Mr Renshaw's evidence in chief I asked if he would describe a typical day as I still felt that I did not have a proper picture of what the case was about. While I appreciate all the work that went into the preparation of the case what would have helped me much more than a survey of employment law would have been a detailed description of the type of work that Mr Renshaw performed throughout the various contracts. By the end of his evidence I had a good idea about this but this type of basic factual evidence should have been available also to the Revenue before the case started. I was even more hampered by the lack of any evidence from NPI, which seems to be a recurring problem with IR35 cases. The client's interests are not the same as the Appellant's and in examining the terms of a hypothetical contract it is necessary to have oral evidence from both parties to such a contract in order to obtain a clear picture. This was particularly the case here where Mr Renshaw had never seen the upper level contracts and the only evidence I originally had from RML was from Mr Summers, who only joined RML in 2002, and the only evidence from the NPI side was Mr Clark's witness statement of less than one and a half pages. What was required was oral evidence to put some flesh on the upper level contract. That would be necessary in any appeal but here there were suggestions that NPI were using an old form of contract that did not reflect the true position and therefore I was being asked to pay attention to an upper level contract dated 15 September 2002 on the assumption that there was an earlier version that could not be found. The Revenue were under the impression that Mr Clark would be called as a witness; the tribunal directed on 14 September 2004 that if he had not consented to give oral evidence within 30 days of the direction the Appellant would make a request for a witness summons. It was also unfortunate that Mr Summers changed a vital date in his witness statement at the start of his evidence which meant that I would have heard no oral evidence from either party to the upper level contract. I gave the Appellant the opportunity of asking an adjournment. Having Mrs Quinn's evidence by telephone conference without any witness statement was very much a second best. I should like to say that I found Mr Faulkner's skeleton extremely helpful. It was clear, succinct and fully cross-referenced to the documents, and his use of different colour paper for different types of contract was most useful. He was faced at the end of the first day with the difficulty that Mr Summers had explained for the first time the relevance of the 15 September 2002 contract that quite reasonably he had treated as irrelevant. The procedural rules are designed to avoid any ambush and they did not work on this occasion.

18. Accordingly I dismiss the appeal.

JOHN F. AVERY JONES

SPECIAL COMMISSIONER
RELEASE DATE: 17 January 2005

SC 3125/03

Authorities referred to in skeletons and not referred to in the decision:
R v IRC ex p. Professional Contractors Group Ltd 74 TC 393
Express & Echo Publications v Tanton [1999] IRLR 367
FS Consulting Ltd v McCaul [2002] STC (SCD) 138
Future on Line v Faulds [2004] EWHC 2597
Hall v Lorimer 66 TC 349
Market Investigations Ltd v Minister of Social Security [1969] 2 QB 173
Massey v Crown Life Insurance [1978] 1 WLR 676
McManus v Griffiths 70 TC 218
Morren v Swinton and Pendlebury BC [1965] 1 WLR 576
Mrs MacFarlane and Mrs Skivington v Glasgow CC EAT/1277/99
Nethermere (St Neots) Ltd v Gardiner [1984] ICR 612
Ready Mixed Concrete (South East) Ltd v Minister of Pensions and National Insurance [1968] 2 QB 497
Secretary of State for Employment v McMeechan [1997] IRLR 353
Synaptek Ltd v Young 75 TC 51
Usetech v Young [2004] STC 1671
Global Plant Ltd v Secretary of State for Social Security [1971] 1QB 139
WHPT Housing Association v Secretary of State for Social Services [1981] ICR 737
Stevedoring & Haulage Services Ltd v Fuller [2001]EWCA Civ 651
Montgomery v Johnson Underwood [2001] IRLR 269
Propertycare Ltd v Gower [2003] EAT/547
Clark v Oxfordshire Health Authority [1997] EWCA 4792
Spring v Guardian Assurance plc [1995] AC 296
Ansell Computer Services Ltd v Richardson [2004] STC (SCD) 472
Narich Pty Ltd v Commissioner of Payroll Tax [1984] ICR 286
Byrne Brothers (Formwork) Ltd v Baird [2002] IRLR 96
Lime IT v IRC [2003] STC (SCD) 15
Horner v Hasted 67 TC 439
Tilbury Consulting Ltd v Griffiths [2004] STC (SCD) 1

NETHERLANE LTD v SIMON YORK (SpC457) (2005)

Sp Comm (Dr John F Avery Jones) 17/1/2005

TAX - EMPLOYMENT

CONTRACT OF EMPLOYMENT : EMPLOYEES : EMPLOYMENT STATUS : INTERMEDIARIES : NATIONAL INSURANCE CONTRIBUTIONS : SOCIAL SECURITY : IT CONSULTANT PROVIDING SERVICES THROUGH INTERMEDIARY COMPANY : IR35 TAX AVOIDANCE PROVISIONS : IR35 : FREELANCE : COMPUTERS : SOCIAL SECURITY CONTRIBUTIONS (INTERMEDIARIES) REGULATIONS 2000 : reg.3 SOCIAL SECURITY CONTRIBUTIONS (DECISIONS AND APPEALS) REGULATIONS 1999 : reg.6 SOCIAL SECURITY CONTRIBUTIONS (DECISIONS AND APPEALS) REGULATIONS 1999

A hypothetical contract under which a freelance IT consultant supported and maintained a company's computer system amounted to an employment contract for the purposes of assessing National Insurance Contributions under the Social Security Contributions (Intermediaries) Regulations 2000.

The appellant company (N) appealed against a decision that arrangements between an individual (R) and a company (P) for the performance of services were such that the Social Security Contributions (Intermediaries) Regulations 2000 applied to R's National Insurance contributions.

R was a freelance IT consultant who had set up N as a vehicle for finding work through a recruitment agency (M).

R had been offered a series of 26 week contracts by M which required N to provide IT services at the premises of its client, P.

Contracts had been exchanged between N and M, and between M and P.

The Revenue had sent N and R notice that the Regulations applied and that R was to be regarded for the purposes of his and N's National Insurance contributions as an employee of P.

N argued that (1) the notice was invalid as it had not been sent to P; (2) that the notice was invalid in that it named P as the client rather than M, which had acted as principal; (3) it was the Inland Revenue's duty under the Inland Revenue Manual to obtain all the evidence before making a decision on status; (4) the Regulations did not apply as any hypothetical contract between R and P did not involve any of the usual features of contracts with employees.

HELD: (1) The decision was made in respect of N and R because it affected their national insurance contributions.

Although P was named so as to make clear to what relationship the notice applied, the decision had not been made in respect of P and so there was no purpose in requiring it to be given notice.

The reference in the Social Security Contributions (Decisions and Appeals) Regulations 1999 reg.3 to persons named had to be construed as meaning persons affected by the notice who were named in it.

(2) The contracts named P as the client.

R was working at P's premises managing a team working on P's computers.

His services were performed, in the words of reg.6, for the purposes of P's business.

It was therefore unarguable that the client was anyone other than P.

(3) If a taxpayer wanted an opinion it was up to the taxpayer to provide all the information so that the Inland Revenue could form an opinion, R v Board of Inland Revenue & anor, ex parte MFK Underwriting Agencies Ltd & ors (1989) BTC 561 applied.

The manual envisaged that the Inland Revenue would help by interviewing people, but that was where the taxpayer requested the interviews.

It was not for the Inland Revenue to go looking for facts that were within the taxpayer's knowledge.

(4) Various factors pointed to the conclusion that R was a notional employee of P for the purposes of the Regulations: R had management responsibility for a team of workers; he regularly reported to a manager; he carried out continuous support and maintenance work rather than a specific assignment;

he was paid a daily rate and could not earn more by working longer hours; he did not work for any other clients; and the arrangement was terminable on four weeks' notice.

(5) The court had found itself extremely short of real evidence, particularly about the circumstances in which R had performed his services, and had been hampered by a lack of evidence from P.

That seemed to be a recurring problem in IR35 cases, where in examining the terms of a hypothetical contract it was necessary to have oral evidence from both parties to such a contract in order to obtain a clear picture. Appeal dismissed.

Counsel: For the appellant: Non-counsel representative For the respondent: Non-counsel representative
LTL 15/7/2005 : (2005) STC (SCD) 305

Document No. AC0107778

[**Articles citing this case**]

Island Consultants Ltd v Revenue & Customs [2007] UKSPC SPC00618 (05 July 2007)

IR 35 – business and data analysis contractor working on a series of three-month contracts for a five-year computer project –whether would be an employee if engaged directly by the client – yes – appeal dismissed

THE SPECIAL COMMISSIONERS

ISLAND CONSULTANTS LIMITED Appellant

- and -

THE COMMISSIONERS FOR HER MAJESTY'S REVENUE AND CUSTOMS Respondents

Special Commissioner: DR JOHN F. AVERY JONES CBE

Sitting in public in London on 28 June 2007

David Smith LLB FTII, Accountax Consulting Limited, for the Appellant

Peter Death, HMRC Appeals Unit North West and Midlands, for the Respondents

DECISION

1. This is an appeal by Island Consultants Limited against a Notice of Decision dated 20 August 2004 for National Insurance Contributions in respect of the period 6 April 2000 to 5 April 2003 and Notices of Regulation 80 Determinations to PAYE dated 20 August 2004 in respect of the three tax years 2000-01 to 2002-03. It concerns what is popularly known as the IR35 legislation. The Appellant was represented by Mr David Smith, and the Revenue by Mr Peter Death.

2. The appeal concerns the work performed by Mr Ian Hough as director and shareholder of the Appellant which contracted with Spring Limited, an IT agency, which contracted with Severn Trent Systems Limited ("STS") (only for periods until October 2001, after which STS did not form part of the chain of contracts) which contracted with the ultimate client, Severn Trent Water Limited ("STW") in connection with a project for a new computerised billing system known as Target. The issue is whether if Mr Hough had contracted with STW he would have been an employee of STW. There is also an issue about whether STS or STW (as stated in the documents under appeal) is the client for the purposes of the legislation.

Facts

3. I heard evidence from Mr Hough, and the Revenue called as witnesses Mr Robert Carson, then project manager of the Target project of STW, and Mr Anthony Sargent, then the person responsible for engaging contractors for capital projects of STW. I find the following facts:

(1) STW, a regulated water company, had a project changing their billing system, the new one called Target. This was a five year project running from the year 2000 involving 3m customers and annual billing of over £100m. It was therefore a large and sensitive project involving data conversion to the new system, replacement of the interfaces to a standard software system (CIS-OV), operational performance of the system, the impact on business processes, system testing and support, training of 1,200 staff in its use, business process changes, and communications to all key parties. Mr Carson managed the entire project. It required management of a mixture of internal staff who would be seconded to work on the project, people from an external software company, and external consultants. The Appellant was one of the external consultants who provided expertise that was not available in-house. STS was a fellow subsidiary of STW that provided software to STW and engaged external IT consultants for STW.

(2) Mr Carson would identify the need for an external contractor, and would prepare a description setting out the skills and experience required. This would be sent to the agencies that were on STW's (or STS's) preferred list of suppliers, which included

Spring, who would put forward candidates who would be interviewed by Mr Carson. STW preferred to have a staff level to cover their base requirements and would use external contractors for peaks of demand for staff even where these lasted for several years, as with the Target project.

(3) The chosen contractor, here the Appellant, would be engaged by contract between STW (or before October 2001, STS) and Spring on a standard form. A sample contract dated 4 April 2001 between STW and Spring relating to the period 9 April 2001 to 5 October 2001 provided for Spring to provide consultancy services which would be provided by its employee ("the Executive"). In fact, the intention of the parties was that Spring would provide the services of other contractors like the Appellant and not its employees. (If STW took over engaging contractors in October 2001 one would expect the party to this contract to be STS but it is STW; in the assignment summary of the Spring-Appellant contract (see paragraph 3(6) below) for the same period names STS as the client. I cannot explain this discrepancy and it is possible that the latter is wrong and the change in fact took place in April 2001, which would tie in with the statement in paragraph 3(7) below, in which case other references to STW taking over in October 2001 should be to April 2001, but the date is not material to this decision.) A later standard form contract applying from 1 January 2003 provides for Spring to supply IT contractor services through a contractor, which gives effect to the intentions of the parties. The standard form contract includes the following provisions:

(a) On control:

"[Spring's] method and timing of work is its own but [Spring] shall and shall procure that the Executive shall:

(i) comply with all reasonable requests of [STW] for information and statements as to progress as the case may require

(ii) co-operate with any of [STW's] personnel concerned with or other company appointed in connection with the project and

(iii) comply with all health and safety requirements and/or policies of [STW].

(b) Neither Spring nor the Executive were entitled to benefits such as holiday entitlement or sick pay.

(c) Either party could terminate the contract on 4 weeks' notice or immediately for cause. In addition Spring may terminate the contract forthwith without notice if STW requested Mr Hough to be removed.

(d) The contract stated that except as expressly provided in the agreement STW had no obligation to use or continue to use the services of Spring.

(4) There was no copy of the Appendix to that contract setting out the details of the particular engagement but a later one relating to 2 January 2004 to 31 March 2004, which I find is likely to have been in similar form to earlier ones, specifies Mr Hough's name; the project's name and phase; Mr Carson is named as project manager; the period of employment is stated; Spring is named as the consultant company; the daily rate is specified; a special condition states that incidental expenses are paid only when specifically authorised by STW; reasons for recruitment are given ("as internal support is not currently available, STW require an external consultant to work on Target Phase 3"); and the previous purchase orders for this contractor are set out.

(5) There were a continuous succession of contracts for three-month periods (or in two cases six-month periods), comprising a total of eleven or twelve separate

contracts (there were copies of 10 contracts up to 31 December 2002 in the documents and a reference to the existence of subsequent contracts for periods up to 31 December 2003). Contracts were often renewed at the last minute by Mr Carson approaching Mr Hough. Mr Hough hoped that the contracts would be renewed but did not necessarily expect this. Mr Carson would have been upset if the Appellant had not renewed the contracts and would have applied moral pressure to encourage it to do so, while recognising that they had no legal liability to do so. Outside the period under appeal Mr Hough worked for STW from February 1998 at least until 2006.

(6) Spring would in turn contract with the Appellant on the following terms:

(a) The contract names the Client: STS until the contract ending 27 October 2001, thereafter STW.

(b) Mr Hough is named as the individual who will provide the services. It states that the Appellant may propose a replacement for the individual but any such replacement shall only take place provided the Client [STW (or as the case may be STS)] is satisfied that the proposed replacement has the necessary qualifications, skills and experience and is suitable to perform services for the Client.

(c) The services are described as "Business Analyst/Data Analyst role."

(d) Time sheets to be provided within 10 days of the end of a month with payment due within the month.

(e) Spring has the right to terminate on 14 days notice for a contract between 8 and 26 weeks duration.

(f) The following is included under the heading Special Conditions:

"The Services Period is to be agreed with the Manager. The Contractor [the Appellant] will provide services at Aqua House Central Birmingham and other Client Midland sites if required. The Contractor will provide services for 4 days per week (32 hours per week) but his manager can request he works a fifth day if the project dictates."

(7) For the period up to October 2001 while STS was in the chain of contracts there was an agreement between STW and STS for STW to pay for STS's work on an arm's length basis as required by STW's water industry regulator. I did not see any copy of this. It was the regulator's insistence of a more formal relationship between the two companies from April 2001 that led to STW taking over engagement of contractors in place of STS in October 2001 (or it may be April 2001, see paragraph 3(3) above).

(8) Finally in the chain of contracts, there was no written contract between the Appellant and Mr Hough.

(9) Mr Hough is an expert in business and data analysis using information technology. Business analysis involves analysing the client's business processes including testing technology from the business perspective by talking to users and identifying and documenting their requirements; data analysis involves analysing the client's data to gain insight into the data used in the business and the data structures required to support the business.

(10) Mr Hough's areas of work on the project at the relevant time were in phase 1 of the project the design of the conversion of the data, including analysis of the data to be converted, definition of the software requirement, and liaison with the software provider and testing of the conversion software. He wrote the terms of reference and

the report into the way audit data would be moved to the new system, and implemented the audit. In phase 2 he was responsible for the design of the conversion of data requiring the merger of data from two old billing systems. He was then responsible for the planning and implementation of the conversion.

(11) In spite of the contractual provision for a four-day week, Mr Hough generally worked five days a week, occasionally six and even seven days during conversion weekends. His hours varied from 5 to 12 hours a day. He worked at the project location except that sometimes he would write a report at home by agreement with Mr Carson. Conversion work had to be done outside normal hours so as not to interfere with normal computer use, usually from 8pm to 10pm and sometimes at weekends. Mr Hough would coordinate this work from his home.

(12) Mr Hough was free to decide the times he attended, the number of hours worked in a day, when he took time off, and when he took breaks during the day. As a matter of courtesy he would agree absences with Mr Carson. Such absences included holidays of normally two weeks at a time taken at less busy periods to fit in with the project.

(13) Mr Hough was expected to correct errors at his own expense. Mr Carson was not aware of this occurring. Mr Hough said that it did occur during conversion when sometimes files would fail to convert properly.

(14) Mr Hough did not manage other people in the STW organisation.

(15) STW provided Mr Hough with a desk at the premises and a laptop for mobile working from other sites, including a dial-in from his home. On three or four occasions he used the Appellant's computer and scanner for this purpose.

(16) Mr Hough had an identity badge showing him as "contractor." He was able to use the canteen and park his car in the STW multi-storey car park. Unlike STW's employees the Appellant did not receive any increase in the rate of payment between April 2002 and January 2006. The Appellant did not receive any holiday pay, sick pay or pension in respect of Mr Hough. Unlike employees Mr Hough did not have a formal annual appraisal. He was in regular contact with Mr Carson. They worked in the same building and would have a formal meeting once a week together with other informal contacts.

(17) There were targets for the number of customers converted by certain times and Mr Hough would report to Mr Carson about progress. Mr Carson did not have IT expertise but could judge the Appellant's work by the progress compared with the targets and by whether the new billing system produced correct bills when tested.

(18) The Appellant billed Spring monthly accompanied by a time sheet on Spring's form specifying the number of days (or half-days) worked by Mr Hough. For three months' invoices the Appellant's VAT registration number was not included on the invoice and STW did not pay the VAT. It took about six months to resolve the problem and a further month to receive interest on the late payment.

(19) Mr Hough personally performed all the duties during the period under appeal. In February 2003 he met Mr Carson one evening and both signed a document headed "confirmation of arrangements between contractor and client." This is a form presumably provided by the Appellant's then advisers containing various alternatives for deleting those that do not apply. The document includes:

"5. The contractor [the Appellant] has the right/ ~~does not have the right~~ to send a substitute to carry our the services specified in the contract in the place of Ian Hough [Mr Hough's name is added in manuscript]

6. The contractor has the right/ ~~does not have the right~~ to subcontract the services to another party.

…

8. If the contractor has the right to subcontract the services and/or to send a substitute, the client [STW] agrees that he will accept that substitute or subcontractor if the latter has the skills to carry out the services specified in the contract…".

In 2005 Mr Carson signed a statement presumably at the Revenue's request, containing the following:

"If Mr Hough were unable to fulfil personally the contractual obligations of [the Appellant] [STW] would be prepared to consider a suitable replacement worker who was recommended and provided by [the Appellant]. This would be subject to [STW] being satisfied that the replacement had the necessary skills and experience to complete the contract."

(20) The 2005 document sets out the true understanding of Mr Carson, and the 2003 document does not. The 2005 document is also in accordance with the agreement between STW (or STS) and Spring. It also represents the obvious commercial reality that STW has an important and sensitive project and they contracted with the Appellant for Mr Hough's services on the basis of his special skills. Another person would find it difficult to pick up the project in the middle and it might take a couple of months to do so unless Mr Hough were directing him.

(21) Mr Hough did not work for any other clients during the period under appeal.

Legislation

4. Regulation 6(1) of the Social Security Contributions (Intermediaries) Regulations 2000 provides:

"These Regulations apply where—

(a) an individual ("the worker") personally performs, or is under an obligation personally to perform, services for the purposes of a business carried on by another person ("the client"),

(b) the performance of those services by the worker is carried out, not under a contract directly between the client and the worker, but under arrangements involving an intermediary, and

(c) the circumstances are such that, had the arrangements taken the form of a contract between the worker and the client, the worker would be regarded for the purposes of Parts I to V of the Contributions and Benefits Act [the Social Security Contributions and Benefits Act 1992] as employed in employed earner's employment by the client."

"Intermediary" is defined in Regulation 5 and it is common ground that the Appellant is an intermediary for this purpose.

5. Similar provisions applying for PAYE purposes are contained in Schedule 12 to the Finance Act 2000:

"1—(1) This Schedule applies where—

(a) an individual ("the worker") personally performs, or is under an obligation personally to perform, services for the purposes of a business carried on by another person ("the client"),

(b) the services are provided not under a contract directly between the client and the worker but under arrangements involving a third party ("the intermediary"), and

(c) the circumstances are such that, if the services were provided under a contract directly between the client and the worker, the worker would be regarded for income tax purposes as an employee of the client."

Contentions of the parties

6. Mr Smith for the Appellant contends:

(1) The notices were bad for the period up to October 2001 in not naming STS as the client since the contract was with STS.

(2) The hypothetical contract between Mr Hough and STW would lack the irreducible minimum requirement for an employment contract as set out by MacKenna J in *Ready Mixed Concrete (South East) v Minister of Pensions and National Insurance* [1968] 2 QB 497, 515 and approved by the House of Lords in *Carmichael v National Power plc* [1999] 4 All ER 897:

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

Here control and mutuality of obligations are absent.

(3) On control the contractual provision quoted in paragraph 3(3)(a) above shows a lack of contractual control. In practice Mr Hough was not under STW's (or STS's) control in relation to where, when and how he worked.

(4) Mutuality of obligations must exist throughout the entire period under appeal, relying on *Synaptek Ltd v Young* [2003] STC 543 at [25] where counsel for the Inspector "accepted that if, taking the period of the notional contract as a whole, EDS was under no obligation to provide work, the necessary element of mutuality was indeed lacking for that period" Mutuality of obligation includes continuing the promises to provide and pay for work throughout the contract. The STW-Spring contract expressly stated that there was no obligation to continue to use Spring.

(5) The Appellant had a right in its 2003 agreement with Mr Carson to send a substitute for Mr Hough.

(6) The Appellant had business risk as demonstrated by the problem with obtaining payment of VAT. Mr Hough had to put right defects in his own time.

(7) The terms were not similar to other employees. Mr Hough was identified on his badge as a contractor. There was no intention that an employment relationship existed. While he did not provide any equipment his office at home had the normal equipment found for someone doing some work at home.

7. Mr Death for the Revenue contends:

(1) The notices correctly showed STW as the client as it was STW's project. STS was a supplier of some of the components for the project.

(2) The control test is of little relevance to an expert such as Mr Hough; see *Morren v Swinton and Pendlebury Borough Council* [1965] 2 All ER 349, 351 per Lord Parker CJ with whom the others concurred:

The cases have over and over again stressed the importance of the factor of control, but that it is not the determining test is quite clear. In *Cassidy v Minister of Health*, Somervell LJ referred to this matter, and instanced, as did Denning LJ in the later case of *Stevenson, Jordan & Harrison v McDonald & Evans*, that clearly superintendence and control cannot be the decisive test when one is dealing with a professional man, or a man of some particular skill and experience. Instances of that have been given in the form of the master of a ship, an engine driver, a professional architect or, as in this case, a consulting engineer. In such cases there can be no question of the employer telling him how to do work; therefore, the absence of control and direction in that sense can be of little, if any, use as a test."

(3) There was sufficient control over where and when Mr Hough worked for him to be an employee under the notional contracts. He was expected to attend during normal office hours and agree absence in advance.

(4) In *Synaptek* the statement that there had to be mutuality of obligations throughout the period of separate contracts was a concession by the Revenue which is not repeated here. It is sufficient that within each separate contract there was an obligation to provide work and payment, see *Cornwall County Council v Prater* [2006] EWCA Civ 102 in which a teacher was engaged to teach a particular pupil at the pupil's home under a succession of separate contracts relating to different pupils. Longmore LJ said:

"[43]…There was a mutuality of obligation in each engagement namely that the County Council would pay Ms Prater for the work which she, in turn, agreed to do by way of giving tuition to the pupil for whom the Council wanted her to provide tuition. That to my mind is sufficient 'mutuality of obligation' to render the contract a contract of employment if other appropriate indications of such an employment contract are present."

Here there was clearly mutuality of obligation within each contract.

(5) So far as the other factors are concerned, the financial risk demonstrated by the late payment of VAT was a minor one. In general the risk of non-payment was no greater than that of STW's employees. While payment by a daily rate is more common for self-employment, here the factor is more neutral as the client sets the rate. Mr Hough was paid a daily rate normally for a five-day week like an employee. He could not increase his remuneration by working harder; by working more than the contractual four-day week he was similar to an employee working paid overtime. He had no overheads and stood no risk of making a loss. Provision of equipment was a neutral factor in a case like this. While a series of short engagements may point to self-employment, here Mr Hough is not similar to a businessman offering his services in the market. A notice period is more consistent with employment; self-employment normally ends when the work is completed. The lack of employee-type benefits is not surprising in a contract between companies. Mr Hough was integrated into the STW organisation, although shown as a contractor. Mutual intention cannot apply to a hypothetical contract but the actual intention was for self-employment. Weighing up all these factors points towards employment.

Reasons for the decision

8. Mr Smith put forward a preliminary argument that the notices were bad in naming STW as the client throughout, rather than naming STS until October 2001. Mr Death contended that STS was merely another link in the chain to STW which was the real end-user since the Target project was in relation to STW's billing system and STS was merely the supplier of software and contractors to STW on an arm's length basis. I agree with Mr Death's analysis. For the legislation to apply the services must be performed "for the purposes of a business carried on by another person ('the client')." Here in the period before October 2001 the services were performed directly for STS which is named as the client in the Spring-Appellant contract but, as the Appellant knew, were performed ultimately for the benefit of STW under contractual arrangements between STW and STS. In my view it is correct for STW to be named as the client because the services were for the purposes of STW's business being an STW project. In my view the notices were valid.

9. Having found the facts of the actual relationship between the parties I have to apply the statutory hypothesis that Mr Hough worked for STW and ask whether he would be an employee. Collapsing the actual contractual arrangement leaves the following contract terms including how they were in fact operated:

   (1) A series of 3 (or in two cases 6) months contracts without any obligation on either party to continue, but which are in fact continued continuously for the three year period under appeal (and for periods before and after).

   (2) Services performed at STW's premises at Aqua House, Birmingham or other Midland sites of STW (or STS) if required. Mr Carson did agree to his doing some work from home.

   (3) Four days per week but Mr Carson can request that he works a fifth day if the project dictates. I understand "request" to be short of "require" but if the project did so dictate Mr Hough might find it morally difficult to refuse, at least if he wanted the contract to be renewed. If fact he always agreed.

   (4) Payment monthly within the following month on the basis of days worked (in practice measured in half days) on presentation of time sheets within 10 days of the end of the month.

   (5) Mr Hough was free to decide the times he attended, the number of hours worked in a day, when he took time off, and when he took breaks during the day. As a matter of courtesy he would agree absences with Mr Carson. Such absences included holidays of normally two weeks at a time taken at less busy periods to fit in with the project.

   (6) Mr Hough was required to perform the services himself but if he were unable to fulfil personally his contractual obligations STW (or STS) would be prepared to consider a suitable replacement worker who was recommended by Mr Hough. This would be subject to STW (or STS) being satisfied that the replacement had the necessary skills and experience to complete the contract. No proposal for a substitute was ever made.

   (7) Mr Hough would have to:

   (i) comply with all reasonable requests of STW for information and statements as to progress as the case may require

   (ii) co-operate with any of STW's personnel concerned with or other company appointed in connection with the project and

   (iii) comply with all health and safety requirements and/or policies of STW.

(8) No normal employee benefits such as holiday pay, sick pay or pension.

(9) STW (or STS) may terminate the contract on 4 weeks notice. Since the provision of the Spring-Appellant contract, under which Spring may terminate that contract immediately if STW requests Mr Hough to be removed, is not replicated in the STW-Spring contract it cannot form part of the hypothetical contract.

10. On whether such a contract contains the irreducible minimum for an employment contract, I find that so far as control is concerned, not much control is expected for an expert like Mr Hough as stated in the quotation above from Lord Parker's judgment in *Morren v Swinton and Pendlebury Borough Council*. There must still be some control and there was some control over where he worked; he could be asked to work at other Midland sites of STW (or STS), and working at home required Mr Carson's agreement. There was some control over when the work was performed were as performing conversion work on the computer outside hours of normal computer use. Mr Hough would have to comply with all reasonable requests of STW for information and statements as to progress, which is rather less than one would expect for an employee, and would have to cooperate with other personnel working on the project. There was something just short of contractual control over the number of days per week worked but if the project dictated that more than a four-day week was required Mr Hough did in fact agree to it. I consider that the totality of these amounted to sufficient control, though rather less than one would expect for a normal employee.

11. On mutuality of obligation, there was no obligation to renew the contract after each three (or six) period. This factor may be relevant to determine whether someone is employed during breaks in work, as in *Carmichael v National Power* [1999] 1 WLR 2042, where it was not in issue that they guides were employed while working. As in *Cornwall County Council v Prater* it is sufficient that within each contractual period there was an obligation on STW to provide work and pay the agreed rate; the contrary decision in *Synaptek* depends on a concession made by the Revenue in that case. There was such an obligation for 4 days work a week, or more days if worked at their request, subject to the possibility of STW terminating the contract on four weeks notice. The reality was that this was a five-year project and there was plenty of work requiring Mr Hough's continuing services. STW was obliged to and did provide and pay for work during each separate contract period.

12. So far as the right of substitution is concerned there was none. The most that STW agreed to was that they would consider a request. In practice this would require considerable scrutiny by STW. I think that the Appellant by asking Mr Carson to sign the 2003 "confirmation of arrangements between contractor and client" may have misled itself into thinking that there was a right of substitution in stronger terms than in the Spring-Appellant contract, and in spite of there being no such terms in the STW-(or STS)-Spring contract. Such a provision would not have made any commercial sense and Mr Carson signed the confirmation of arrangements trusting Mr Hough.

13. Accordingly I conclude that the hypothetical contract would have the necessary irreducible minimum to constitute an employment contract.

14. Although the argument at the hearing concentrated on the above factors, the parties' skeletons dealt with the need to stand back and look at the arrangements as a whole as in *Hall v Lorimer* (1994) 66 TC 349. The following factors have been identified in the authorities as relevant, and there is no need for me to cite authority for each well-known factor; my conclusions on each are as follows:

(1) In business on own account. Mr Hough could earn more by working more than four days a week but this depended on the project dictating it. In practice the project did normally dictate it and so he would effectively have a 5 day a week job in the hypothetical contract. He did not work for other clients or offer his services elsewhere

and could not increase his remuneration above the daily rate, which was set by STW. He had virtually no overheads and there was no possibility of making a loss.

(2) Payment terms. Payment within the following month after submitting time sheets within 10 days of the end of the month involves a longer period of risk than for normal employees.

(3) Financial risk. Within each contract the only risk was of non-payment during the period before payment but all employees take some risk of non-payment although with some statutory protection (which would be deemed to apply to the hypothetical contract if it is an employment contract). While defective work had to be put right in his own time, payment was calculated on days of varying length and any corrections were made within that flexibility. There was a delay in paying VAT on one occasion but this was caused by the Appellant not putting the VAT registration number on its invoices.

(4) Provision of equipment. This is not a factor that is relevant to this type of work as he was working on STW's mainframe computer and was provided with a laptop. On rare occasions (only three or four occasions in the three year period) he used the Appellant's computer and scanner while working at home.

(5) Length and number of engagements, and exclusivity. Here there was an expectation, but no legal obligation, that the contracts would be renewed. Both parties knew that this was a five-year project requiring Mr Hough's services as they were not available in-house. A series of short engagements is a slight pointer towards self-employment. Mr Hough did not work for anyone else in the period under appeal.

(6) Provision of benefits. He did not receive any of the fringe benefits received by normal employees. I assume that since he was satisfied with the rate of payment, including the fact that it was not increased during several years, it must have made up for the loss of benefits.

(7) Rights of termination. Termination on four weeks' notice is more usual for employment than self-employment.

(8) Intention of the parties. It is not possible for the parties to have any intention over a hypothetical contract. The actual contracts were necessarily not employment contracts.

(9) Part and parcel of the organisation. Mr Hough had a desk and computer terminal and had the same car-parking facilities and access to the canteen as normal employees, although his badge named him as a contractor (as he was). He was working on a particular project rather than as part of STW's organisation, although other employees were seconded to work on the project alone. He was no in charge of other staff.

15. Standing back and considering the position as a whole, the factors predominantly point towards employment, although a somewhat unusual one. The only factors pointing away from employment are the longer payment terms than normal for an employee, which is not important; and the intention of the parties, which is not directed to the hypothetical situation. Although the number of separate contracts would normally point away from employment, and there was a risk of the contracts not being renewed, while the project needed his services and he was satisfactorily performing his duties, this was not a real commercial risk, and it is inherent in IR35 that one must consider the contracts separately because one starts with the actual contracts.

16. Accordingly I conclude that Mr Hough would be an employee of STW under the hypothetical contract and dismiss the appeal.

17. By way of postscript I should like to thank the two STW witnesses for their witness statements and for attending when this as an additional burden which is of no benefit to them. I have commented in the past about there being either no or inadequate information from the client. In this case I had the fullest information which was most helpful to me.

JOHN F. AVERY JONES

SPECIAL COMMISSIONER

RELEASE DATE: 5 July 2007

SC 3213/06

Authorities referred to in skeletons and not referred to in the decision:

Bank voor Handel en Scheepvart v The Administrator of Hungarian Property [1954] 2 WLR 867

Market Investigations Ltd v Minister of Social Security [1968] 2 QB 173

Global Plant Ltd v Secretary of State for Health and Social Security [1971] 3 All ER 386

Massey v Crown Life Insurance [1978] 2 All ER 576

Nethermere (St Neots) Ltd v Gardiner [1984] IRLR 240

Barnet v Brabyn [1966] STC 716

McManus v Griffiths (1997) 70 TC 218

Express & Echo Publications Ltd v Tanton [1999] IRLR 367

Montgomery v Johnson Underwood [2001] EWCA Civ 318

Stuncroft v Havelock (2001) EAT/1017/00

Propertycare v Gower [2003] UKEAT/054703

Usetech Ltd v Young [2004] STC 1671

Tilbury consulting Ltd c Gittins [2004] STC (SCD) 72

FS Consulting Ltd v McCaul [2002] STC (SCD) 138

Lime IT Ltd v Justin [2003] STC (SCD) 15

Ansell Computer Services v Richardson [2004] STC (SCD) 472

Mal Scaffolding v HMRC [2006] STC (SCD) 253

Parade Park Hotel v HMRC [2007] UKSC SPC00599

Spc00656

INCOME TAX and NIC – IR 35 Legislation – If there had been a direct engagement would it have been an employment? In the circumstances No – appeal allowed

THE SPECIAL COMMISSIONERS **SC/3108/2006**

DATAGATE SERVICES LIMITED **Appellant**

– and –

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

Special Commissioner: ADRIAN SHIPWRIGHT

Sitting in public in London on 23 July 2007

John Antell, Counsel for the Appellant instructed by LawSpeed Limited

Michael Faulkner of Appeals Unit South, HM Revenue and Customs for the Respondents

DECISION

Introduction

1. This decision concerns:

a. An appeal against a determinations under Regulation 80 Income Tax (PAYE) Regulations 2003 against Datagate Services Limited ("Datagate") in the amount of:

i. £ 8,895.46 for 2001-02

ii. £9,539.76 for 2002-03

iii. £10, 339.16 for 2003-04

b. An appeal against a decision under section 8 Social Security Contributions (Transfer of Functions) Act made on 21 July 2005 that Datagate is liable to pay primary and secondary class one National Insurance contributions of £17,482.87 in respect of the period to 6 April 2001 to 5 April 2004.

2. The parties are agreed that if the "IR 35" provisions applied, the amount shown in the determinations and decision is correct. I am also told that the Special Commissioner's decision will be followed for the years ended 5 April 2005 and 2006.

The Issue

3. The Parties agreed that the point at issue is whether, had the arrangements taken the form of a contract between Mr Barnett and MBDA, Mr Barnett would have been regarded as an employee of MBDA.

4. The Parties also agreed that the position was the same in these circumstances for both income tax and national insurance.

The Law

The Legislation

5. The Law for income tax purposes is found in Chapter 8 Part 2 ITEPA (re-enacting Schedule 12 FA 2000). It provides so far as is relevant:

"48 Scope of this Chapter

(1) This Chapter has effect with respect to the provision of services through an intermediary. ….

49 Engagements to which this Chapter applies

(1) This Chapter applies where—

(*a*) an individual ("the worker") personally performs, or is under an obligation personally to perform, services for another person ("the client"),

(*b*) the services are provided not under a contract directly between the client and the worker but under arrangements involving a third party ("the intermediary"), and

I the circumstances are such that, if the services were provided under a contract directly between the client and the worker, the worker would be regarded for income tax purposes as an employee of the client.…

(4) The circumstances referred to in subsection (1)I include the terms on which the services are provided, having regard to the terms of the contracts forming part of the arrangements under which the services are provided.

(5) In this Chapter "engagement to which this Chapter applies" means any such provision of services as is mentioned in subsection (1). …

56 Application of Income Tax Acts in relation to deemed employment

(1) The Income Tax Acts (in particular, the PAYE provisions) apply in relation to the deemed employment payment as follows.

(2) They apply as if—

(*a*) the worker were employed by the intermediary, and

(*b*) the relevant engagements were undertaken by the worker in the course of performing the duties of that employment.

(3) The deemed employment payment is treated in particular—

(*a*) as taxable earnings from the employment for the purpose of securing that any deductions under Chapters 2 to 6 of Part 5 do not exceed the deemed employment payment; and

(*b*) as taxable earnings from the employment for the purposes of section 232.

..."

6. The Law for Social Security Contributions purposes is found in the Social Security Contributions (Intermediaries) Regulations 2000.

The Authorities

7. I was provided with copies of the following authorities which I have read and considered carefully:

Hall v Lorimer [1992] STC 599

Ansell Computer Services v Richardson [2004] STC (SCD) 472

WHPT Housing Association v SOSS [1981] ICR 737

The Evidence

8. An agreed bundle of documents was produced. No objection was taken to any of them and they were all admitted in evidence.

9. I heard oral evidence from:

Bret Barnett, the Appellant's director and shareholder of Datagate;

Simon Wycherley of MBDA, the relevant Team Leader;

Nicole Hartland, formerly an HR Manager at MBDA's Stevenage office.

10. Witness statements were provided for all three. A witness statement was also provided for Roger Bartlett. Unfortunately, he was unable to give evidence and be cross-examined because his wife was having a baby.

11. A statement of facts not in dispute was also produced.

12. Ms Hartland's evidence was necessarily of a general nature and by reference to a generalised document concerning employment at MBDA. I found her an entirely honest and competent witness but unable to shed light on Mr Barnett's precise circumstances. Whilst I am grateful for the helpful way she gave her evidence it did not assist me in my task which is concerned with Mr Barnett's individual circumstances not the general employment position at MBDA.

Findings of Fact

13. From the evidence I make the following findings of facts:

(1) Mr Barnett is a person with wide experience of the design and development of computer software.

(2) Mr Barnett is the sole director and shareholder of Datagate. It is a closely held company under his control. He has no written Contract with Datagate.

(3) Datagate was incorporated on 2 February 1999 and began trading on 29 March 1999. The accounts describe its principal activity as computer consultants.

(4) Datagate entered into a contract with Technology Project Services International Limited ("TPS").

(5) The terms of this contract, an hourly rate plus VAT invoice.

(6) Clause 8 provided so far as relevant:

> 8.1 This Contract is a contract for the provision of Professional Consultancy Services; the relationship governed by this contract is neither that of agent-principal, nor that of the employer-employee. Any Consultants provided by you are and will remain employed by you; they are not employed by us, and during this Contract will not be employed by the Client. ...
>
> 8.5 This Contract is not exclusive, and you and your Consultants are and remain at liberty to also provide services of third parties.

(7) Clause 9 of the Contract restricted the provision of services to the Client other than through TPS for a period of six months. I find that this was not a restriction of a type normally find in an employment contract.

(8) TPS had an arrangement with MBDA for the supply of services.

(9) TPS entered into the initial arrangement on 10 January 2001 which ended on 10 April 2001. The arrangement was extended until the 30 September 2004.

(10) Work had to be carried out by a particular person because of security (cf Ansell)

(11) There was no provision for a minimum number of hours to be worked. There was also an ability to take time off.

(12) There was a right to provide substitute so long as suitable security clearance was obtained.

(13) Mr Barnett could arrive when he liked. He could leave when he liked. He tended to arrive after 0930 hours and leave before 1600 hours so as to suit his lifestyle.

(14) Mr Barnett could take time off when wanted to but of courtesy discussed it with the team leader.

(15) Mr Barnett worked with the relevant team but was provided with discrete sections of work. MBDA wish to learn from him.

(16) I find that Mr Barnett's relationship with the MBDA team was that of a professional consultant providing independent services when looked at as a whole.

The Submissions of the Parties

The Appellant Submissions in outline

14. In essence, the Appellant submitted that:

a. Mr Barnett was not an employee, he was like any other "self employed" consultant.

b. There was nothing in the documentation to show he was employed as an employee.

c. The rate was fixed with the agency by Datagate.

d. There was no Contract of Employment. What Mr Barnett did was act as Consultant, as an independent contractor.

e. The precise way this was done was for security reasons and the convenience of the parties. This did not make him employee.

f. Accordingly, the appeal should be allowed.

HMRC's Submissions

15. In essence, HMRC submitted Mr Barnett was effectively an employee.

16. This was because:

a. MBDA had a right of control.

b. The *Ansell* case was different (see particularly paragraph 24 of his decision).

c. Mr Barnett's obligations were those of an employee.

d. The Purchase Orders were the Contract.

e. The documents show this was the equivalent of a Contract of Employment.

f. All the evidence shows Mr Barnett was treated in the same way as employee. He worked in the same way.

g. The time he worked was agreed with MBDA.

h. The work he did was agreed with MBDA.

i. Mr Barnett took part in a trip to Portsmouth at MBDA's request.

j. The HR document showed he was an employee.

k. He wore a work badge.

l. The pay rates were employee pay rates.

m. There was a disciplinary procedure which was the same as the other employee.

n. Mr Barnett was integrated into MBDA's business because there were three in team producing an integrated product.

o. Accordingly, the appeal must be dismissed.

Discussion

Introduction

17. From *Ansell* it is clear that the question that I have to answer is "looking at the picture as a whole [do] I find as a primary fact that Bret Barnett was in business on his own account and was not a person working as an employee in someone else's business" in all the circumstances of the case. I also remind myself that the onus of proof is on the Appellant.

18. HMRC Manuals' draft letter sets out a list of relevant factors which I consider of use. These factors include:

a. Whether there is an ultimate right of control on the part of the engager over what tasks have to be done, where the services have to be performed, when they have to be performed and how they have to be performed.

b. Whether personal services required.

c. Whether the worker has the right to provide a substitute or engage helpers.

d. Who has to provide the equipment and/or materials.

e. Whether the worker has a real risk of financial loss.

f. Whether the worker has the opportunity to profit from firm management, for example by reducing overheads and organising work effectively.

g. The basis of payments.

h. Whether there are "employee type" benefits, for example, sick pay, pensions, holiday pay, etc.

i. Whether the worker works exclusively for the engager.

j. Whether the worker is part and parcel of the engager's business or organisation.

k. Whether there is a right to terminate the engagement by giving notice of a specific length.

l. Factors personal to the worker, for example, number of engagements in business organisation.

m. The intention of the engager and worker as regards employment status.

19. I have carefully considered these factors. In considering these factors I have borne in mind that there is a strong security requirement here.

20. I do not consider that there was an ultimate right of control on the part of MBDA of the type the Manual implies. The engager MBDA could have continued with the engagement had it chosen to, or chosen not to renew the engagement. I do not consider here the position was one of an ultimate right of control as would be the case of an employee. Even if there were I do not consider in the particular circumstances that this would be of the same nature as for an employee. If there was an ultimate right of control this was because of the security requirements and not anything akin to that underemployment law.

21. There is nothing in the documents requiring personal service.

22. The documentation allowed for a substitute to be provided or help us engage.

23. The equipment and materials were provided by MBDA but given the security context it would have been surprising had it been otherwise.

24. The requirement that the worker has a real risk of financial loss is somewhat circular. If the worker is in business on his own account there must be a risk of financial loss. Here, he risked not being continued to be engaged.

25. Mr Barnett was able to profit from sound management by organising his work effectively so as to save himself time and give himself more free time which he had told me was part of the reason that he organised his work in the way that he did.

26. The basis of payment was a fee basis. This is entirely consistent with self employment. On the evidence before me there was no employee type benefit such as sick pay or pensions provisions.

27. There was no requirement that Mr Barnett work exclusively for MBDA.

28. Whilst the position was that Mr Barnett was engaged in assisting MBDA's business I do not consider that he was "integrated" as an employee in the way that the Tort cases sometimes suggest. There was evidence that MBDA sought to give him specific projects which so far as possible which were self contained. I find as a fact that Mr Barnett was not integrated into MBDA's business or organisation.

29. The engagement could be terminated but I do not regard this as being the equivalent of being able to give notice under a contract of employment.

30. I do not find that the number or continuation of employment gives rise to employment status.

31. The intention of the parties seems to have been that there should be no employment. Why else would this structure have been set up? I find as a fact that the parties intention was that there should be no employment.

32. Standing back and "looking at the picture as a whole I find it a primary fact that Bret Barnett was in business on his own account and was not a person working as an employee in someone else's business on the hypothetical requirements that the legislation requires. He chose to do this through his company.

33. Accordingly, the appeal is allowed.

SPECIAL COMMISSIONER
RELEASE DATE: 20 December 2007

SC/3108/2006

DATAGATE SERVICES LTD v REVENUE & CUSTOMS COMMISSIONERS (SpC656) (2007)

Sp Comm (Adrian Shipwright) 20/12/2007

TAX - EMPLOYMENT

CONSULTANCY AGREEMENTS : EMPLOYMENT STATUS : PAYE : ARRANGEMENT FOR PROVISION OF CONSULTANCY SERVICES : EMPLOYMENT STATUS OF CONSULTANT

In the circumstances, the Revenue had been wrong to consider that arrangements made between two companies through an intermediary for the provision of professional consultancy services had the effect of making the consultant involved an employee of the company engaging his services.

The appellant (D) appealed against determinations made by the respondent Revenue under the Income Tax (Pay As You Earn) Regulations 2003 reg.80, and against a decision made under the Social Security Contributions (Transfer of Functions, etc.) Act 1999 in respect of its liability to pay primary and secondary Class One National Insurance contributions.

D was a company under the control of its sole director and shareholder (B).

Its principal activity was computer consultancy.

D had entered into a contract with another company (T) for the provision of consultancy services and, in turn, T had an arrangement with a third company (M) for the supply of those services.

B worked with M's team: M wished to learn from him and he was provided with discrete sections of work.

There was no provision for the minimum number of hours to be worked, he could arrive and leave when he liked and he could take time off when he wanted.

The issue was whether, had the arrangements taken the form of a contract between B and M, B would have been regarded as an employee of M.

D submitted that B was not an employee but was, rather, like any other self employed consultant.

The Revenue argued that B was effectively an employee because, amongst other things, M had a right of control and B was treated in the same way as an employee, worked in the same way as an employee and had the obligations of an employee.

HELD: Looking at the picture as a whole, the effect of the arrangements was that B's relationship with M was that of a professional consultant providing independent services.

He was in business on his own account and was not a person working as an employee in someone else's business on the hypothetical requirements that the legislation required, Ansell Computer Services Ltd v Richardson (Inspector of Taxes) (2004) STC (SCD) 472 applied.

There was no ultimate right of control on the part of M, there was nothing in the documents requiring personal service, the basis of payment was a fee basis and there was no requirement that B work exclusively for M.

Whilst B was engaged in assisting M's business, he was not integrated as an employee.

Moreover, the parties' intention was that there should be no employment.

Appeal allowed

Counsel: For the appellant: John Antell For the respondents: Non-counsel representative Solicitors: For the appellant: LawSpeed Ltd For the respondents: Revenue and Customs

LTL 18/1/2008 (Unreported elsewhere)

Judgment: Official - 8 pages

Document No. AC0116049

DRAGONFLY CONSULTING LTD v REVENUE & CUSTOMS COMMISSIONERS (SpC00655) (2007)

Sp Comm (Charles Hellier) 11/12/2007

TAX - EMPLOYMENT

CONTROL : EMPLOYMENT STATUS : INFORMATION TECHNOLOGY : INTERMEDIARIES : MUTUALITY OF OBLIGATION : NATIONAL INSURANCE CONTRIBUTIONS : PAYE : PROVISION OF SERVICES THROUGH INTERMEDIARY : WORKER REGARDED AS EMPLOYEE IF SERVICES PROVIDED DIRECTLY TO CLIENT : IR 35 : Sch.12 FINANCE ACT 2000 : reg.6 SOCIAL SECURITY CONTRIBUTIONS (INTERMEDIARIES) REGULATIONS 2000

The taxpayer company, which supplied the services of its sole director as an IT system tester to a client through an intermediary, was liable to account for income tax under the Finance Act 2000 Sch.12 and national insurance contributions under the Social Security Contributions (Intermediaries) Regulations 2000 reg.6, where a contract directly between the director and the client would have been a contract of employment.

The appellant company (D) appealed against a decision and determinations made by the respondent commissioners that it was liable in respect of national insurance contributions and PAYE tax under the "IR 35" provisions.

D had supplied the services of its sole director (B), who also owned 50 per cent of the shares in D, to a client (C) via an agency.

B was an IT system tester.

His services were supplied to C to work on the testing of IT projects being undertaken by C.

The services were supplied for a period of nearly three years.

During that period B worked almost exclusively for C.

The effect of the IR 35 legislation, contained in the Finance Act 2000 Sch.12 for direct tax and the Social Security Contributions (Intermediaries) Regulations 2000 reg.6 for national insurance, was in outline that if the circumstances were such that, had B performed his services under a contract directly between him and C, that contract would have been one of employment, then D would be liable for national insurance contributions and PAYE calculated broadly on the basis that the payments it received were emoluments it paid to B.

D contended that under such a contract B would not have been an employee.

HELD: (1) The notional contracts between B and C would have been for the personal service of B in return for remuneration, with a limited possibility of B sending a substitute in his place.

The notional contract would contain provisions requiring B to be subject to the guidance of his team and team manager.

The right of C to direct B through the operation of the team and the guidance of the team manager was enough, in the case of a skilled professional man, to be able to say that there was sufficient control.

Therefore the first two preconditions for a contract of employment in Ready Mixed Concrete (South East) Ltd v Minister of Pensions and National Insurance (1968) 2 QB 497 were satisfied, Ready Mixed Concrete applied.

The requirement for mutuality was satisfied by an obligation to work in return for an obligation to remunerate and that requirement was satisfied by the notional contracts.

An obligation on the employer to provide work, or in the absence of available work to pay, was not a precondition for the contract being one of employment, but only an indicator Usetech Ltd v Young (Inspector of Taxes) (2004) EWHC 2248 (Ch), (2004) STC 1671 and Cornwall CC v Prater (2006) EWCA Civ 102, (2006) 2 All ER 1013 considered; Propertycare Ltd v Gower not followed.

(2) Considering the other factors which might indicate employment or consistency or otherwise with employment, there was nothing which pointed strongly to the conclusion that B would have been in business on his own account, Ready Mixed Concrete and Market Investigations Ltd v Minister of Social Security (1969) 2 QB 173 applied.

By contrast, standing back and looking at the overall picture, it appeared that B was someone who worked fairly regular hours during each engagement, who worked on parts of a project which were allocated to him as part of C's teams, who was integrated into C's business, and who had a role similar to that of a professional employee.

B did not get paid for, or go to work to provide, a specific product; instead he provided his services to C to be used by them in testing the parts of a project which from time to time were allocated to him.

He was engaged in relation to the work to be done on a specific project but not to deliver anything other than his services in providing testing in relation to that project.

He would have been an employee had he been directly engaged by C.

Appeal dismissed

Counsel: For the appellant: Non-counsel representative Solicitors: For the respondents: Revenue and Customs

LTL 21/1/2008 (Unreported elsewhere)

Judgment: Official - 27 pages

Document No. AC0116046

Spc00655

Income tax – Worker supplied through intermediaries – "IR 35" – Schedule 12 FA 2000 – Whether circumstances were such that had the services been provided under a contract directly with the worker the worker would have been an employee – Held : yes

National Insurance – Worker supplied through intermediaries – "IR 35" – SI 2000/727 Regulation 6 – Whether circumstances were such that had the arrangements taken the form of a direct contract with the worker the worker would have been an employee – Held : yes

THE SPECIAL COMMISSIONERS

DRAGONFLY CONSULTING LTD **Appellant**

- and –

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

Special Commissioner: CHARLES HELLIER

Sitting in public in London on 20 and 21 September 2007

Dave Smith and Nicola Smith of Accountax Consulting Ltd, Chartered Tax Advisers, for the Appellant

Mike Faulkner of HMRC Appeals Unit for the Respondents

DECISION

1. Dragonfly Consulting Ltd appeals against the following decision and determinations made by the Respondents under what are commonly known as the IR 35 provisions:

> (i) a decision issued on 30 April 2004 for the period 6 April 2000 to 5 April 2003 in respect of National Insurance Contributions; and
> (ii) determinations issued on 18 June 2004 in respect of PAYE for the same period.

By these determinations and this decision the Respondents seek some £99,000 from the Appellant.

2. In the relevant period Mr Jon Bessell who was the director of, and owner of 50 per cent of the shares in, the Appellant had, via arrangements between (1) him and the Appellant, (2) the Appellant and an agency, DPP International Ltd (DPP), and (3) between DPP and the AA, provided his services to the AA.([*])

3. In outline, the IR 35 legislation, which I shall describe later, provides that if the circumstances are such that, had Mr Bessell performed his services under a contract directly between him and the AA, that contract would have been one of employment, then the Appellant will be liable for NI contributions and PAYE calculated broadly on the basis that the payments it received were emoluments it paid to Mr Bessell. The Appellant contends that under such a contract Mr Bessell would not have been an employee.

4. The argument before me related to the nature of the hypothetical contract, and whether or not Mr Bessell would have been an employee in relation to it, and not to the amounts involved. This is therefore a preliminary decision.

5. In the remainder of this decision I shall first discuss the evidence and set out my findings of fact, then address the relevant law, and then reach my conclusions on the appeal.

Evidence and Findings of Fact

6. There was a joint bundle of documents. I heard oral evidence from Mr Bessell; from Jane Tooze, who had, through her own service company provided services to the AA in the relevant period and who had been responsible for part of the project on which Mr Bessell worked in the period October 2002 to April 2003; from Alan Palmer who was an employee of the AA in the relevant period acting as an IS Test Manager, and responsible for part of the projects on which Mr Bessell worked between February and July 2000, and between May 2002 and September 2002; and

[*] The AA was [acquired] during the relevant period by Centrica. I have used `the AA' to refer to companies in the combined group.

from Alan Kersley who in the relevant period was Head of Change Delivery at the AA. All of them provided witness statements. In the days before the hearing the Appellants produced a letter from Christine White who described herself as The AA Commerce Programme Manager. Ms White did not give oral evidence.

General Findings of Fact

7. I find the following facts:-

(i) Mr Bessell is a highly skilled IT system tester. His principal expertise is designing and implementing tests on IT systems software which will give the user of the software the required level of confidence that the software will work as intended or required. This work involves determining the expectations of the users translating those expectations into requirements of the system and testing the system (for example by creating a large number of test usings of the system) to assess whether it meets those requirements. Mr Bessell does this job well and his skills were appreciated by those with whom he worked at the AA. Those skills are both analytical and personal, for the first stage of the exercise in particular requires interaction with other people.

(ii) Mr Bessell is the sole director and the holder of 50 per cent of the shares in the Appellant.

(iii) Under the contractual arrangements which I shall describe shortly, in the period April 2000 to January 2003 Mr Bessell provided his services to the AA. These services were predominantly directed to the testing aspects of three IT projects then being undertaken by the AA:-

(a) the first project lasted 7 months from January 2000 to July 2000 and related to the replacement of an `Ingres' database with an `Oracle' database;

(b) the second project lasted 22 months from August 2000 until April 2002 and related to the AA.com website;

(c) the third project was concerned with the AA's travel insurance product, OATI, and Mr Bessell was involved in testing between May 2002 and the end of January 2003.

(iv) It was in October 1998 that the Appellant first contracted with DPP for the supply of Mr Bessell's services. In the period 1 April 2000 to 28 February a series of fixed term contracts were made between the Appellant and DPP. There were seven such contracts. With the exception of 1 April 2001, 29, 30 and 31 December 2001, 1 January 2002, and 28 and 29 September 2002, the combined period of these contracts includes every day in the period between 1 April 2000 and 28 February 2003. Each contract took the form of a schedule which specified inter alia the period of the contract, the rate of payment and invoicing arrangements, and annexed General Terms and Conditions which were materially the same for each contract (save in those respects I discuss

later). The schedule indicated that it set out the principal terms and conditions on which the Appellant would provide a consultant to perform services for DPP's client. The first and the seventh schedules indicated the name of the consultant to be provided by the Appellant: "Jonathan Bessell".

(v) DPP contracted with the AA to provide consultancy services and temporary staff to the AA. There was in the bundle before me a copy of such a contract dated 12 October 1998. Clause 2 provided that the contract should continue for no more than 12 months. This document provided for details of the services to be provided to be set out in a schedule. There were, in the bundle, copies of schedules (not to that agreement but conforming with its terms) covering the period 3 January 2000 to 2 July 2000. I find from the evidence of Mr Palmer and Mr Kersley and from the copy invoices from DPP to the AA that for the period under appeal Mr Bessell's services were provided through DPP. I find that it is more likely than not that those services were provided under agreements between DPP and the AA which, so far as is material, contained the same general terms as the agreement dated 12 October 1998. The two schedules I have mentioned state "Name of individual: Jon Bessell; Job Title: consultant", and set out rates of payment and the period of the contract.

(vi) There was no written contract between Mr Bessell and the Appellant.

(vii) During the relevant period Mr Bessell worked mainly at the AA's premises (but see also paragraph 28 below in relation to the AA.com project). In relation to all three projects it was necessary to spend time there to talk to those for whom the system was being tested (those who would use it) and other members of the development teams; in relation to the first and third projects it was also necessary to work mainly at the AA's premises in order to work on the AA's computer system. During the second project, the AA.com project, Mr Bessell could access the AA's computer from home. In this period he had an ISDN telephone line installed at home to access the AA mainframe computer and was provided with a customised laptop by the AA.

(viii) When working at the AA's premises (which changed from time to time) Mr Bessell was provided with a desk and computer and worked alongside other employees (and other contractors). He required a pass to enter the buildings. The pass bore a "C" which differentiated the bearer as a contractor rather than an employee. He was able to use the onsite canteen. He would be invited to events such as the project Christmas Party. Towards the end of the relevant period Mr Bessell provided at his own expense or that of the Appellant a special chair to use at the AA offices to help with problems with his back.

(ix) At home Mr Bessell had a designated office room with a desk, two laptop computers, fax, scanner and office furniture. The laptops were not

bought specifically for the AA work but the ISDN line referred to previously was, and was installed at the Appellant's expense.

(x) During the period of the second project the Appellant paid some £400 for a training course undertaken by Mr Bessell. The course was undertaken for the benefit of his work on the AA.com project. The cost was not reimbursed by the AA.

(xi) During the period under appeal the only other work undertaken by the Appellant was some assistance given to a nursery near Mr Bessell's home. Mr Bessell solved a problem it had with a software package and the Appellant was paid. I find that the sum paid was modest in comparison to the Appellant's annual income from DPP. After the end of the period under appeal, the Appellant, through Mr Bessell, embarked on a joint venture project with the nursery for the creation of a new software system which could be widely marketed to nursery operators.

(xii) During the relevant period, the Appellant would invoice DPP and DPP would invoice the AA for work done. The invoiced amounts were calculated by reference to an hourly or daily rate multiplied by the hours or days charged for.

(xiii) Mr Bessell would complete and submit to persons at the AA records of time worked and charged for. Two different records were submitted : one indicated the time Mr Bessell had actually been engaged on the work he was doing, and the other the time for which a charge would be made. The first record was used for the AA's control and forecasting purposes; the second for the authorisation of payment by the AA to DPP. The times could differ. From the evidence of Miss Tooze, and Mr Palmer I find that there was an understanding that generally the hours (or days) charged for would be those indicated in the schedule to the contract between DPP and the AA so that a few extra hours actually worked one week could cancel out a few fewer hours actually worked another week, but that it was expected that Mr Bessell would have worked on average for at least the time billed for. Where the work demanded substantially more time, then additional time could be, and was, billed.

Mr Palmer told me, and I accept, that those in the testing function were "tail end charlies" and that as a result it was rare that they would find themselves with nothing to do on a project. If one stage in the testing of a project had been completed more expeditiously than planned then Mr Bessell would not be expected to sit around and do nothing : there would always be something else to be done on the project, and Mr Bessell, I find, would set about that something and his billed time would reflect the time actually spent working (subject to the comments in the previous paragraph) rather than billing a fixed larger amount for the stage finished ahead of time.

(xiv) During the relevant period Mr Bessell took holidays. He did not submit time sheets for, nor did DPP or the Appellant bill in respect of the time spent on holiday. The times of holidays were agreed between Mr Bessell and those at the AA working on the project. Mr Bessell took care not to arrange holidays at busy times for the project. Sometimes plans could be remade and responsibilities reassigned but there was not a time when Mr Bessell took a holiday at a seriously inconvenient time for the project on which he was engaged.

(xv) Mr Bessell had problems with his back towards the end of the third project. He was unable to work. No payment was made to DPP or the Appellant in respect of this period.

(xvi) Mr Bessell occasionally travelled to visit suppliers. When he did so his expense of travel would be reimbursed by the AA.

(xvii) There was no evidence that Mr Bessell had made errors which he had had to rectify.

(xviii) The AA did not consider itself obliged, and Mr Bessell did not consider that the AA or DPP were obliged, to offer a new contract at the end of the term of any existing contract. Neither DPP nor the Appellant was obliged to accept any offer of a new term.

(xix) During the first project and part of the second project Mr Bessell's activities were contracted to be paid for at an hourly rate. During the second project this changed to a rate per day. At the time of this change Mr Bessell negotiated a higher daily rate than had initially been offered on the basis that, as he said to me, he should be "compensated for not being able to charge 60 hours per week." From an hourly rate of £50 per hour he moved to a daily rate of £480 per day. Later on, market rates for IT expertise fell, and the AA paid only £375 per day. Mr Bessell believed to have no contractual right to insist on the maintenance of the higher rate in subsequent contracts.

(xx) The Appellant submitted invoices by reference to the number of days worked at a daily rate. This was the case even when the contracts provided for hourly rates.

Substitution

8. At no time in the relevant period did the Appellant or DPP supply any other person in place of Mr Bessell.

9. I should now describe some of the evidence relating to the issue of whether or not in practice a substitute could have been provided for Mr Bessell by DPP and the

Appellant. I am here discussing the oral evidence and not the formal contractual documents.

10. The AA engaged a number of `contractors' – at times 50 or more people – who were not its employees. Jane Tooze and Mr Palmer recalled one such contractor who had been engaged under arrangements pursuant to which a substitute could be, and was provided in place of the original individual. I accept that evidence.

11. Mr Kersley said he was aware that substitutes had been used. He said that if a contractor wished someone to substitute his attitude would depend on the circumstances and upon who recommended the substitute; he would almost always want a second opinion from someone he trusted and would want to see a C.V. He said that he would be unhappy if a substitute turned up unannounced and unforeshadowed : that just would not happen. In any event to work on the premises a security card was needed. I accept that evidence.

12. Mr Palmer's evidence was that he expected Mr Bessell to do the work personally and would not have expected him to send a substitute. If Mr Bessell had been unable to perform then he thought that he would have been replaced by a worker engaged through the normal procedures including interviews with new workers. I accept that as evidence of what Mr Palmer would have done.

13. I also find that towards the end of the third project Mr Bessell and Miss Tooze discussed the staffing of the next phase of OATI. It was plain that Miss Tooze wished Mr Bessell to be engaged for it. But Mr Bessell had been having back problems and he agreed with Miss Tooze that he could provide a substitute for the period for which he was not available. (In the event the second phase was cancelled and this did not happen.)

14. Mr Bessell, when asked if Miss Tooze could have decided that she did not want a substitute, replied "absolutely".

15. The letter from Christine White offered in evidence by the Appellant indicated that on one occasion she was approached by one of the contractors in her team, and that it had been agreed that a substitute whose work the contractor had guaranteed could be provided while he was away. This she said had worked well in practice and she had been content to allow it again with other contractors. The letter did not indicate the dates or period when this was done. Given the evidence of Mr Kersley and Miss Tooze I accept that there was an occasion when a substitute was agreed but I do not regard this letter as compelling evidence that in the relevant period substitution was generally permitted or permitted without prior consent.

16. There was in the bundle a copy of a letter from Lyn Lake who was the IS Resource manager at the AA, and who administered the contracts with agencies for the supply of contractors. The letter was written to the Appellant and made various statements about the relationship between the Appellant and the AA. In the fourth paragraph she said that the Appellant "will vet and supply a suitable substitute for the

assigned consultant. [The Appellant] will manage the selection process with input from the assigned consultant. Any training costs … would be … at [the Appellant's] expense.". The letter was dated 28 April 2003, after the end of the period under appeal, and was in a form which had been used to send to a number of other contractors who had requested confirmation of the matters contained in it (for tax purposes or otherwise). Although the letter did not indicate that the AA would wish to approve the substitute first, it was not to my mind absolutely clear that the writer intended to say that the AA did not regard itself as being entitled to require that it approved the substitution or that it would in practice wish to do so in the relevant period. Ms Lake did not give oral evidence.

17. I conclude that, in the period under appeal, unless the Appellant could have shown that it (and DPP) was contractually entitled to send a substitute in place of Mr Bessell, the AA would have accepted (and paid for) a substitute only if the substitute's presence and person had been expressly agreed by it, and that the AA would not, unless as above, have acted as if it was bound to accept any substitute for Mr Bessell or even one who, when offered, was found to be acceptable.

18. Further it was clear to me that the AA regarded itself as having engaged the services supplied by Mr Bessell. He had been interviewed at the outset of his contracts with the AA. His services were highly valued. He was specifically sought by Miss Tooze and others. The AA did not want any competent tester, it wanted Mr Bessell.

Control

19. Mr Bessell was a skilled man engaged in a complex task. He was not subject to detailed instructions as to how he should undertake what he did.

20. In the first project he worked as part of a team of two testers, himself and Mr Palmer. The test manager was Alan Palmer. In the second project he worked as part of a team of 5 testers. In the third project he again worked as part of a team of testers reporting initially to Alan Palmer and later to Miss Tooze.

21. From Mr Palmer's evidence I find that at the outset of a test analyst's involvement with a project the first task would be to settle a plan for the testing of the application. The Test Manager would draw up an initial strategy, and the testers, having got to grips with what the organisation wanted from the application and the background to its implementation, would work as a team to improve and settle that plan, and plan the detailed testing programme. When the application was made available to the test team Mr Bessell would then undertake some of the planned tests. The allocation of tasks to the members of the team was usually done through a communal review taking into account what was available to test, what tests were to be done and who preferred to do which tests. It was a group effort under the co-ordinating influence of the team manager to determine the best division of labour to tackle the work to be done. If having decided on a timetable for testing the delivery

of part of the application was delayed, or if problems arose with parts of it then the tasks would be reallocated in the same way.

22. Thus, once the initial phase of settling the plan had been completed, on a typical day Mr Bessell would have had allocated to him in the project plan as modified by the group discussions a number of aspects of the application to test, and would continue testing those he had started to test and perhaps commence the testing of one or more other aspects of those parts of the application that had been made available. He was not told how to conduct the tests but he was expected to conduct the tests which had, in consultation with the team, been allocated to him.

23. The team manager would review the progress of the work being undertaken by members of the team. There were usually weekly team meetings to review progress. Mr Bessell attended those meetings. There were also ad hoc discussions to deal with more pressing issues. Mr Bessell participated in these.

24. Mr Bessell's progress through the tasks he was allocated would be monitored by the team manager. There was however no detailed review of the work he had undertaken. However it seems to me that Mr Bessell's reputation indicates that he worked effectively: he would not have had a high reputation if things he had tested and approved often turned out to be faulty, of if faults he identified were often found to be illusory. It seems to me that there was an ongoing informal appraisal of the quality of his work. Miss Tooze attended a meeting with HMRC on 10 May 2005. She approved a note of that meeting with her amendments. In those notes she indicated that work was not checked automatically but would be checked if there was a complaint. I accept that that would have been the case.

25. Mr Palmer said, and I accept, that as part of his management checks he would occasionally ask Mr Bessell to run a specific test so that he could be satisfied that his work was acceptable and to get a view on the quality of the application that was being delivered. It was clear however that Mr Palmer would not be involved in reviewing or approving the technical detail of what Mr Bessell was doing. Miss Tooze indicated that no one told Mr Bessell how to do his work although in the approved notes of her meeting with HMRC she indicated that she "could spot check Jon's work if she had reason to".

26. The findings I make above are drawn principally from the evidence of Mr Palmer and Miss Tooze. Neither of them were responsible for Mr Bessell in the period of the second project. There was no AA test team manager for this project. In the earlier stages of this project, its management was outsourced by the AA to Net Decisions, but in July 2001 the AA took over its development. The testing however was undertaken by people engaged or employed by the AA. There were five testers including Mr Bessell; one was an employee of the AA. In the earlier stages Mr Bessell would report to someone on Net Decisions' staff, and in the later stages to persons engaged or employed by the AA. Mr Bessell was the senior tester on this project.

27. There was no evidence before me to suggest that in this period the way Mr Bessell's activities were guided, monitored or determined was any different from the position I have described above. I conclude that it is more likely than not that it was the same.

28. I should however note that the arrangements in relation to the place where Mr Bessell worked during the second project were different from those for the first and third projects: I find that he worked from home for about 25% of his time during the AA.com project. In addition there were times when Mr Bessell made himself available in the late evening during the course of the project to discuss problems with the website on the phone with those to whom he reported at the AA.

The Statutory Provisions

29. For the relevant periods the legislation relating to direct tax was contained in Schedule 12 FA 2000. It provided so far as relevant to this appeal that where an individual or an associate receives from an intermediary (it is accepted that the Appellant is an intermediary for those purposes) or has rights to receive from an intermediary a payment or benefit not taxable under Schedule E then the intermediary is to be treated as making a payment chargeable to Schedule E of the amount of that payment or benefit. The provisions apply where para 1(1) Schedule 10 applies, namely where:-

> "(a) an individual ("the worker") personally performs, or is under an obligation personally to perform, services for the purposes of a business carried on by another person ("the client")".

Pausing there, this provision was clearly satisfied. Mr Bessell personally performed services for the purposes of the AA's business.

> "(b) the services are provided not under a contract between the client and the worker but under arrangements involving a third party ("the intermediary")."

Pausing again, this condition was also satisfied: Mr Bessell had no contractual relationship with the AA. His services were provided under arrangements involving the Appellant and DPP. Each of them were third parties.

> "(c) the circumstances are such that, if the services were provided under a contract directly between the client and the worker, the worker would be regarded for income tax purposes as an employee of the client."

It was this last condition which was in dispute in the appeal.

30. Before leaving the income tax provisions of Schedule 10, I should note the provision of paragraph 1(4):

> "(4) The circumstances referred to in sub-paragraph (1)(c) include the terms on which the services are provided, having regard to the terms of the contracts forming part of the arrangements under which the services are provided."

31. The National Insurance provisions, to be found in regulation 6 of SI 2000/727, provide that a worker will be treated as in employed earner's employment and receiving benefits calculated in accordance with regulation 7 of that statutory instrument where the three conditions in regulation 6(1) are satisfied. Subparagraphs (a) and (b) of regulation 6(1) are identical to subparagraphs (a) and (b) of paragraph 1(1) Schedule 10 set out above. Paragraph (c), the third condition, is, strangely, phrased differently:

> "(c) the circumstances are such that, *had the arrangements taken the form of a contract* between the worker and the client, the worker would be regarded for the purposes of Parts I to V of the Contributions and Benefits Act as employed in employed earners employment." (My italics).

32. There is to my mind a potential difference between the effect of paragraph 1(1)(c) Schedule 10 and regulation 6(1)(c). It is this: regulation 6(1)(c) appears to require the notional contract between the client and the worker to be constituted by the arrangements: "had the arrangements taken the form of a contract". Thus potentially there is no requirement to consider whether anything else would have been included in the notional contract. By contrast paragraph 1(1)(c) Schedule 10 may require a wider enquiry into what the terms of a direct contract between client and worker would have been had there been such a contract: there is no limitation in the words "if the services were provided under a contract directly between the client and the worker" to contract terms which are encompassed in the arrangements or the circumstances.

33. In *Usetech Ltd v Young (HM Inspector of Taxes*) 2004 TC 811, Park J did not however see any difference between the two formulations. At paragraph 35, after reciting the relevant extracts he said:

> "The two wordings are not identical, but the meanings are. There was not a direct contract [between the parties in that case] but the provisions require it to be assumed that there was. What would it have contained? …".

It seems to me that Park J is there saying that both provisions require a determination of what such a contract would have contained from a consideration of all the circumstances, rather than the construction of a contract where content was limited to the arrangements. Likewise at paragraph 9 he says:

> "subpara (c) involves an exercise of constructing a hypothetical contract which did not in fact exist, and then enquiring into what the consequences would have been if it had existed. There may be room in some cases for dispute about what the hypothetical contract would contain, and in the present case there is …".

34. On the other hand in *Synaptek v Young (HM Inspector of Taxes*) (2003) 75 TC 51, Hart J seem to adopt the more limited approach. That case however dealt only with the provision of regulation 6 and Hart J makes no reference to the corresponding provisions of Schedule 10. At paragraph 11 he says:

> "… The inquiry which Regulation 6(1) directs is in the first instance an essentially factual one. It involves identifying first, what are the "arrangements involving an intermediary" under which the services are performed, and, secondly what are the "circumstances" in the context of which the arrangements have been made and the services performed. *The legal hypothesis which then has to be made is that the arrangements had taken the form of a contract between the worker and the client."* (my emphasis).

This is potentially a different approach from considering what would the contract have contained. It seems to me that this difference exists at least in theory even when it is acknowledged that the `arrangements' are not limited to the words of the formal contracts between the relevant parties but include all relevant circumstances (see para 47 in *Usetech*). What actually happened will be part of the arrangements: the practice may indicate a variation in the formal agreements; it may also illuminate the formal agreements and be something which falls short of contractual rights and duties. But even where account is taken of all the actual arrangements there may be a difference between the notional contract formed by encapsulating those arrangements and the notional contract whose terms would be determined by asking "What would have been agreed?"

35. I shall return to this issue later but I note that Park J said, at paragraph 1(4): "However no-one has suggested to me, nor do I consider, that that [difference] or the other minor differences between the two statutory provisions affects this case or opens a possibility of the case being decided are way for NICs and another way for income tax and corporation tax."

<u>Employment – the Case Law</u>

36. I was referred to a number of authorities and there was some difference in the parties' approach to them. I set out below my understanding of the principles to be derived from these authorities. I hope that in doing so I will have dealt with the points made to me in relation to them by Mr Smith and Mr Faulkner.

37. In *Ready Mixed Concrete v Minister of pensions and National Insurance* (1967) 2 QB 497, MacKenna said that "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 a sufficient degree to make that other master;

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

38. In 2001 Buckley J in the Court of Appeal in *Montgomery v Johnson Underwood Ltd* (2001) EWCA Civ 318 indicated that this passage was the safest starting point in considering whether a person was an employee, and showed how it had been approved by the House of Lords and the Court of Appeal as setting out the irreducible minimum by way of legal requirement for a contract of employment to exist. He continued at paragraph 23:

> "It permits tribunals appropriate latitude in considering the nature and extent of `mutual obligations' in respect of the work in question and the `control' an employer has over the individual. It does not permit these concepts to be dispensed with altogether. As several recent cases have illustrated, it directs tribunals to consider the whole picture to see whether a contract of employment emerges. It is though important that `mutual obligation' and `control' to a sufficient extent are first identified before looking at the whole."

39. I shall refer to the three links of MacKenna's test as the `mutual obligations condition', the `control condition' and the `consistency condition'. Whilst the nature of the last two of these flow directly from the words of MacKenna J, there is possibly something in the use made in the cases and before me of the term `mutual obligations' which may encompass something more than the words of paragraph (i). I shall return later to discuss mutuality and control. But when I came to consider whether the notional contract was one of employment my first steps must be to consider whether `mutuality' and `control' are present in sufficient degree to be able to say that the contract could be one of employment.

40. In *Market Investigations Limited v Minister for Social Security* [1969] 2 QB 173 at 184-185 Cooke J said that the fundamental test to be applied was this: Is the person performing these services as a person in business on his own account? He said this after referring to the conditions laid out by MacKenna J set out above and noting that the first condition was in that case, fulfilled. He had then considered the `control' condition and found it was not determinative. His "business on his own account" test was the next step in his judgment. It is clear to me that, having considered mutuality and control, I should then address this test. It is in my view comparable with MacKenna J's consistency condition.

41. In *Hall v Lorimer* (1993) 66 TC 349 at 375F, Nolan LJ said:

> "In order to decide whether a person carries on business on his own account it is necessary to consider many different aspects of that person's work activity.

This is not a mechanical exercise of running through items on a check list 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 making an informal, considered qualitative appreciation of the whole … Not all details are of equal weight … The details may also vary in importance from one situation to another."

42. The authorities indicate that the consideration of certain indicia which may point one way or the other may be helpful in considering that picture. (*Lee Ting Sang v Chung Chi-Keung* 2 AC 374, and *Hall v Lorimer*). Those indicia include those mentioned by Cooke J in *Market Investigations*. The following may be relevant:-

(a) does the taxpayer provide his own equipment?
(b) does the taxpayer hire his own helpers?
(c) what degree of financial risk does the taxpayer bare and what opportunity for profit does the taxpayer have?
(d) what degree of responsibility for investment and management does the taxpayer have?
(e) is the taxpayer part and parcel of his "employer's" organisation (see *Hall v Lorimer*);
(f) the degree of control to which the taxpayer is subject (rather than the mere existence of a right of `control');
(g) termination provisions – termination on notice may be a pointer towards employment in some cases (it was found to be so in *Morren v Swinton* (1965) 1 WLR 576 but found to be neutral in *McManus v Griffiths* 1997 70 TC 218);
(h) the intention of the parties.

43. I now turn to the mutual obligations condition and the control condition identified by MacKenna J.

Mutuality

44. There are two relevant aspects to the condition. The first flows directly from MacKenna J's words: does the putative employee agree to provide "his own work and skill". If he does not the condition is failed. But if he agrees to provide his own work and skill but also or in some circumstances alternatively that of another, then when does that cause the condition to be failed? I discuss that below under the heading "substitution".

45. The second aspect of this condition I need to discuss is the extent to which it can be regarded as imposing a precondition that there must be obligations imposed upon the employer other than merely to pay remuneration for what is done. There are statements in some of the cases which can be read as if they had that import, and that

was the stance taken by Mr Smith before me. I discuss this issue under the heading "Employer's obligation – Mutuality" below.

Substitution

46. Mr Smith drew my attention to Peter Gibson LJ's statement in his judgment in *Express Echo Publications v Tanton* 1999 IRLR 367 at paragraph 31:

> "It is in my judgment established … that where … a person who works for another is not required to perform his services personally, then as a matter of law the relationship … is not that of employee and employer."

However, following the setting out of his three conditions in *Ready Mixed Concrete* MacKenna J added some words of explanation. He said that freedom to do a job either by one's own hands or by another's is inconsistent with employment "though a limited or occasioned power of delegation may not be."

47. Mr Faulkner relied upon the review of the case law conducted by Park J in *Usetech*. Park J set out his conclusions at paragraph 53. He repeated that whether a relationship is one of employment depends upon all the circumstances: that the context is one where the answer depends upon the relative weight of a number of potentially conflicting indicia, and said:

> "The presence of a substitution clause is a indicium which points towards self-employment and, if the clause is as far reaching as the one in *Tanton* it may be determinative by itself."

Mr Smith cautions against taking this extract out of context. He says that in *Usetech* there was a relatively weak substitution clause: in that context Park J was saying that the clause was merely another factor to be considered.

48. It seems to me that if there is a right to substitution then that may be relevant at two stages. First one asks: is that right such that this cannot properly be treated as a contract for personal service? If the answer is yes, that is an end of the matter. If the answer is no, then, if the other precondition hurdles are surmounted, the existence of the right goes into the pot – or the overall picture – to be evaluated along with other relevant features.

Control

49. MacKenna J's test required a "sufficient degree" of control. Mr Smith took me to Buckley J's statement in the Court of Appeal in *Montgomery* at paragraph 23:

> "mutuality of obligation and the requirement of control are the irreducible minimum for the existence of a contract of employment."

I accept that there must be something in the contract which can reasonably be called a right for the employer to control the employee. But such a right need not be a right to control every aspect of what is done: what is done, how it is done, when and where it is done; instead a restricted right may be adequate. MacKenna J accepted that in many cases the employer or controlling management have no more than a general idea of how the work is done are no inclination to interfere, but "some sufficient framework of control most surely exist" (paragraph 19), and at paragraph 23 indicated that tribunals should exercise appropriate latitude in determining the question of control.

Mr Smith suggested that control exercised through an independent agent such as Ms Tooze was not sufficient. He pointed to the comments of the Special Commissioner in *MAL Scaffolding* at paragraph 49. But those comments were directed to whether site agents exercised control over scaffolders such as to make them employees; the Special Commissioner was not considering the position of agents generally. It seems to me that a company can only exercise control through the agency of real people and when considering whether or not the company has exercised control it matters not whether those people are agents because they are employees or agents because a specific power has been delegated to them. To my mind the actions of the company are those of its agent Ms Tooze. (See also *Morren* at page 351).

Employer's obligation – Mutuality

50. In *Ready Mixed Concrete* MacKenna J's first condition was:

> "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."

This first condition is often referred to as a requirement for mutual obligation, but as described by Mackenna J that mutuality is fairly one sided: his condition relates to an obligation of the employee to perform a service for a consideration. There is nothing in these words suggesting that the putative employer must be obliged to provide work or even to pay if there is no work to be done; all that is clear from condition (i) is that the employer must be bound to pay for the service performed.

51. In *Nethermere (St Neots) v Taverna* [1984] 1 RLR 240 the Court of Appeal considered the finding of an Industrial Tribunal that two women who worked as home workers sewing garments were employees. At paragraph 18 Stephenson LJ asked "does the law require any and what mutual obligations before there can be a contract of service?" At paragraph 19 he considers employers' obligations and says "[b]ut later cases have shown that the normal rule is that a contract of employment does not oblige the master to provide the servant with work in addition to wages". At paragraph 20 he considers employees' obligations and treats MacKenna J's three conditions in *Ready Mixed Concrete* as an expansion of the nature of a true employee's obligation to serve. At paragraph 22 he says that there must "be an

irreducible minimum on each side to create a contract of services. I doubt if it can be reduced any lower than the sentences I have just quoted …". In the judgments of Kerr and Dillon LJJ the need for mutuality is asserted but I can find nothing which points to either Lord Justice dissenting from or agreeing with its description by Stephenson LJ. Kerr LJ's dissenting judgment makes clear that in his view the absence of an obligation on the employee to work is fatal, but that much is also clear in the phrases I have quoted from Stephenson LJ.

52. Thus in *Nethermere* I find support for the three conditions in *Ready Mixed Concrete* as regards the employee's obligations but no clear indication as to the nature of the obligation which the employer must bear as a prerequisite of the contract being one of employment.

53. In *Carmichael and another v National Power plc* [1999] 4 All ER 897, the House of Lords agreed that Mrs Lease' and Mrs Carmichael's argument that they were employees "founder[ed] on the rock of mutuality". These ladies worked from time to time as part time guides at a Power Station. Lord Irvine noted that no issue arose as to their status when they were actually working as guides: the question was whether they were employees when they were not working. He held that there was no contractual relationship of any kind when they were not working, and it was on that rock that their case foundered. But in the course of his speech he considered whether a certain construction of particular documentation might determine the appeal and said that he construed it so that `no obligation on the part of the CEGB to provide casual work, nor on Mrs Lease and Mrs Carmichael to undertake it was imposed'. Referring to Stephenson LJ in *Nethermere* and to *Clark v Oxford Health Authority* he said that therefore on that basis there would be an absence of that irreducible minimum of mutual obligation necessary to create a contract of service.

54. It is clear to me that Lord Irvine considered the obligation of an employer to provide work (or to pay a retainer) as an important consideration, but given, in particular, his citation of Stephenson LJ in *Nethermere* – whose comments reproduced above indicate a lesser prerequisite for the employer's obligation than that of being obliged to provide work, it seems that Lord Irvine may not have considered such an obligation as a necessary condition for the existence of an employment.

55. In *Propertycare Ltd v Gower* 2003 UKEAT/0547/03, the EAT said at paragraph 9:

> "The cases, starting with *Ready Mixed Concrete* … show that mutuality of obligations means more than a simple obligation on the employer to pay for the work done; there must generally be an obligation on the employer to provide work and the employee to do the work. That is how we understand the first of MacKenna J's tests in *Ready Mixed Concrete*. In *Clark v Oxfordshire* … Sir Christopher Slade allowed of the possibility that paying a retainer when no work was available might give rise to mutuality of obligations, but there must be some mutuality of obligations. The principle

was affirmed by the House of Lords in *Carmichael* and subsequently by the Court of Appeal in *Montgomery* …" (my emphasis).

56. As can he seen from the discussion of *Ready Mixed Concrete*, *Carmichael* and *Montgomery* above, I cannot find in the judgments a statement of principle as wide as that which the EAT found in *Propertycare*. (The example given by Sir Christopher Slade in *Clark* was in relation to a `global' contract spanning periods of engagement.) It is clear to me that a condition is that the employee is obliged to render personal service for a reward, but the extent of the condition applicable to the employer's obligation is less clear. The fact that Lord Irvine considered that the CEGD's lack of obligation to provide work was, when coupled with the ladies' lack of obligation to perform, fatal suggests strongly that he puts the condition somewhat higher than did Stephen LJ in *Nethermere*. The formulation adopted by Buckley J in *Montgomery* suggest some flexibility in the application of this condition in any event.

57. In *Usetech* at paragraph 28 the tribunal said:

> "… certainly there must be mutuality of obligation, but that does not imply that the "employer" is required to provide work : so much was made clear by Stephenson LJ in *Nethermere* … the requirement of mutuality is satisfied by the obligation on the one hand, to work and, on the other to remunerate. That was the position in the *Market Investigations* case."

Park J commented thus at paragraph 11:

> "I would accept that it is an over simplification to say that the obligation of the putative employer to remunerate the worker for the services performed in itself always provides the kind of mutuality which is the touchstone of an employment relationship."

I note that Park J speaks of a "touchstone" rather than a necessary condition. He continues at paragraph 64:

> "The cases indicate … that the mutuality requirement for a contract of employment to exist would be satisfied by a contract which provided for payment (in the nature of a retainer) for hours not actually worked. It is only where there is both no obligation to provide work and no obligation to pay the worker for time in which work is not actually provided that the want of mutuality precludes the existence of a binding contract of employment."

58. That statement would I believe conclude the matter for me were it not for the observations of the Court of Appeal some 18 months later in *Cornwall County Council v Prater* [2006] EWCA Civ 102. The issue in this case was whether a home tutor engaged by the council to teach particular pupils was employed by the council. The teaching assignments were for particular pupils and were of durations from a few months to 5 years. The council maintained that she had a series of short fixed term discrete individual teaching engagements which individually lacked the requisite

irreducible minimum mutual obligations: the mutuality created by Mrs Prater being contractually obliged to work during each successive engagement was not enough for the irreducible minimum – there had to be a continuing obligation to guarantee and provide more work and an obligation on the worker to do that work (see para 30). Mummery LJ held that the tribunal was entitled to find that there was mutuality of obligation in the individual contracts between Mrs Prater and the council. Summing up, at paragraph 40, he said:

> "(5) Nor does it make any difference to the legal position that, after the end of each engagement the Council was under no obligation to offer her another teaching engagement or that she was under no obligation to accept one. The important point is that, once a contract was entered into and while that contract continued, she was under an obligation to teach the pupil and the Council were under an obligation to pay her for teaching the pupil made available to her by the Council under that contract. That was all that was necessary to support the finding that each individual teaching assignment was a contract of service …"

I accept that at paragraph 11 of his judgment Mummery LJ had said that the "Council was obliged to continue to provide that work [tutoring the particular pupil] until the particular engagement ceased", but in the summary set out above that factor is not treated as relevant to his conclusion. Longmore LJ, at paragraph 43, said he could not accept the submission that mutuality required an on-going duty to provide work and an on-going duty to accept work. He said:

> "There was mutuality of obligation in each engagement namely that the County Council would pay Mrs Prater for the work which she, in turn, agreed to do by giving tuition to the pupil for whom the Council wanted her to provide tuition. That to my mind is sufficient "mutuality of obligation" to render the contract a contract of employment if other appropriate inclinations of such an employment contract are present."

There is no hint here that "mutuality of obligation" required any obligation on the part of the Council other than to pay for work done.

Lewison J was yet more direct: "I would have thought that the question of mutuality of obligation goes to the question of whether there was a contract at all, rather than what kind of contract there was, if a contract existed." He agreed with Mummery and Longmore LJJ.

59. The sentiments expressed by the Court of Appeal in this case are to my mind more aligned with the approach taken by the tribunal in *Usetech* than the judgment of the EAT in *Propertycare*. In these circumstances it is with some diffidence that I set out my conclusions in relation to mutuality:-

> (i) For there to be an employment contract there must be a contract. That requires some mutual obligations.

(ii) That contract cannot be an employment contract unless the `employee' is obliged to provide his labour.

(iii) An obligation on the employer to provide work or in the absence of available work to pay is not a precondition for the contract being one of employment, but its presence in some form (such as for example an obligation to use reasonable endeavours to provide work, to allocate work fairly, or not to remove the ability to work e.g. by removing the pupil to be taught) is a touchstone or a feature one would expect to find in an employment contract and where absence would call into question the existence of such a relationship.

Discussion

60. I now turn to consider what the terms of the hypothetical contract between the AA and Mr Bessell would have been. I shall then consider whether, in the circumstances I have identified, had Mr Bessell been engaged under that contract, he would have been an employee.

61. It is important to consider the terms of the notional contract because some of the conditions for employment (e.g. control and mutuality) and other important indicia of employment or otherwise flow from the legal rights and duties of the parties rather than from the general relationship between them.

62. Mr Bessell was the sole director of the Appellant. It seems to me, as it did to the Special Commissioner in *Netherlane* SpC 457 that in the absence of any formal contract between him and the Appellant, straightforward to treat him as effectively a party to the Appellant's contract with DPP in conducting this exercise.

63. I approach this question by asking first, what would the contract have contained? and then I ask whether my answer would be any different if I simply reduced the arrangements to a contract (the embodied arrangements basis).

64. In my opinion the terms of the notional contracts would have been these:

(1) There would be a series of contracts each with a fixed term. The term of each contract would match the periods of the DPP/Dragonfly contracts. There would have been no requirement for the AA to offer renewal and no obligation for Mr Bessell to accept any offer of an extension.

I reach the same conclusion on the embodied arrangement basis.

(2) Each contract would be terminable before the end of its fixed term by 28 days notice in writing by either party.

I reach this conclusion because: (1) clause 9.2 of the DPP/AA agreement of 12 October 1998 (see para 7(v) above) provides that "either party may give the

other 28 days' notice to terminate this Agreement and/or any Schedule", and I have found that provision is likely to have applied for the whole of the period under approval; (2) clause 8.1 of the Dragonfly/DPP agreement provides that DPP may give Dragonfly 28 days notice, but Dragonfly has no clear right of early termination during an assignment; (The Special Terms in the Schedule to all the contracts bar one provide that 4 weeks notice may be given; but it is not clear by which party.); and (3) had there been a contract between Mr Bessell and the AA it seems very likely to me that it would have encompassed the 28 day termination right of the AA, and, given that the AA conceded such a right to DPP, it seems likely that the AA would have been conceded it to Mr Bessell.

On the embodied arrangements basis it is clear that the AA could give 28 days notice; but read together the arrangement would not permit that right to Mr Bessell.

(3) Each contract would also be terminable by written notice if Mr Bessell's performance was unsatisfactory. That is because (1) clause 8.2 of the AA/DPP agreement of 12 October 1994 provides that DPP shall on notification remove a staff member whose service is unsatisfactory or for misconduct, (2) clause 8.2.1 of the DPP/Dragonfly agreement permits that agreement to be terminated early if there is unsatisfactory performance, and (3) I would therefore expect such a provision to be included in the notional contract.

My conclusion on the embodied arrangements basis would be the same.

(4) Each contract would be for the services of Mr Bessell. The contract would provide that Mr Bessell could send a substitute in his place but only if the AA had given notice that that particular substitute was acceptable in place of Mr Bessell for such period as it should specify.

That is for the following reasons.

First, it seems to me that the DPP/AA agreement contains no right for DPP to supply a substitute, and the agreement or sub-agreement made via the Schedule is an agreement for the supply of a particular individual. Clause 3 of the Agreement sets out the framework for the supply by DPP of a person to the AA: the AA is to indicate its need; DPP sends CVs of persons it proposes to fill the need, and the AA selects the persons it requires. A schedule is completed to record the agreement in respect of the person selected. Where Mr Bessell's name appears on such schedules (and I have found it is more likely than not that it did throughout the relevant period) there was an agreement between DPP and the AA for the supply of Mr Bessell. There is no clause or provision of the agreement which deals with substitution. Clause 8.4 deals with the replacement of an unsatisfactory employee but that is a far cry from a right of any sort to substitute.

Clause 3.2 of the Dragonfly/DPP agreement provides that Dragonfly has the right to substitute a suitably qualified person. But clause 3.3.1 restricts that right to circumstances where DPP has given prior written consent (for contract up to 2 January 2002), or where the AA has been satisfied that the "new consultant is trained and suitable to undertake the services" (for contracts between 2 January 2002 and 1 January 2003), or without satisfying both DPP and the AA that the new consultant is suitable (thereafter).

In the first period it seems to me that the combined effect of these clauses is that DPP would not consent to a substitute unless it obtained the specific agreement of the AA – without which it would be in breach of its agreement. In the later periods Dragonfly could not substitute unless the AA were satisfied of the substitute's suitability. Given that DPP had no right to substitute it seems to me that a coalescing of these agreements into one could only be one wherein substitution was permissible only if the AA agreed to the substitute. And if one asks at this stage what would have been agreed? then, given what was agreed by the AA it seems to me that no right of substitution would have been conceded other than substitution with formal consent at the AA's discretion.

Second, it seemed to me that there was no course of conduct between DPP and the AA from which it could be concluded that the AA/DPP agreement had been varied. The evidence that there had been one or two substitutions was not enough to convince me that the AA permitted substitution at will rather than substitution in circumstances where it had agreed specifically to the substitute. Christine White's letter to my mind did not clearly indicate that specific agreement to a substitute was not required, and Lyn Lake's letter did not clearly relate to the period of the appeal nor to my mind unambiguously indicate that the consent of the AA to the person substituted would not be required. Without hearing their evidence in person I am unwilling to take a broader view of their statements.

Third, I concluded at paragraph [17] above, that in practice the AA would not have accepted a substitute unless either it expressly agreed to a particular substitution, or it could be shown it was contractually obliged to agree. I conclude above that it was not so contractually obliged.

Therefore if I ask the question what would the notional contract have contained? I answer: only a provision under which substitution could be made only with the express agreement of the AA. Coalescing the arrangements into a contract I come to the same conclusion.

(5) `Control'

The Schedule to the first agreement between Dragonfly and DPP provides at the top of the page:

> "This Schedule sets out the principal terms upon which we shall engage you to provide a consultant to perform certain services for you under your direct supervision and control." (my emphasis)

Mr Smith, in his skeleton argument, described this as "the engagement of [Dragonfly] to provide a consultant to perform the services under [Dragonfly's] direction supervision and control." I do not agree. The language is not clear, but the "you" for whom the services are to be performed is not [Dragonfly], and the "your" does not therefore suggest to me that [Dragonfly]'s control is intended. In my view what was intended by those words is what appears at the top of the next schedule in the sequence of engagements namely:

> "to provide a consultant to perform certain services for the Client under the client's direction."

The Client being the AA. This formulation appears in the second and third schedules. In the remaining four schedules (April 2001 onwards) the words "under the Client's direction" are omitted.

Mr Smith suggested that the first formulation clearly indicated where control lies namely with Dragonfly. I do not think it does, if anything these phrases suggest that at least in the early contracts control was to lie with the AA.

Clause 3.8 of the AA/DPP contract provides that the staff supplied by DPP "shall be under the full control and supervision of [the AA] on a day-to-day basis only regarding performance of duties".

Up until 2 January 2002 Clause 2.1.1 of the Dragonfly/DPP contract provided that Dragonfly would procure that the consultant would comply with the AA's customary rules and regulations and working procedures. For contracts on and after 2 January 2002, clause 3.1.1 merely requires that the consultant will comply with the AA's health and safety and similar regulations, adding "(the company's method of working shall be its own)".

It seems to me that for the period up to 2 January 2002 the effect of these arrangements was to give the AA an indirect contractual right to require that Mr Bessell comply with the AA's customary rules and regulations and working procedures. There was no evidence to indicate any variation in these contracts by conduct.

In the period after 2 January 2002 the provisions of the two sets of contracts do not give such an indirect right to the AA: although the AA/DPP contract gives control to the AA, the Dragonfly/DPP contract does not. Thus control cannot be spelt out of the words of the formal contracts.

In practice Mr Bessell worked as part of the team, undertaking the work on the project which was allocated to him as part of the team discussion and by the team manager. The engagement simply would not have worked if he did not do what was allocated to him. His work was also informally monitored.

Putting this together it seems to me that if there had been a contract between Mr Bessell and the AA it would have contained a provision that Mr Bessell undertake the tasks allocated to him with a specified but reviewable timeframe and accept the AA's reasonable directions in relation to what he was doing (rather than how he did it).

On the embodied arrangements approach I come clearly to the same conclusion as regards the period up to 2 January 2002. For the period thereafter it seems to me that the arrangements were that Mr Bessell should do the work allocated to him within the framework of the project timetable, and be subject to the guidance of the team and its manager. That requirement was part of the arrangements and would therefore form part of his notional contract notwithstanding the lack of a specific control provision in the Dragonfly/AA contract.

(6) Payment

Payment would be made for the number of days on which Mr Bessell worked at the relevant daily rate (for the engagements for which the schedules specified an hourly rate, the daily rate would represent 8 hours' work).

The schedule to the DPP/AA contract indicates:

"Hours per week	40 hours …
Other information	10% maximum overtime."

This is a schedule recording the details for the "supply [of] temporary staff". I read the contract as making provision for staff to be made available to the AA for at least 40 hours per week in return for payment. What the AA does with the staff made available is irrelevant: payment is made for making them available. The provision of a 4 week notice period suggests to me that the parties recognised that the work might run out and the AA would no longer wish to pay for the supply of staff it was no longer able to use. Taken together those provisions suggest to me that so long as Mr Bessell was present and available, the AA had to pay whether or not work was available for him to do. If however Mr Bessell was working for more than 40 hours then overtime payments would be due.

The Dragonfly/DPP contracts provided that Dragonfly should `provide the Services of a Consultant to the Client'. "Services" was defined by reference to the description in the schedule which normally read "specialist tester". The schedule specified "Standard Weekly Hours : 40 hours" and set an overtime

rate. It seems to me that the draftsman's use of the capitalised "Services" was a mistake or at best confusing, but that the intent was that payment should be made for the supply of Mr Bessell by reference to the time for which he was provided.

Putting these together it seems to me that the terms of the notional contract would (on the embodied arrangement approach – and at this stage considering only the formal contracts) have provided for payment for Mr Bessell's availability for work rather than simply for his working hours, together with payment when he worked overtime. That conclusion is in particular consistent with the notice periods in the relevant contracts – without an obligation to pay for availability what was the point of the notice periods?

It seems to me that in practice (see 7(xiii) above) Mr Bessell was very rarely left twiddling his thumbs and so payment was hardly ever made in respect of `availability' rather than work. His billed time generally reflected only time spent working although there may have been some flexibility or averaging in some weeks. Thus there was no conduct materially varying these formal contract terms.

In relation to this heading of the notional contract the two approaches lead me to different conclusions. If I ask: what would have been agreed? I conclude that Mr Bessell would have been paid only for the days (or hours) actually worked: he would have accepted that so both sides would have so provided in the contract.

But if I ask what the arrangements were I find that nothing in the practice varied the agreement between the parties because the requirement to pay simply for availability never arose and was never tested. Thus the "arrangements" included payments for availability rather than just for work done and the notional contract in that basis would have had the same provision.

(7) In relation to the first and third projects Mr Bessell would have been required to work most of his time at the AA's premises. To be there was necessary to make any of the contracts in relation to that period work. It would have been an implied term of the contracts and would on any view have been a term of the notional contract. For the AA.com project he would have been required to work at the AA's premises to the extent necessary to do the testing properly.

(8) There would have been no provision for pension, holiday pay or sick pay.

(9) There would have been no provision for appraisal.

65. I now turn to consider whether, under each of these notional contracts Mr Bessell would have been an employee.

Preconditions

66. I find that the first two *Ready Mixed Concrete* preconditions were satisfied:-

(i) the contracts would have been for the personal service of Mr Bessell in return for remuneration. The limited possibility of substitution would not have prevented them being for contracts for his services;

(ii) The right of the AA to direct through the operation of the team and the guidance of the team manager seems to me to be enough, in the case of a skilled professional man, to be able to say that there was sufficient control. Mr Smith argued that there is a difference between a right of control and simply co-ordinating the work of a worker. But I have found that the notional contract would contain provisions requiring Mr Bessell to be subject to the guidance of his team and team manager. That it seems to me is a sufficient right of control.

I therefore conclude that subject to the third condition it was possible for these contracts to be contracts of employment.

Mutuality

67. In relation to the question of mutuality in relation to any one of the series of notional contracts the question of obligations to offer or accept extensions or further contracts is irrelevant.

68. I concluded at para 59 above that the mutuality condition was satisfied by an obligation to work in return for an obligation to remunerate. That condition is satisfied by the notional contracts. I also concluded that a requirement to make work available (or to pay when it was not) was a significant pointer (a touchstone) towards employment. At paragraph 64(6) above I conclude on the embodied contract approach that such a requirement would have been included in the notional contract. Thus on that basis (and so far income tax purposes) there was a clear pointer towards employment.

But on the what-would-it-have-contained approach I concluded that the notional contract would have obliged the AA to pay only for work done. That may therefore point away from, or put a doubt over, whether it was a contract of employment. However in these circumstances it is not in my view a serious doubt because it is compensated by the fact that work always was available to the "tail end charlies" and that it was known that it would be available during the period of the contract.

69. I note that if I am wrong in my conclusion of law and an obligation on the employer to provide work or to pay where there is no work is a necessary condition for there to be employment, and if I am right at paragraph 64(6) above about what the contract would have contained, and if the what-would-it-have-contained is the right approach at least for income tax purposes, then for income tax purposes (but not for NI purposes) the condition for the application of schedule 12 FA 2000 would have failed.

70. I now turn to the other factors which may indicate employment or consistency or otherwise with employment:-

(i) the very limited right of substitution is not inconsistent with employment and does not point strongly away from it;

(ii) the degree of control was that which one would expect from a skilled professional employee and points towards employment;

(iii) the intention of the parties as regards whether or not there was to be an employment seems irrelevant;

(iv) the nature of the work required Mr Bessell to use the AA's computer and premises. That use therefore does not point to employment. Mr Bessell provided some of his own equipment. That points marginally away from employment;

(v) Mr Bessell, via Dragonfly, bore the costs of training and phone lines. These were not significant costs. They point only weakly away from employment;

(vi) Mr Bessell undertook work for only one other client, the nursery, in the period and that work did not provide a significant point of his income. This is a weak pointer away from employment.

(vii) Mr Bessell's ability to increase his profit during the period of a contract was limited. He suffered the risks associated with being paid on invoice but during the course of each contract in my view risked little economically and had little opportunity to increase his profit. He risked the costs associated with having no sick pay. He negotiated a higher daily rate of pay, and accepted lower rates when the market turned down. These factors point only weakly away from employment.

71. Overall I find nothing which points strongly to the conclusion that Mr Bessell would have been in business on his own account; by contrast when I stand back and look at the overall picture I see someone who worked fairly regular hours during each engagement, who worked on parts of a project which were allocated to him as part of the AA's teams, who was integrated into the AA's business, and who had a role similar to that of a professional employee. Mr Bessell did not get paid for, or go to

work to provide, a specific product; instead he provided his services to the AA to be used by them in testing the parts of a project which from time to time were allocated to him. He was engaged in relation to the work to be done on a specific project but not to deliver anything other than his services in providing testing in relation to that project. In my opinion he would have been an employee had he been directly engaged by the AA.

72. I therefore dismiss the appeal.

CHARLES HELLIER
SPECIAL COMMISSIONER

RELEASED: 11 December 2007

Authorities referred to in skeletons and agreed bundle of authorities and not referred to in the decision:-

Bank voor Handel en Scheepvaut NV v Administrator of Hungarian Property [1954] 2 WLR 867
Global Plant Ltd v Secretary of State for Health and Social Security [1971] 3 All ER
Massey v Crown Life Insurance [1978] 2 All ER 576
Barnet v Brakyn (HMIT) [1996] STC 716
McManus v Griffiths [1997] 70 C 218
Stuncroft v Havelock [2001] EAT/1017/00
Tilbury Consulting Limited v Giltens [2004] STC (SCD) 72
FS Consulting Limited v McCaul (2002) STC (SCD) 138
Lime-IT Limited v Justin (2003) STC (SCD) 15
Ansell (2004) UKSC SPC 425
Parade Park Hotel v HMRC (2007) UKSC SPC 599
Island Consulting Ltd v HMRC (2007) UKSC SPC 618

MKM COMPUTING LTD v REVENUE & CUSTOMS COMMISSIONERS (SpC653) (2007)

Sp Comm (Charles Hellier) 11/12/2007

TAX - AGENCY - EMPLOYMENT

CONTRACTS OF AGENCY : CONTRACTS OF EMPLOYMENT : EMPLOYMENT STATUS : INDEPENDENT CONTRACTORS : NATIONAL INSURANCE : PAYE : SERVICE PROVISION : DIFFERENCE BETWEEN CONTRACT FOR SERVICE AND CONTRACT OF SERVICES IN TAX CONTEXT : TAX LIABILITY : Sch.12 FINANCE ACT 2000 : Sch.10 para.1 FINANCE ACT 2000 : reg.6 SOCIAL SECURITY CONTRIBUTIONS (INTERMEDIARIES) REGULATIONS 2000

For the purposes of liability to pay National Insurance contributions and PAYE, the court considered how to determine whether a work arrangement was a contract for service or a contract of services, and established that, in the instant case, the conditions in the Finance Act 2000 Sch.12 and Sch.10 para.1 and in the Social Security Contributions (Intermediaries) Regulations 2000 reg.6 were met.

The appellant company (M) appealed against a decision and two determinations made by the respondent commissioners under the IR35 provisions introduced by the Income Tax (Earnings and Pensions) Act 2003 that it was liable to National Insurance and PAYE on money received by its sole director (E) in return for his services to another company (L) as a contract analyst programmer.

M had agreed to make E's services available to an agency, and the agency had, in turn, reached an agreement for the supply of those services to L.

L provided databases for the insurance business and managed peaks and troughs in the demand for the services of analysts and programmers by using contractors.

It had entered into a written agreement with the agency to use E's services for 26 weeks, but the agreement had been extended 13 times and had run for two-and-a-half years.

M had delivered weekly invoices to the agency.

He had worked as part of a team, attending every day at fixed times, performing tasks allocated to him by his team manager and reporting progress to the managers and the team.

The commissioners had determined M's liability on the basis that if E had contracted with L directly, he would have been found to be an employee in respect of his earnings with L.

They had found that E met the conditions in the Finance Act 2000 Sch.12 and Sch.10 para.1 and in the Social Security Contributions (Intermediaries) Regulations 2000 reg.6.

HELD: (1) On the facts, under a notional contract, E would have been an employee because he would have been allocated tasks, would have provided his own work to do those tasks, and would have been paid for a 37.5 hour week in the same way as other expert-skilled, independently-minded professionals who worked for L on fixed term contracts.

On the evidence, L regarded the arrangement with the agency as being for the supply of E's services only, and whilst they may have accepted a substitute if he had been unable to work, they did not regard themselves as being bound to do so.

The conditions in Sch.12 of the Act and in reg.6(1) of the Regulations were fulfilled.

(2) There was a potential difference between the effect of Sch.10 para.1(1)(c) of the Act and reg.6(1)(c) of the Regulations.

The latter appeared to require the notional contract between the client and the worker to be constituted by the arrangements: "had the arrangements taken the form of a contract".

There was no requirement to consider whether anything else would have been included in the notional contract.

By contrast, Sch.10 para.1(1)(c) may require a wider enquiry into what the terms of a direct contract between the client and the worker would have been if there had been such a contract; there was no limitation in the words "if the services were provided under a contract directly between the client and the worker", Usetech Ltd v Young (Inspector of Taxes) (2004) EWHC 2248 (Ch), (2004) STC

1671 and Synaptek Ltd v Young (Inspector of Taxes) (2003) EWHC 645 (Ch), (2003) STC 543 considered.

Those authorities demonstrated a difference of approach and that difference existed, at least in theory, even when it was acknowledged that the "arrangements" were not limited to the words of formal contracts, but included all relevant circumstances.

(3) A good starting point when considering whether a contract was one of employment was to consider the mutuality test, the control test and the inconsistency test, Ready Mixed Concrete (South East) Ltd v Minister of Pensions and National Insurance (1968) 2 QB 497 applied.

The mutuality and control tests were not rigid, but depended on individual circumstances, and the court considered relevant aspects of those tests in the context of the difference between a contract for service and a contract of services, Usetech and Morren v Swinton and Pendlebury BC (1965) 1 WLR 576 considered.

Having considered whether those tests were satisfied, all the circumstances had to be considered, including whether the taxpayer was in business on his own account.

That did not involve a mechanical exercise of running through items on a checklist, but involved viewing all the details from a distance and making an informal, qualitative appreciation of the whole.

In the instant case, the court resolved the issue by considering first what the terms of the hypothetical contract between L and E would have been, and second whether, if that hypothetical contract had actually existed, E would have been L's employee.

Appeal dismissed

Counsel: For the appellant: Non-counsel representative For the respondents: Non-counsel representative
Solicitors: For the appellant: Odos Consulting

LTL 18/1/2008 (Unreported elsewhere)

Judgment: Official - 25 pages

Document No. AC0116047

Spc00653

Income tax – Worker supplied through intermediaries – "IR 35" – Schedule 12 FA 2000 – Whether circumstances were such that had the services been provided under a contract directly with the worker, the worker would have been an employee – Held : yes

National Insurance – Worker supplied through intermediaries – "UR 35" – SI 2000/727 Regulation 6 – Whether circumstances were such that had the arrangements taken the form of a contract directly with the worker, the worker would have been an employee – Held : yes

THE SPECIAL COMMISSIONERS

M K M COMPUTING LTD **Appellant**

- and –

THE COMMISSIONERS FOR HER MAJESTY'S REVENUE & CUSTOMS Respondents

Special Commissioner: CHARLES HELLIER

Sitting in public in London on 26 September 2007

Mr C Whittaker of Odos Consulting, for the Appellant

Mrs C D Cumming, Inspector of Taxes, for the Respondents

DECISION

1. Martin Ellwood is the sole director of, and owner of 50 per cent of the shares of, MKM Computing Ltd ("MKM"). In September 1998 the Appellant agreed to make Mr Ellwood's services available to Proactive Appointments Ltd ("Proactive") a company engaged in the business of making contract workers available to its clients. Proactive agreed with London General Holdings Ltd ("LGL") to make Mr Ellwood's services available to LGL. Mr Ellwood rendered his services as a contract analyst programmer for the benefit of LGL under these arrangements. The arrangements continued as the result of a number of extensions until 2002.

2. On 11 June 2004 the Respondents made a Decision and two Determinations under what is commonly called the IR 35 legislation. They concluded that the circumstances were such that had Mr Ellwood been directly contracting with LGL the nature of the arrangements would have led to the conclusion that he was an employee and accordingly that, under the IR 35 legislation the Appellant was liable to NI and PAYE. The Appellant appeals against that Decision and those Determinations.

3. The Decision appealed against relating to National Insurance Contributions and is:

> "That Mr M Ellwood is treated as an employed earner in respect of his engagement with MKM Computing for the period 6/4/2000 to 5/4/2002. That MKM Computing Ltd is liable to pay primary and secondary class one contributions in respect of the earnings from that engagement.
>
> The amount MKM Computing is liable to pay in respect of this engagement is £6,316.45."

4. The Determinations appealed against relate to PAYE. The first is for the year 2000-01 and is for £8,086.40; the second is for the year 2001-02 and is for £13,012.00.

5. There was no dispute as to the amounts involved. The only issue before us was whether the conditions in the relevant pieces of legislation for the making of the Decision and Determinations were satisfied : in particular whether, had Mr Ellwood contracted directly with LGL, he would have been an employee.

<u>The Statutory Provisions</u>

6. For the relevant periods the legislation relating to direct tax was contained in Schedule 12 FA 2000. It provided so far as relevant to this appeal that where an individual or an associate receives from an intermediary (it is agreed that the Appellant is an intermediary for those purposes) or has rights to receive from an intermediary a payment or benefit not taxable under Schedule E then the intermediary is to be treated as making a payment chargeable to Schedule E of the amount of that

payment or benefit. The provision apply where para 1(1) Schedule 10 applies, namely:-

> "(a) an individual ("the worker") personally performs, or is under an obligation personally to perform, services for the purposes of a business carried on by another person ("the client")".

Pausing there, this provision was satisfied. Mr Ellwood personally performed services for the purposes of LGL's business.

> "(b) the services are provided not under a contract between the client and the worker but under arrangements involving a third party ("the intermediary")."

Pausing again, this condition was also satisfied: Mr Ellwood had no contractual relationship with LGL. His services were provided under arrangements involving the Appellant and Proactive. Each of them were third parties.

> "(c) the circumstances are such that, if the services were provided under a contract directly between the client and the worker, the worker would be regarded for income tax purposes as an employee of the client."

It was this last condition which was in dispute in the appeal.

7. Before leaving the income tax provisions of Schedule 10, I should note the provision of paragraph 1(4):

> "(4) The circumstances referred to in sub-paragraph (1)(c) include the terms on which the services are provided, having regard to the terms of the contracts forming part of the arrangements under which the services are provided."

8. The National Insurance provisions to be found in regulation 6 of SI 2000/727 provide that a worker will be treated as in employed earner's employment and receiving benefits calculated in accordance with regulation 7 of that statutory instrument where the three conditions in regulation 6(1) are satisfied. Subparagraphs (a) and (b) of regulation 6(1) are identical to subparagraphs (a) and (b) of paragraph 1(1) Schedule 10 set out above. Paragraph (c), the third condition, is, strangely, phrased differently:

> "(c) the circumstances are such that, *had the arrangements taken the form of a contract* between the worker and the client, the worker would be regarded for the purposes of Parts I to V of the Contributions and Benefits Act as employed in employed earners employment." (My italics).

9. There is to my mind a potential difference between the effect of paragraph 1(1)(c) Schedule 10 and regulation 6(1)(c). It is this: regulation 6(1)(c) appears to require the notional contract between the client and the worker to be constituted by the arrangements: "had the arrangements taken the form of a contract". Thus potentially there is no requirement to consider whether anything else would have been included in the notional contract. By contrast paragraph 1(1)(c) Schedule 10 may

require a wider enquiry into what the terms of a direct contract between client and worker would have been had there been such a contract: there is no limitation in the words "if the services were provided under a contract directly between the client and the worker" to contract terms which are encompassed in the arrangements or the circumstances.

10. In *Usetech Ltd v Young (HM Inspector of Taxes*) 2004 TC 811, Park J did not however see any difference between the two formulations. At paragraph 35, after reciting the relevant extracts he said:

> "The two wordings are not identical, but the meanings are. There was not a direct contract [between the parties in that case] but the provisions require it to be assumed that there was. What would it have contained? …".

It seems to me that Park J is there saying that both provisions require a determination of what such a contract would have contained from a consideration of all the circumstances, rather than the construction of a contract whose content is limited to the arrangements. At paragraph 9 he says:

> "subpara (c) involves an exercise of constructing a hypothetical contract which did not in fact exist, and then enquiring into what the consequences would have been if it had existed. There may be room in some cases for dispute about what the hypothetical contract would contain, and in the present case there is …".

11. On the other hand, in *Synaptek v Young (HM Inspector of Taxes*) (2003) 75 TC 51, Hart J seemed to adopt the more limited approach. That case however dealt only with the provision of regulation 6 and Hart J makes no reference to the corresponding provisions of Schedule 10. At paragraph 11 he says:

> "… The inquiry which Regulation 6(1) directs is in the first instance an essentially factual one. It involves identifying first, what are the "arrangements involving an intermediary" under which the services are performed, and, secondly what are the "circumstances" in the context of which the arrangements have been made and the services performed. *The legal hypothesis which then has to be made is that the arrangements had taken the form of a contract between the worker and the client."* (my emphasis).

This is potentially a different approach to considering what would the contract have contained? It seems to me that this difference exists at least in theory even when it is acknowledged that the `arrangements' are not limited to the words of the formal contracts between the relevant parties but include all relevant circumstances (see para 47 in *Usetech*). What actually happened will be part of the arrangements: the practice may indicate a variation in the formal agreements it may also illuminate the formal agreements or indicate something which falls short of contractual rights and duties. But even where account is taken of all the actual arrangements there may be a difference between the notional contract formed by encapsulating those arrangements

and the notional contract whose terms would be determined by asking "What would have been agreed?"

12. I shall return to this issue later but I note that Park J, at paragraph 1(4) said: "However no-one has suggested to me, nor do I consider, that that [difference] or the other minor differences between the two statutory provisions affects this case or open a possibility of the case being decided one way for NICs and another way for income tax and corporation tax."

13. I now turn to the facts to identify the "arrangements" involving the intermediary and the circumstances in which those arrangements existed and the nature of the services provided by Mr Ellwood.

The Evidence and Findings of Fact

14. I heard oral evidence from Mr Ellwood and from Paul Jarrett who was IT Director at LGL during the relevant period. Both provided witness statements. I also had before me a statement of facts not in dispute, copies of contracts and their extensions between the Appellant and Proactive, and between Proactive and LGL. There were also copies of invoices, of a note of a meeting between the Respondents' officers and Mr Jarrett, and of some correspondence between the Appellant on LGL in 2002. I set out below my principle findings of fact.

Mr Ellwood, the Appellant and LGL

15. Mr Ellwood was the sole director of the Appellant. He holds 50 per cent of its shares. His wife was the company secretary and the only other employee. She held the other half of its shares.

16. Mr Ellwood is a skilled analyst programmer. His particular expertise lies in programming mid-range computers. The services he performed at LGL related to those types of computer. His personality and skills were much appreciated by those at LGL.

17. LGL's business includes the provision of databases for the insurance business of its clients. There are entities such as Comet, Toyota or motor traders who provide warranty or insurance packages. Its business includes fronting calls for the public purchasers of their clients' products. The demands of its clientele changed rapidly and demands were often made for new and different services. The IT department had to react speedily to the clients' demands. This lead to peaks and troughs in the demand for the services of analysts and programmers. Its IT department had permanent employed staff. At times of greater demand these people were supplemented by external resource in the form of contractors. LGL used Proactive to obtain such contractors.

18. MKM advertised in yellow pages, had its own notepaper and website and prepared accounts which properly encompassed the income from LGL. From 25 February 2002 Mr Ellwood had the use of a laptop computer provided by MKM.

19. There was no evidence that MKM had undertaken any other material activity in relevant period other than providing Mr Ellwood to Proactive. MKM had no other employee with Mr Ellwood's skills.

The contracts

20. On 16 September 1998 Proactive wrote to LGL confirming that, on the basis of their attached Terms and Conditions they would provide the services of a Contract Analyst Programmer. The letter then set out the following:

"Name of Contractor:	Martin Ellwood
Position:	Analyst/programmer
Start Date:	21 September 1998
Finish Date:	19 March 1999
Contract period:	26 weeks
Notice period:	4 weeks from either party
Hours per week:	37½ hours
Hourly rate:	[£ a specified sum]"

The terms and conditions attached included the following provisions:-

> "3. … d) [Proactive] may terminate the Assignment of [LGL] is in wilful default … becomes insolvent or of a petition is appointed for its winding-up …
>
> (e) [Proactive] reserves the right to replace the Worker [defined as `staff assigned from time to time by [Proactive] to provide services for [LGL]] with another of similar ability and experience should for whatever reason the current worker be unable to complete the Assignment. The replacement Worker to be mutually approved by [LGL].
>
> (b) It is the responsibility of [LGL] to supervise and control the Worker; to ensure that the Worker undertakes the work for which he or she was hired; to make sure that safe working conditions are provided; to ensure that the Worker is adequately covered by insurance whilst the Worker is in the employ of [LGL]."

21. There are also provisions relating to timesheets, invoices, payments, confidentiality and the poaching of the Worker by Proactive's client.

22. Shortly before the end of the contract period set out above an extension of the contract for 26 weeks was agreed. Subsequent contiguous extensions of varying

lengths were agreed which ran until 29 March 2002. Neither of the parties were compelled to offer or accept any extension.

23. On 17 September 1998 (the day after the date of Proactive's letter to LGL described above) Proactive and the Appellant signed a written form of contract. The document was headed:

> "Contract between MKM Computing Limited
> for the services of Martin Ellwood
> and
> Proactive Appointments Limited"

The front page then provided:

> "This contract confirms [Proactive's] agreement with you that MKM Computing Limited … will provide services to and for the benefit of the undermentioned Client based on the Terms and Conditions below and attached.

Name of Company (the Client)	[LGL]
…	
Position ("The Assignment")	Contract Analyst Programmer
Report to	David Wainwright
Start Date	21 September 1998
Final Date	19 March 1998
Hourly Rate	£ [so much] per hour
Weekly Hours	37½ hours
Length of Contract	26 weeks
Notice Period	4 weeks from either party".

24. The attached Terms and Conditions appear to be in a standard form and to envisage more than the one Assignment described on the front sheet. There are provisions relating to the provision of time sheets signed by the Client and for the payment of fees – which "will be delayed no longer than 1 month." Payments may be withheld if MKM fails to work to the required standard or is unable to complete the assignment. MKM is required to have Employer's Liability and Public Liability Insurance. Clause 9(d) provides that Proactive may terminate with pay in lieu of notice in the event of unsatisfactory work by MKM's staff. There are restrictions upon MKM or its "staff" supplying other services to the Client.

25. Shortly before the Finish Date set out on the front sheet an extension of the contract for 26 weeks was agreed. Subsequent contiguous extensions were signed which ran until 29 March 2002. Neither party was compelled to offer or accept any extension.

The Work Done

26. In the period 8 April 2000 to 6 April 2002 MKM delivered, with 9 exceptions, weekly invoices to Proactive. The exceptions related to weeks when Mr Ellwood did not work because, for example, he was on holiday. The majority (55 out of 94) of the invoices were for 37.5 hours work with a normal range of between 30 and 39 hours. The arithmetic mean was 37.8 hours for those weeks he worked. The invoices were for `Programming Services' and specified the number of hours and rate per hour.

27. At LGL Mr Ellwood worked within a team. A team had a project manager. 6 project managers reported to Mr Jarrett, the IT director. Mr Ellwood was allocated tasks by his team manager. There tasks included: understanding the user requirements by speaking to client managers and employees, drafting requirement documents, writing software, developing software, testing software, carrying out quality assurance and installing the software. The allocation of the tasks did not include instruction as to how to perform them.

28. Mr Jarrett would generally use contract staff for particular projects. Permanent employees were allocated tasks more fluidly. Mr Ellwood worked on a succession of such projects in the relevant period. Each contractual period related to one or two projects only. The periods of renewal of the proactive/LGL contract sometimes did and sometimes did not encompass the time actually needed to complete a particular project.

29. Mr Jarrett, having decided that he needed extra contract staff would arrange for an agency like Proactive to supply them. Generally the nature of project for which he required staff would be communication to the agency. Towards the end of the period of a contractor's contract there would be a telephone conversation with the agency about renewing the contractor's contract. Mr Ellwood would hear formally from the agency if a renewal of the contract was being offered, but would as the result of informal conversations at LGL have some idea of whether it would be and what projects would be involved. In the relevant period the contract was extended some 13 times.

30. The period for any extension was fixed by Mr Jarrett by reference to his estimate for the time needed for the work he had in mind. He would reach that estimate by discussion with those involved at LGL including at times the contractor who might be involved in the project. Mr Ellwood was involved in some discussions for future projects in which he became involved. Where a project over-ran its estimate the contractor's contract might be extended. This happened with a number of the projects on which Mr Ellwood was involved.

31. If a project were to finish early or looked likely to do so Mr Jarrett would have contacted the agency and told it that he would find something else for the contractor to work on.

32. Although when working at LGL Mr Ellwood would spend his time principally on the project or projects which had been assigned to him he would occasionally be asked by people at LGL to help on other matters: for example if a problem arose in relation to something he had previously been involved in; and generally, after consulting Mr Jarrett or the project manager, he would supply the help required as part of his contracted hours.

33. As part of the discussion of a new project with Mr Ellwood there would be discussion of any holiday he wished to take in the projected period for the project. There would be some give and take bearing in mind the LGL time constraints and Mr Ellwood's need for a holiday. Having settled the period he would take as holiday the period for which the contract would be extended would be fixed. He did not submit invoices for those days on which he was on holiday.

34. Mr Ellwood generally attended LGL's premises on working days between 6.45am and 3.30pm. He liked to leave early to avoid the traffic. He said that the client "was sympathetic to traffic difficulties and would let me go early." It was necessary for his work that he was at LGL when others were there : there would be matters he would need to discuss and clarify with other people at LGL. He did not, and was not expected to wander in and out as he pleased.

35. The LGL computer systems were fairly reliable and crashed infrequently. If the system crashed then everyone including Mr Ellwood would sit around for a bit, perhaps read a technical magazine or twiddle their thumbs. Likewise if he arrived at LGL and the overnight back-ups were running late. If Mr Ellwood was in a good mood on such an occasion he said he would not count the downtime as hours to be billed; if he was in a bad mood he said he would charge. I accept that evidence. Given his regular working hours and the consistency of his billed hours I conclude that generally payment was made in respect of such down or unavailable time.

36. If Mr Ellwood's work was defective (he recalled only one such occasion) he would rectify it in his own time.

37. In the Autumn and early winter of 2001 Mr Ellwood was engaged under two 13 week contract extensions for which in each case one of the two specified projects was the EMS Australia Project. After the work had been done on the project in the UK Mr Ellwood went, at Mr Jarrett's instigation, to Australia to train the local personnel and to implement the system which had been written. His expenses of travel were paid by LGL. While he was there he had regular telephone contact with Mr Jarrett, reporting to him how the work was going, Mr Ellwood had prepared a plan and he let Mr Jarrett know how progress was being achieved by reference to that plan. Mr Jarrett said he saw his role as offering help, and, where necessary, the facilitation of help and assistance from elsewhere in the organisation. It was clear to me that Mr Ellwood had been asked rather than commanded to go to Australia, but also clear that Mr Jarrett was monitoring and would guide what he was doing.

38. If the approach of a deadline meant that it might be desirable that more than 37½ hours be spent on a project in a particular week, Mr Jarrett would discuss the need with Mr Ellwood. Mr Jarrett did not feel able to compel Mr Ellwood to work additional hours but would expect an amicable helpful result.

Control

39. Once Mr Ellwood had been given a project he would get on and do it. He was not subject to detailed orders as to how to do what and when. But he was part of a team: he reported his progress to Mr Jarrett or other project managers and discussed what he was doing with other members of the team. Although these interchanges did not consist of giving orders it was clear to me that they would have affected what he did, when he did it, and how he did it.

40. If Mr Ellwood wished to take an unscheduled holiday he would discuss it with the relevant personnel at LGL. Mr Jarrett said, and I accept, that there had been an occasion when he had refused a day off when they had been really up against a deadline.

41. Mr Ellwood's computer programme coding was not reviewed for quality and he was not subject to the employee appraisal system. If his work was deficient he would not be offered a new contract.

Substitution

42. Before the commencement of the first contract Mr Ellwood was interviewed by a member of LGL's staff. He was asked some technical questions. Mr Ellwood described part of the interview as a check that he had not yet two heads.

43. In a document prepared by Mr Ellwood on 2 April 2002 and signed by Mr Jarrett on 5 June 2002 the relationship between MKM and LGL was described thus:

> "[MKM] has the right to provide a substitution worker in addition to or in place of Martin Ellwood. If a substitute worker were to be proposed [MKM] would be required to satisfy [LGL] that the substitute has the necessary skills, qualifications and experience …"

In the relevant period there was no occasion when Mr Ellwood sent or proposed a substitute for himself.

44. In the course of a meeting with Respondents' officers Mr Jarrett, having been asked what would happen if one day Mr Ellwood said he was going on leave and would send someone in his place, replied that that conversation just would not happen. In cross-examination Mr Jarrett said that if the conversation started his response would depend on the circumstances. Generally he would expect a new contract to be entered into with the agency. If Mr Ellwood were not to turn up he would contact the agency. If the agency sent a Mr Smith and if, having met him, Mr

Jarrett decided that Mr Smith was OK he would expect a new contract with the agency for the provision of Mr Smith. In deciding whether or not to accept Mr Smith, Mr Jarrett said it would have been relevant that Mr Smith was from MKM because Mr Ellwood might well have communicated his knowledge of MKM to Mr Smith: it would give Mr Smith an advantage.

45. Mr Jarrett said that he would not have been concerned if Mr Ellwood had arranged for Mr Smith to conduct some of the work off LGL's premises: if it contributed to the project being done in time he would have been happy. If Mr Jarrett "was not paying it would be no cost" to him and he would not mind.

46. Mr Ellwood said in evidence that he regarded the right for MKM to substitute another person in place of himself as an implicit right in the contract between MKM and Proactive. If for example he had been ill and unable to go to LGL but had found a substitute he would have rung the agency, offered the substitute and proceeded from there.

47. My conclusion is that LGL's management regarded the arrangement it had with Proactive as being for the supply of Mr Ellwood's services only. That was whom they interviewed, and whom later they knew: that was who they thought they would get. Whilst they would consider any proposed substitute they did not regard themselves as being bound to do so, and even if a proposed substitute were interviewed and found acceptable they did not regard themselves as bound to accept him (although had Mr Ellwood been truly unable to perform the expected duties and an acceptable substitute been offered by Proactive I believe that they would have recognised their obligation under clause 3(d) of the Proactive/LGL contract to accept that substitute in place of Mr Ellwood). I found the demeanour and oral evidence of Mr Jarrett on this question more convincing that the statement quoted above signed by him on 5 June 2002: in particular his oral insistence that a substitute would be subject to a new contract indicated to me that he did not regard Proactive as having even a limited right of substitution (but that was without consulting the detailed terms of the Proactive/LGL contract).

48. I find that the highest that Mr Ellwood's expectation can be put at the relevant time is that he had a confident expectation that if he was ill and could find a suitable substitute it was very likely that that substitute would be accepted by LGL. As regards MKM's relationship with Proactive I find that Mr Ellwood would have regarded the question as determined by the terms of the Proactive/MKM contract properly construed.

49. <u>*Other Matters*</u>

(i) No payment was due or was made under any contract when Mr Ellwood was sick or on holiday.

(ii) LGL provided no training for Mr Ellwood. He kept abreast of technical developments by reading in his own time (apart from reading during

occasional downtime of the LGL computers) magazines MKM purchased, and on the internet.

(iii) There was no canteen at LGL. There was a vending machine which Mr Ellwood was able to use.

(iv) Free coffee was available to Mr Ellwood in common with other employees in the early morning.

(v) LGL had car parking facilities. These were limited in number. They were available only to employees once they reached the top of a waiting list. Mr Ellwood was not entitled to use the car parking facilities or to join the waiting list.

(vi) In common with other employees Mr Ellwood had an e-mail address at LGL.

(vii) Unlike employees Mr Ellwood had no right to use the social and sports club.

(viii) Mr Ellwood worked in an open plan office at LGL alongside other employees of LGL. The vast majority of his recorded time was spent working at LGL's premises, although he did work at home, and there was the trip to Australia.

(ix) Mr Ellwood was not required to provide and use a laptop by LGL nor did it provide one. But, latterly, he used a laptop provided by MKM.

(x) Unlike employees Mr Ellwood was not subject to the LGL appraisal process.

(xi) Mr Ellwood would have been invited as a guest to the Christmas office function but not automatically invited by the LGL HR function as an employee would have been.

(xii) Mr Ellwood completed weekly time sheets which were approved by a member of LGL's staff such as Mr Jarrett and then sent to Proactive. On the basis of the time sheets MKM would invoice proactive. Staff who were LGL employees were clearly not subject to these procedures, although, like contractors, they did record their time against projects for management accounting purposes. These records were reviewed by Mr Jarrett as part of his overall control of the projects.

(xiii) It would not have been possible for a substitute sent by Mr Ellwood in his place to get into LGL's building to go to work at Mr Ellwood's desk without the prior issue of a relevant pass.

(xiv) Mr Ellwood worked for no one else in the relevant period.

The Case Law Tests in relation to Employment

50. I was referred to a number of cases on the difference between a contract for service and a contract of services. I take from them the following principles:-

(i) There is an irreducible minimum for a contract of employment. That minimum was described in *Ready Mixed Concrete v Minister of Pensions and National Insurance* (1967) 2 QB 497, MacKenna J there set out three necessary conditions for a contract of services:

> "(i) [the mutuality test] The servant agrees that in consideration of a wage or other remuneration, he will provide his own work and shall in the performance of some service for his master;
>
> (ii) [the control test] 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 inconsistency test] the other provisions of the contract are consistent with its being a contract of service."

These tests are a good starting point when considering whether a contract is one of employment and it is important that mutual obligation and control are identified before moving on to consider other factors (see Buckley J at paragraph 23 in *Montgomery v Johnson Underwood* Ltd (2001) EWCA Civ 318). Whilst the tests are necessary conditions for employment the nature and extent of the requirements for mutuality and control are not rigid but depend upon the circumstances. I discuss this below. MacKenna's third condition has to my mind much in common with the overall picture and in business on his own account tests I describe below. In particular the third test the inconsistency test seems to me to be capable of embracing the `overall picture' approach and the use of the various indicia. But the mutuality test and the control test require some further comment.

(ii) Mutuality. There are two aspects to this. First that there is some mutuality of obligation. Second that the contract is for "his own work" – for his personal service. The second aspect gives rise to the question as to whether a right for the taxpayer to substitute another person in his place can prevent a contract being one for service. I discuss that below. The first aspect clearly covers the requirement that there be an obligation on the one hand to work and on the other to remunerate. The more difficult question is whether there is or it also encompasses an obligation for the employer to provide work (or to pay when there is no work to be done). It seems to me that the former is a condition for there to be employment; the latter a strong pointer towards employment. (See *Cornwall County Council v Prater* 2006 EWCA Civ 102

per Mummery LJ at paragraph 40(5), Longmore LJ at paragraph 43 and Lewison J at paragraph 51; by contrast Park J in *Usetech* regards an employer's obligation to provide work or to pay if there is none as a "touchstone" of employment – see paragraph 60.)

(iii) Substitution. The contract must be for personal service. Nevertheless a limited or occasional power of delegation or right to substitute another person may be consistent with a contract of personal service. (*Usetech* : paras 49-52). In particular it seems to me that a contract containing a right to substitute if and only if the `employer' consents is, until consent is given a contract which plainly satisfies the personal service condition, although the presence of that right may be an indicium which points towards self-employment.

(iv) Control. MacKenna J says "control in a sufficient degree to make that other the master". That is no indication that absolute control is required. In *Morren v Pendlebury Borough Council* (1965) 1 WLR 576 Parker C J indicates that in the case of a professional person there can be cases where there is no question of the employer telling him how to do the work in the absence of control and direction "in that sense" can be little, if any use, as a test. It seems to me that something which can be called control is a necessary feature of an employment relationship even one for a skilled employee; but the nature of the power of control which suffices may differ with the nature of the job: the hospital will tell the surgeon to try to meet the targets; the company will tell the ship master where to take the ship; the school governors may tell the headmaster or headmistress how many staff he or she may engage.

(v) Having considered whether these conditions are satisfied, the tribunal should then consider all the circumstances and in doing so may use the following tests and guidance.

(vi) To ask whether the taxpayer is in business on his own account? (*Market Investigations Ltd* see below)

(vii) "In order to decide whether a person carries on business on his own account it is necessary to consider many different aspects of that person's work activity. This is not a mechanical exercise of running through items on a check list 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 making an informal, considered qualitative appreciation of the whole … Not all details are of equal weight … The details may also vary in importance from one situation to another." (*Hall v Lorimer* (1993) 66 TC 349 at 375F.)

(viii) Nevertheless the consideration of certain indicia which may point one way or the other may be helpful in considering that picture. (*Lee Ting Sang v*

Chung Chi-Keung 2 AC 374, and *Hall v Lorimer*). Those indicia include those mentioned by Cooke J in *Market Investigations Ltd v Minister of Social Security* (1969) 2 QB 173. The following may therefore be relevant:-

(a) does the taxpayer provide his own equipment?
(b) does the taxpayer hire his own helpers?
(c) what degree of financial risk or opportunity for profit does the taxpayer have?
(d) what degree of responsibility for investment and management does the taxpayer have?
(e) is the taxpayer part and parcel of his "employer's" organisation see *Hall v Lorimer*);
(f) the degree of control to which the taxpayer is subject;
(g) termination provisions – termination on notice may be a pointer towards employment in some cases (it was found to be so in *Morren v Swinton* (1965) 1 WLR 576 but found to be neutral in *McManus v Griffiths* 1997 70 TC 218);
(h) the intention of the parties; and
(i) the extent of mutual obligations and of the "employer's" obligation to provide work or pay in lieu of so doing.

Discussion

47. I shall now consider first what the terms of the hypothetical contract between LGL and Mr Ellwood would have been, and then consider, against conditions for, and the indicia of, employment and self-employment developed in those cases whether, the circumstances were such that if that hypothetical contract were in existence, Mr Ellwood would have been an employee of LGL. I have endeavoured to take into account the submissions of the parties in the discussion below without rehearsing them in detail. Mr Ellwood was the sole director of MKM it seems to me as it did to the Special Commissioner in *Netherlane* [2005] SpC 457 proper in the absence of any form of contract between him or MKM, straightforward effectively to treat him as a party to the Appellant's contract in conducting this exercise.

The notional contract

48. It is important to consider the terms of the notional contract because some of the more important conditions for, and indicia of, employment or otherwise flow from the legal rights and duties of the parties rather than from the general nature of the relationship between the parties.

49. I start by asking myself the question posed by Park J at paragraph 35 of his judgment in *Usetech*: had there been a contract between LGL and Mr Ellwood, "What would it have contained?" but I note below when the alternative approach would give a different result. In my view there would have been a series of fixed term contracts each of which would have contained the following provisions:-

(1) It would be for a fixed term (mirroring for each engagement the term of the corresponding contracts between Proactive and LGL, and Proactive and MKM).

(2) It would be terminable early (a) on 4 weeks notice from either party. That is because the contract confirmation letter between Proactive and LGL provides for 4 weeks' notice from either party, and the front page of the Proactive/MKM contract made the same provision. There would also be provision for termination in other circumstances such as default, insolvency or misconduct.

(3) It would be for Mr Ellwood to work as an Analyst/Programmer on the projects specified for the assignment. This seems to me to be clear from (i) the definition of Assignment in the Proactive/LGL contract:

> "The Assignment – means the services which have been specified by [LGL] to [Proactive] and are allocated by Proactive to the Worker for performance",

(and the corresponding definition in the Proactive/MKM contract), together with (ii) my factual finding that LGL did indicate to Proactive, and Mr Ellwood knew, the project for which the worker was required. I come to that conclusion despite the absence of any express requirement in either contract that the Assignment be performed. That requirement is to my mind implicit in both contracts and was what happened in practice. The contractual requirement would be to work on the projects, not for the delivering of a completed project.

What I have said hitherto under this heading flows directly from the arrangements (reflecting the formal agreements and the obligations undertaken in practice) but if I am asking the question : what would have been contained in such a contract? There would in my view have been a further requirement namely for Mr Ellwood to provide assistance in such other matters as might arise from time to time within Mr Ellwood's competence but only for a small part of his working time.

(4) Except for periods of holiday specified in the contract or later agreed by LGL and periods of sickness Mr Ellwood would work on average for about 37½ hours each week. He would be paid at the hourly rate for the hours worked. (I deal at (8) below with the question as to whether he would be paid for working or being available to work.)

Whereas both the Proactive/LGL and Proactive/MKM contracts specify Hours Per Week of 37½, it was clear that these provisions had been varied by the conduct of the parties: holidays were factored into a contract renewal (and not treated as hours of work) and the actual hours varied around the 37½ hours figure.

(5) Mr Ellwood would work at LGL's premises using LGL's computer systems during hours when those computer systems were generally available and for hours which permitted the discussion and interaction with other people at LGL necessary for the projects he was assigned.

This term is not in the Proactive/LGL contract. (There is a requirement however in clause 7(a) of the Proactive/MKM contract to conform to LGL's normal hours of work.) But it was clear that Mr Ellwood could do the tasks assigned to him only if he was on LGL's premises during fairly normal working hours on most days. That is what was expected and what happened. It was a necessary term of the arrangements. As part of the arrangements it would have been part of a direct contract on either view of the legislative requirement.

Mr Ellwood could also work at home when he could do so effectively.

In relation to the REMS Australia project Mr Ellwood would be required to work in Australia for part of his time on the project.

(6) Mr Ellwood would submit weekly time sheets showing the hours worked in a particular week and would be paid at a fixed hourly rate for that work within 2 months of the end of each month worked. (This follows from clauses 4 and 8 of the Proactive/LGL contract and clauses 4 and 5 of the proactive/MKM contract and what happened in practice.)

(7) There would be no express contractual right to BUPA, PFI, Pension, Sick Pay, Holiday Pay, car parking benefits, or staff parties.

(8) <u>Periods when no work was available.</u>

There is no express provision in the Proactive/LGL of the Proactive/MKM contract dealing with this issue. Whilst those contracts provide for 37½ hours work per week it is clear that that provision was varied by conduct (see paragraph 26 above) so that somewhat more or less than those hours were worked and paid for. The contracts refer to an Assignment but do not expressly limit the work to be done to the assignment and in practice work was done (and the hours paid for) outside the particular assignment. The notice period of 4 weeks could be indicative of an obligation on LGL to continue paying so long as Mr Ellwood turned up even if the expected work had dried up. The evidence before me was that there had not been a situation in which the work had completely dried up so there was no practice to illuminate the agreement.

Mr Jarrett in his evidence gave me the impression that he saw the 4 week notice period as a protection available to LGL if the work dried up. That was indicative of a presumption that LGL would be liable to continue to pay so

long as Mr Ellwood turned up. Mr Ellwood's own fair and candid evidence that when LGL's computer was down he would sometimes charge for his time was an indication that to some extent he regarded the arrangements as providing for continuing payment even when the work dried up. On the other hand he said that if the work were to have dried up he would have `backed off' and agreed to early termination.

The early termination provision of the LGL/Proactive contract enabled LGL to terminate even if the work had not dried up but also provided a measure of protection for Mr Ellwood (and Proactive) in the 4 weeks' notice. It seems to me that the notice period together with the description of the essential terms of the contracts on the first schedules suggest that payment would continue to be made if Mr Ellwood was available to work even if no work was in fact available. On this basis and in view of the actual approach of the parties it seems to me that the arrangements provided for payment for a maximum of 37½ hours in a week so long as Mr Ellwood turned up and was available to do what was allocated to him.

And, if one asks Park J's broader question "What would the contract have contained?" then I believe that each of the fixed term contracts would have contained provision for payment if there had been no work to do. That was how Mr Jarrett appeared to view the contract – that was why he would have sought another project for a contractor if his assigned project ceased – and that was the importance of the 4 week notice period for him. If a direct contract had been negotiated that is what it would have contained.

(9) Control

Clause 7(a) of the Proactive/MKM contract provides that MKM agrees:

> "To co-operate with [LGL]'s staff and accept the direction supervision and instruction of any person in [LGL]'s organisation to whom it is responsible …".

Clause 3(b) of the Proactive/LGL contract provides that it is:

> "the responsibility of [LGL] to supervise and control the Worker …".

The evidence before me led me to the conclusion that Mr Ellwood had not in practice been given orders but in the course of a project to which he was assigned his interaction with others within LGL affected what he did, when he did it and how he did it.

Whilst the covenant in clause 7(a) above is given by MKM it seems to me that it can be taken as applicable to any person MKM supplied and would be applicable to Mr Ellwood as MKM's supplied worker.

Whether one considers simply a contractual embodying of the arrangement or what would have been included in a national contract, I conclude that at a very minimum the hypothetical contract would have required Mr Ellwood to report his progress regularly to persons at LGL, to discuss with such person the content and progress of his work, and to co-operate with them and to adapt the course of his work so as to ensure the most effective progress of the work he was doing as a result of those consultations and discussions.

(10) Substitution

Clause 3(e) of the Proactive/LGL contract provides that:

> "[Proactive] reserves the right to replace the Worker with another of similar ability and experience should for whatever reason the Current Worker be unable to complete the Assignment. The replacement Worker to be mutually approved by the Client."

This gives a limited right of substitution where the Worker is "unable" to perform.

The standard Terms and Conditions annexed to the Proactive/MKM agreement – the agreement bearing in its title the words "for the services of Martin Ellwood" – contain no express provision for the substitution of one worker for another. Those Terms and Conditions impose obligations on MKM to do certain things and impose restrictions on what its staff may do. Mr Whittaker says that the detailed terms and conditions of the MKM/Proactive contract refer to the work being done by MKM's staff (defined he says as employees and representatives of MKM), and that this indicates that it was agreed that persons other than Mr Ellwood could perform the services. I do not agree. The references to MKM's staff in that contract do not expressly refer to an obligation on MKM's staff to provide the services, rather they are restrictions and obligations imposed on the conduct of its staff and so to my mind are to be construed as restrictions and obligation applicable to the member of staff agreed to be supplied, namely Mr Ellwood. In my view the Terms and Conditions contain nothing which varies the terms specified in the front sheet which are for the provision by MKM of Martin Elliott. There is in this agreement no express or implied right for MKM to supply anyone else in his place however able he might be. There was no evidence of practice or conduct in the relevant period relevant to this contract which would indicate variation of the formed provisions of this contract. However, I believe it is likely that if LGL consented to a substitute Proactive would also have consented.

I concluded above that LGL regarded the arrangement as being for the services of Mr Ellwood only and that at the relevant time the most that Mr Ellwood had was an expectation that LGL would consider favourably a substitution introduced by him.

I conclude that if the arrangements had been incorporated into a contract between Mr Ellwood and LGL there would have been no provision under which Mr Ellwood could provide a substitute for his own personal service unless Mr Ellwood was unable to work for LGL and LGL approved the substitute in advance.

I now ask the alternative question: what would the contract have contained? Mr Whittaker says that the evidence showed that had the parties got together and discussed substitution a precise right to substitute would have been agreed and that such a right would therefore have been contained in the notional contract. I agree that if the question had been raised some agreement would have been arrived at. But I do not believe that LGL would have agreed to accept anyone sent along by Mr Ellwood : they valued Mr Ellwood and his abilities, they would have wanted to be sure that they were satisfied that any substitute was as good as Mr Ellwood and could take over what he was doing quickly and without disruption. In my view the right would have been very limited – it would have been to substitute only a person approved in advance by LGL.

A contract of or for services

50. I now turn to consider whether had Mr Ellwood been directly engaged by LGL on the terms of the contract I have discussed above, he would, in the circumstances I have found, have been engaged under a contract of service. I start by considering the various indicia from the case law.

51. Mutuality of obligation

(a) obligation

There was no obligation to renew any of the contracts at the end of their respective terms. But that is not relevant to whether there was mutuality during the period of each fixed term contract. I consider here whether there would have been mutuality during the course of each fixed term.

During each fixed term Mr Ellwood would have been obliged to work and LGL would have been obliged to remunerate him.

I have found, that on either approach to determining the terms of the notional contract that there would have been no obligation to provide work for Mr Ellwood but that there would have been an obligation to pay if work was not available.

(b) for personal service

I have concluded that the notional contract would contain only a very limited right of substitution. The finding that substitution would have been permitted only where LGL approved indicates to my mind that until LGL approved the notional contract was a contract for Mr Ellwood's personal service. In my view that limited right is not sufficient to prevent the contract being one for "his own work".

(c) conclusion

I conclude that the first of MacKenna J's conditions is fulfilled. Under the notional contract it can properly be said that Mr Ellwood would have agreed to provide his own work for consideration.

The lack of a substantial right of substitution in those circumstances is a position towards employment.

Control

52. Mr Whittaker says that although LGL monitored the progress of a project, there is a significant difference between monitoring a worker and controlling him. He points to the evidence of the time Mr Ellwood was in Australia when he reported back to Mr Jarrett but Mr Jarrett's role was to provide help and facilitation for Mr Ellwood not to tell him what to do. He accepts that Mr Ellwood worked fairly standard hours but that was necessary to do the work not because he was commanded to keep those hours. Overall he says that there was not that degree of control present which would have made Mr Ellwood the servant of LGL.

53. Mr Ellwood, in my opinion would have been subject to the kind of control which in the context of a professional employee would be sufficient to say that LGL was his master.

54. Under the notional contract LGL would have had a right to require him to undertake a project in co-operation with other persons at LGL and to adapt the course of his work to ensure the most effective progress as determined by internal discussions. That right would in my view be sufficient in the case of a professional skilled person to say that LGL had a right to control what Mr Ellwood did and, generally when he did it, or to say that he was so subject to LGL's control (albeit exercised through guidance and discussion rather than command) as to make LGL his master.

55. I therefore conclude that the second of MacKenna J's conditions is fulfilled. I also regard the nature of the constraints and guidance to which he was subject as an indication of employment.

Other factors consistent with a contract of service

56. I deal in paragraphs 59 to 69 below with the other indicia but none of them seem to me to permit the conclusion that the contract was inconsistent with a contract of service.

57. Had the contract been simply for the delivery of a particular project – the development, the code, and the implementation that it could have been inconsistent with a contract of service. But it was not, it was for expert time to be spent in the development and delivery of the project. Mr Ellwood was not in the position of a painter engaged to paint a room; he was in the position of a painter employed to paint such parts of the house as his employer would from time to time require.

58. I therefore conclude that none of MacKenna J's conditions was failed, and thus that it is possible for the national contract to constitute one `of service'.

Business Risk

59. Like an employee Mr Ellwood was financially dependent upon one payer. Whilst by working a few extra hours Mr Ellwood could earn more, the scope for extra work was limited. Mr Ellwood was at risk if his work was substandard and there was an occasion when he worked uncharged for hours to remedy a defect. A professional employee he accepted might also work unpaid overtime to remedy a defect, but overall I did think that Mr Ellwood was more at risk on this front than a normal professional employee. Mr Ellwood's wages would have been paid some time after each month and which would be unusual in the case of an employee.

Overall these factors pointed gently away from employment but not vigorously so.

60. Mr Whittaker pointed to the financial risk inherent in final term contracts some of which lasted for only four weeks. That was quite different he said from the position of a normal employee. I agree that it is different from the position of an employee on an indefinite contract, but an employee could also be engaged for a fixed term. If that term were long enough or if the term were extended the employee might acquire statutory employment protection which could fetter the employer's ability to determine the contract, but those statutory rights derive from being an employee and are not a feature of what it means to be an employee. I do not think therefore that the fixed term nature of the engagements is a pointer away from employment. If one views the succession of contracts as a whole then the effect of the arrangements is a continuing notional contract with irregular break points. That would be an unusual form of employment contract today (probably as a practical effect of the employment protection legislation) but it does not to my mind point strongly away from employment.

In business on his own account?

61. Do these financial considerations, the short term nature of the contracts and the other circumstances point towards Mr Ellwood being in business on his own account if engaged under the notional contracts? In my view they do not. Mr Ellwood would have had little opportunity to increase his profit and was not conducting any form of undertaking. His position was quite different from the mixer in *Lorrimer*: he worked for one company only for a succession of engagements over many years.

Equipment and expense

62. Mr Ellwood's work was mainly on LGL's computer. It had to be. This factor is neutral. A laptop was provided by MKM in 2002 – towards the end of the period under appeal – and it paid for Mr Ellwood's continuing education. These factors together point somewhat away from employment but not substantially.

On the other hand when Mr Ellwood worked in Australia on the Australian project his expenses of travel were met by LGL. It would, Mr Whittaker says not be unusual to pay a decorator for the wallpaper he uses in what would clearly be a contract of service. I also note that a professional firm may charge its clients separately for specific out of pocket expenses. Overall I find that in relation to that project this indicator did not point towards employment but did not point strongly towards self employment.

Benefits

63. The lack of contractual benefits such as holiday pay, sick pay, car parking or pension arrangements point towards self-employment.

Termination

64. Termination on notice is less usual in a contract for service although as Mr Whittaker pointed out there will be cases where a notice period will be included: he gave the example of a contract to build a house where there might be provision for early termination on notice if the parties fell out. But, in my view, the weeks' notice provision points more towards employment than self-employment.

Intention of the parties

65. The parties' intention as to whether there should be an employment relationship are clearly irrelevant. Their intention in relation to specific circumstances was in my view relevant to the consideration of the notional contract on the what-would-it-contain basis and has been considered elsewhere.

Part and Parcel

66. I had the impression that while he was working at LGL Mr Ellwood was part and parcel of the organisation. I accept that he was recognised as a contractor rather than as a permanent member of staff, but he sat alongside other members of staff discussed future projects, and was called upon for help in emergencies and worked along with them on the projects as would a permanent employee.

Conclusion

67. Standing back and looking at the whole picture I am left with the distinct impression that under the notional contract Mr Ellwood would have been an employee. He would have been providing his own work to do those tasks allocated to him and would have been paid broadly for a 37½ hour week. To me it appears that his job was working for LGL, not that he made his money by providing something to LGL. He was an expert skilled independently minded professional who worked at LGL and for no one else on terms (as to what he did, when he was there and how his work was organised) which were substantially similar (although not identical) to those applicable to an employee but on fixed term contracts.

68. Accordingly I find that the conditions in Schedule 12 FA 2000 and SI 2000/727 were fulfilled. On that basis I dismiss the appeal against the Determinations.

69. The Decision made in relation to National Insurance decided that Mr Ellwood was to be treated as "an employed earner in respect of his engagement with MKM Computing for the period 6/4/2000 to 5/4/2002. The contracts before me related only to the period up to 28 March 2002 and my decision therefore relates only to that period. This was recognised by the parties and in the agreed statement of facts it was stated that `if the appeal is not upheld, the period in the section 8 decision should be revised to "6 April 2000 to 29 March 2002". Regulation 10 of the Social Security Contributions (Decisions and Appeals) Regulations 1999 gives the tax appeal Commissioners power to vary a decision. Accordingly, given my conclusions as to the satisfaction of the conditions in SI 2000/727 I find that the Decision should be varied as described but otherwise shall stand.

CHARLES HELLIER
SPECIAL COMMISSIONER

RELEASED: 11 December 2007

SC 3029/2006

Authorities referred to in skeleton arguments and the agreed bundle of authorities not referred to in the decision:-

Nethermare (St Neots) Ltd v Gardiner and Another (1984) ICR 612
McManus v Griffiths (1997) 70 TC 218
Tilbury Consulting Ltd v Giltens (2003) SpC 390
Netherlane Ltd v York (2005) SpC 457

FIRST WORD SOFTWARE LTD v REVENUE & CUSTOMS COMMISSIONERS (SpC652) (2007)

Sp Comm (AN Brice (Chairman)) 2/12/2007

TAX - EMPLOYMENT

COMPUTERS : CONTROL : EMPLOYMENT STATUS : INFORMATION TECHNOLOGY : INTERMEDIARIES : MUTUALITY OF OBLIGATION : NATIONAL INSURANCE CONTRIBUTIONS : PAYE : PROVISION OF SERVICES THROUGH INTERMEDIARY : WORKER REGARDED AS EMPLOYEE IF SERVICES PROVIDED DIRECTLY TO CLIENT : COMPUTER CONSULTANTS : LEGACY SYSTEMS : MIGRATION : IR 35 : Sch.12 FINANCE ACT 2000 : reg.6 SOCIAL SECURITY CONTRIBUTIONS (INTERMEDIARIES) REGULATIONS 2000

The taxpayer company, which supplied the services of its sole director and shareholder as a computer consultant to a client through an intermediary, was not liable to account for income tax under the Finance Act 2000 Sch.12 and national insurance contributions under the Social Security Contributions (Intermediaries) Regulations 2000 reg.6, where a contract directly between the director and the client would not have been a contract of employment.

The appellant company (F) appealed against three decisions of the respondent commissioners that it was liable to pay national insurance contributions and income tax under PAYE by reason of the application of the "IR 35" legislation.

F's sole director and shareholder (N) was a computer consultant.

For some 16 months F had supplied the services of N, through an agency (P), to a client (R).

The agreement between F and P was for the supply of services to R to migrate its human resources and payroll computer systems onto a single application.

F agreed to provide the services of one or more consultants including N.

N designed a solution for the migration project and worked at R's offices as well as at home until the project was completed.

The effect of the IR 35 legislation, contained in the Finance Act 2000 Sch.12 for direct tax and the Social Security Contributions (Intermediaries) Regulations 2000 reg.6 for national insurance, was in outline that if the circumstances were such that, had N performed his services under a contract directly between him and R, that contract would have been one of employment, then F would be liable for national insurance contributions and PAYE calculated broadly on the basis that the payments it received were emoluments it paid to N.

The commissioners took the view that the circumstances were such that, if the services had been performed under a contract between N and R, N would have been regarded as an employee of R, and that F was liable to pay national insurance contributions and PAYE tax accordingly in respect of the payments made to N.

F contended that, if the services had been performed under a contract between N and R, N would not have been regarded as an employee of R so that the IR 35 legislation did not apply.

HELD: (1) The question as to whether a person was employed under a contract of service, or whether he was self-employed and engaged under a contract for services, was a question of fact in each case to be determined having regard to all the relevant circumstances.

Relevant factors could be: whether the worker had to provide his own work and skill or whether he could substitute the work and skill of another; whether the worker was subject to a sufficient degree of control; whether there was mutuality of obligation so that there was an obligation on the worker to work and on the other party to pay him and to continue to make work available during the time of the contract; whether the worker was in business on his own account; whether the worker was paid by reference to the volume of work done; and the duration of the particular engagements and whether the relationship was permanent and the number of people by whom the individual was engaged, Ready Mixed Concrete (South East) Ltd v Minister of Pensions and National Insurance (1968) 2 QB 497, and Market Investigations Ltd v Minister of Social Security (1969) 2 QB 173 applied; Hall (Inspector of Taxes) v Lorimer (1994) 1 WLR 209 and Cornwall CC v Prater (2006) EWCA Civ 102, (2006) 2 All ER 1013 considered.

(2) Applying the principles established by the authorities N would not be regarded as an employee of R.

Although N did in fact do the work personally, the intention of the parties was that F could assign the obligations and benefits of its agreement with P so long as the assignee was acceptable to R.

N was engaged for his specific expertise and only for a particular project.

The way in which that was done was left to him.

He was not subject to the same control as an employee and was free to work for others at the same time as he worked for R.

The arrangements were consistent with the conclusion that N acted as a sub-contractor, with responsibility for part of a larger project, and not as an employee.

As far as mutuality of obligation was concerned, if, for any reason, N had been unable to work on the project during the period of the agreement, then R would not have had to find him other work to do and would not have had to pay him.

N was in business on his own account before working for R and afterwards.

The arrangements pointed to the conclusion that N would not be regarded as an employee of R.

N was paid an hourly rate and his relationship with R was not permanent.

N brought his own expertise and intellectual property rights to the project and retained ownership of them.

He also retained ownership of the processes he devised for the purposes of the project.

Appeal allowed

Counsel: For the appellant: Non-counsel representative For the respondents: Non-counsel representative

LTL 21/1/2008 (Unreported elsewhere)

Judgment: Official - 15 pages

Document No. AC0116040

Spc00652

NATIONAL INSURANCE CONTRIBUTIONS – provision of services through intermediary – whether, if the arrangements had taken the form of a contract between the worker and the client, the worker would be regarded as employed by the client - no – appeal allowed - Social Security Contributions and Benefits Act 1992 s 4A; Social Security Contributions (Intermediaries) Regulations 2000 SI 2000 No. 727 reg 6(1)(c)

INCOME TAX – provision of services through intermediary – whether the circumstances were such that, if the services were provided under a contract directly between the individual and the client, the individual would be regarded for income tax purposes as an employee of the client - no – appeal allowed - FA 2000 s 60 and Sch 12

THE SPECIAL COMMISSIONERS

FIRST WORD SOFTWARE LIMITED

Appellant

- and -

THE COMMISSIONERS FOR HER MAJESTY'S REVENUE AND CUSTOMS

Respondents

Special Commissioner : DR A N BRICE

Sitting in London on 1 and 2 November 2007

Matt Boddington of Accountax, Chartered Tax Advisers, for the Appellant

Graham Conway, of the Appeals Unit, for the Respondents

DECISION

The appeal

1. First Word Software Limited (the Appellant) appeals against three decisions of the Commissioners for Her Majesty's Revenue and Customs (the Revenue). All the decisions were dated 14 July 2006. The first decision related to the period from 4 September 2000 to 31 January 2002 and was that the Appellant was liable to pay national insurance contributions of £18,793.00. The second decision related to the year 2000-01 and determined that income tax under PAYE of £17,187 was due. The third decision related to the year 2001-02 and determined that income tax under PAYE of £27,264 was due.

2. The sole director and shareholder of the Appellant is Mr Neill Atkins who is a computer consultant. From 4 September 2000 to 31 January 2002 Mr Atkins supplied services to the Appellant who supplied them to an organisation called Plexus Personnel (Plexus) who supplied them to Reuters Limited (Reuters). The disputed decisions were made because the Revenue were of the view that the circumstances were such that, if the services had been performed under a contract between Mr Atkins and Reuters, Mr Atkins would be regarded as employed by, and as an employee of, Reuters. From that it followed that the Appellant, as an intermediary, was liable to pay national insurance contributions and income tax under PAYE in respect of the payments made to Mr Atkins. The Appellant appealed because it was of the view that, if the services had been performed under a contract between Mr Atkins and Reuters, Mr Atkins would not be regarded as employed by, or an employee of, Reuters and so the provisions about the supply of services through an intermediary did not apply.

The legislation

3, The legislation relating to the first disputed decision, about the payment of national insurance contributions, is contained in the Social Security Contributions and Benefits Act 1992 (the 1992 Act) which contains separate provisions applicable to employed earners on the one hand and self-employed earners on the other. After 22 December 1999 a new section 4A was inserted in the 1992 Act and provides that regulations may make provision for securing that, where a worker personally performs services for a client, and where the performance of those services is referable to arrangements involving a third person, and where the circumstances are such that the worker would be regarded as employed by the client, then relevant payments are to be treated as earnings paid to the worker.

4. The regulations made under the provisions of section 4A are the Social Security Contributions (Intermediaries) Regulations 2000 SI 2000 No 727 (the 2000 regulations). The relevant parts of regulation 6 provide:

> **"6(1) These regulations apply where –**
> **(a) an individual ("the worker") personally performs, or is under an obligation to perform, services for the purposes of a business carried on by another person ("the client"),**

(b) the performance of those services by the worker is carried out, not under a contract directly between the client and the worker, but under arrangements involving an intermediary, and

(c) the circumstances are such that, had the arrangements taken the form of a contract between the worker and the client, the worker would be regarded, for the purposes of Parts I to V of the Contributions and Benefits Act as employed in employed earner's employment by the client."

5. Regulation 6 goes on to provide that, where the regulations apply, the worker is treated as employed in employed earner's employment by the intermediary.

6. The legislation relating to the second and third disputed decisions, about income tax under PAYE, was, at the relevant time, contained in section 60 of the Finance Act 2000 (the 2000 Act) which provided that, for income tax purposes, Schedule 12 had effect with respect to the provision of services through an intermediary. Paragraph 1 of Schedule 12 provided:

"1(1) This Schedule applies where –

(a) an individual ("the worker") personally performs, or is under an obligation to perform, services for the purposes of a business carried on by another person ("the client"),

(b) the services are provided not under a contract directly between the client and the worker but under arrangements involving a third party ("the intermediary"), and

(c) the circumstances are such that, if the services were provided under a contract directly between the client and the worker, the worker would be regarded for income tax purposes as an employee of the client."

7. Schedule 12 went on to provide that, if the other conditions of the Schedule were met, and if the worker received from the intermediary a payment that was not chargeable to tax under Schedule E, then the intermediary was treated as making, and the worker was treated as receiving, a payment chargeable to income tax under Schedule E.

The issues

8. It was agreed that Mr Atkins personally performed services for Reuters within the meaning of section 4A(1) of the 1992 Act, regulation 6(1)(a) of the 2000 regulations and paragraph 1(1)(a) of Schedule 12 of the 2000 Act. Thus the issue for determination in the appeal was whether, had the arrangements taken the form of a contract between Mr Atkins and Reuters, Mr Atkins would be regarded as employed by, or as an employee of, Reuters.

The evidence

8. A bundle of documents was produced. There was a statement of agreed facts. Oral evidence was given on behalf of the Appellant by Mr Atkins. Oral evidence was given on behalf of the Revenue by Mr Khalil Ayub who is now the Technology Careers Manager at Reuters and by Mr Stephen John Turner, who is now the programme director for Reuters.

9. Also put in evidence was a letter dated 2 September 2003 written by Mr Richard Shaw, Director of Finance/HR Systems at Reuters, to the Appellant's previous advisers. Mr Shaw's letter contained answers to a number of questions raised by the Revenue. However, many of the statements in the letter conflicted with the oral evidence of Mr Atkins.

10. Mr Shaw did not give oral evidence at the hearing. Mr Turner's evidence was that Mr Shaw's letter was a true reflection of how contractors were managed at the time when Mr Atkins worked for Reuters. However, Mr Turner admitted that he had no specific knowledge of the contractual arrangements between Reuters and Plexus nor of the arrangements between Plexus and the Appellant nor did he have any specific knowledge of the work done for Reuters by Mr Atkins. The evidence of Mr Ayub was that, from information which he had obtained by talking to his colleagues, it was his opinion that Mr Shaw's letter was, for the most part, an accurate reflection of how Reuters managed its relationships with contractors. However, Mr Ayub admitted that he was only in a position to comment on how things operated since 2003 and could not comment on the arrangements for the period in issue in this appeal; also he had no specific knowledge of the Appellant or of the project on which Mr Atkins worked for Reuters.

11. I heard and saw Mr Atkins give oral evidence and I found him to be a credible witness. Where the evidence of Mr Atkins conflicted with the statements of Mr Shaw, I preferred the evidence of Mr Atkins. Mr Atkins spoke from his personal experience and was questioned on his evidence. Mr Shaw was not available to be questioned. Neither Mr Ayub nor Mr Turner were able to give direct evidence of events between 2000 and 2002.

The facts

12. From the evidence before me I find the following facts

Mr Atkins and the Appellant

13. In 1995 Mr Atkins ceased to be employed by an employer for whom he had worked for eight years. He decided to start his own business and established the Appellant. He then put all his efforts into the Appellant and has worked for many clients of the Appellant. Mr Atkins has a particular expertise in the migration of human resource and payroll systems.

14. The Appellant was incorporated on 11 April 1995 and commenced trading on 5 June 1995. Its principal activity is the provision of computer consultancy services. Its sole director and shareholder is Mr Atkins. The Appellant has an office at Mr Atkins' home. The Appellant has no written contract with Mr Atkins.

Reuters

15. In 2000 Reuters had a number of legacy computer systems in a large number of countries. They wished to merge these into one single, global system. As a representative of the Appellant, Mr Atkins heard that Reuters were looking for specialist skills, particularly in the area of the migration of human resource and payroll systems. The Appellant forwarded to Reuters a *curriculum vitae* describing the work previously done by Mr Atkins. Some time before September 2000 Mr Atkins, representing the Appellant, had an interview with a technical manager at Reuters. The

interview lasted for an hour and a half. All the questions were directed towards finding whether the Appellant could supply the technical skills necessary to achieve the required task. At the interview Mr Atkins was not asked about his personal interests or his ability to work with other employees.

The 1998 agreement between Reuters and Plexus

16. Meanwhile on 2 November 1998 Reuters had entered into an agreement (the 1998 agreement) with Plexus under which Plexus agreed to provide Reuters with software consultancy services in return for which Reuters would pay Plexus a fee. The agreement was stated to be effective from 2 November 1998 to 2 May 1999. In it Plexus agreed to supply the services of a named consultant to complete a stated task. The named consultant was not Mr Atkins, the task stated was not the task undertaken by the Appellant, and the duration of the agreement meant that it had expired before Mr Atkins worked for Reuters. Thus the 1998 agreement is not relevant to this appeal. I accept that some similar agreement was most probably in force because on 1 September 2000 Plexus entered into an agreement (the 2000 agreement) with the Appellant about the supply of services to Reuters. However, where the provisions of the 1998 agreement conflict with the provisions of the 2000 agreement or the oral evidence of the witnesses, I prefer the latter.

17. Clause 1.2 of the 1998 agreement provided that, at Reuters' option, Plexus was to submit a report to Reuters about the work done The report was to be to two stated employees of Reuters and clause 1.2 also provided that instructions were to be taken from the same named employees. Mr Atkins did not send his reports to the two employees named in the 1998 agreement but to a different manager in Geneva.

18. Clause 4 of the 1998 agreement provided that all works by Plexus or under its direction, including all developments in software, were the sole and complete property of Reuters and Plexus agreed to assign all proprietary rights in the works and developments to Reuters. This provision conflicted with clause 9 of the 2000 agreement which I prefer.

19. Clause 5.3 of the 1998 agreement provided that either party could terminate the agreement by giving the other party one month's notice. Clause 6.2 provided that neither party could assign its rights or obligations under the agreement without the prior written consent of the other party. Clause 6.3 provided that, should some of the services be performed by other employees or agents of Plexus, the prior consent of Reuters was required on their names.

The 2000 agreement between Plexus and the Appellant

20. On 1 September 2000 Plexus entered into an agreement with the Appellant under which it was agreed that Plexus would make payments to the Appellant and that the Appellant would supply specified services to Reuters. The specified services were stated to be "for the design, development and migration of Reuters' subsidiary human resource and payroll computer systems onto a single global instance of Oracle Applications III (Project Leapfrog) as required by Reuters". The project was to be based at Reuters' premises in London but involved consultation with customers on various other global Reuters' sites. The Appellant agreed to provide certain non-exclusive resources in support of the specified services. These included one or more consultants and it was agreed that Mr Atkins would lead the project on behalf of the Appellant. The

non-exclusive resources also included a personal computer based at the Appellant's offices. The consideration payable by Plexus to the Appellant was at a stated hourly rate for the actual time spent on the specified services. The total price was estimated to be £143,000 (which represented 2080 hours at the stated hourly rate).

21. The 2000 agreement provided that it was to commence on 4 September 2000 and was to run until completion of the project although the agreement could be terminated at any time by mutual consent. Under the agreement the Appellant agreed to take all reasonable steps to comply with any timetable or other targets for progress or delivery or completion of the specified services as agreed between the Appellant and Reuters.

22. Clause 6.1 of the 2000 agreement provided that the Appellant's method of work should be its own but that the Appellant would comply with all reasonable requests from Reuters to abide by procedural and quality standards documented on the project. I accept the evidence of Mr Atkins that the relevant standards were set by Oracle and that the work he did had to integrate with Reuter's overall system. For this reason those responsible for the overall system could be asked to comment on his finished job and at the user acceptance test stage he welcomed their views.

23. Clause 6.3 of the 2000 agreement provided that the Appellant might assign the obligations and benefits of the agreement provided that Reuters was satisfied within its absolute discretion that the proposed assignee possessed the necessary skills, expertise and resources to fulfil the specified services and that the assignee would comply with Reuter's rules on health, safety, security and confidentiality. Clause 7.1 provided that the Appellant warranted to Reuters that the specified services would be provided using reasonable care and skill and, as far as reasonably possible, in accordance with any agreed timetables or other targets.

24. Clause 9 of the 2000 agreement contained provisions about intellectual property. It provided that Reuters was to retain ownership of all intellectual property rights in the documents, data or other information provided to the Appellant and was not deemed to have granted the Appellant any right to use that information other than for the purposes of the agreement. Clause 9 also provided that the Appellant should retain ownership of all intellectual property rights in all documents, data or other information and devices or processes provided or created by the Appellant save that the Appellant was deemed to have granted Reuters a non-exclusive licence to make use of such information in the context of the specified services. This provision conflicts with clause 4 of the 1998 agreement and, for the reasons I have mentioned, I prefer the provisions of the 2000 agreement. I accept the evidence of Mr Atkins that he retained the right to re-use for other clients the processes which he devised for the purposes of the work he did for Reuters.

25. The 2000 agreement also provided, in Schedule 1, that additional services (that is, services not included within the specified services) would only be undertaken by mutual consent between the Appellant and Reuters before the commencement of the work; the Appellant had the right to negotiate a separate agreement for the provision of additional work for Reuters through Plexus. The schedule to the 2000 agreement provided that the contractor should charge a stated hourly rate for work performed and that time worked over 40 hours a week was to be by prior agreement.

Mr Atkins' methods of work

26. At the beginning of the project the Appellant worked out the requirements of the project and Mr Atkins designed a solution for Reuters' problem with the migration of human resource and payroll systems. The Appellant initiated its own plan for the development and completion of the project and provided Reuters with a way to migrate its information. Reuters told the Appellant that they wanted to migrate the information by a specified date and the Appellant was expected to manage its own project and was responsible for delivery, quality and timescales The Appellant set milestones and Mr Atkins was expected to meet them.

27. Because of the demands of the project, and the type of work being undertaken, Mr Atkins attended at the London offices of Reuters where he was provided with a desk and a computer. He could be accessed by email at Reuters. He was given a security identity card as a contractor so that he could access that part of the premises which contained his desk and also Reuters' computer systems. There was a team of about twenty people working on Project Leapfrog; some were employees but most were contractors. Mr Atkins described the whole of Project Leapfrog as "a big jig saw" of which his task was a small piece. Only he worked on the migration of the human resource and payroll systems. There was no hierarchy.

28. All who extracted data from the legacy systems had to work to timescales and provide information to the functional consultants and to a project manager. Mr Atkins sent his weekly up-dates to a manager based in Geneva. Communication was informal and could be by email or telephone and occasionally the manager would come to London for a meeting. I accept the evidence of Mr Atkins that all that the manager wanted to know was that "it was happening"; otherwise he adopted a "hands-off" approach. However, as the manager oversaw the whole of the project he had the final decision on tasks and the re-alignment of project plans. If Mr Atkins had a problem he would discuss it with a technical colleague and conversely he would assist his colleagues if they had a problem.

29. Mr Atkins had no interaction with the management of Reuters in the United Kingdom; he provided the Reuters manager in Geneva with weekly updates on progress. No-one at Reuters told him what to do or how to do it; he was expected to meet the time scales within the project plan. He did not ask permission to go on holiday. If he were going to take a holiday he let people know and sent an email to the manager in Geneva so that the manager did not expect an update during that period. Mr Atkins had no responsibility for managing others at Reuters.

Mr Atkins' hours of work

30. There was no agreement with Reuters about Mr Atkins' hours of work but Mr Atkins was expected to achieve the timescales and milestones relating to the project.

Mr Atkins' hours of work depended upon the demands of the project. Normally he started work between 8.00 am and 9.00 am and worked until 4.15 pm or 4.20 pm. Sometimes he worked longer or shorter hours. He did not have to ask permission to leave Reuters' offices. It was left to him to make sure that he delivered the project in time. When he wanted to finish early he said good-bye to the people working with him and left. He did not tell the manager in Geneva if he was to be absent for half a day.

31. Each week Mr Atkins completed a time sheet recording the number of hours he had worked; the timesheet was countersigned by any employee of Reuters. The Appellant submitted the time sheet with an invoice to Plexus showing the hours supplied the previous week, charged at the agreed hourly rate. The Appellant invoiced Plexus weekly. During the relevant period Mr Atkins worked for Reuters for seventy weeks. For a little more than one third of the total number of weeks he worked for forty hours; for a little less than a third he worked for less than forty hours; and for the remaining number of weeks he worked for more than forty hours. In the week that the project "went live" he worked for 109 hours and stayed in a London hotel that week.

32. In addition to the work he did on Reuters' site Mr Atkins also did work from home where he used the Appellant's computer and network to undertake work for Reuters. Also, on his journey home he worked on the train using a laptop computer belonging to the Appellant. Sometimes he worked in the evening using the Appellant's computer. During this time the hours spent by Mr Atkins working on the train or at home were not invoiced by the Appellant to Plexus. I accept the evidence of Mr Atkins that he achieved a lot on the train and that if he had not done that work he would have struggled to meet the timescales and milestones of the project. I also accept his evidence that he wanted to give a good impression to Reuters that he was meeting the milestones and not seeking to maximise the amount of money he claimed.

Mr Atkins' status at Reuters

33. Mr Atkins was identified as a contractor in Reuters' telephone directory. He did not receive holiday pay, sick pay or any pension benefit. He was not given a copy of any staff handbook He was paid for the hours he worked and no more. Unlike Reuters' employees he did not receive an annual salary. Unlike the employees of Reuters he did not receive any increase of pay each year after the annual review. Again, unlike the employees of Reuters, he did not receive a formal yearly appraisal. Insurance for professional indemnity, public liability and employer's liability was held by the Appellant.

Substitution

34. Mr Atkins had no official post or job title within the Reuters organisation and was free to work for other clients at the same time so long as he worked the hours needed to meet Reuters' requirements. In fact, he did not work for anyone else during the relevant period.

35. Clause 6.3 of the 2000 agreement between the Appellant and Plexus provided that the Appellant might assign the obligations and benefits of the agreement so long as Reuters were satisfied with the assignee. In practice there was no substitution. However, I accept the evidence of Mr Atkins that he could have assigned his work to a well-qualified contractor and he knew a number of contractors who would be able to

pick up the work with a hand-over period of two or three days. I accept the evidence of Mr Turner that, if an agency wished to replace one contractor with another, then Reuters would wish to interview the replacement contractor in order to establish their credentials and would look for a hand-over period. Reuters contracted with Plexus and they would negotiate the replacement with Plexus. I accept the evidence of Mr Ayub that Reuters did not contract with the contractor but with the agency.

36. Accordingly I find that, although Mr Atkins did in fact do the work personally, the intention of the parties was that the Appellant could assign the obligations and benefits of its agreement with Plexus so long as the assignee was acceptable to Reuters. In other words, the intention of the parties was that Mr Atkins did not necessarily have to do the work personally.

37. I also accept the evidence of Mr Atkins that if he had been unable at any stage to work on his part of Project Leapfrog he would not expect Reuters to find him other things to do; he was only there to work on the migration of the human resource and payroll systems. This evidence was confirmed by Mr Turner who said that if Project Leapfrog had been terminated then Reuters would have terminated the arrangements with the Appellant; Reuters did not find other work for contractors to do – that was why they used contractors.

October 2001 – the project "goes live"

38. The initial work for Project Leapfrog was completed by October 2001 when the project "went live". The work relating to countries outside the United Kingdom had been relatively straightforward but the work relating to the United Kingdom was more complicated and some further verifications were needed. Mr Atkins continued working for Reuters until 31 January 2002 on United Kingdom "support issues". The project was successful and the contract of 4 September 2000 ended on 31 January 2002.

39. From about mid-2001 there were problems with Plexus and the Appellant's invoices were paid late. Initially the delays were four weeks and then extended to six weeks. The Appellant used to chase up the late payments but I accept the evidence of Mr Atkins that it did not make any difference.

40. Between 1 September 2000 and 1 February 2002 the Appellant claimed for 2,644 hours worked by Mr Atkins and was paid £182,859.91.

Mr Atkins' work at Reuters after 1 February 2002

41. After 1 February 2002 Mr Atkins was asked to continue working for Reuters to resolve developmental and migration issues. The Appellant entered into a new contract with Plexus on 4 February 2002 at a reduced hourly rate. There was some uncertainty as to how long that contract lasted because Plexus became insolvent at about the same time. Thereafter, and until August 2002, Mr Atkins had a contract direct with Reuters and worked for Reuters exclusively from his home using the Appellant's computer. During this time the Appellant was connected to broadband and Mr Atkins could access Reuters' computer through the Appellant's computer and small network. During the period from about February or March 2002 to August 2002 the Appellant sent invoices direct to Reuters who paid them. The period after 1 February 2002 is not the subject of this appeal.

Later events

42 Some time in or about February 2002 Plexus became insolvent All the Appellant's invoices which had been sent to Plexus had been paid but two colleagues of Mr Atkins had not been paid and lost significant amounts.

43. Since the successful completion of the migration of data for Reuters Mr Atkins has undertaken similar work for other large national companies and two government departments. In about 2004 Mr Atkins and a business partner formed another company and started to trade through that company which now has a turnover of about £700,000 and seven employees. The Appellant is now no longer trading and is dormant.

The Revenue's enquiries

44. On 30 April 2003 the Revenue wrote to the Appellant's previous representatives asking a number of questions about the terms and conditions under which Mr Atkins had worked for Reuters. The letter requested the representatives to arrange for Reuters to supply the information. It was for this reason that Mr Shaw of Reuters wrote his letter dated 2 September 2003 to the Appellant's previous representatives.

The arguments

45. For the Appellant Mr Boddington cited *Ready Mixed Concrete (South East) Limited v Minister of Pensions and National Insurance* [1968] 2 QB 497 for the principle that a person could only be regarded as an employee if he was obliged to give personal service (with no substitution); if the work provider had to offer work or pay if no work was available; if the worker was controlled; and if the other provisions of the contract were consistent with a contract of service. He went on to argue that Mr Atkins had not been obliged to perform the services personally; that there had been no obligation on Reuters to provide work for Mr Atkins or to pay him if there were no work; the Mr Atkins had not been subject to control by Reuters; and that the other arrangements were inconsistent with a contract of service.

46. Mr Boddington cited *Lime-It v Justin* [2003] STC (SCD) 15 for the principle that it was necessary to look at all the circumstances of the case; he also relied upon *Hall v Lorimer* 66 TC 349 at 376D and argued that Mr Atkins took the financial risk of bad debts and outstanding invoices and held his own professional indemnity insurance and public liability insurance. Mr Boddington cited *Market Investigations Limited v Minister of Social Security* [1968] 3 All ER 732 for the principle that it was necessary to

consider whether Mr Atkins would be considered to be in business on his own account; since 1995 Mr Atkins had worked for a number of clients of which Reuters was only one and had developed his business over the years; he had worked unpaid overtime for Reuters in order to promote his own business; Mr Atkins had not been part and parcel of Reuter's business. Finally Mr Boddington cited *Express & Echo Publications Limited v Ernest Tanton* [1999] EWCA Civ 949 and argued that the intention of the parties was relevant and in this appeal the intention of Mr Atkins and Reuters was that Mr Atkins was not employed by Reuters.

47. For the Revenue Mr Conway accepted the principles in *Ready Mixed Concrete*. However, he argued that Mr Atkins had been subject to "a sufficient degree" of control by Reuters, relying upon *Ready Mixed Concrete* at 515C and clause 6.1 of the 2000 agreement. He agreed that the arrangements, including the hours of work, had been flexible and informal but argued that that was appropriate for a senior, skilled employee. He relied upon clause 1.2 of the 1998 agreement and the provisions about reporting and taking instructions. The evidence was that Reuters' project manager had the final decision as to what work should be done when. He also relied upon clause 3.3 of the 2000 agreement and argued that Mr Atkins had to comply with the timetable as set by Reuters; Mr Atkins had to have his time sheets approved by Reuters and under Schedule 1 of the 1998 agreement needed permission to work more than forty hours a week; his arrangements for going on leave were the same as for a senior employee. The 2000 contract provided that Project Leapfrog was based at Reuters' London office and Mr Atkins in fact attended there on a daily basis. .

48. Mr Conway accepted that, if there were a right of substitution, then the fact that it was not exercised was not relevant. However, he argued that there was no right of substitution in either the 1998 contract or the 2000 contract. He accepted that clause 6.3 of the 2000 contract gave a right of assignment but argued that that was not the same as a right of substitution. If there were an assignment then the assignor would have no further interest in the agreement but if there were a substitution the rights would be retained but another person would perform the contract. In this appeal Reuters had specifically wanted Mr Atkins' personal services and they had interviewed him for one and a half hours to ensure that he had the specialised skills they needed. The evidence of Mr Ayub was that a proposed replacement would have had to be interviewed by Reuters. However, even if there were a right of substitution this was a far cry from a contractual right to send a substitute and was merely a pointer towards self-employment.

49. Mr Conway went on to argue that there was mutuality of obligation because the 2000 agreement provided that the Appellant had to supply the services of Mr Atkins and that Reuters would pay the Appellant. He cited *Cornwall County Council v Prater* [2006] EWCA Civ 120 at [40(5)] for the principle that the fact that a contract need not be renewed was not relevant; it was enough that, while the contract continued, the worker was under an obligation to work and the client was under an obligation to pay for the work made available by the client.

50. Finally, Mr Conway argued that Mr Atkins had not taken any financial risk as all his invoices had been paid and he could not increase his profit by good management. Mr Atkins was part and parcel of Reuters and used their equipment. Mr Atkins did not own all the rights to his intellectual property; Mr Atkins did send regular reports to Geneva; He cited *Netherlane Ltd v York* (2005) SPC 457 at 14 and

Island Consultants Limited v The Commissioners for Her Majesty's Revenue and Customs [2007] SPC 618 at 13 for the principle that it was not possible for the parties to have an intention over the hypothetical contract postulated by the statutory provisions.

Reasons for decision

51. The issue for determination in the appeal is whether had the arrangements taken the form of a contract between Mr Atkins and Reuters, Mr Atkins would be regarded as employed by, or as an employee of, Reuters.

The authorities

52. I start by considering the authorities cited by the parties to see what legal principles they establish.

53. In *Ready Mixed Concrete* (1968) the issue was whether a worker was within the class of employed persons under the National Insurance Act 1965 as being an employed person under a contract of service. McKenna J said at 515C:

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

54. McKenna J added at 515F:

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

55. The judge then went on to identify a number of factors to be taken into account in deciding whether a contract was a contract of service. These included: whether the contractor was to provide at his own expense the necessary plant and material; whether the contractor hired his own employees; whether the contractor provided and maintained his own tools and equipment; whether the contractor was paid by reference to the volume of work done; whether the contractor had invested in the enterprise and bore the financial risk; whether the contractor had the opportunities of profit or the risk of loss; and whether the relationship was permanent.

56. In *Market Investigations* (1968) Cooke J said at 184G that the fundamental test was whether a person performed services as a person in business on his own account. No exhaustive list could be compiled of the considerations which are relevant in determining that question. At 185A he said that although control was relevant it was not the sole determining factor; when one was dealing with a professional man, or a man of some particular skill and experience, there could be no question of the employer telling him how to do the work. At 185B he said that a relevant factor could be whether a person who engaged himself to perform services

did so in the course of an already established business of his own but this factor was not decisive.

57. In *Hall v Lorimer* (1993) the taxpayer was a vision mixer who undertook work for a number of different television companies and whose engagements consisted of short term contracts lasting one or two days. In four years he worked on over 800 days. The Court of Appeal held that there was no single path to a correct decision. The question whether an individual was in business on his own account might be helpful but might be of little assistance in the case of one carrying on a profession or vocation. Factors which were critical in that appeal were the duration of the particular engagements and the number of people by whom the individual was engaged.

58. In *Cornwall County Council* (2006) the issue was whether a teacher engaged by a local authority was entitled to be regarded as an employee throughout the ten year period in which she was paid for her work as a home tutor in performing multiple individual teaching assignments of varying duration under a succession of separate contracts. The Council was under no obligation to offer pupils and the teacher was under no obligation to accept them. However, if the teacher took on a pupil she was obliged to teach that pupil, and the Council was obliged to provide that work, until that particular engagement ceased. At paragraph 33 of the judgment Mummery LJ said that the authorities did not support the argument that there was mutuality of obligation over and above the mutual obligations existing within each separate contract, namely the obligation on the teacher to teach the pupil and the obligation on the part of the Council to pay her for teaching the pupil whom they continued to make available for teaching by her.

The principles

59. From these authorities I derive the principle that the question as to whether a person is employed under a contract of service, or whether he is self-employed and provides a contract for services, is a question of fact in each case to be determined having regard to all the relevant circumstances. Relevant factors could be: (1) whether the worker has to provide his own work and skill or whether he may substitute the work and skill of another; (2) whether the worker is subject to "a sufficient degree" of control"; (3) whether there is mutuality of obligation so that there is an obligation on the worker to work and an obligation on the other party to pay him and to continue to make work available during the time of the contract; (4) whether the worker was in business on his own account; relevant factors here could be: whether the worker had to provide at his own expense the necessary plant and material, hire his own employees and provide and maintain his own tools and equipment; whether the worker has invested in the enterprise and bears the financial risk; whether the worker has the opportunities of profit or the risk of loss; and whether the worker engaged himself to perform services in the course of an already established business of his own; (5) whether the worker is paid by reference to the volume of work done; and (6) the duration of the particular engagements and whether the relationship is permanent and the number of people by whom the individual was engaged.

60. I now turn to apply the principles established by the authorities to the facts of this appeal.

(1) – Right to substitute

61. Beginning with substitution, I have already found that, although Mr Atkins did in fact do the work personally, the intention of the parties was that the Appellant could assign the obligations and benefits of its agreement with Plexus so long as the assignee was acceptable to Reuters. In other words, the intention of the parties was that Mr Atkins was not obliged to perform the services personally. This points to the conclusion that Mr Atkins would not be regarded as an employee of Reuters.

(2) - Control

62. In considering whether Mr Atkins was subject to "a sufficient degree" of control by Reuters I bear in mind that Mr Atkins was engaged for his specific expertise and was engaged only for a particular project. To the extent that the provisions of the 1998 agreement are inconsistent with the oral evidence and the 2000 agreement I prefer the latter. Clause 6.1 of the 2000 agreement provided that his method of work should be his own. The evidence was that Mr Atkins was engaged to provide "a small piece of a large jig saw" and the way in which that was done was left to him. Although Reuters decided the thing to be done, (namely the migration of the legacy computer systems) Mr Atkins decided the way in which the migration of the human resource and payroll systems was to be undertaken. He also decided on the means to be employed in doing it and the time when it was to be done so long as it met the overall requirements of the main project. Mr Atkins could, and did, choose his hours of work so long as he met the timescales and milestones of the project. During the period of the relevant contract Mr Atkins worked at Reuters' office in London because he needed to access Reuters' computer; however he also chose to do work on the train and at home. Although Mr Atkins sent up-dates to a technical manager in Geneva, the evidence was that the manager did not control Mr Atkins in the way he worked in the way that an employer controls an employee, even a senior professional employee. Finally, Mr Atkins was free to work for others at the same time as he worked for Reuters. The arrangements were consistent with the conclusion that Mr Atkins acted as a sub-contractor, with responsibility for part only of a larger project, and not as an employee.

(3) -Mutuality of obligation

63. As far as mutuality of obligation is concerned, the evidence of both Mr Atkins and Mr Turner was that if, for any reason, Mr Atkins had been unable to work on Project Leapfrog during the period of the agreement, then Reuters would not have to find him other work to do and would not have to pay him. Reuters were under no obligation to continue to make work available for the duration of the 2000 agreement. These arrangements point to the conclusion that Mr Atkins was not an employee of Reuters.

(4) – In business on his own account?

64. In considering whether Mr Atkins was in business on his own account it is relevant that he did in fact provide his own computer for work on the train or at home although the main work was done in London with Reuters' computer. Mr Atkins had also invested in his own enterprise by establishing the Appellant, which in 2000, was an already established business and had been so for five years. After his work for Reuters ceased Mr Atkins continued in business on his own account. During his time with Reuters Mr Atkins had some financial risk of unpaid invoices and bad debts

because Plexus became insolvent. Both before and after his work for Reuters Mr Atkins had the risk of an insufficient number of engagements. Also, although he was given work throughout the agreement with Reuters, he might not have been. These arrangements point to the conclusion that Mr Atkins would not be regarded as an employee of Reuters.

(5) - Volume of work done and other factors

65. Mr Atkins was paid by reference to the volume of work done inasmuch as he was paid an hourly rate which meant that some weeks he was paid less and some weeks more. Mr Atkins' relationship with Reuters was not permanent; it was temporary only and was always to terminate when the project was completed. As mentioned, Mr Atkins could have worked for others at the same time as he worked for Reuters. Other relevant factors are that Mr Atkins did not receive holiday pay, sick pay, or pension benefit. He did not get a weekly wages or an annual salary. And he was not treated like an employee by Reuters. All these factors point to the view that Mr Atkins should not be regarded as an employee of Reuters.

66. Finally, clause 9 of the 2000 agreement makes it clear that Mr Atkins brought his own expertise and intellectual property rights to the project and retained ownership of them. He also retained ownership of the processes he devised for the purposes of Project Leapfrog. This points to the conclusion that Mr Atkins would not be regarded as an employee of Reuters.

Conclusion

67. A consideration of the relevant factors in this appeal point to the conclusion that Mr Atkins would not be regarded as an employee of Reuters.

Decision

68. My decision on the issue for determination in the appeal is that, had the arrangements taken the form of a contract between Mr Atkins and Reuters, Mr Atkins would not be regarded as employed by, or as an employee of, Reuters.

69. That means that the appeal is allowed.

DR NUALA BRICE

SPECIAL COMMISSIONER

RELEASE DATE: 11 December 2007

Authorities referred to at the hearing but not mentioned in the Decision

Island Consultants Limited v The Commissioners for Her Majesty's Revenue and Customs (2007) SPC 00618

Montgomery v Johnson Underwood Limited [2001] EWCA Civ 318

Morren v Swinton and Pendlebury Borough Council [1965] 1 WLR 576

Propertycare Limited v Gower and others UKEAT transcript of judgment of 14 November 2003 at [9(3)]

*Synaptek Limited v Young (*2003) 75 TC 52 at 73E

Usetech Limited v Young (2004) 76 TC 811 at 836D and 841E

Wright v Redrow Homes (Yorkshire) Ltd [2003] 3 All ER 98 at [35] and [36]

ALTERNATIVE BOOK CO LTD v REVENUE & CUSTOMS COMMISSIONERS (SpC00685) (2008) (full text here)

Sp Comm (Michael Tildesley (Chairman)) 19/5/2008

TAX

EMPLOYEES : INCOME TAX : INDEPENDENT CONTRACTORS : NATIONAL INSURANCE : PERSONAL SERVICE COMPANIES : SUBSTITUTION : SUPPLY OF SERVICES : PROVISION OF SERVICES THROUGH INTERMEDIARY : APPROPRIATE FACTORS UNDER IR35 LEGISLATION AS TO WHETHER SERVICES SUPPLIED AS EMPLOYEE

Where an individual supplied his services through a personal service company to a client, in deciding, pursuant to the IR35 legislation, whether the services provided were given as an employee rather than genuinely as an independent contractor, each case should be decided on its own individual circumstances, and the Revenue and Customs Commissioners were not required to evaluate the hypothetical contract in the context of service providers in the same line of business.

The appellant company (B) appealed against determinations of the respondent commissioners requiring it to pay tax and national insurance on deemed payments to its sole director and shareholder (S).

S, a skilled information technology consultant, provided services to a company (G) through a series of two connected contracts.

The first was a contract between B and a recruitment agency (C), to perform services for G.

The second was a contract between C and G to supply the services of B using S.

The issue was whether S would have been an employee of G if he had contracted directly with G under a hypothetical contract presupposed by the IR35 legislation.

B submitted that (1) a hypothetical contract between S and G would have included a substitution clause, in which case there would have been no requirement for S to perform the services personally for G, and so the hypothetical contract would not as a matter of law constitute a contract of employment; (2) the stated mutual intentions of the parties were highly relevant in determining the status of the hypothetical contract; (3) when all the facts were considered in the context of the business of a software consultant, the hypothetical contract would have been a contract for services.

HELD: (1) It was necessary first to determine as fact the precise effect and nature of the substitution clause, and only then was it possible to decide whether the clause was a tie-breaker or a fact among others, Usetech Ltd v Young (Inspector of Taxes) (2004) EWHC 2248 (Ch), (2004) STC 1671 applied.

On the facts, no substitution clause would have been included in the hypothetical contract.

The substitution clause in the connected contracts was window dressing and had no practical effect on how the contract would operate, R (on the application of Professional Contractors Group Ltd) v Inland Revenue Commissioners (2001) EWHC Admin 236, (2001) STC 629 considered.

If G had negotiated the contract with S direct, it would not have agreed to such a clause as G was only interested in the skills and personal services of S.

(2) The parties' mutual intention formed part of the circumstances which were to be taken into account in the analysis of the hypothetical contract.

The weight to be attached to the evidence of mutual intention would vary from case to case.

(3) The commissioners were not required to evaluate the hypothetical contract in the context of service providers in the same line of business.

Each case should be decided on its own individual circumstances, and the facts that might be compelling in one case in the light of all the circumstances might not be compelling in the context of another case, Market Investigations Ltd v Minister of Social Security (1969) 2 QB 173 QBD and Hall (Inspector of Taxes) v Lorimer (1994) 1 WLR 209 CA (Civ Div) applied.

(4) The relationship between G and S was overwhelmingly one of employment.

The hypothetical contract would have the necessary irreducible minimum to constitute an employment contract.

Appeal dismissed

Counsel:

For the appellant: John Antell

For the respondents: Non-counsel representatives

Solicitors:

For the appellant: Lawspeed Ltd

LTL 30/6/2008 : (2008) STC (SCD) 830

Document No. AC0117445

Spc00685

INCOME TAX & NATIONAL INSURANCE – IR35 - ***Worker supplied through intermediaries – whether circumstances were such that had the services been provided under a contract directly with the worker the worker would have been an employee –Ye s– Appeal dismissed***

SPECIAL COMMISSIONERS

ALTERNATIVE BOOK COMPANY LIMITED **Appellant**

- and -

HER MAJESTY'S REVENUE and CUSTOMS **Respondents**

Special Commissioner: MICHAEL TILDESLEY OBE

Sitting in public in Cardiff on 22 and 23 January 2008 with final representations by 27 February 2008

John Antell counsel instructed by Lawspeed Limited for the Appellant

Susan Jones and Colin Williams, HM Inspectors of Taxes for the Respondents

DECISION

The Appeal

1. The Appellant was appealing against determinations requiring it to pay tax for the years 2000-01 and 2001-02 and national insurance contributions for the period 6 April 2000 to 5 April 2002 on deemed payments to Keith Shepherd, the Appellant's sole director and shareholder, in respect of his work for Gerling NCM (now known as Atradius). The notices of the determination under regulation 80 of the Income Tax (PAYE) Regulations 2003 and section 8 of the Social Security Contributions (Transfer of Functions) Act 1999 were made on 9 December 2005.

2. The determinations were made under what is commonly known as the IR35 legislation which was enacted for the purpose of curbing the tax advantages enjoyed by some individuals who supplied their services through a personal service company to a client. Under the IR35 legislation if it was found that the services provided by the person were given as an employee rather than genuinely as an independent contractor the fees paid to his personal service company would not be treated as company revenue upon which corporation tax was payable but rather as deemed salary to him. The company would then be responsible for the accounting of tax and national insurance contributions on the deemed salary.

3. Mr Shepherd who was a skilled IT consultant provided his services to Gerling NCM through a series of two connected contracts. The first was a contract between the Appellant and Computer People Limited, a recruitment agency, to perform services for Gerling (NCM) ("the lower level contract"). The second was a contract between Computer People Limited and Gerling NCM to supply the services of the Appellant using Mr Shepherd ("the upper level contract"). The Appellant had no written contract with Mr Shepherd. There was no issue taken about the interposition of Computer People Limited in the contractual sequence.

4. The Appellant was incorporated on 10 April 1997 and commenced trading on that day. Mr Shepherd was the sole director and shareholder of the Appellant. Gerling NCM was incorporated on 15 October 1998 with offices in Cardiff and across the world. The UK arm of its business came into operation following the privatisation of a government agency. The business activity of Gerling NCM was the provision of export and domestic credit insurance. The initial contract to provide services to Gerling NCM (presumably its predecessor) started 2 February 1998.

5. The parties were in agreement that for the purposes of the IR35 legislation Mr Shepherd was the worker, the Appellant the intermediary, and Gerling NCM the client.

6. The substantive issue in dispute was whether Mr Shepherd would have been an employee of Gerling NCM if he had contracted direct with Gerling (NCM) under the hypothetical contract presupposed by the IR35 legislation. The parties were content for a decision to be made in principle on the substantive issue.

The Evidence

7. I heard evidence from Mr Shepherd for the Appellant. The Respondents called four witnesses who were:

(1) Mr Christopher Saunders, HMRC Employer Compliance Officer, who was present at the interviews with Mr Shepherd on 10 October 2002 and 10 December 2004.

(2) Mr David Lewis, HM Inspector of Taxes, who carried out the investigation into the Appellant's tax affairs.

(3) Mr Derek Gigg, Head of Service Delivery Management at Gerling NCM, who was previously a manager responsible for software development at Gerling NCM, and one time manager to whom Mr Shepherd reported.

(4) Mr Stephen Prentice, Manager IT Services at Gerling NCM, Mr Shepherd nominated Mr Prentice as the person to speak to the Respondents about his working relationship at Gerling NCM.

8. The parties prepared five bundles of agreed documents which together with additional documents submitted at the hearing were admitted in evidence. Further the parties supplied skeleton arguments and a Respondents' response together with eight bundles of authorities at the hearing.

9. The contract documentation included in the bundles consisted of:

(1) The Upper Level (Computer People Limited & Gerling NCM): copies of contracts extending the terms of assignment covering the period 16 August 1999 to 26 April 2002, and copies of contract SP862 and extension from 27 April 2002 until 25 October 2003. A copy of the first known main contract, SP861, was not available.

(2) The Lower Level (Computer People Limited & Appellant): copies of contracts extending the terms of assignment of CPL98 covering the period 3 April 2000 to 29 September 2000, copies of an unsigned CPL00 and extensions covering the period 2 October 2000 to 25 April 2002 and a copy of, CPL02 covering the period 25 April 2002 to 25 October 2002, outside the periods under appeal. A copy of the first known main contract, CPL98, was not available

10. The parties in their submissions referred to the contract documentation under the generic groupings of lower level and upper level. I adopted the same convention in this decision except when reference was made to a term in a specific contract or contract extension. The Respondents did not take issue with the missing contracts, since there was evidence of contract documentation for the periods under Appeal. There were no significant inconsistencies between the terms of the lower and upper level contracts.

11. Following the end of the hearing on 23 January 2008 directions were issued requesting further representations on the issue of mutual intention which were received by the due date of 27 February 2008.

Preliminary Issue

12. On 11 January 2008 the Respondents made an application for directions that the issue to be decided should be restricted to whether IR35 applied in principle during the 2000/01 and 2001/02 tax years. The Respondents objected to the Application pointing out that the directions issued on 15 March 2007 identified the issue to be:

> "whether the services which Mr Shepherd provided to Astradius (formerly Gerling NCM) under a number of separate assignments… to 2005 were caught by the IR35 legislation."

13. On 17 January 2008 I directed that

> (1) The question for determination is whether the IR35 legislation should apply in principle to the whole of the work undertaken by the Appellant for Gerling NCM for the tax years 2000/01 and 2001/02.
>
> (2) The parties are entitled to call evidence relating to events and arrangements outside the tax years 2000/01 and 2001/02 provided the evidence is relevant to the disputed issue and no severe prejudice is caused to the other party by the late disclosure of the evidence.

14. The real dispute between the parties regarding the preliminary issue was whether the Appellant could rely on facts, particularly the tax treatment and business activities of Mr Shepherd outside the tax years in dispute. I considered the dispute was not one of admissibility of evidence but about its weight and relevance which was best assessed by examining it as part of the whole factual context of the Appeal. The Respondents were not prejudiced by the late admission of evidence. Their skeleton argument covered the majority of the points raised by the Appellant. Further they placed some reliance on the fact that Mr Shepherd provided his services to Gerling NCM from 1998 to 2005.

The Legislation

15. The IR 35 legislation is found in schedule 12 of the Finance Act 2000 (the 2000 Act) for income tax and in regulation 6 of the Social Security Contributions (Intermediaries) Regulations 2000 (the 2000 Regulations) for national insurance contributions.

16. Paragraph 1 of schedule 12 of the 2000 Act provides so far as is relevant:

> '1--(1) This Schedule applies where--
>
> (a) an individual ("the worker") *[Mr Shepherd]* personally performs, or is under an obligation personally to perform, services for the purposes of a business carried on by another person ("the client") *[Gerling NCM]*,

(b) the services are provided not under a contract directly between the client *[Gerling NCM]* and the worker *[Mr Shepherd]* but under arrangements involving a third party ("the intermediary") *[Alternative Book Club]*, and

(c) the circumstances are such that, if the services were provided under a contract directly between the client *[Gerling NCM]* and the worker *[Mr Shepherd]*, the worker would be regarded for income tax purposes as an employee of the client *[Gerling NCM]*. ...

(4) The circumstances referred to in sub-paragraph (1)(c) include the terms on which the services are provided, having regard to the terms of the contracts forming part of the arrangements under which the services are provided.'

17. Regulation 6 of the 2000 Regulations provides so far as is relevant

'6--(1) These Regulations apply where--

(a) an individual ("the worker") *[Mr Shepherd]* personally performs, or is under an obligation personally to perform, services for the purposes of a business carried on by another person ("the client") *[Gerling NCM]*,

(b) the performance of those services by the worker *[Mr Shepherd]* is carried out, not under a contract directly between the client *[Gerling NCM]* and the worker *[Mr Shepherd]*, but under arrangements involving an intermediary *[Alternative Book Club]*, and

(c) the circumstances are such that, had the arrangements taken the form of a contract between the worker *[Mr Shepherd]* and the client *[Gerling NCM]*, the worker *[Mr Shepherd]* would be regarded for the purposes of Parts I to V of the Contributions and Benefits Act as employed in employed earner's employment by the client *[Gerling NCM]*.'

Construction of the Legislative Provisions

18. Park J in *Ustech Ltd v Young (Inspector of Taxes)* [2004] STC 1671 at page 1686 paragraph 9 said:

"A more general point of construction is worth spelling out at this stage. The conditions of sub-paragraphs (a) and (b) involve an analysis of the actual facts and legal relationships, but when that analysis shows that those two sub-paragraphs are satisfied sub-paragraph (c) involves an exercise of constructing a hypothetical contract which did not in fact exist, and then enquiring what the consequences would have been if it had existed. There may be room in some cases for dispute about what the hypothetical contract would contain and in the present case there is".

19. The respective provisions of the 2000 Act and the 2000 Regulations are not identical, in particular regulation 6 does not contain a provision like paragraph 1(4) of schedule 12 to the Finance Act 2000, expanding on what is covered by 'the circumstances' referred to in sub-paragraph (c) of regulation 6(1).

20. The special commissioner in *Dragonfly Consultancy Limited v HMRC* (2007) Spc00655 at paragraph 32 considered that the potential difference between the 2000 Act and the 2000 Regulations might have an impact on the factual matrix for making

the decision under the respective provisions. In his view a decision under the 2000 Regulations may be restricted to considering the arrangements between the parties which in this case would be the lower and upper level contracts. Whereas a decision under the 2000 Act would require a determination of what the hypothetical contract would contain from a consideration of all the circumstances including the formal arrangements between the parties.

21. Park J in *Ustech Ltd v Young (Inspector of Taxes)* [2004] STC 1671 at page 1686, paragraph 10 did not consider the potential difference between the 2000 Act and the 2000 Regulations material:

> "However, no-one has suggested to me, nor do I consider, that that or the other minor differences between the two statutory provisions affects this case or opens a possibility of the case being decided one way for NICs and another way for income tax and corporation tax".

22. Mr Justice Burton in *The Queen and Commissioners of Inland Revenue ex parte Professional Contractors Group Limited and another* [2001] EWHC Admin 236 Case Number: CO/2302/00 stated at paragraph 48(iii) that

> "It appears to me clear that the Revenue must bear in mind that under IR35 they are not considering an actual contract between the service company and the client but imagining or constructing a notional contract which does not in fact exist. In those circumstances of course the terms of the contract between the agency and the client as a result of which the service contractor will be present at the site are important, as would be the terms of any contract between the service contractor and the agency. But particularly given the fact that, at any rate at present, a contract on standard terms may or may not be imposed by an agency, or may be applicable not by reference to a particular assignment, but on an ongoing basis, and may actually bear no relationship to the (non- contractual) interface between the client and the service contractor, such documents can only form a part, albeit an important part, of the picture."

My Approach

23. The parties' submissions took the form of analysing the terms of the lower level and upper level contracts and the wider circumstances against a range of legal principles derived from case law on employment status, in order to arrive at their respective conclusions on whether the hypothetical contract was one of employment or not. I consider the parties' approach had the wrong emphasis and carried the risk that the dispute turned into one about employment status rather than on the construction of the hypothetical contract. I adopted an approach of finding facts to determine the terms of the hypothetical contract between Mr Shepherd and Gerling NCM followed by an assessment of the terms and contextual circumstances against case law principles on employment status to decide whether it was a contract of service. I concluded that the adopted approach was consistent with the statutory provisions and the general point of construction made by Park J in *Ustech Ltd* at page 1686. Further I decided that the different wording in the 2000 Act and the 2000 Regulations was not material. The factual matrix for decisions under the 2000 Act and the 2000 Regulations was the same, comprising the terms of the lower and upper

level contracts and all the circumstances on which Mr Shepherd provided his services to Gerling NCM.

24. The structure for the decision starts with the legal principles derived from employment status case law, next the facts, the submissions and my findings followed by a construction of the hypothetical contract and its assessment against the principles.

The Legal Principles

25. The IR35 legislation left in place the established case law-based test of employment status. The parties endorsed the general principles established by the leading cases but disagreed on the relevance and the weight to be attached to certain indicators of employment status. The disputed indicators were: the intentions of the parties, whether a substitution clause if existed was a tie-breaker, and whether Mr Shepherd's circumstances should be considered in the context of service providers in the same kind of business.

26. In *Ready Mixed Concrete* (*South East*) *Ltd v Minister of Pensions and National Insurance* [1968] 2 QB 497 the issue was whether a worker was within the class of employed persons under the National Insurance Act 1965 as being an employed person under a contract of service. MacKenna J said ([1968] 2 QB 497 at 515):

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

27. MacKenna J added ([1968] 2 QB 497 at 515):

> 'Control includes the power of deciding the thing to be done, the way in which it shall be done, the means to be employed in doing it, the time when and the place where it shall be done.'

28. In *Market Investigations Ltd v Minister of Social Security* [1969] 2 QB 173 Cooke J said that the fundamental test was whether a person performed services as a person in business on his own account. Although control was relevant it was not the sole determining factor; when one was dealing with a professional man, or a man of some particular skill and experience, there could be no question of the employer telling him how to do the work.

29. In *Hall (Inspector of Taxes) v Lorimer* [1994] STC 23, [1994] 1 WLR 209 the taxpayer was a vision mixer who undertook work for a number of different television production companies and whose engagements consisted of short term contracts lasting one to two days. In four years he worked on over 800 days. The Court of

Appeal held that there was no single path to a correct decision whether a person was an employee or self employed:

> In order to decide whether a person carries on business on his own account it is necessary to consider many different aspects of that person's work activity. This is not a mechanical exercise of running through items on a check list 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 matter 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 important from one situation to another.

30. The Court Of Appeal then went onto identify a non-exhaustive list of relevant factors taken from decided cases about whether a person was employed or self employed. The list included:

(1) the express or implied rights and duties of the parties;

(2) the degree of control exercised over the person doing the work;

(3) whether the person provides his own equipment and the nature of the equipment involved in his work;

(4) whether the person hires any staff to help him;

(5) the degree of financial risk taken by him;

(6) the degree of responsibility for investment and management;

(7) the opportunity of profiting from sound management of the task.

31. The Court of Appeal also identified other possible relevant factors including:

(1) the understanding or intentions of the parties;

(2) whether a person has set up a business-like organisation of his own;

(3) the degree of continuity in the relationship between the person performing the services and the person for whom he performs them;

(4) how many engagements he performs, and whether they are performed mainly for one person or for a number of different people;

(5) whether the person performing 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.

32. My intention is to group the evidence and findings of fact against the indicators of employment and self employment as identified by the above authorities.

The Facts

Established Tax Treatment of Mr Shepherd

33. Since leaving British Steel in 1978 Mr Shepherd generally provided his services as a self employed person under a partnership with his wife The last time he was regarded as an employee was in 1985 when he worked for six months for Symon Systems. From 1985 to 1995 Mr Shepherd was engaged as a contractor with the Horserace Totalisator Board (the Tote) developing database systems, in particular a staff selection system. In 1997 Mr Shepherd dissolved the partnership, and offered his services through his company Alternative Book Company Limited. His first engagement was with St Ivel which lasted six months. In February 1998 Mr Shepherd commenced work at Gerling NCM. From April 2003 Mr Shepherd supplied his services through a different personal service company, KES Computer Services Limited.

34. Mr Shepherd considered that working as a self employed contractor enabled him to broaden his expertise in business and computer systems, and the opportunity to meet new people. The disadvantages were the lack of job security, no pension scheme and holiday pay, and having responsibility for self development and running a business.

Continuity of the Relationship with Gerling NCM, Exclusivity of Service and Business on Own Account

35. Mr Shepherd worked for Gerling NCM full time, averaging around 36 hours per week from February 1998 to April 2004 except for a break of four weeks between 29 June 2001 and 23 July 2001. From April 2004 Mr Shepherd was engaged for 24 hours per week at his request until July 2005. Mr Shepherd's services were supplied via the Appellant up to 25 April 2003, and then through another personal service company, KES Computer Software Limited.

36. The contractual arrangements for Mr Shepherd's work at Gerling NCM were a series of term contracts generally ranging from three to six months between the Appellant and Computer People Limited, and between Computer People Limited and Gerling NCM. Mr Shepherd gave evidence that there was no guarantee that Gerling NCM would offer a new contract to the Appellant on expiry of the previous one. There was one occasion in April 2000 when Mr Gigg of Gerling NCM intimated to Mr Shepherd that a new contract would not be offered. However, Mr Gigg was unable to find employees to take on the project work done by Mr Shepherd with the result that the Appellant's contract was renewed. Further Mr Shepherd on behalf of the Appellant would make a conscious decision about whether to accept a new contract, in particular whether the project would enhance Mr Shepherd's curriculum vitae. Mr Shepherd, however, accepted in cross examination that the Appellant would not have other work lined up for him on expiry of the contract with Gerling NCM. Mr Shepherd indicated that he would await an offer of a new contract from Gerling NCM before seeking other work.

37. Mr Shepherd obtained the engagement with Gerling NCM from seeing an advert on the website of Computer People Limited which then arranged an interview for Mr Shepherd with Gerling NCM. At the interview Gerling NCM assessed Mr Shepherd's

technical expertise and interpersonal skills for working in a team not the capacity of the Appellant to supply the right personnel for the position.

38. The Appellant adduced no evidence of marketing its services or taking active steps to find alternative work for Mr Shepherd during the period of his engagement with Gerling NCM. The Appellant's accounts for the years ending 31 July 2000, 2001, and 2002 showed that there was no investment or expenditure programme which developed and expanded the business. Computer equipment constituted the sole fixed assets for the business. The Appellant's balance sheets for the accounting years of 2000, 2001 and 2002 recorded expenditure on computers at £1,119.00, £340, and £1,255.00.

39. At various times during the periods of his engagement with Gerling NCM, Mr Shepherd worked on three other assignments. Mr Shepherd supplied ongoing support to the Tote of the systems he created when he worked there between 1985 and 1995. The time spent by Mr Shepherd, however, on support work for the Tote during his contracts with Gerling NCM was not significant. During the periods under Appeal the time spent on Tote work totalled 29 hours and 58 minutes in 2000/01, and 15 hours and 44 minutes in 2001/02. Around April 2000 Mr Shepherd completed a one-off project with J Patterson & Sons converting data files for which he received a VAT inclusive fee of £2,190.56.

40. Finally Mr Shepherd together with a friend developed a computer game named *"Pen'em"* which tested participants' skills on dog handling in the context of sheepdog trials. Mr Shepherd stated that he began work on the computer game in May 2002 which was carried on concurrently with his work for Gerling NCM. Mr Shepherd negotiated a reduction in his hours with Gerling NCM from 36 to 24 hours per week from May 2004 in order to concentrate on the computer game. Mr Shepherd used another company, Digi-Game Limited, of which he was sole director and shareholder, to market the game. Mr Shepherd adduced no evidence of the actual time spent on the development of the game. The game was not brought onto the market until November 2005. Digi-Game Limited did not trade in 2004. The published accounts for Digi-Game Limited ending 31 October 2005 revealed income of £850 and administration expenses of £420. Mr Shepherd did not receive a salary from Digi-Game.

41. The Appellant's turnover for the period 6 April 2000 to 5 April 2002 was an estimated £180,549 gross of VAT, of which the "non-Gerling" work accounted for £6,803 gross of VAT.

42. At the hearing there was a dispute between Mr Shepherd and the representatives of Gerling NCM about whether he was permitted to take phone calls at the Cardiff premises of Gerling NCM from the Tote in respect of the support contract. Mr Gigg stated that Mr Shepherd's contract would have been terminated if he was found to be doing work for another organisation whilst working at Gerling's premises. The analysis of Mr Shepherd's timetable of work done for the Tote revealed that he received a total of 21 telephone calls over a period of two years (2000 -2002). Mr Shepherd confirmed that he did his work for the Tote from home.

43. Clause 14 of the Terms and Conditions of the contract CPL00 (October 2000 to April 2002) between the Appellant and Computer People, restricted the Appellant from accepting any other contract which might have created a conflict of interest with the services performed for Gerling NCM. Under Clause 3.5 of CPL00, the Appellant gave a warranty that it was not prevented by any other contract or agreement from fulfilling its obligations under the agreement.

Mutual Intention

44. Mr Gigg stated that he would prefer to take on employees but it was company policy to engage contractors to work on projects because of budgetary restrictions and limits on headcount. Mr Prentice explained that the engagement of contractors gave Gerling NCM flexibility, in that their contracts could be terminated at short notice if the workload fell. Further there were no overheads of employee indirect costs attached to contractors. The fees, however, paid to contractors were twice the annual salary of a member of staff doing equivalent work.

45. The lower and upper level contracts contained a clause to the effect that the respective agreements did not constitute an employment relationship between the parties. Under the contracts Mr Shepherd had no entitlement to holiday or sickness payments and ineligible to join the pension scheme of Gerling NCM. The Appellant under the low level contract was responsible for PAYE, income tax, corporation tax, national insurance contributions and VAT payments on the fees received.

46. Under the upper level contract the fee rate for Mr Shepherd's services was expressed as a weekly rate for 36 hours. Overtime was calculated on a pro-rata basis. The fee in the lower level contract was altered to an hourly rate from the 8 May 2002.

47. Payment of the fee by Gerling NCM would occur on the presentation of an invoice from Computer People Limited. The payment from Computer People Limited to the Appellant was by bank transfer. The Appellant was required to provide Computer People Limited with a record of the work done for Gerling NCM.

48. A period of four weeks written notice was required to terminate both sets of contracts. The contracts did permit termination with immediate effect on the occurrence of specific events.

Mutuality of Obligation and Hours Worked

49. Under the lower level contract the Appellant provided services to Gerling NCM in consideration of a payment of fee. The person supplying the service was Mr Shepherd. In the upper level contract Computer People Limited assigned Mr Shepherd to provide consultancy services to Gerling NCM for a fee. The contracts could not be terminated without notice if there was no work for Mr Shepherd except in the case of Force Majeure. Computer People Limited advised Gerling NCM in the upper level contract to give advance warning if it wished to extend the services of Mr Shepherd.

50. The summary of Mr Shepherd's time sheets for the tax years 2000/2001 and 2001/2002 revealed that he worked for Gerling NCM for a total of 3,666.85 hours which averaged out at 35.25 hours each week.

Personal Service

51. The upper level contract named Mr Shepherd as the consultant whose services were being hired. No mention was made of the Appellant in the upper level contract until 27 April 2002. The lower level contract identified Mr Shepherd as a consultant or personnel.

52. Mr Prentice confirmed that Mr Shepherd would have been tested at interview on his expertise and skills. Mr Shepherd's appointment as a contractor would have been on the basis of his suitability to do the work. Gerling NCM was not interested in the Appellant or its capacity to provide the services required. Mr Prentice doubted whether the existence of the Appellant would have been mentioned at interview. Mr Shepherd offered expertise in *Oracle* database and *PsQuel, Cobal* and *Visual Basic 6* programme languages. Mr Gigg, however, did not consider that the particular skills offered by Mr Shepherd were in short supply.

53. The lower and upper level contracts commencing 3 April 2000 did not contain a substitution clause permitting the Appellant to supply the services through a consultant other than Mr Shepherd. From 2 October 2000 the contracts included the following clause:

- The Appellant must give 14 days written notice for replacement of personnel.
- The original personnel's absence must not interfere with the performance of the specification or with any agreed timeframe.
- Gerling NCM has the right to refuse the personnel on any reasonable grounds.

54. Mr Shepherd produced a statement from Mr Gigg dated 16 February 2005 which stated that

> The following confirms the contractual arrangements between Gerling NCM (Client) and Alternative Book Company Limited (Contractor):
>
> - The services are to be supplied by Keith Shepherd on behalf of the Contractor.
> - The Contractor has the right to replace Keith Shepherd with a substitute who will carry out the services as specified in the contract.
> - If the Contractor provides a substitute who has the necessary skills to carry out the services specified in the contract, the Client agrees to accept that substitute.
> - The Contractor remains responsible for the payment of, and the work done by the substitute.

55. Mr Gigg in his evidence distanced himself from the above statement. Mr Gigg testified that the words in the statement were not his. Further he told Mr Shepherd that there would be no circumstances under which he would accept a substitute. Mr Gigg, acknowledged in cross-examination that a Mr D might have been a suitable substitute.

Mr D, however, was not a realistic possibility because he was already working for Gerling NCM as an independent contractor and about to retire. In February 2005 several contractors were asking Mr Gigg to sign similar worded statements as a way of getting round the IR35 legislation.

56. PriceWaterhouseCoopers in their capacity as Gerling's representatives, wrote to the Respondents on 6 July 2005 saying that Gerling NCM would consider a substitute if one was offered by the Appellant but would assess the substitute and his capabilities. Gerling's acceptance or rejection of the substitute would depend upon his capabilities. To date no substitute has been offered by the Appellant. Mr Gigg indicated that a substitute would be subjected to the same recruitment process as experienced by Mr Shepherd when appointed as a consultant.

57. When interviewed on 10 October 2002 Mr Shepherd told the Respondents that the substitution clause had been inserted into the assignments as its omission would have been a stronger pointer towards the work falling within 'IR35'. Further in practice Gerling NCM would either tolerate his absence and he would continue with the contract, or Gerling NCM would terminate his contract and find someone else.

58. The Appellant never sent a substitute for Mr Shepherd during his seven years with Gerling NCM. Also the Appellant did not have the capacity to provide a substitute since Mr Shepherd was its sole employee.

Control

59. The lower level contract that ran from 2 October 2000 to 26 April 2002 stated that the Appellant and Mr Shepherd would:

> "devote such time, attention, skill and ability as is necessary to attain a high standard of performance of the service in accordance with the requirements of the client [Gerling NCM] at the location or at such location as the client may reasonably require".

60. The terms and conditions of the upper level contract with effect from 27 April 2002 defined personnel as the person employed by the Appellant to provide the IT services required by Gerling NCM.

61. The lower and higher level contracts for the 6 month period commencing 3 April 2000 contained no details of the services supplied by the Appellant and Mr Shepherd. The subsequent contracts from October 2000 had the same generic description of the services to be provided by the Appellant which was:

> "As agreed between the Gerling NCM and the Appellant services shall include quality initiative projects and associated mini projects".

62. Mr Shepherd gave evidence that each contract with Gerling NCM was for work on a discrete individual project. Mr Prentice, however, indicated that if Gerling's priorities changed Mr Shepherd would have been assigned to other projects. Mr Shepherd did not agree with Mr Prentice's understanding of the contract. Mr Shepherd insisted that he had the right to say no to working on another project. Mr Shepherd, however, gave a different account during his interview on 10 October 2002

when he acknowledged that if he had been unable to continue with his project for any reason, he would be transferred to another project and not left idle, which happened on one occasion when he did some programming to help out another team.

63. Mr Shepherd gave the impression in his evidence that he had considerable freedom in how he carried out his work. He would use his skills and experience to determine the method and manner of performing the services. He worked mostly on his own. Mr Shepherd's interview in October 2002 provided a different insight of how he performed his duties. Mr Shepherd stated that whilst working on a project he was given timescales to solve specific problems. The project manager allocated the task, with Mr Shepherd reporting to him on progress. Mr Prentice confirmed that Mr Shepherd was required to make frequent informal progress reports and a formal report every month to the project manager. The Quality Assurance Team would carry out testing and acceptance checks on Mr Shepherd's work. He would be expected to rectify his errors. Further Mr Shepherd could be over-ruled by a full time senior member of staff, and that Gerling NCM would have the final say on Mr Shepherd's standard of work. Mr Shepherd accepted that he could be overruled, although this never happened.

64. According to Mr Prentice, Mr Shepherd did not work on his own. On the *Puma* project he worked with one other worker, otherwise he worked as part of a team. Mr Prentice pointed out that Gerling NCM did not supervise work in the traditional sense of overseeing every aspect. Gerling NCM was only interested in delivering schedules on time. The control mechanisms of reporting and quality assurance applied to all persons working in the organisation whether contractors or members of staff.

65. Mr Shepherd performed his services at the offices of Gerling NCM at Cardiff. This location was stipulated by Gerling NCM in the lower and upper level contracts. The specified location arose from the necessity to work on the mainframe computer of Gerling NCM. Mr Shepherd estimated that he spent four hours a week at home on tasks for Gerling NCM. Mr Shepherd, however, accepted at his interview on 12 October 2002 that home working was done out of choice, in order to demonstrate his commitment to the job which would make it more likely that his services would be retained when the contract came up for renewal.

66. Mr Shepherd in evidence stated that he was able to work at any time at his discretion provided the pre-agreed delivery dates for the projects were met. He disagreed with the evidence of Messrs Gigg and Prentice that he was expected to be at work during the core hours of 9:30am to 11:30am, and 2:00pm to 3:30pm. An examination of Mr Shepherd's time sheets for tax year 2000/01 showed that there were only 13 occasions when Mr Shepherd was not working during the core hours. The majority of the 13 occasions involved Mr Shepherd starting slightly later than 9.30am. Mr Prentice accepted that Mr Shepherd could choose his own start and finish times outside the core hours. However, this was no different from that which applied to employees under the flexible working staff policy.

67. Under the lower and upper level contracts Mr Shepherd was required to do 36 hours per week. The summary of Mr Shepherd's time sheets showed that he rarely

worked a flat 36 hours, generally he worked around 40 hours per week. However when his hours were averaged out over the two tax years in dispute it produced a figure of 35.25 hours per week. Mr Gigg acknowledged that contractors sometimes worked more or less hours than they were contracted to do. However, if he discovered that a contractor was taking advantage of the situation, he would instruct the contractor to fall back into line. Mr Gigg had not warned Mr Shepherd over his time-keeping.

68. Mr Shepherd completed a weekly time-sheet of hours worked, which required authorisation by Gerling NCM. Employees likewise completed time sheets but with different codes for the staff flexi-hour system. According to Mr Gigg, Mr Shepherd would need permission to work hours in excess of the contracted hours or at the weekends.

69. Mr Shepherd denied that he needed permission from Gerling NCM for absences or leave. The lower level contract from October 2000 to April 2002, however, included a term requiring Mr Shepherd to seek permission from Gerling NCM for any absence. The contract extension commencing on 1 January 2001 showed that a one week holiday was agreed in advance for the period 25 June 2001 to 29 June 2001. Mr Prentice said that work was planned in advance to take account of any known absences. Mr Gigg stated that if a contractor asked for time off to complete work for another organisation then, so long as the absence did not affect any Gerling deadlines, then the request would be granted.

Provision of Equipment

70. Gerling NCM provided Mr Shepherd with a computer terminal, desk, chair and phone on its premises. Mr Shepherd accepted that Gerling NCM provided him with the equipment to do the job. Mr Prentice on behalf of Gerling NCM accepted that Mr Shepherd was allowed to work from home out of choice. This happened relatively infrequently and was not a feature of the engagement.

Financial Risk

71. Mr Shepherd was paid hourly and his earnings were fixed during the duration of each contract. The only way he increased his income from the assignment with Gerling NCM was to do extra hours or work at weekend which were paid at the same hourly rate and required prior authorisation from Gerling NCM. Mr Shepherd was engaged to perform a particular service. He was not remunerated on a project or fixed fee basis. The Appellant and Mr Shepherd did not invest capital in the project. The payments under the contract were guaranteed on production of time sheets and made at regular pre-defined intervals under the terms of the lower and upper level contracts. Mr Prentice said that Mr Shepherd would be paid for rectifying errors in his work. Mr Shepherd acknowledged that there was no question of him rectifying mistakes in his own time

72. Under Clause 4 of the lower level contract (2 Oct 00 – 26 April 2002) the Appellant agreed to indemnify Computer People Limited for any financial loss arising out of or in connection with any act or omission of Mr Shepherd.

73. The lower level and upper level contracts gave Mr Shepherd no job security, no entitlement to redundancy and no legal recourse in the event of unfair dismissal. He was required to provide his own training so that he could maintain his skills in a competitive environment. Mr Shepherd took financial risks with the development of the computer game, *"Pen'em"*, which eventually was a loss making enterprise.

74. Mr Shepherd reduced his overheads by working from home and working the whole day when at the Cardiff premises. Mr Shepherd accepted that the terms of the assignment with Gerling NBC provided limited scope for efficiency savings.

Part and Parcel

75. Mr Shepherd stated that he worked largely on his own and that he would liaise occasionally with employees of Gerling NCM. In contrast Mr Prentice asserted that Mr Shepherd worked as part of a mixed team of employees and contractors. According to Mr Prentice, Mr Shepherd was the team leader for a particular project, although as team leader he did not have responsibilities for the personnel management of team members. Mr Shepherd disputed that he was ever a team leader at Gerling NCM.

76. Mr Prentice stated that Mr Shepherd would be required to make progress reports to project managers. The contents of Mr Shepherd's interview on 10 October 2002 corroborated aspects of Mr Prentice's evidence regarding reporting arrangements.

77. Mr Shepherd was given a security pass with his photograph to gain access to the Cardiff premises of Gerling NCM. He was expected to observe the Staff Code of Conduct. Mr Prentice stated that an information pack about the work practices of Gerling NCM would have been given to Mr Shepherd on appointment but Mr Prentice could not recall giving a pack personally to Mr Shepherd.

78. Mr Gigg considered that Mr Shepherd became part of the scenery at Gerling NCM. Mr Shepherd was invited to the company's Christmas dinner, which he declined. He took part in five a side football matches, which were informal social events organised by the participants rather than the company.

79. Mr Shepherd was not included in the staff appraisal scheme and had no career path within Gerling NCM.

The Submissions

The Appellant

80. Counsel contended that a hypothetical contract between Mr Shepherd and Gerling NCM would have included a substitution clause, in which case there was no requirement for Mr Shepherd to perform the services personally to Gerling NCM. Counsel submitted if that was the case the hypothetical contract would not as a matter of law constitute a contract of employment.

81. As authority for his proposition Counsel cited the Court of Appeal decision in *Express & Echo Publications Ltd v Tanton* I.C.R. [1999] 693. The case primarily

turned upon a substitution clause (3.3) in an agreement for services which stated that if

> "the driver was unable or unwilling to perform the services personally he shall arrange at his own expense entirely for another suitable person to perform the services"

82. Lord Justice Gibson at page 698 found that

> " ….in my judgment, it is plain from clause 3.3 that the applicant, as a matter of contract, was not obliged to perform any services personally himself if he was unwilling or unable to do so, provided that he could find a substitute driver".
>
> " In those circumstances, it is, in my judgment, established on the authorities that, where, as here, a person who works for another is not required to perform his services personally, then as a matter of law the relationship between the worker and the person for whom he works is not that of employee and employer".

83. If his submission about the tie breaker nature of the substitution clause did not find favour, counsel contended that the facts of Mr Shepherd's engagement with Gerling NCM should be evaluated against the case law principles on employment status in the context of other "service providers" in the same kind of business. Thus as an example the fact that Mr Shepherd only made a modest investment in capital assets for his business was not necessarily a factor pointing towards employment. A computer software consultant in business was principally selling his IT skills which did not require the same capital investment as a road haulier running his business.

84. Counsel considered that the established tax treatment of Mr Shepherd as a self-employed person was significant when determining whether the work carried out for Gerling NCM was under a contract for services. *Barnett v Brabyn* 69 TC 133 decided that established tax treatment as self-employed was *a cogent factor* pointing to a contract for services. Similarly the fact that Mr Shepherd was in business on his own account carrying out other work at the same time as supplying his services to Gerling NCM was a strong indication that the hypothetical contract would not be one of employment. Cooke J in *Market Investigations* at page 185B said :

> "The application of the general test may be easier in a case where the person who engages himself to perform the services does so in the course of an already established business of his own; but this factor is not decisive, and a person who engages himself to perform services for another may well be an independent contractor even though he has not entered into the contract in the course of an existing business carried on by him"

85. Counsel pointed to the evidence of Messrs Gigg and Prentice that Gerling NCM did not want an employment relationship with Mr Shepherd. They wanted a contractor with no strings attached. Equally Mr Shepherd was prepared to take the attendant risks of a self employed contractor in return for a fee which was roughly twice the hourly rate enjoyed by employees. Counsel submitted that the stated mutual intentions of the parties were highly relevant in determining the status of the

hypothetical contract between Gerling NCM and Mr Shepherd. Counsel disagreed with the Respondents' view that mutual intention was not relevant when construing a hypothetical contract. *Hall v Lorimer* cited mutual intention as a potential factor for deciding employment status. The High Court in *Professional Contractors Group Limited* confirmed that the case law principles on employment status applied to the IR35 legislation. Counsel cited two special commissioners' decisions *Battersby v Cambell* [2001] STC 189 and *FS Consulting v McCaul [2002]* STC 138 where evidence of mutual intention had been taken into account in cases involving IR35 determinations. Essentially Counsel submitted that mutual intention was relevant to an IR35 analysis, the precise weight to be attached to it, however, was a matter for the fact finding tribunal.

86. Counsel considered that Mr Shepherd could exercise considerable discretion in how and when he performed his services for Gerling NCM. Mr Shepherd was only paid for work done and did not have the job security and benefits enjoyed by employees.

87. The facts which pointed towards employment, such as provision of equipment by Gerling NCM, the place of work and the notice period of four weeks in the lower and upper level contracts were not significant. Counsel concluded that when all the facts were considered in the context of a business of a computer software consultant, the hypothetical contract between Mr Shepherd and Gerling NCM would have been a contract for services.

The Respondents

88. The Respondents contended that the minimum obligation necessary for a contract of service was the obligation on the part of the engager to pay the worker remuneration and for the worker to provide his services in consideration of that remuneration (*Nethermere v Taverna and Gardiner* [1984] IRLR 240). In this Appeal the Respondents submitted that the question of mutuality of obligation posed no difficulty. The evidence clearly demonstrated that Mr Shepherd would have provided services in return for remuneration under the terms of a hypothetical contract between Gerling NCM and Mr Shepherd.

89. The Respondents considered that the evidence showed that the personal service of Mr Shepherd was required by Gerling NCM and that in reality the replacement of Mr Shepherd by a substitute would not have been practical. At the highest the substitution clause in the lower and upper contracts was merely a right to propose a replacement in which case it was not a tie breaker but simply one fact among others in assessing the weight to be given to it, when deciding the status of the hypothetical contract (*Synaptek Ltd v Young* [2003] STC 543).

90. According to the Respondents the work undertaken by Mr Shepherd for the Tote during the contract with Gerling NCM was insufficient to satisfy business on own account. The income received from the Tote venture was small in comparison with that received from Gerling NCM. In any event the existence of the Tote venture did not preclude Mr Shepherd from being an employee of Gerling NCM under a hypothetical contract.

91. The Respondents submitted that no weight should be attached to Mr Shepherd's activities developing the computer game *"Pen'em"*. These activities were not those of the Appellant but of Mr Shepherd's other personal service companies. Further the activities occurred outside the period under investigation. The legislation required the Tribunal to consider the nature of the Appellant's arrangements with Gerling NCM during the period of the Appeal. The computer game was not part of those arrangements.

92. The Respondents argued that the intention of the parties was not a relevant consideration for determining the status of a hypothetical contract under the IR35 legislation. In employment status cases the Respondents contended that the intentions of the parties were only pertinent in borderline cases when the status of the work relationship was ambiguous. Lord Denning in *Massey v Crown Life Insurance Co* [1978] IRLR 31 at page 33 said:

> "The law as I see it is this: If the true relationship of the parties is that of master and servant under a contract of services, the parties cannot alter the truth of that relationship by putting a different label upon it …..On the other hand, if their relationship is ambiguous and is capable of being one or the other, then the parties can remove that ambiguity, by the very agreement itself which they make with one another. The agreement itself then becomes the best material from which to gather the true relationship between them".

93. According to the Respondents in an employment status case situation a direct relationship existed between the engager and the worker, and in those circumstances it was possible to arrive at a conclusion about whether the parties intended to create a contract of service or a contract for services. On the other hand, an IR35 situation comprised a three party arrangement where the contracting parties' intentions would always be to contract on a self employed basis. Thus the construction of the hypothetical contract would start with the premise that the parties intended it to be a contract for services which from the Respondents' point of view was not a tenable position and would undermine the purpose of the IR35 legislation. In their view the special commissioners in *Netherlane Limited* (2005) SPC00457 and *Dragonfly* were right in their findings that it was not possible for the parties to have any intention over a hypothetical contract. Finally the Respondents commented that in this Appeal it may have been the parties' intentions not to enter into an employment relationship but it was apparent from the evidence that Gerling NCM wanted Mr Shepherd to provide services under arrangements akin to those which applied to its employees.

94. The Respondents contended that the degree of control exercised by Gerling NCM over Mr Shepherd was sufficient to be consistent with a contract of service in a hypothetical relationship. The absence of financial risk, the provision of equipment, and the four weeks notice of termination were all pointers towards employment. Further the evidence indicated that Mr Shepherd had become an integral part of the Gerling organisation.

95. The Respondents concluded that the picture painted by the facts of this Appeal was one of a contract of service rather than a contract for services.

Findings of Fact

96. I find under *mutuality of obligation* that Mr Shepherd was required to perform services to complete IT projects for which Gerling NCM was obliged to pay a fee. I am satisfied that under the arrangements and circumstances of the engagement Gerling NCM was also obliged to provide work for Mr Shepherd. The indications to the contrary were that Gerling NCM would only pay for the hours worked, and no specific term in the lower and upper level contracts requiring Gerling NCM to make work available. I consider those contrary indications were outweighed by:

(1) The termination provisions in the contracts, Gerling NCM could not finish the contract on the grounds of no work without giving four weeks notice.

(2) The periods of the contract which were relatively short and aligned to the duration of specific projects.

(3) The clear expectation on the face of the contracts that Gerling NCM would supply 36 hours of work per week.

(4) The fact that Mr Shepherd did work on average 35.25 hours per week throughout the two tax years under Appeal, which included weeks when Mr Shepherd chose to take a holiday.

97. There was a clear conflict between Mr Shepherd's evidence and that of Messrs Gigg and Prentice in respect of *control*. I preferred the evidence of Messrs Gigg and Prentice which was consistent with the terms of the lower and upper level contracts. Also the contents of Mr Shepherd's interview on 10 October 2002 were more in line with the accounts given by Messrs Gigg and Prentice than with his evidence in chief given before me. I find on the issue of control:

(1) *The what*: Gerling NCM assigned Mr Shepherd to specific IT projects in accordance with its priorities. Within a project Mr Shepherd was allocated certain tasks to do. Gerling NCM retained the right to move Mr Shepherd to other projects which happened on one occasion. I was not convinced by Mr Shepherd's evidence that he would only accept a contract if the project met his needs. The tenor of Mr Shepherd's evidence was that he was keen to show commitment to guarantee the renewal of the contract with Gerling NCM. Further he took no steps to find alternative work but awaited the offer of a new contract. His evidence suggested that he would accept whatever the work given to him by Gerling NCM.

(2) *The how*: Mr Shepherd was not subjected to daily supervision by a line manager. Mr Prentice for Gerling NCM was focussed on delivering projects on time to the correct quality standard, which were achieved by project team members reporting regularly on progress and subjecting outcomes to quality assurance processes. Mr Shepherd was obliged to report regularly on progress and provide the project manager with formal reports monthly. The quality of his work was assessed by the quality assurance team. The controls of reporting and quality assurance exercised over Mr Shepherd's work were the same as those applied to Gerling's

employees working on IT projects. Finally I am satisfied that Mr Shepherd worked as a member of team not generally on his own.

(3) *The where*: Mr Shepherd accepted that he was required to attend the offices of Gerling NCM in Cardiff to perform his services. The work done from home was minimal and generally out of choice.

(4) *The when*: I am satisfied from the evidence that Mr Shepherd did not have freedom to choose his hours of work and take leave without prior authorisation. I find that Mr Shepherd could choose his start and finish times provided he was in attendance during the core hours. This was the same arrangement given to members of staff working flexi-time. Mr Shepherd required prior authorisation to take leave as was clear from the contract documentation and the evidence of Messrs Gigg and Prentice.

98. The Appellant's submission that Gerling NCM did not require Mr Shepherd to perform the contracted services personally relied upon the substitution clause in the contracts which was added in October 2000, and the existence of no right under the contracts to sue Mr Shepherd for non-performance. I find that the Appellant's submission was without substance, and that Gerling NCM had effectively contracted with Mr Shepherd to perform the required services. I reach that conclusion for the following reasons:

(1) The upper level contracts specified Mr Shepherd as the consultant supplying the services. The Appellant was not identified in the upper level contracts until 27 April 2002. The lower level contracts also named Mr Shepherd as the consultant.

(2) Gerling NCM recruited Mr Shepherd directly for his IT expertise. Gerling NCM interviewed Mr Shepherd as an individual not in his capacity as a director of a service company.

(3) The substitution clause added to the contracts from 2 October 2000 did not give the Appellant an unfettered right to provide a substitute in place of Mr Shepherd. Gerling NCM was entitled to refuse the substitute offered on any reasonable grounds. I placed no weight on the joint statement of Mr Gigg and Mr Shepherd dated 16 February 2005 which indicated that Gerling NCM would accept a substitute with the necessary skills. I accepted Mr Gigg's explanation that the words used in the statement were not his, and that any substitute offered would have to go through the same recruitment process as applied to Mr Shepherd. Mr Shepherd admitted in his interview on 10 October 2002 that the substitution clause was of no practical effect: Gerling NCM would either tolerate his absence allowing him to continue with the contract, or would terminate his contract and find someone else. In the same interview Mr Shepherd accepted that the substitution clause was inserted to meet any potential IR35 challenge. Further the facts showed Mr Shepherd performed the services throughout the seven years he worked for Gerling NCM. The Appellant offered no substitute during the seven years, which in any event would not have been possible because Mr Shepherd was its sole employee. I attach no weight to

the example given of Mr D, which was hypothetical since Mr D was retiring. Overall I conclude that the substitution clause was window dressing, and that Gerling NCM would have replaced Mr Shepherd if he was unable to carry out the work.

(4) The substitution clause at its highest was no more than a right to nominate another person in the event of Mr Shepherd being unable to perform his duties. However, on the facts found I consider that if Gerling NCM had been contracting directly with Mr Shepherd it would not have agreed to a substitution clause. This conclusion was supported by the fact that the contracts up to October 2000 did not include a substitution clause.

(5) Although there was no right to sue Mr Shepherd for non-performance, the lower level contract could be terminated without notice if Gerling NCM considered Mr Shepherd to be technically incompetent.

99. Whilst under contract with Gerling NCM I am satisfied that Mr Shepherd was required to provide his services exclusively during the hours worked. I accept the evidence of Mr Gigg that Mr Shepherd's contract would have been terminated if he had been carrying out external assignments without consent, whilst working for Gerling NCM. I have no reason to doubt Mr Shepherd's evidence that he received phone calls from the Tote at the Cardiff offices of Gerling NCM. However the number of phone calls taken was infrequent, 21 over two years with the longest being 22 minutes, and probably not noticed by Mr Gigg or Mr Prentice. Further Mr Shepherd actually did the work for the Tote in his own time at home, which suggested that Mr Shepherd accepted that he should not be doing other work when at the Cardiff premises.

100. I find no compelling evidence that the Mr Shepherd was in business on his own account during his engagement with Gerling NCM. He worked for Gerling NCM for a period of seven years albeit under a series of fixed term contracts. During that time he effectively had only one other engagement which was with the Tote. The time spent on work for the Tote was minimal in the disputed years averaging out at less than 30 minutes per week during 2000/01 and 2001/02. Further the Tote was not new work gained whilst working for Gerling NCM but a long-standing arrangement stemming from an assignment completed in 1995. The Appellant and Mr Shepherd did not market their services or seek other assignments. Mr Shepherd was content to await the offer of another contract by Gerling NCM. The Appellant cited Mr Shepherd's development of the computer game, *"Pen'em"* to demonstrate that he was in business on his own account. The facts showed that the game was not marketed until 2005, no development work was undertaken during the disputed years. The scale of the enterprise was modest realising a turnover of £850 for the year ending 31 October 2005. I placed no weight on the evidence of *"Pen'em".* The evidence was too remote from the tax years under Appeal and was not part of the arrangements under investigation since it did not involve the Appellant. Finally the modest scale of the enterprise had the hallmarks of a personal project rather than a business.

101. I find that Mr Shepherd was integrated within the IT department of Gerling NCM. He worked there for seven years, doing on average 36 hours a week until April 2004. Mr Shepherd worked generally as a member of team, which included employees. As with other members of staff working on IT projects, he was required to make progress reports and submit his work to the quality assurance team. I consider that Mr Gigg's statement that Mr Shepherd was part of the scenery was an accurate description of Mr Shepherd's relationship with Gerling NCM.

102. I find that the lower and upper level contracts specified that the agreements did not constitute or imply an employment relationship between the parties. Mr Prentice explained that Gerling NCM engaged contractors to comply with agreed staff establishment levels and to provide flexibility in the event of a downturn in business. Mr Shepherd sought engagement as a consultant rather than as an employee. The insertion of this clause in the hypothetical contract, however, would not be decisive about the nature of the working relationship between Mr Shepherd and Gerling NCM. The effect of the clause has to be considered in the context of the contract as a whole.

103. There was no substantive dispute between the parties on the facts regarding established tax treatment, provision of equipment, and financial risk. They, however, disagreed about their significance for deciding whether the hypothetical contract between Mr Shepherd and Gerling NCM was a contract for services or a contract of service, which I will deal with when I consider the hypothetical contract. I formally make the following findings:

> (1) Mr Shepherd had an established record of paying tax as a self employed person.
>
> (2) Gerling NCM provided Mr Shepherd with the equipment necessary to do the job.
>
> (3) Mr Shepherd was not exposed to significant financial risk with his engagement with Gerling NCM. He was remunerated on a fixed fee basis and had no capital invested in the assignment. Mr Shepherd, however, did not have job security or the benefit of sickness pay. There was a possibility that his contract would not be renewed, although on the evidence Mr Shepherd expected it to be renewed as he would await the offer of a new contract before looking for other work.

The Hypothetical Contract

104. Under the legislation I am required to construct a hypothetical contract between Gerling NCM and Mr Shepherd for the tax years in question from my findings on the arrangements and wider circumstances and decide whether the terms of the contract as a whole in the contextual circumstances constituted a contract for services or a contract of service.

105. I find that the hypothetical contract would contain the following terms:

(1) During the period of the hypothetical contract there would be several fixed term contracts typically ranging from three to six months. The contract would have a clause requiring Gerling NCM to give notice whether it intended to renew the contract on the same or similar terms.

(2) A requirement for Mr Shepherd to provide personally the services of an IT specialist

(3) Mr Shepherd would be assigned by Gerling NCM to quality initiative projects and associated mini projects.

(4) A requirement on Mr Shepherd to report on progress to the project manager at regular intervals and subject finished work to testing by the quality assurance team.

(5) The place of work would be at the Cardiff offices of Gerling NCM with a provision to work occasionally from home with prior agreement of the project manager

(6) The hours would be 36 hours per week Monday to Friday with a requirement to work the core hours of 9:30 am to 11:30am and 2:00pm to 3:30pm. Mr Shepherd would have a discretion on start and finish times outside the core hours.

(7) The fee for the work would be expressed at an hourly rate with the figure for 36 hours. The fee would be payable weekly in arrears by bank transfer and on production of an authorised completed time sheet for the week.

(8) The hourly fee rate would be significantly higher than a permanent employee in a similar position.

(9) Overtime and working at weekends would require specific authorisation of the project manager. The fee rate for overtime and weekend working would be at the same rate as for the 36 hours.

(10) Any leave taken during the term of the contract would require prior authorisation of the project manager.

(11) An obligation on Mr Shepherd to inform the project manager of his inability to attend work through illness or other exceptional reason.

(12) The equipment necessary to do the job would be provided by Gerling NCM.

(13) A term prohibiting Mr Shepherd from taking on other work during the term of the contract except with the consent of Gerling NCM. The consent could not be unreasonably withheld.

(14) Written notice of 4 weeks from either party would be required to terminate the contract early. There would be a residual clause permitting Gerling NCM to terminate the contract unilaterally in defined exceptional circumstances.

(15) No entitlement to paid leave or sickness benefit.

(16) Not eligible to be a member of the pension scheme.

(17) A clause to the effect that the parties did not intend to create an employment relationship

106. Before deciding whether the terms of the hypothetical contract would constitute a contract of service or a contract for services I wish to deal with the three specific points raised by Appellant's counsel namely: substitution clause; mutual intentions, and evaluating the contract in context of service providers in the same line of business.

107. Appellant's counsel submitted that the existence of substitution clause was a tie breaker in that if it existed the contract could not be an employment one. However, as Park J found in *Usetech* after reviewing the authorities starting with *Tanton* it was necessary first to determine as fact the precise effect and nature of the substitution clause, and only then would it be possible to decide whether the clause was a tie-breaker or fact amongst others. Park J stated at 1699 paragraph 53:

> "As it seems to me the present state of the law is that whether a relationship is an employment or not requires an evaluation of all of the circumstances. In the words of Hart J in *Synaptek Ltd v Young* [2003] STC 543, 75 TC 51, paragraph 12, the context is one *'where the answer to be given depends on the relative weight to be given to a number of potentially conflicting indicia'*. The presence of a substitution clause is an indicium which points towards self-employment, and if the clause is as far-reaching as the one in *Tanton* it may be determinative by itself. In this case, however, if, contrary to my view, the hypothetical direct contract between Mr Hood and ABB has to be assumed to have contained a substitution clause similar to that in the Usetech/NES contract, in my opinion (agreeing with the Special Commissioner) it would not be sufficient to override the effect of all the other considerations which led the Commissioner to decide that the relationship would have been that of employee and employer.

108. In this Appeal I found as fact that the substitution clause in the lower and upper level contracts was at its highest no more than a right to nominate another worker, and certainly did not have the far reaching characteristics of the clause considered by the Court of Appeal in *Tanton.* However, I have gone one step further in that I hold on the facts found that no substitution clause would be included in a hypothetical contract between Mr Shepherd and Gerling NCM. I found that the substitution clause in the lower and upper level contracts was window dressing and had no practical effect on how the contract would operate. I consider that if Gerling NCM had negotiated the contract with Mr Shepherd direct it would not have agreed to a substitution clause because Gerling NCM was only interested in the skills and personal services of Mr Shepherd.

109. I consider on a correct construction of the IR35 legislative provisions that I am entitled to conclude from the wider circumstances that the hypothetical contract would not include a substitution clause even though it appeared in both the lower and upper level contracts. Park J in *Usetech* decided after consideration of the all circumstances to exclude the substitution clause from the hypothetical contract. His rationale for so doing was based on the observations of Burton J in *R (on the*

application of Professional Contractors Group Ltd) v IRC [2001] EWHC Admin 236, [2001] STC 629, 74 TC 393, paragraph 48:

> "In those circumstances, of course the terms of any contract between the agency and the client as a result of which the service contractor will be present at the site are important, as would be the terms of any contract between the service contractor and the agency. But, particularly given the fact that, at any rate at present, a contract on standard terms may or may not be imposed by an agency, or may be applicable not by reference to a particular assignment, but on an ongoing basis, and may actually bear no relationship to the (non-contractual) interface between the client and the service contractor, such documents can only form a part, albeit obviously an important part, of the picture."

110. There may be an argument that the circumstances of the non-contractual interface is only relevant when there is a conflict between the lower and upper level contracts which was the case in *Usetech Limited.* I consider that argument is not supported by the observation of Burton J which emphasised that the terms of the contracts only formed part of the picture for the hypothetical contract. If, however, I am wrong about the extent of the observation of Burton J, the factual circumstances of this Appeal were within the territory of resolving a conflict between contractual terms by reference to the facts of the non-contractual interface. The conflict in this Appeal was between the lower and upper level contracts commencing 3 April 2000 which contained no substitution clause, and those contracts which did, starting from 2 October 2000. The fact that there was no substitution clause in the contracts prior to 2 October 2000 gave support to my conclusion that Gerling NCM would not have agreed to a substitution clause had it negotiated the contract direct with Mr Shepherd.

111. I am grateful to the parties for their detailed submissions on the relevance of the mutual intention of parties to the disputed issue of whether the hypothetical contract is a contract of service or not. Essentially I agree with the legal analysis of Appellant's counsel. Under the common law of employment mutual intention of the parties expressed as a statement in a written contract and or an actual intention established by evidence may be a relevant factor amongst others in establishing the correct status of a contract for work. Evidence of mutual intention is unlikely to be conclusive, its importance may vary according to the circumstances of the case. The true nature of the relationship, however, cannot be altered by simply putting a different label on the agreement. The IR35 legislation leaves in place the legal principles on employment status established by case law. The circumstances for determining the contents of a hypothetical contract include the terms of the contracts and the context in which the services are provided. A statement of mutual intention or evidence thereof may form part of the circumstances as defined by the 2000 Act and the 2000 Regulations.

112. The Respondents' contention that evidence of mutual intention should be excluded was based on the proposition that its inclusion skewed the IR35 analysis which was unfair and defeated the purpose of the legislation. I consider their proposition merged the two stages of identification of the evidence and its evaluation, and assumed that the IR35 analysis started with a blank canvass rather than a set of

actual arrangements which purport to be a contract for services. I conclude that the parties' mutual intention forms part of the circumstances which are taken into account in the analysis of the hypothetical contract. The weight to be attached to the evidence of mutual intention would vary from case to case. A mere statement asserting contract for services carries no evidential weight unless that intention has been translated into actual substantive arrangements of self-employment.

113. I was not convinced by Appellant's counsel submission that I should evaluate the hypothetical contract of Mr Shepherd in the context of service providers in the same line of business. Counsel relied on the judgments in *Market Investigations* and *Hall v Lorimer* for his submission. I consider these judgments are authorities for the proposition that each case should be decided on its own individual circumstances, and that the facts which may be compelling in one case in the light of all the facts may not be compelling in the context of another case.

114. Turning to the evaluation of the terms of the hypothetical contract, I find that

(1) Mutuality was satisfied by the obligations upon Mr Shepherd to perform the services of an IT specialist and upon Gerling NCM to pay him for those services throughout the period of the fixed term contracts.

(2) Mr Shepherd was obliged to provide his services personally and exclusively during the hours contracted.

(3) Gerling NCM was required to provide work of 36 hours per week under the contracts which could only be terminated early by four weeks notice or on exceptional grounds.

(4) Gerling NCM had the right to assign Mr Shepherd to specific work projects and teams, and require him to report on progress and submit his work for checking by quality assurance team. Mr Shepherd was obliged to attend the offices of Gerling NCM during specified hours. The controls exercised over Mr Shepherd were the same as those for Gerling's employees and consistent with a contract of service.

(5) The obligation upon Mr Shepherd to obtain prior authorisation for extra hours and absence, and the obligation upon Gerling NCM to provide equipment indicated a contract of service.

(6) No employee benefits was, in my view neutral, particularly as Mr Shepherd's fee, twice the payment rate for an equivalent member of staff, provided him with more than adequate compensation for the loss of benefits.

(7) I placed no weight on the term that the parties did not intend to create an employment relationship. This intention was not reflected in the other terms found for the hypothetical contract or in the actual work arrangements for Mr Shepherd which were similar if not the same for a Gerling employee doing equivalent work.

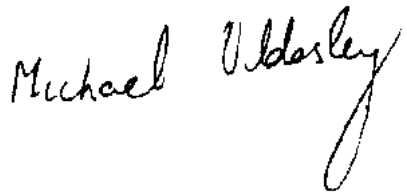
115. Under the contextual circumstances I found that Mr Shepherd was not exposed to significant financial risk from his engagement with Gerling NCM. Mr Shepherd

was part of the scenery at Gerling NCM. There was no compelling evidence that Mr Shepherd was in business on his own account during his engagement with Gerling NCM. His established tax treatment as a self-employed person did not prevent him from being an employee of Gerling NCM and of no significance in the light of all the circumstances.

116. I find that the hypothetical contract would have the necessary irreducible minimum to constitute an employment contract. When I stand back and consider the position as a whole I conclude that the picture painted of the relationship between Gerling NCM and Mr Shepherd was overwhelmingly one of employment.

Decision

117. In the light of my findings I decide in principle that if the services were provided under a contract directly between Mr Shepherd and Gerling NCM, Mr Shepherd would be regarded for income tax purposes as an employee of the Gerling NCM for the tax years 2000/01 and 2001/02, and for the purposes of Parts I to V of the Contributions and Benefits Act as employed in employed earner's employment by Gerling NCM for the period 6 April 2000 to 5 April 2002. I, therefore dismiss the Appeal.



MICHAEL TILDESLEY OBE
SPECIAL COMMISSIONER
RELEASE DATE: 19 May 2008

LON/

Authorities referred to in skeletons and bundles but not referred to in the decision:

Airfix Footwear Ltd v Cope [1978] IRLR 396
Ansell Computer Services Ltd v Richardson (Inspector of Taxes) [2004] STC (SCD) 472.
Datagate Services v HMRC [2007] SPC 00656
Davies v Braithwaite [1931] 2KB 628
Esterson, R v Revenue and Customs [2005] EWHC 3037 (Admin)

Ferguson v John Dawson [1976] IRLR 346
Future Online v Foulds [2004] 76 TC 590
Island Consultants Ltd v The Commissioners for HMRC [2007] SPC 00618
Global Plant Ltd v Secretary of State for Health and Social Security [1972] 1 QB 139 [1971] 3 All ER 385.
Lime-IT Ltd v Justin (Officer of the Board of Inland Revenue) [2003] STC (SCD) 15
Massey v Crown Life Insurance Co [1978] 1 WLR 676, [1978] ICR 590, [1978] 2 All ER 576, [1978] IRLR 31, CA.
McManus v Griffiths (Inspector of Taxes) [1997] STC 1089, 70 TC 218
Morren v Swinton and Pendlebury Borough Council [1965] 2 All ER 349
MKM Computing Ltd v HMRC [2007] SPC 00653
Netherlane Limited v Simon York [2004] SPC00457
Nethermere (St Neots) Ltd v Gardiner [1984] ICR 612, [1984] IRLR 240, CA.
Prater v Cornwall County Council [2006] 2 AllER 1013
WHPT Housing Association Limited v The Secretary of State for Social Services 1981 Unreported SJ/465/80
Young v Woods [1980] IRLR 201

Tilbury Consulting Ltd v Gittins (HMIT) (2003) Sp C 379

Dr AN Brice.

Decision released 15 August 2003.

Income tax – service company – IR35 – Whether individual would be regarded as employed – application for witness summons objected to – whether commercial risk to taxpayer overrode interests of justice – Special Commissioners (Jurisdiction and Procedure) Regulations 1994 (SI 1994/1811), reg. 5(1).

HEADNOTE

In an appeal relating to the status of an individual who supplied consultancy services through his own company, the interests of justice were best served by granting a witness summons even where there was a real commercial risk to the taxpayer in doing so.

Facts

T, a director of the taxpayer company, contracted with the taxpayer which contracted with C to provide his services, C in turn contracting with F. An issue arose whether, had the arrangements taken the form of a contract between T and F, T would have been regarded as employed in employed earner's employment by F (see *FS Consulting Ltd v McCaul* (2002) Sp C 305, at para. 8(2)).

On 7 September 2001, T contacted the Revenue for an opinion about his status. With T's consent, the tax inspector contacted B (a representative of F) asking for information to enable her to establish the exact nature of the terms and conditions which existed in respect of T's engagements and asking B to provide information in reply to 22 detailed questions. When she received the reply, the inspector formed the opinion that, if there had been a contract between F and T, it would be considered to be a contract of service. There was further correspondence and, without informing the taxpayer of her intention to do so, the inspector wrote again to B asking for further information about the use of a substitute if T were not available. B replied but the tone of his response gave the impression that F was not happy about being troubled again about the matter.

The inspector refused to change her view of T's position and the taxpayer appealed. The Revenue wanted a witness summons to be issued to B under the *Special Commissioners (Jurisdiction and Procedure) Regulations* 1994, reg. 5(1) requiring his attendance at the hearing of the appeal to give oral evidence but the taxpayer objected arguing that there was a real commercial risk to the taxpayer if the witness summons was issued since the indications were that B was losing patience and F might conclude that the arrangements with T were more trouble than they were worth. One of T's contracts had already been terminated. The appellant argued that B's evidence could be given in writing on the basis of the replies he had already given.

Issue

Whether it was appropriate to issue a witness summons.

Decision

The special commissioner (Dr AN Brice) (directing the issue of the witness summons to B) said that the interests of justice had to be balanced against the commercial risk to T on the other. The interests of justice were the overriding objective. Although reg. 5 gave the special commissioners a discretion whether to issue a witness summons the presumption was that an application for such a summons would normally be granted. Regulation 5(11) provided that a person on whom a witness summons had been served might apply to have it set aside and no doubt that would be done if a summons was not applied for in good faith, or if the witness was unable to give relevant evidence, or if the application was irrelevant, speculative or oppressive.

In the present appeal the commissioner was satisfied that the application was none of those things and it was clear that B had relevant evidence to give. The explanatory leaflet entitled 'IR35 Appeals' published by the Presiding Special Commissioner and the decision of the special commissioners in *Lime-IT Ltd v Justin* (2002) Sp C 342) emphasised the desirability of B giving evidence. It was also relevant that, although the taxpayer in this appeal was the company, there would be no difficulty in T personally giving oral evidence about his notional contract with F. It was therefore desirable for the other party to do so and B's evidence might well be expanded or clarified by oral evidence. While fully appreciating that T's main argument was the commercial risk, the interests of justice were best served by granting the application for the witness summons.

REASONS FOR DIRECTION

Background

1. On 12 June 2003 the special commissioners gave notice of a preliminary hearing in this appeal which is an appeal by Tilbury Consulting Ltd ('the appellant') against a decision of Mrs Margaret Gittins ('the respondent'). Thereafter the parties corresponded and agreed a number of directions. However, the respondent wanted a witness summons to be issued to Mr Ian Baker of Ford Motor Co ('Ford') requiring his attendance at the hearing of the appeal to give oral evidence but the appellant objected. The preliminary hearing was held on 18 July 2003 and a number of directions were given at that hearing. Direction (2) was that, on the application of the respondent, the witness summons would be issued. Direction (2) stated that reasons for the direction would be given separately. These are the reasons referred to.

The regulations

2. The procedure before the special commissioners is governed by the *Special Commissioners (Jurisdiction and Procedure) Regulations* 1994 (SI 1994/1811). Regulation 5 contains the provisions about the summoning of witnesses and the relevant part provides:

'5(1) Where a party to any proceedings requires the attendance of a person at the hearing of those proceedings to give evidence or to produce any document in his possession, custody or power relevant to the subject matter of the proceedings, a Special Commissioner may, on the application of that party, issue a summons (in this regulation referred to as a "witness summons") requiring the attendance of that person at the hearing, or the production of the document, wherever that person may be in the United Kingdom.'

The facts relevant to the application

3. Mr Roger Tilbury, a director of the appellant, contracts with the appellant who contracts with Compuware who contracts with Ford. The issue in the appeal is whether, had the arrangements taken the form of a contract between Mr Tilbury and Ford, Mr Tilbury would be regarded as employed in employed earner's employment by Ford (see FS Consulting Ltd v McCaul (2002) Sp C 305 at para. 8(2)).

4. On 7 September 2001 the representatives of Mr Tilbury contacted the Inland Revenue and asked for an opinion about his status. With the consent of Mr Tilbury, the respondent wrote on 19 February 2002 to Mr Ian Baker of Ford. The respondent said that she had received an enquiry in respect of Mr Tilbury who supplied consultancy services through his own limited company to Ford. She said that she needed to establish the exact nature of the terms and conditions which existed in respect of the engagements and asked Mr Baker to provide information in reply to 22 detailed questions.

5. On 18 July 2002 Mr Baker sent a reply by facsimile transmission to the respondent's 22 questions. On 6 August 2002 the respondent wrote to the appellant's representatives to say that she had considered the information supplied by Ford and was of the opinion that, if there had there been a contract between Ford and Mr Tilbury, it would be considered to be a contract of service. Further correspondence between the parties followed and, on 4 December 2002, the respondent wrote again to the appellant's representatives to say that she had not changed her view. The last paragraph of that letter stated that the opinion in it did not create a decision subject to appeal but the appellant could request a s. 8 decision against which there was a right of appeal.

6. Without informing the appellant of her intention so to do the respondent wrote again to Mr Baker on 6 January 2003 and asked for some further information about the use of a substitute if Mr Tilbury were not available. Mr Baker replied on 14 January 2003 to give the information requested. The tone of his reply gave the impression that he had not been too pleased to have been troubled again about the matter.

The arguments of the Inland Revenue

7. For the Inland Revenue Mr Williams applied for the witness summons. He argued that, in order to decide the issue in the appeal, it was necessary for the special commissioners to have evidence from both parties to the notional contract and he referred to the supplement to the explanatory leaflet about appeals and other proceedings before the special commissioners entitled *'IR35' Appeals* published by the presiding special commissioner on 21 March 2002. He also relied upon para. 10 in Lime-IT Ltd v Justin (2002) Sp C 342. If a witness summons were not issued it would mean that the appeal would be decided without oral evidence from one of the parties to the notional contract and the special commissioners would be unable to see and hear a witness give that evidence and ask questions of their own. It would not be adequate for further information to be obtained in writing or through the appellant's representatives. Mr Williams argued that the interests of justice overrode the arguments put forward on behalf of the appellant.

The arguments of the appellant

8. For the appellant Miss Naylor argued that there was a real commercial risk to the appellant if the witness summons were issued. One of Mr Tilbury's contracts had already been terminated and there was a real risk that Mr Baker or Ford might conclude that the arrangements with Mr Tilbury were more trouble than they were worth. The tone of Mr Baker's second letter of 14 January 2003 indicated that he might be losing his patience. Further, Mr Baker had already written twice to the Inland Revenue and so his evidence was in writing. The appellant did not challenge the written evidence and the oral

evidence would only duplicate it. Ms Naylor distinguished *Lime-IT* where there was no evidence from the client but in this appeal there was evidence in writing from Ford. Ms Naylor relied upon reg. 17(6) which provided that the tribunal could not refuse to admit evidence which would be admissible in proceedings before a court of law. She argued that, under reg. 5(4)(b), Mr Baker could not be cross-examined by the Inland Revenue and it was, therefore, difficult to see what his presence would add.

Reasons for directions

9. Before considering the arguments of the parties I set out the relevant provisions of the supplement to the explanatory leaflet referred to by Mr Williams. The relevant paragraphs state:

'1. *What is an IR35 appeal?*

An IR35 appeal is an appeal against a decision of the Inland Revenue that payments made to intermediaries such as service companies should be treated as earnings of the worker for the purposes of income tax and/or national insurance contributions.

In IR35 appeals the worker is called "the worker", the service company (or other intermediary) is called "the intermediary", and the person, firm or company to whom the worker supplies work is called "the client".

5. *Why is an IR35 income tax appeal unusual?*

An IR35 income tax appeal is unusual because it is the intermediary which receives the decision from the Inland Revenue and so it is the intermediary which is the appellant in the appeal. However, the two persons most affected by the decision of the Inland Revenue are the worker and the client and neither of these are the appellant in the appeal.

8. *What oral evidence is likely to be needed?*

Since the question to be decided is whether the worker should be regarded as an employee of the client it would be helpful for both the worker and someone from the client to give oral evidence about the factors mentioned in 6 above. Oral evidence would also be useful about: the extent to which the terms of the written contracts have been carried out; whether there has been any unwritten variation in the contracts; and whether any additional terms have been implied in the contracts.

9. *How should I get evidence from the client?*

You can ask someone from the client to attend at the hearing of your appeal and to give evidence on your behalf.

If you wish to make sure that someone comes then you can apply in writing for a witness summons. Please read paragraph 6 of the Explanatory Memorandum which tells you how to do this.'

10. These paragraphs explain the desirability of producing evidence from both the worker and the client. In *Lime-IT* there was no witness to give evidence on behalf of the client and the special commissioner said, in para. 10:

'In future cases on this legislation (and its income tax equivalent) the special commissioners will wish to explore at a preliminary hearing whether it is possible to obtain evidence from the client.'

11. Once again this emphasises the desirability of producing evidence from both the worker and the client.

12. With those matters in mind I turn to consider the arguments of the parties and here I have to

balance the interests of justice on the one hand and the commercial risk to Mr Tilbury on the other.

13. Dealing first with the interests of justice this is, of course, the overriding objective. Although reg. 5 gives the special commissioners a discretion as to whether to issue a witness summons the presumption must be that an application for such a summons will normally be granted. Regulation 5(11) provides that a person on whom a witness summons has been served may apply to have it set aside and no doubt that would be done if a summons were not applied for in good faith, or if the witness was unable to give relevant evidence, or if the application were irrelevant, speculative or oppressive. In this appeal I am satisfied that the application is none of those things and it is clear that Mr Baker has relevant evidence to give. The document published by the presiding special commissioner, and the decision in *Lime-IT*, emphasise the desirability of his giving it. It is also relevant that, although the appellant in this appeal is Tilbury Consulting Ltd, there will be no difficulty in Mr Tilbury personally giving oral evidence about his notional contract with Ford. It is, therefore, desirable for the other party to the notional contract (Ford) to give oral evidence about it as well.

14. The appellant argues that Mr Baker's evidence is already in documentary form and that the oral evidence will only repeat this. However, that is not inevitable and the documentary evidence may well be expanded and/or clarified by oral evidence.

15. The appellant's main argument is the commercial risk faced by Mr Tilbury. Whilst fully appreciating this I have nevertheless concluded that the interests of justice are best served by granting the application for the issue of the witness summons.

Direction

16. For the above reasons a direction has been given that a witness summons be issued to Mr Ian Baker of Ford requiring his attendance at the hearing of the appeal to give oral evidence. When the date of the hearing has been fixed the summons will be issued.

(Application granted)

Case No: CH/2008/APP/0289

Neutral Citation Number: [2008] EWHC 3284 (Ch)
IN THE HIGH COURT OF JUSTICE
CHANCERY DIVISION

Royal Courts of Justice
Strand
London WC2A 2LL

Monday, 24 November 2008

BEFORE:

SIR DONALD RATTEE

BETWEEN:

HER MAJESTY'S REVENUE & CUSTOMS

Applicant/Claimant

- and -

LARKSTAR DATA LTD

Respondent/Defendant

No representation provided

Approved Judgment

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1. SIR DONALD RATTEE: This is an appeal by Her Majesty's Revenue & Customs against a decision of the General Commissioners allowing an appeal by Larkstar Data Ltd against a determination by Her Majesty's Revenue & Customs of liability to income tax under PAYE regulations and social security contributions for the period of 6 April 2001 to 5 April 2003.

2. The relevant background facts can be stated fairly shortly. Larkstar Data Ltd, to which I will refer simply as Larkstar, is a company which describes its business as "the provision of computer consultancy services". One Mr Alan Brill is its sole director.

3. Technology Project Services International Ltd ("TPS"), is a company which acts as an agency for the engagement of contractors by a third company, Matra Bae Dynamics UK Ltd ("MBDA") which at the material time worked on defence missile systems and was engaged on a long project which required specialist computer services.

4. For the purpose of acquiring these services MBDA entered into agreements with TPS for their procurement.

5. Starting on 11 August 2000 Larkstar entered into a series of agreements with TPS for the provision of computer consultancy services to MBDA. Pursuant to those agreements Larkstar provided to MBDA the specialist services of Mr Brill, which he provided for MBDA at its premises. There was no direct contract between Mr Brill and MBDA. He was the person whom Larkstar provided for the purpose of fulfilling its contractual obligations to TPS.

6. However HMRC took the view that these arrangements were such as to fall within the anti-avoidance provisions contained in schedule 12 to the Finance Act 2000, dealing with income and corporation tax, and regulation 6 of the Social Security Contributions (Intermediaries) Regulations 2000, Statutory Instrument 727 of 2000 ("the Social Security Regulations"), dealing with national insurance contributions. These provisions together are commonly referred to as the IR35 legislation.

7. The Revenue served notices of determination and decision on Larkstar on the basis that the IR35 legislation applied.

8. The purpose of the IR35 legislation was explained by Robert Walker LJ, as he then was, in R (on the application of Professional Contractors Group Ltd and others) v Inland Revenue Commissioners [2001] EWCA Civ 1945 reported in 2002 Simon's Tax Cases at 165 as follows:

> "…to ensure that individuals who ought to pay tax and NIC as employees cannot, by the assumption of a corporate structure, reduce and defer the liabilities imposed on employees by the United Kingdom's system of personal taxation."

9. The IR35 legislation provides, so far as material for present purposes, as follows. Regulation 6 to the Social Security Regulations provides:

> **"6.** (1) These Regulations apply where –

(a) an individual ("the worker") personally performs, or is under an obligation personally to perform, services for the purposes of a business carried on by another person ("the client"),
(b) the performance of those services by the worker is carried out, not under a contract directly between the client and the worker, but under arrangements involving an intermediary, and
(c) the circumstances are such that, had the arrangements taken the form of a contract between the worker and the client, the worker would be regarded for the purposes of Parts I to V of the Contributions and Benefits Act as employed in employed earner's employment by the client.
(3) Where these Regulations apply –
(a) the worker is treated, for the purposes of Parts I to V of the Contributions and Benefits Act, and in relation to the amount deriving from relevant payments and relevant benefits that is calculated in accordance with regulation 7 ("the worker's attributable earnings"), as employed in employed earner's employment by the intermediary, and
(b) the intermediary, whether or not he fulfils the conditions prescribed under section 1(6)(a) of the Contributions and Benefits Act for secondary contributors, is treated for those purposes as the secondary contributor in respect of the worker's attributable earnings.
And Parts I to V of that Act have effect accordingly."

10. The corresponding provisions, so far as material, of schedule 12 to the Finance Act 2000 are as follows:

> "(1) This Schedule applies where:
> (a) an individual ("the worker") personally performs, or is under an obligation personally to perform, services for the purposes of a business carried on by another person ("the client"),
> (b) the services are provided not under a contract directly between the client and the worker but under arrangements involving a third party ("the intermediary"), and
> (c) the circumstances are such that, if the services were provided under a contract directly between the client and the worker, the worker would be regarded for income tax purposes as an employee of the client.
> (4) The circumstances referred to in sub-paragraph (1)(c) include the terms on which the services are provided, having regard to the terms of the contracts forming part of the arrangements under which the services are provided."

11. I need not refer to the provisions of the 2000 Act setting out the consequences of schedule 12 applying. They are not in issue. Suffice it to say that, as with the Social Security Regulations, they treat the worker as employed by the intermediary. I am only concerned on this appeal, as were the General Commissioners, with the question of whether schedule 12 does apply to the present case. It is common ground that there is no relevant difference for present purposes between the terms of Regulation 6 of the Social Security Regulations and Schedule 12 to the 2000 Act.

12. The General Commissioners rejected the view of the Revenue that the IR35 legislation did apply in the present case. They concluded that, had Mr Brill, "a worker" for the purpose of the IR35 legislation, provided the services he did to MBDA, "the client" for the purpose of the legislation, under a direct contract with MBDA, he would properly have been regarded as an independent contractor with, and not an employee of, MDBA, with the result that the IR35 legislation did not apply.

13. The Revenue appeals to this Court against that decision on four grounds set out in its grounds of appeal. The grounds of appeal are:

> "The General Commissioners erred in law in that they
> (1) misdirected themselves in law and in particular having identified the correct question they did not answer it and applied the wrong test in determining whether or not the arrangements would have amounted to a contract of or for service if they had been entered into directly with the client.
> (2) misdirected themselves in law in their approach to the issues of
> (a) control (b) mutuality of obligation and (c) the relevance of a number of considerations to the question they had to determine.
> (3) took into account irrelevant considerations and based their decision on a number of findings of fact which were either not supported by the evidence or inconsistent with other findings of fact.
> (4) reached a conclusion which was not open to them on the evidence before them."

14. In the Case Stated by the General Commissioners they set out facts found by them in paragraph 5. I shall refer to some of those findings which are as follows.

15. (1) On 11 August 2000 Larkstar entered into the first agreement with TPS for the provision of consulting services to MBDA.

16. (2) This was followed by four further successive such agreements. In fact the agreements were each for a period of six months immediately following the previous agreement, making a total of two and a half years during which Mr Brill's services were provided to MBDA pursuant to those agreements.

17. (3) Remuneration to be paid by MBDA was based on an hourly rate.

18. (4) There was no provision in the contracts for sickness, holidays, pensions, bonuses or employee's rights and privileges, such as car parking, sports facilities or medical services.

19. (5) An ongoing project known as ASRAAM, being worked on by MBDA, was the sole purpose of the contracts entered into between Larkstar and TPS.

20. (6) The work to be done by Mr Brill had to be performed exclusively at MBDA's premises for security reasons.

21. (7) Mr Brill was encouraged to work during MBDA's core hours for the purpose of co-ordinating his work with that of others, but he was free to decide when to work outside these core hours.

22. (8) Once Mr Brill and MBDA had negotiated the next stage of the ASRAAM project no control over how Mr Brill did his work was exercised by MBDA.

23. (9) Each of the five contracts allowed a substitute to be provided for Mr Brill, but the overriding security arrangements required substitutes to undergo procedures as rigorous as contractors and in practice that did not happen.

24. (10) Each of the five contracts required Mr Brill to provide his own equipment, but the overriding security arrangements required him to use MBDA's on-site equipment.

25. (11) Mr Brill was deliberately set apart by MBDA from their company's structure so that he could independently analyse and criticise and test their systems so as to further the success of the project. His professional independence was what MBDA hired. Without it there was no point in hiring him.

26. (12) He occupied no post and had no title. His badge described him as a contractor.

27. (13) When the project ended, or, if it had been terminated prematurely, the engagement ended, there was no obligation on MBDA to provide work outside or beyond each contract and, if it had been offered, no obligation on Mr Brill to do it.

28. (14) Mr Brill was free to work for other clients but did not in fact do so.

29. (15) The engagement could be terminated (i) at the end of each contract without notice (ii) by either party giving the other one month's notice within the contract period and (iii) at the end of the project without notice, as in fact happened.

30. (16) Mr Brill had no financial risk apart from loss of income (i) on premature termination and (ii) on having to redo unsatisfactory work at his own expense.

31. (17) Larkstar's involvement with MBDA ended on or about 31 October 2003.

32. On this appeal the Revenue submits that I should set aside the General Commissioners' conclusion because they misdirected themselves in law in various respects and made findings of fact unsupported by the evidence. I shall consider each of the four grounds of appeal in turn.

33. Ground 1 (and I re-quote it for purposes of convenience) is:

> "The General Commissioners misdirected themselves in law. In particular having identified the correct question they did not answer it and applied the wrong test in determining whether or not the arrangement would have amounted to a contract of or for service if they had been entered into directly with the client."

As developed by Mr Nawbatt for the Revenue, the substance of its complaint here is that the General Commissioners purported to answer the question they had identified by reference to the actual facts found by them without carrying out the process required by law of constructing a hypothetical contract between Mr Brill and MBDA.

34. As authority for the correctness of this latter process Mr Nawbatt relied on various dicta in other cases and in particular on a passage in the judgment of Park J in Usetech Ltd v Young (HM Inspector of Taxes) 76 Tax Cases 811. In paragraph 9 of his judgment, after setting out the relevant provisions of paragraph (ii) of schedule 12 to the Finance Act 2000, Park J said this:

> "A more general point of construction is worth spelling out at this stage. The conditions of sub-paragraphs (a) and (b) involve an analysis of the actual facts and legal relationships, but when that analysis shows that those two sub-paragraphs are satisfied sub-paragraph (c) involves an exercise of constructing a hypothetical contract which did not in fact exist, and then inquiring what the consequences would have been if it had existed. There may be room in some cases for dispute about what the hypothetical contract would contain."

35. While I agree that this is an accurate analysis of the process to be carried out, I am afraid I fail to see any real substance in the Revenue's objection to the Case Stated on this ground. It is true that the General Commissioners did not so express the task they were performing, but it is, in my judgment, clear from the Case Stated that the General Commissioners were considering whether, on the facts they have found, including the terms of the actual contracts between Larkstar and TPS, the relationship between Mr Brill and MBDA would have been one of master and servant or one of independent contractors, had Mr Brill been doing what he did in the way he did and in the circumstances he did under a contract between himself and MBDA.

36. Although it is no doubt true that the General Commissioners could have described their process in more precise legal terms, such as those used by Park J and other judges, I am not satisfied that the process they did adopt was not that required by paragraph 12(1)(c) of schedule 12 to the 2000 Act. So, I reject this first ground of appeal.

37. Ground 2 is as follows:

> "Misdirected themselves in law in their approach to the issues of (a) control (b) mutuality of obligation (c) irrelevance of a number of considerations to the question they had to determine."

38. As to (a), the question of control, Mr Nawbatt made the following submissions:
(1) The General Commissioners failed to have regard to the dictum of Lord Parker, CJ, in Morren v Swindon & Pendelbury Borough Council [1965] 2All ER 349, to which the General Commissioners had been referred by the Revenue. The dictum concerned, directed to the identification of a contract of service as opposed to a contract for services, is as follows:

> "The cases have over and over again stressed the importance of the factor of superintendence and control, but that it is not the determining test is quite clear. In *Cassidy v Minister of Health*, Somervell LJ

> referred to this matter, and instanced, as did Denning LJ in the later case of *Stevenson, Jordan & Harrison v MacDonald & Evans*, that clearly superintendence and control cannot be the decisive test when one is dealing with a professional man, or a man of some particular skill and experience. Instances of that have been given in the form of the master of a ship, an engine driver, a professional architect or, as in this case, a consulting engineer. In such cases there can be no question of the employer telling him how to do work; therefore, the absence of control and direction in that sense can be of little, if any, use as a test."

39. The Revenue submit that the statements by the General Commissioners in paragraph 9(b)(iv) of the Case Stated that the fact that Mr Brill was a consultant and that there was no control by MBDA as to how he did his work indicated that he was independent, without any reference to Lord Parker, CJ's dictum, show that the General Commissioners took no proper account of the principle enunciated in that dictum. I think there is force in this submission and it is supported by the unfortunate fact that the General Commissioners appear to have overlooked the fact that the Revenue representative appearing before them had referred them to authority in the form of decided cases - see paragraph 8 of the Case Stated. That paragraph reads as follows:

> "At the conclusion of the parties' submissions, and having regard to the fact that none of the cases in Bundles A and B had been referred to, the Chairman of the Commissioners asked the Inspector whether he wished to draw attention to any of the reported cases. The Inspector declined."

40. This is quite wrong and the error in the draft case was drawn to the attention of the clerk to the General Commissioners with a reminder that the Inspector had referred to no less than nine authorities and provided the clerk with a copy of his typed speaking brief during the hearing. If, as appears to be the case, the General Commissioners took no account of the authorities to which they were referred, one can well understand how they may have come to misdirect themselves on the law, and I accept that they did in this respect.

41. (2) Mr Nawbatt for the Revenue relied on another unsatisfactory feature of paragraph 9(b)(iv) of the Case Stated and the General Commissioners' findings on the question of control, and that is that it refers back to the finding of fact in paragraph 5.6 that:

> "Mr Brill was encouraged to work during MBDA's core hours"

when in fact it is apparent from paragraph 7(4)(viii) of the Case Stated that Mr Brill's own evidence was to the effect that he was required to work 37 hours a week including the core times of 9.30am to 12 noon and 1.00pm to 4.00pm. There was no other evidence to the contrary save perhaps a document that did not come into existence until 2005, long after the relevant period, dealing with relations between MBDA and what were called in the document their "sub-contractors".

42. Bearing in mind the General Commissioners' statement in paragraph 9(a)(iv) of the Case Stated that they found Mr Brill's evidence to be convincing and to be preferred in

all cases of apparent conflict, I find it impossible to see how the finding that Mr Brill was only encouraged as opposed to required to work the core hours can be justified by the evidence. I accept Mr Nawbatt's submission that, had they made a finding in accordance with Mr Brill's evidence that he was required to work these hours, they might well have taken the view that such finding pointed to employment rather than, as they say in paragraph 9(b)(iv) "being neutral as between employment and independent sub-contracting."

43. As to ground 2(b), that the General Commissioners misdirected themselves in law on the issue of mutuality of obligation, Mr Nawbatt made the following submissions: (1) the General Commissioners considered the issue of mutuality of obligation in paragraph 9B 10 and 9(b)(xii) of the Case Stated, which I shall read. Paragraph 9(b)(x) is as follows:

> "Whether the worker works continuously for the client or whether the worker has a series of engagements. Throughout Mr Brill worked only on the ASRAAM project but under a series of five contracts. When the project ended, or if it were terminated prematurely, his engagement would end. There was no obligation on the employer to provide work outside or beyond each contract. This indicates that he was independent."

44. Then paragraph 9(b)(xii) under the heading "Whether the client is obliged to offer work and whether the worker is obliged to do the work", reads as follows:

> "There was no obligation either way. The obligations of the parties were contained in and confined by the contract. This indicates that he was independent."

45. (2) Mr Nawbatt submitted that the General Commissioners misdirected themselves in law in directing themselves that the absence of any obligation in one six-month contract to offer work to Mr Brill after the end of that contract indicated that Mr Brill was not employed by MBDA. In so finding the General Commissioners completely ignored statements of principle by the Court of Appeal in Cornwall County Council v Prater [2006] EWCA Civ 102. The issue in that case was whether Mrs Prater, who during a ten-year period, had had a series of work contracts with the council to teach pupils unable to attend school, was, by those contracts, an employee of the council or an independent contractor.

46. At paragraph 40 of the transcript Mummery LJ said this:

> "To sum up, the legal position between the Council and Mrs Prater was as follows.
> (1) During that period 1988 to 1998 Mrs Prater had a number of work contracts with the Council. The issue was whether or not they were contracts of service. If they were, she enjoyed continuity of employment, notwithstanding the breaks between the contracts.
> (2) Under the contracts Mrs Prater was engaged and was paid to teach individual pupils unable to attend school.

> (3) There can be no doubt that, if she was engaged to teach the pupils in a class, collectively or individually, at school under a single continuous contract to teach, Mrs Prater would have been employed under a contract of service.
> (4) It makes no difference to the legal position, in my view, that she was engaged to teach the pupils out of school on an individual basis under a number of separate contracts running concurrently or successively.
> (5) Nor does it make any difference to the legal position that, after the end of each engagement, the Council was under no obligation to offer her another teaching engagement or that she was under no obligation to accept one. The important point is that, once a contract was entered into and while that contract continued, she was under an obligation to teach the pupil and the Council was under an obligation to pay her for teaching the pupil made available to her by the Council under that contract. That was all that was legally necessary to support the finding that each individual teaching engagement was a contract of service."

47. Longmore LJ referring to a submission that:

> "There was no or no sufficient "mutuality of obligation" which was part of the irreducible minimum which had to exist before a contract could be a contract of employment."

said this at paragraph 43 and following of the transcript:

> "43. I cannot accept this submission. There was a mutuality of obligation in each engagement; namely that the County Council would pay Ms Prater for the work which she, in turn, agreed to do by way of giving tuition to the pupil for whom the Council wanted her to provide tuition. That to my mind is sufficient "mutuality of obligation" to render the contract a contract of employment if other appropriate indications of such an employment contract are present.
> 44. If Ms Prater had been seeking to prove that there was a long-term or global contract of employment, the fact that the Council were not obliged to offer her any work and that, if they did offer her work, she was not obliged to accept that offer would, no doubt, mean that no such long-term or global contract existed. But Ms Prater put forward no such argument. She was only saying that the individual commitments, or engagements, once entered into, constituted contracts of employment. The Employment Tribunal held that this was indeed the position in paragraph 14 of their decision and I can detect no error of law in their conclusion."

48. (3) Those statements of the relevant law seem to have been ignored by the General Commissioners, because what they say in paragraph 9(b)(x) and (xii) of the Case Stated is quite inconsistent with them.

49. (4) In paragraph 9(c) of the Case Stated the General Commissioners indicate that they regarded the alleged lack of mutual obligation as one of the most compelling factors indicating, in their view, independent contracting.

50. (5) This conclusion is vitiated by the clear misdirection by the General Commissioners of themselves on the relevant law.

51. Mr Stafford on behalf of Larkstar, the respondent on this appeal, argued that, and I quote from his skeleton argument:

> "Seen in the context of the findings of fact made by the General Commissioners, it can be seen that the point which they were making was not that there was no mutuality of obligation during the currency of any of the fixed term contracts. Indeed, the explicit words of the finding of fact and of paragraph 9B(l0) & (12) reveals this to be so. Instead, the General Commissioners were drawing a contrast between project work and employment. All employee who is given a task remains employed even when that task IS completed, and his employer is generally going to look for something else for him to do. If something is found, then an employee cannot simply turn his nose lip at it. By contrast, someone who is only engaged for the duration of a project cannot expect an entitlement to be offered other work, nor can the end-user be required to find other work."

52. I am afraid I do not find this provides any answer to the Revenue's argument. The relevant question for the General Commissioners was whether Mr Brill would have been employed by MBDA during the two and a half years of the hypothetical contract or contracts between them. The decision of the Court of Appeal in Prater seems to me clearly to indicate that the fact relied on by the General Commissioners, namely that MBDA would have been under no obligation to offer further work outside the terms of these contracts, is irrelevant to the question in issue. Thus I accept Mr Nawbatt's submission that here one finds a clear misdirection of themselves by the General Commissioners as to the law.

53. I turn then to (c) of ground of appeal (2), namely that the General Commissioners misdirected themselves in their approach to the relevance of a number of considerations to the question they had to determine. Some of the points relied on by Mr Nawbatt under this heading were the following.

54. Mr Nawbatt's first point relates to the provisions for termination on one month's notice of each contract between Larkstar and TPS which the General Commissioners assumed would be in the hypothetical contracts between Mr Brill and MBDA. The General Commissioners find this to be one of the most compelling indicia of a contract for services rather than employment. The Revenue submits that this was again a result of a misdirection by the General Commissioners of themselves on the relevant law.

55. Mr Nawbatt points out that in McManus v Griffiths 70 Tax Cases 218 at page 232 Lightman J expressed the view that a condition for termination on three months' notice was no indication of whether the contract was of service or for services. In Morren v Swindon & Pendelbury Borough Council [1965] 2All ER349 at page 351 Lord Parker, CJ considered that a provision for one month's notice indicated a contract of service. The General Commissioners do not seem to have taken account of either of these authorities.

56. While I see force in the Revenue's argument, I am not convinced that it is fair to say that the General Commissioners misdirected themselves in law on this point. It follows from the apparent conflict between the dicta cited by Mr Nawbatt, to which I have referred, that there does not seem to be any clear law on the point.

57. The remainder of the considerations referred to in ground (2)(c) of the grounds of appeal constitute a list of factors which the General Commissioners regarded as indicia of a contract for services, or rejected as indicia of a contract of service. In each case the Revenue submits that the General Commissioners erred in the significance they attached to these factors. I do not believe it helpful to go through the list.

58. I have already indicated that I accept that the General Commissioners did misdirect themselves on the law in relation to their consideration of what they found to be the important questions of control and mutuality of obligation and made one finding of fact in relation to the former question, namely that Mr Brill was only encouraged to work the core hours, unjustified by the evidence before them.

59. It follows in my judgment that the appeal must be allowed and I am afraid the matter must be remitted to the General Commissioners to be re-heard *de novo* by a differently constituted panel, for I cannot be satisfied that they would have reached the same conclusion as they did, had they not made the errors of law and unjustified finding of fact which I have identified.

60. In these circumstances it does not seem appropriate to express a view on the Revenue's further list of matters under ground of appeal (2)(c) as to which I do not find any point of law on which I can say the General Commissioners misdirected themselves.

61. Particularly having regard to the comparatively small amount of money at stake on this appeal it is in my opinion unfortunate that there has to be all the expense and delay of a re-hearing by the General Commissioners, but I have to accept Mr Stafford's submission that I cannot myself properly determine questions of fact central to Larkstar's appeal. Hence submissions before me were properly directed only to particular criticisms of the decision made by the General Commissioners and not to the question of whether in fact Mr Brill would, under the hypothetical contract, have been employed or self-employed.

62. That was consistent with the fact that the Revenue in its Notice of Appeal indicated that the only order sought by it on this appeal is an order "setting aside" the decision of the General Commissioners. They did not indicate that they sought any alternative order.

63. I have not yet said anything about the Revenue's 3rd and 4th grounds of appeal. Mr Nawbatt for the Revenue accepted rightly that ground (3) really adds nothing to ground (2). As to ground (4), namely that the General Commissioners erred in law and that they reached a conclusion not open to them on the evidence before them, the only additional argument relied on by Mr Nawbatt was directed at paragraph 9(d) of the Case Stated in which the General Commissioners said:

> "We were invited to apply to the facts of this casethe analogy of a surgeon employed by a hospital. He has complete professional freedom, but is nevertheless an employee. We prefer the analogy of a householder engaging a builder. However many the additions or amendments to the original contract, and however pernickety or demanding the householder, the builder remains an independent contractor. And so it was in this case."

64. Mr Nawbattt criticises the analogy of a builder chosen by the General Commissioners and submits that it is so inept as to indicate that the General Commissioners must have misdirected themselves in law. I agree that the analogy is certainly not a happy one, but I do not think that the choice of it by the General Commissioners would of itself have been sufficient to establish an error of law by them.

65. For the reasons I have given, however, I shall allow the Revenue's appeal and remit the matter to the General Commissioners for re-hearing by a different panel.

66. As no one is here representing either party what I propose to do is to make the order I have indicated, order that the respondent shall pay the Revenue's costs of this appeal to be the subject of a detailed assessment in the absence of agreement, and I will direct that either party may make an application to me within the next 28 days (such application to be in writing via the Chancery Listing Office, as I shall not be sitting any more this term) to make some further order or to change the wording of some order I have indicated I shall make - not, of course, an application to amend the judgment.

67. So, the order I make is that the appeal is allowed with costs, costs to be the subject of a detailed assessment in the absence of agreement, and the subject matter of the appeal shall be remitted to the General Commissioners for re-hearing by a differently constituted panel from the panel that heard the appeal on the previous occasion.

TC00912

Appeal number TC/2009/13115

Social Security Contributions, employed earner - income tax, employee - independent service provider - services of design engineer - IR35 legislation – hypothetical contract – appeal allowed

FIRST-TIER TRIBUNAL
TAX CHAMBER

MBF DESIGN SERVICES LIMITED **Appellant**

- and -

THE COMMISSIONERS FOR HER MAJESTY'S REVENUE AND CUSTOMS (*income tax*) **Respondents**

TRIBUNAL: Judge Malachy Cornwell-Kelly
Mr Christopher Perry C. Eng.

Sitting in public at Vintry House, Wine Street, Bristol on 15 & 16 November 2010

Mr Matthew Boddington and Ms Nicola Smith of Accountax Consulting for the taxpayer

Mr Colin Williams and Mr David Lewis of Her Majesty's Revenue and Customs for the Crown

DECISION

Introduction

1 The appeals before us were made on 9 March 2009 as follows.

2 Firstly, there is an appeal against a notice of decision dated 18 February 2009 issued to MBF Design Services Limited (MBF) under section 8(1)(m) of the Social Security Contributions (Transfer of Functions, etc) Act 1999 and regulation 6(4) of the Social Security Contributions (Intermediaries) Regulations 2000 covering the years 2001-02 to 2006-07. Secondly, there is an appeal against determinations also dated 18 February 2009 issued to MBF under regulation 80 of the Income Tax (Pay As You Earn) Regulations 2003 for the same years.

3 The appeals concern the supply of the design engineering services of the sole director of the taxpayer company (MBF), Mr Mark Fitzpatrick, to Airbus UK Limited (Airbus) through a series of contracts involving MBF, two intermediaries and Airbus. The periods now under appeal are the tax years 2003-04 and 2004-05, and we are invited formally to allow the taxpayer's appeals in respect of the years 2001-02, 2002-03, 2005-06 and 2006-07.

4 The issue before the tribunal involves applying to the facts of the case the statutory hypothesis, explained further below, which requires us to establish whether, had the arrangements with Airbus taken the form of a contract between Mr Fitzpatrick and Airbus, they would have resulted in his being (i) an employed earner of Airbus for the purpose of National Insurance Contributions and (ii) an employee of Airbus for

income tax purposes. The notice and determinations under appeal decided that Mr Fitzpatrick was such an employed earner and employee. It was agreed that for the purposes of this appeal the two tests are not materially different.

5 We find the facts related hereafter to have been proved on the balance of probabilities, except where we indicate in terms that our finding is otherwise.

Facts – the contracts

6 The parties agreed that of the various contracts by which Mr Fitzpatrick's services were supplied to Airbus, the following might be taken for the purposes of this appeal as representative of each stage in the chain. There were no written contracts between Mr Fitzpatrick and MBF, and no board minutes approving those made by MBF, but we are satisfied that Mr Fitzpatrick was the sole controlling mind of MBF and that its contracts were duly authorised and competent.

7 First, came a contract between MBF and GED-Sitec Limited (GED) dated 23 April 2003 for services to be provided by MBF, through GED, to Airbus. The "Nature of Assignment (Project)", was described simply as "Designer". The start date was 28 April 2003, the duration "until 24 October 2003"; two hourly rates were specified: £21.47 per hour "for the initial 35 hours per week" and £22.34 per hour "for hours above the initial 35 /week"; the notice period was stated to be 7 days.

8 The contract was preceded by a "Request for Services" from GED, which provided that –

> "Should the services supplied prove substandard in any way, or the conduct or attendance record give rise to a legitimate claim by our client to withhold

payment, we reserve the right in turn to reclaim/withhold the money from [MBF]."

9 Detailed printed conditions formed part of the contract as follows:-

- Mr Fitzpatrick was not named anywhere, but clause 1.1 provided that " 'Operatives' means any person, firm or company engaged by [MBF] or its subcontractors in connection with the project".

- Clause 2.1 stated that the terms and conditions "contain the entire agreement" between the parties.

- Clause 3.1 required MBF to comply with the Working Time Regulations 1998 and where necessary to obtain any agreements to opt out of the 48 hour working week limit.

- Clause 3.2 provided that MBF "will use its reasonable endeavours to ensure that the Operative(s) work the normal working hours".

- Clause 3.3 said that GED might on reasonable notice require MBF to "supply the Operative(s) ... for periods of time in excess of the normal working hours" at a fee to be agreed.

- Clause 3.4 provided that the services were to be performed "at such location as [GED] and [MBF] may agree from time to time".

- Clause 3.5 stated that "[MBF] or the Operative (sic) shall have reasonable autonomy in the provision of the Services, but shall

comply with any reasonable request of [GED] or [Airbus] whilst on their premises".

Clause 5.1 required MBF to "ensure that all Operatives are suitably trained and qualified at the cost of [MBF]", and clause 5.2 required MBF to "rectify at its own cost any defective work it carries out in relation to the Project". There was no mention of the nature of the "designer" services to be supplied, or of the level of competence required.

- Clause 7.3 provided for the vesting of all intellectual property rights originated in the performance of the contract in Airbus.

- Clauses 8 and 9 also made it clear that there was no obligation to provide any particular "Operative" and that the Operative provided did not have "any of the statutory or common law rights of an employee", specifically excluding employee's common law or statutory rights, illness or holiday pay or protection under the legislation relating to unfair dismissal or redundancy.

- Clause 11 imposed a requirement for GED "and the Personnel" (not specified) to carry insurance against public, employer's and professional indemnity risks of £250,000.

10 The second contract in the chain was dated 24 April 2003 and made between GED and Morson Human Resources Limited (Morson). The client is stated to be Airbus, the fees are £23.25 an hour, and the project period is "from 28.04.03 until completion of the Project", the project itself being

described simply as "Airbus". A special term is that the requirement for professional indemnity insurance in the printed conditions (which would have required GED to carry insurance against public, employer's and professional indemnity risks) did not apply.

11 The printed conditions define the "Operatives" as "any person firm or company engaged by [GED] or its subcontractors in connection with the Project". They go on to include the following stipulations:-

- Clause 3.1: neither Morson nor Airbus shall be "entitled to or seek to exercise any supervision, direction or control over [GED] or the Operatives in the manner of performance of the Project."

- Clause 3.2 required MBF to comply with the Working Time Regulations 1998 and where necessary to obtain any agreements to opt out of the 48 hour working week limit.

- Clause 5 contained requirements for GED to ensure that all Operatives were suitably trained at its own expense, to rectify defective work at its own cost and to ensure that computer equipment used was in good order and virus-protected.

- Clause 6.1.4 enabled the contract to be terminated on 7 days' notice.

- Clause 7.3 provided for the vesting of all intellectual property rights originated in the performance of the contract in Airbus.

- Clause 8.1: the "relationship of employer and employee" between Morson and GED or the

Operatives, or between Airbus and GED or the Operatives, is specifically excluded.

- Clause 8.2 reinforces 8.1, specifically excluding employee's common law or statutory rights, illness or holiday pay or protection under the legislation relating to unfair dismissal or redundancy.

- Clause 9.1: GED is not obliged to provide the services of any named individual for the project.

- Clause 9.3: GED is free to provide its services and those of the Operatives to any person other than Morson or Airbus.

12 For the third contract taken as typical there are two examples, because their terms are not completely identical. The first example was originally dated 17 September 2003 made between Airbus and Morson, though the copy of this contract is also dated 23 January 2004 under the rubric "date changed". It is agreed that no point arises on this double dating, which simply indicates that a further contract was being made on the template of the previous one.

13 Whereas the first and second contracts provided only for the services of unnamed 'operatives' to be provided, this contract provides for the services of no fewer than 53 named persons, including Mr Fitzpatrick, to be supplied. The contract has clearly been adapted from one normally used for the purchase of goods, and the individuals named are listed beside the headings "quantity" and "net price". The quantities are specified in hours beside each group of persons, and the net prices are the hourly rates applicable to them.

14 Thus, in the group of 16 persons in which Mr Fitzpatrick's name appears, the total hours purchased by Airbus is 42,500,

and the hourly rate is £23.72. There is no distinction as to the hours to be worked or as to the rate per hour between the individuals in the group. Each of the 12 groups listed has a different overall total of hours to be worked and a different hourly rate applicable to its members.

15 The period of the order is stated to be 1 October 2003 to 31 December 2004. The special conditions include:-

> "All on-site subcontractors booking to Airbus cost centre EO3 recording hours via the Airbus electronic timesheet process – PMITS."
>
> "The following time reporting procedure is applicable to this purchase order:
>
> > 'On site subcontract time reporting for design work.'
>
> "Quality requirement:
>
> Clause 5 – Inspection Code 5.1(c)
>
> > '[Morson] shall ensure that the order is carried out in conformity with the quality requirements of his Airbus UK approval.' "
>
> "Note:
>
> > 1) All individuals working 'on site' must complete the electronic timesheet on a weekly basis."

16 The second example of the third contract was again double-dated 13 January and 7 February 2005, and again no point arises on this feature which has the same explanation as before; and as before, the parties are Morson and Airbus. Again, there are schedules of persons whose services are to be supplied, 45 in all. Mr Fitzpatrick appears in two groups: in the first group of 16 persons, he is shown as "resource valid until 28.01.05 (168 hours allocated) requirement transferred to item 8"; in group 8, consisting of four persons, against Mr Fitzpatrick's name is then noted "resource allocated from 31.01.05 (1,832

hours added) requirement transferred from item 6". The total hours for group 6 are 30,001 and the "net price" or hourly rate is £24.04; for group 8 the figures are 7,712 and £25.14 respectively.

17 The period of the order is stated to be 4 January to 31 December 2005. The special conditions are the same as in the first example save that relating the quality requirement, which reads:-

> "Quality requirement:
>
> Clause 5 – Inspection Code 5.1(e)
>
> > 'No release required – all work undertaken must be checked and approved by Airbus UK staff prior to formal acceptance.' "

18 The special conditions in both examples of the third contract also state that "The terms and conditions of this purchase order are detailed within letter Ref: D33/RNC/1852 dated 15th September 2003"; that letter was not shown to us by either party, and not relied on in argument, and we must therefore conclude that it has no relevance to the matter at issue.

19 There were detailed printed conditions relevant to both examples of this contract. The conditions were in two editions dated 2001 and 2005; we were told that there was no material distinction between them in so far as this appeal was concerned. Morson was identified in the contract as "the Supplier", which was not further defined. The conditions included the following:-

- Clause 4.1 obliged the Supplier to "provide the supplies in all respects in accordance with the Order".
- Clause 5 dealt with quality conditions.

5.1 stated that "The Supplies shall be subject to whichever of the following Quality Assurance Conditions are specified on the face of the Order-

....

c) The Supplier shall ensure that the Order is carried out in compliance with the quality requirements of his Airbus UK Limited approval.

...

(e) Exceptional arrangements determined by the Quality Manager/Chief Inspector and shown on the face of the Order.

- Clause 13.1.3 required any breach capable of remedy to be remedied within 28 days of notice by Airbus at the Supplier's expense.

- Clause 13.5 stated that the Order might be cancelled by Airbus at any time on written notice (no period was stated), and that while a "fair and reasonable price" was to be paid for all work done, Airbus's liability was not to exceed "the agreed price".

- Clause 14 vested all intellectual property created as a result of the work undertaken by the Supplier or its subcontractor in Airbus.

- Clause 16 required the Supplier to effect legal liability insurance of not less than £5M if its employees, agents or subcontractors were present on the Airbus site, in respect of loss of or damage to Airbus's property or death or injury resulting from performance of the Order.

- Clause 17.3 provided that any information given to the Supplier by Airbus should remain the absolute property of Airbus.

- Clause 20 placed the responsibility of complying with statutory and "other" requirements on the Supplier.

- Clauses 2 and 27 provided that the written contract was (a) to supersede any prior agreement between the parties and (b) could only be amended by a signed written document.

Facts – the oral evidence

20 We heard oral evidence from Mr Mark Fitzpatrick; Mr Alan Cooper a former employee of Airbus during the appeal period; Mr Josef Dudman a contractor during the appeal period; and Mr Minh Pham a lead designer employed by Airbus during the appeal period, leading a team of four employed designers and responsible for up to 40 contracted designers – including for a small part of the period Mr Fitzpatrick. Their witness statements had been served beforehand.

21 We regarded these witnesses as straightforward and honest, with the exception of Mr Pham. We did not doubt Mr Pham's honesty, but he admitted that his witness statement had been prepared for him by HMRC and he had considerable difficulty - due apparently to a limited command of English - in reading it out; and he was hesitant and uncertain in his replies to cross-examination. We were not satisfied that Mr Pham fully understood the contents of his witness statement.

22 After hearing submissions we declined, pursuant to rule 15(2)(b)(iii), to admit unsworn witness statements by two officials of Airbus, Mr Paul Messenger a team leader for most of Mr Fitzpatrick's time at Airbus, and Mr Steve Hoskins the Head of Product Related Services at Airbus. The statements in question were disputed as to their contents, which related to issues central to the appeal, and the tribunal had given no previous directions that they were to be admitted as they stood

without the presence of the witnesses. No witness summonses had been sought for the attendance of the individuals concerned, and in the circumstances it appeared to us to be unfair that these statements should be admitted when they would not be open to challenge by cross-examination, or questioning by the tribunal.

23 The evidence given at the hearing establishes the following facts.

(i) Recruitment

24 Mr Fitzpatrick established MBF in 1996 after the company he had worked for ceased business. Mr Fitzpatrick's introduction to Airbus was via another contractor who did work for them; initial contact failed to produce a satisfactory outcome, but further negotiations followed and Mr Fitzpatrick was offered a higher rate by the agency involved and (so far as this appeal period was concerned) began work around April 2003. MBF had provided Mr Fitzpatrick's services to Airbus in earlier periods as well and was registered for VAT.

25 MBF was offered a number of contracts during the appeal period but Mr Fitzpatrick did not consider that it was obliged to accept them: he gave as an example one project in May 2004 where Airbus had requested him to take overall responsibility for the Flight Test Instrumentation for the A380, which Mr Fitzpatrick declined on behalf of MBF because good enough terms were not available. As has been seen in the third level contracts, the periods of each stage of the work and the total resources in hours which Airbus required for it were settled anew at various dates as the project progressed.

26 In practice, there was never any question of providing a substitute for Mr Fitzpatrick (though he asserted that the Morson-Airbus contract entitled the latter to send a substitute

for him if they chose). The evidence was that substitution would from Airbus's point of view have been very difficult to manage, but it would not have been impossible to organise, changing Mr Fitzpatrick's security clearances and passwords, etc. If Mr Fitzpatrick was absent when work from him was needed, it would either await his return or be done by another designer; if he sent a substitute, a complaint would have been made to the agency because Airbus wanted Mr Fitzpatrick's services specifically. Airbus would normally want to see and verify the CVs of persons doing work for them.

27 MBF had a history of contracting out Mr Fitzpatrick's services of the kind featured in this appeal to a number of different clients, including Westland Helicopters, Strachan & Henshaw and Western Design Systems, both before and after the appeal period.

(ii) Work content

28 The work concerned the A380 aircraft and producing acceptable design solutions for components specific to that project. It included incorporating instrumentation devices for measuring and verifying the design specification parameters obtainable from the aircraft, together with routing the data acquisition devices and their connections through the aircraft structure; this enabled the validation of its design for certification by all the relevant aviation authorities worldwide. Mr Fitzpatrick's activity involved also gathering data on the performance of the aircraft and preparing specifications for the instruments and adapting standardised instruments. Mr Fitzpatrick was entitled to do his own research for this work, and did so both at Airbus and on his own account.

(iii) Supervision

29 Certain design criteria would be offered to Mr Fitzpatrick by Airbus, though often it was up to him to decide what to refer to. It is clear that his work was in principle subject to Airbus approval, but it is also clear that that was so not because of any need to supervise Mr Fitzpatrick's work as such but because of the need to integrate the work of each contractor in the overall design of the aircraft and to measure it against the requirements of the aviation authorities worldwide, and especially the Civil Aviation Authority in the UK.

30 Thus, both Mr Paul Messenger Mr Fitzpatrick's team leader or Mr Minh Pham on later occasions, or as occasion required other Airbus officials, did check the work done with a view to ensuring its harmonisation with the rest of the project and its suitability in that context, including its conformity with the technical protocols being used in the project or required by the authorities. It was up to the designer to do the detail of the design. The checking was not therefore primarily for the purpose of quality supervision but more as part of the team leader's task of co-ordination, not least with other work being done simultaneously.

31 It was explained in this respect that Airbus worked with a system known as 'concurrent engineering', in which several designers would be working on related items of design at the same time: as one posted his or her work on the computer system, the others could see to what extent – if any – their own designs needed modifying to fit with what had been done. There was therefore from time to time the need for corrective work to be undertaken by designers such as Mr Fitzpatrick, which they would usually undertake on their own initiative.

32 Reworking due to another designer having altered the landscape in this way would be part of the contract for which Airbus would pay. But if a designer such as Mr Fitzpatrick

saw, by contrast, that his work was technically at fault, it would be for him to correct it at his own expense and not as a charge to Airbus; Mr Fitzpatrick had sometimes done so on his own initiative but never at the request of Airbus. If Airbus were dissatisfied with Mr Fitzpatrick's work, they would discuss the matter with him or, if the problem was serious enough, they would terminate his contract.

33 Naturally, Airbus's team leaders had the task of co-ordinating the work being done on a particular phase of the project and would give out instructions to the designers, employed or contractors, as to what should be done next or as to the work priorities. Airbus would, as the owner and driver of the project, have the final say as to what should be done and when, but they would not control the precise manner of the work.

34 Mr Fitzpatrick was not subject to the disciplinary or grievance procedures, nor given job appraisals.

(iv) Location

35 The location of the work done was usually, but not invariably, Airbus's premises at Filton, near Bristol. That was both for security reasons and because Mr Fitzpatrick's services normally involved logging into and using the computer and design facilities of Airbus on site as the aircraft developed. On occasion, however, Mr Fitzpatrick would do research work at home and in his own time.

(v) Hours

36 Mr Fitzpatrick did not work set days or hours: he would begin work at any time from 6.30 am to midday and finish up to 6.30 pm to suit himself. Usually, Mr Fitzpatrick took no more than 30 minutes for lunch but at times he took up to two

hours; if he had decided to work a short day, Mr Fitzpatrick would then take no lunch break at all.

37 As has been seen from the third level contracts, the keeping of time records by contractors was required. There was a conflict of evidence as to whether the keeping of core hours was an obligatory feature of this in so far as the contractors were concerned, Mr Pham claiming at first that it was; on further consideration, Mr Pham was not sure whether this was actually a contractual requirement or merely "a gentlemen's agreement" by contractors to fall in line with the hours kept by employees, but he said it was Airbus's policy that all operatives should be present during core hours.

38 For his part, Mr Fitzpatrick said that he did not know what the core hours were supposed to be and that he came and went when he chose, but that he kept Airbus informed of what he was doing. A timesheet covering 34 weeks of 2005 was in evidence and showed that for this period anyway Mr Fitzpatrick would often work more than the standard 35 hours, in the majority of cases for 40 hours a week or more, and in only five of the 34 weeks did he put in fewer than 35 hours.

39 Our finding on the matter of core hours is that, while the keeping of core hours was strictly speaking a definite requirement by Airbus, the practical outworking of the matter was that the policy was not enforced if effective co-ordination of the contractors' work with that of the rest of the establishment was achieved. It was thus left to the professional good sense of contractors to ensure that their working practices were sufficiently integrated with those of the staff for the overall operation to continue efficiently, and that we find was the case in Mr Fitzpatrick's situation.

40 It happened on occasion that the power supply to Airbus's computers failed and that it was impossible to continue useful work accordingly. In that case, the employees of the company would try and find something to do and make themselves look busy. By contrast, contractors would, as soon as it became clear that the outage was not going to be remedied quickly and that there was nothing else they could be doing, simply be sent home; in this situation, the contractors found themselves stood down and unpaid until the problem was remedied.

(vi) Conditions

41 Mr Fitzpatrick worked alongside Airbus employees and other contractors and while the proportion of one to the other varied, it was mostly about 4 to 5 contractors to one Airbus employee. The security passes issued differentiated between the two classes of persons.

42 MBF issued weekly VAT invoices to GED referable to the number of hours Mr Fitzpatrick had worked in the week. There was no holiday pay or sick pay for Mr Fitzpatrick or his fellow contractors, and they were not in principle invited to the social events organised for Airbus staff or entitled to their various benefits, such as the employee car scheme, the pension scheme, healthcare scheme and so on: there were 25 in all in the list put in evidence. The same applied to occasional benefits, such as Christmas presents or the opportunity for family members to see the A380's first flight.

43 Airbus would be informed by Mr Fitzpatrick when he was going to take his holidays but, though it was sensible to coordinate the periods in question with Airbus, the latter did not have control as such of Mr Fitzpatrick's holiday absences; if they did not find his timing acceptable, Airbus were entitled to terminate Mr Fitzpatrick's involvement with them - he

thought on 7 days' notice (though the Morson/Airbus contract makes it clear that no notice period was specified). Airbus in fact did just that in August 2005, not because of any disagreement over holidays or hours, but because it suited their business interest to do so, giving MBF 4 days' notice to terminate a contract whose period had commenced less than a month before.

(vii) Training

44 Some of the specialist technical training Mr Fitzpatrick needed for this highly specific work was done at Mr Fitzpatrick's expense and in his own time. Thus, Mr Fitzpatrick did not have formal training in the use of the 'Primes' database, which controlled the parts list for the designs and their issue status; he was self-taught in the matter.

45 The same was true in regard to the CATIA version 5 system – a 3D modelling system Airbus introduced to replace an older one; a formal certificate of competence in regard to this was needed. Mr Fitzpatrick could have been trained for CATIA at his own cost on Airbus's system, but together with others he opted to be trained elsewhere by IBM at a lower cost and at more convenient times.

46 By contrast, Mr Fitzpatrick was trained by Airbus at its expense in the use of the computer-aided design system known as CADD, as Airbus specified the software to be used by the designers.

Legislation

47 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)."

48 Section 4A of that Act makes provision in relation to the earnings of workers supplied by service companies: -

"4A Earnings of workers supplied by service companies etc

(1) Regulations may make provision for securing that where—

(a) an individual ("the worker") personally performs, or is under an obligation personally to perform, services for the purposes of a business carried on by another person ("the client"),

(b) the performance of those services by the worker is (within the meaning of the regulations) referable to arrangements involving a third person (and not referable to any contract between the client and the worker), and

(c) the circumstances are such that, were the services to be performed by the worker under a contract between him and the client, he would be regarded for the purposes of the applicable provisions of this Act as employed in employed earner's employment by the client,

relevant payments or benefits are, to the specified extent, to be treated for those purposes as earnings paid to the worker in respect of an employed earner's employment of his."

49 The Social Security Contributions (Intermediaries) Regulations 2000, regulations 5 & 6, provided further: -

"5 Meaning of intermediary

(1) In these Regulations "intermediary" means any person, including a partnership or unincorporated association of which the worker is a member—

(a) whose relationship with the worker in any tax year satisfies the conditions specified in paragraph (2), (6), (7) or (8), and

(b) from whom the worker, or an associate of the worker—

(i) receives, directly or indirectly, in that year a payment or benefit that is not chargeable to tax [as employment income under ITEPA 2003], or

(ii) is entitled to receive, or in any circumstances would be entitled to receive, directly or indirectly, in that year any such payment or benefit.

(2) Where the intermediary is a company the conditions are that—

(a) the intermediary is not an associated company of the client, within the meaning of section 416 of the Taxes Act, by reason of the intermediary and the client both being under the control of the worker, or under the control of the worker and another person; and

(b) either—

(i) the worker has a material interest in the intermediary, or

(ii) the payment or benefit is received or receivable by the worker directly from the intermediary, and can reasonably be taken to represent remuneration for services provided by the worker to the client.

(3) A worker is treated as having a material interest in a company for the purposes of paragraph (2)(a) if—

(a) the worker, alone or with one or more associates of his, or

(b) an associate of the worker, with or without other such associates,

has a material interest in the company.

(4) For this purpose a material interest means—

(a) beneficial ownership of, or the ability to control, directly or through the medium of other companies or by any other indirect means, more than 5 per cent of the ordinary share capital of the company; or

(b) possession of, or entitlement to acquire, rights entitling the holder to receive more than 5 per cent of any distributions that may be made by the company; or

(c) where the company is a close company, possession of, or entitlement to acquire, rights that would in the event of the winding up of the company, or in any other circumstances, entitle the holder to receive more than 5 per cent of the assets that would then be available for distribution among the participators.

In sub-paragraph (c) "close company" has the meaning given by sections 414 and 415 of the Taxes Act, and "participator" has the meaning given by section 417(1) of that Act.

6 Provision of services through intermediary

(1) These Regulations apply where—

(a) an individual ("the worker") personally performs, or is under an obligation personally to perform, services [for another person] ("the client"),

(b) the performance of those services by the worker is carried out, not under a contract directly between the client and the worker, but under arrangements involving an intermediary, and

(c) the circumstances are such that, had the arrangements taken the form of a contract between the worker and the client, the worker would be regarded for the purposes of Parts I to V of the Contributions and Benefits Act as employed in employed earner's employment by the client.

(2) Paragraph (1)(b) has effect irrespective of whether or not—

(a) there exists a contract between the client and the worker, or

(b) the worker is the holder of an office with the client.

(3) Where these Regulations apply—

(a) the worker is treated, for the purposes of Parts I to V of the Contributions and Benefits Act, and in relation to the amount deriving from relevant payments and relevant benefits that is calculated in accordance with regulation 7 ("the worker's attributable earnings"), as employed in employed earner's employment by the intermediary, and

(b) the intermediary, whether or not he fulfils the conditions prescribed under section 1(6)(a) of the Contributions and Benefits Act for secondary contributors, is treated for those purposes as the secondary contributor in respect of the worker's attributable earnings,

and Parts I to V of that Act have effect accordingly.

(4) Any issue whether the circumstances are such as are mentioned in paragraph (1)(c) is an issue relating to contributions that is prescribed for the purposes of section 8(1)(m) of the Social Security Contributions (Transfer of Functions, etc) Act 1999 (decision by officer of the Board)."

50 The Income Tax (Earnings and Pensions) Act 2003 makes similar provision as follows:-

"49 Engagements to which this Chapter applies

(1) This Chapter applies where—

(a) an individual ("the worker") personally performs, or is under an obligation personally to perform, services [for another person] ("the client"),

(b) the services are provided not under a contract directly between the client and the worker but under arrangements involving a third party ("the intermediary"), and

(c) the circumstances are such that, if the services were provided under a contract directly between the client and the worker, the worker would be regarded for income tax purposes as an employee of the client.

(2) . . .

(3) The reference in subsection (1)(b) to a "third party" includes a partnership or unincorporated body of which the worker is a member.

(4) The circumstances referred to in subsection (1)(c) include the terms on which the services are provided, having regard to the terms of the contracts forming part of the arrangements under which the services are provided.

(5) In this Chapter "engagement to which this Chapter applies" means any such provision of services as is mentioned in subsection (1).

50 Worker treated as receiving earnings from employment

(1) If, in the case of an engagement to which this Chapter applies, in any tax year—

(a) the conditions specified in section 51, 52 or 53 are met in relation to the intermediary, and

(b) the worker, or an associate of the worker—

(i) receives from the intermediary, directly or indirectly, a payment or benefit that is not employment income, or

(ii) has rights which entitle, or which in any circumstances would entitle, the worker or associate to receive from the intermediary, directly or indirectly, any such payment or benefit,

the intermediary is treated as making to the worker, and the worker is treated as receiving, in that year a payment which is to be treated as earnings from an employment ("the deemed employment payment").

(2) A single payment is treated as made in respect of all engagements in relation to which the intermediary is treated as making a payment to the worker in the tax year.

(3) The deemed employment payment is treated as made at the end of the tax year, unless section 57 applies (earlier date of deemed payment in certain cases).

(4) In this Chapter "the relevant engagements", in relation to a deemed employment payment, means the engagements mentioned in subsection (2).

51 Conditions of liability where intermediary is a company

(1) Where the intermediary is a company the conditions are that the intermediary is not an associated company of the client that falls within subsection (2) and either—

(a) the worker has a material interest in the intermediary, or

(b) the payment or benefit mentioned in section 50(1)(b)—

(i) is received or receivable by the worker directly from the intermediary, and

(ii) can reasonably be taken to represent remuneration for services provided by the worker to the client.

(2) An associated company of the client falls within this subsection if it is such a company by reason of the intermediary and the client being under the control—

(a) of the worker, or

(b) of the worker and other persons.

(3) A worker is treated as having a material interest in a company if—

(a) the worker, alone or with one or more associates of the worker, or

(b) an associate of the worker, with or without other such associates,

has a material interest in the company.

(4) For this purpose a material interest means—

(a) beneficial ownership of, or the ability to control, directly or through the medium of other companies or by any other indirect means, more than 5% of the ordinary share capital of the company; or

(b) possession of, or entitlement to acquire, rights entitling the holder to receive more than 5% of any distributions that may be made by the company; or

(c) where the company is a close company, possession of, or entitlement to acquire, rights that

would in the event of the winding up of the company, or in any other circumstances, entitle the holder to receive more than 5% of the assets that would then be available for distribution among the participators.

(5) In subsection (4)(c) "participator" has the meaning given by section 417(1) of ICTA.

59 Provisions applicable to multiple intermediaries

(1) The provisions of this section apply where in the case of an engagement to which this Chapter applies the arrangements involve more than one relevant intermediary.

(2) All relevant intermediaries in relation to the engagement are jointly and severally liable, subject to subsection (3), to account for any amount required under the PAYE provisions to be deducted from a deemed employment payment treated as made by any of them—

(a) in respect of that engagement, or

(b) in respect of that engagement together with other engagements.

(3) An intermediary is not so liable if it has not received any payment or benefit in respect of that engagement or any such other engagement as is mentioned in subsection (2)(b).

(4) Subsection (5) applies where a payment or benefit has been made or provided, directly or indirectly, from one relevant intermediary to another in respect of the engagement.

(5) In that case, the amount taken into account in relation to any intermediary in step 1 or step 2 of section 54(1) is reduced to such extent as is necessary to avoid double-counting having regard to the amount so taken into account in relation to any other intermediary.

(6) Except as provided by subsections (2) to (5), the provisions of this Chapter apply separately in relation to each relevant intermediary.

(7) In this section "relevant intermediary" means an intermediary in relation to which the conditions specified in section 51, 52 or 53 are met."

The case law

51 It will be seen the statutory hypothesis which has to be applied to the actual facts found is this: what contract would in the circumstances have existed between them if the worker (Mr Fitzpatrick) had been engaged directly by the client (Airbus)? It is on the basis of that hypothetical contract that the fiscal consequences are determined.

52 The process of reaching this conclusion involves what Sir Stephen Oliver QC, sitting as Presiding Special Commissioner in *Tilbury Consulting Ltd v. Gittins (No 2)* [2004] STC (SCD) 72, at [6], has described in these terms:-

> "The legislation calls for a two stage exercise. The first is to find the facts as they existed during the period covered by the decision. The facts to be found are those that serve to identify the 'arrangements' involving the intermediary and the circumstances in which those arrangements existed and the nature of the services performed by the 'worker'. The second is to assume that worker [Mr Fitzpatrick] was contracted to perform services to the client [Airbus] and to determine whether in the light of the facts as found [Mr Fitzpatrick] would be regarded as [Airbus's] employee."

53 From the considerable case law on this subject, we deduce the following guidelines for the tribunal in constructing the hypothetical contract.

(i) The contractual terms

In determining the relationship which existed, regard should be had primarily to the actual contract terms rather than to what in fact occurred: per Peter Gibson LJ in *Express Echo Publications v. Tanton* [1999] IRLR 367 at [25]. But in

determining the 'circumstances' in which they are supplied (particularly where there is no privity of contract between the worker and the client), the legislation requires a view to be taken of the combined effect of the contracts and of their practical outworking: per Hart J in *Synaptek Limited v. Young* [2003] EWHC 645, 75 TC 51, at [11] – but see also the observations of Henderson J in *Dragonfly Consultancy Limited v. HMRC* [2008] STC 3030 at [14] to [19].

(ii) Personal service

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]. That that view is applicable in every situation has however been doubted at High Court level several times: see e.g. per Henderson J in *Dragonfly* at [32] and [37] in favour of regarding a right of substitution being an indicator only of self-employment and not as necessarily a guarantor of it.

It does not follow that the terms of the notional contract would not reflect the terms of the third level contract with the end-user client (such as the absence of a right of substitution) merely because the service provider had at the time necessarily been unaware of those terms: per Park J in *Usetech Limited v. Young* (2004) 76 TC 811, at [43] to [47].

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* (1969) 2 QB 173, at 187.

(iii) Mutuality of obligation

There may be mutuality of obligation in individual contracts made in an ongoing series of engagements, even though there is no obligation on either party to continue the series after the expiry of any of the individual contracts. The requirement for mutuality is satisfied if in each individual contract there is an obligation on the employer to continue paying, and the employee to continue working, until the specified work is complete: per Mummery LJ in *Prater v. Cornwall County Council* [2006] 2 All ER 1013, at [40] and Longmore LJ at [43].

Mutuality does not require the employer to provide the employee with work in addition to wages: per Stephenson LJ in *Nethermere (St Neots) v. Taverna* [1984] IRLR 240, at 246. It is only where there is both no obligation to provide work and no obligation to pay the worker for time in which the work is not provided that the want of mutuality precludes the existence of a continuing contract of employment: per Park J in *Usetech* at [64].

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: per Special Commissioner Hellier at first instance in *Dragonfly Consultancy Limited v. HMRC* [2008] STC (SCD) 430 at [59]. A termination notice clause implies an obligation on the employer to provide work until the right to terminate is exercised: per Hart J in *Synaptek* at [27].

(iv) Control

Control of an employee's work has traditionally been seen as a feature of a contract of service, and it includes the power of deciding the thing to be done, the way in which it shall be done, the means to be employed in doing it, the time and place where it shall be done; the right of control need not be unrestricted for an employee relationship to exist, particularly in the case of professional or skilled work. 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 (South East) Limited v. Minister of Pensions and National Insurance* (1968) 2 QB 497, at 516; and per Cooke J in *Market Investigations* at 185.

(v) Business on own account

If the facts show that the service provider was effectively in business on his own account, that points to a contract for services but the weight to be given to it is a matter for the tribunal: per Hart J in *Synaptek* at [20]. Among the factors relevant 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 185; and the fact of invoicing for payment: per Special Commissioner Avery Jones in *Lime-IT v. Justin* SpC 342 (2002).

A course of business dealings in which the company (or its controlling director) has had a series of engagements with a succession of clients may be material to this issue: per Park J in *Usetech* at [31]. The risk of bad debts and outstanding invoices is not normally associated with employment: per Nolan LJ in *Hall v. Lorimer* [1994] STC 23, at 30.

In order to consider whether a person carries on business on his own account it is necessary to consider many different aspects of that person's work activity. The object of the exercise is to paint a picture from the accumulation of detail: per Nolan LJ approving Mummery J in *Hall v. Lorimer* at 29.

(vi) Intention of the parties

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; and, in the context of the intermediaries legislation, statements of intention made in relation to actual contracts with an agency are unlikely to throw more than minimal light on the proper characterisation of the notional contract between the worker and the client, though an expression of intention in such a contract remains a possibility: per Henderson J in *Dragonfly* at [54] and [55].

(vii) Overall view

The test of being an employee does not rest on a submission to orders but depends on whether the person is 'part and

parcel' of the organisation: per Denning LJ in *Bank voor Handel en Scheepvaart NV v. Slatford* (1953) 1 QB 248, at 295. But see also the dissent from this proposition of MacKenna J in *Ready Mixed Concrete* at 525.

Submissions

54 There has been substantial agreement between the parties as to the effective tests required by the legislation to be applied and, as we have noted, there is agreement in particular that there is for the purpose of this appeal no material difference between the 'employed earner' and the 'employee' tests and that the same criteria can be referred to in relation to each. Although there may in some cases be a distinction to be drawn between the two statutory formulations, we see none in the circumstances of this case and we are reassured by the observations of Henderson J in *Dragonfly*, at [17], that "Nine times out of ten, perhaps ninety nine times out of a hundred, the two tests will lead to the same answer".

55 For the taxpayer it was submitted as follows:-

- Both the written contracts and the day to day circumstances in which Mr Fitzpatrick's work was performed, and indeed Mr Fitzpatrick's business circumstances at large, must be taken into account.
- Careful regard should be paid to whether the evidence shows as present the 'irreducible minimum' referred to by Stephenson LJ in *Nethermere* at 246 as necessary for a contract of service, namely a mutual obligation between the employer to provide payment and the employee to provide his own skill and work.

- A right of substitution is clear from the first and second level contracts and although Morson would have difficulties under its contract with Airbus in the event that substitution was required, such a right would be contained in the hypothetical contract. It had been admitted by Mr Pham that substitution would not have been impossible and could have been arranged. The fact of actual personal service throughout should not alter this.

- The appellant company was engaged for the performance of a specific project in circumstances typical of the freelance contracting marketplace, and atypical of an employment relationship.

- The general supervision and direction found in this case do not amount to control in the sense which is characteristic of employment relationships. The willingness of the court in *Morren v. Swinton & Pendlebury Borough Council* (1965) 1 WLR 576 to relax the requirement for control in the case of a skilled worker has not been reflected in the more recent authorities.

- The absence of sick pay, pension rights, healthcare facilities and holiday pay for Mr Fitzpatrick, invoicing for fees by MBF, its previous course of contracts and its VAT registration were all typical features of a business being carried on as such, and inconsistent with the notion of Mr Fitzpatrick being an employee. The cost of training being borne by MBF and the risk of bad debts occurring were to the same effect.

- The intention of both parties – Airbus and Mr Fitzpatrick - in constructing the hypothetical contract would clearly be to avoid employment status being created. Consistently with this, HMRC's Employment Status Manual, at para 3286, assumes in cases of doubt a mutual intention to create a contract for services.

- The right of cancellation contained in clause 13.5 of the third level contract is inconsistent with the required mutuality of obligation in the case of employment; this is exemplified further in contractors being sent home without pay if there was for the time being no work for them to do.

- Clauses 3.2 and 3.3 of the first level contract MBF to GED should be construed as not *requiring* any work at all to be done, albeit that the rates per hour for work which was done were specified. The evidence showed that if Mr Fitzpatrick accepted a package of work then he would complete it but not that Airbus had any obligation to provide it.

- Clause 5.1(c) and(e) of the Airbus/Morson contract's special conditions – the quality conditions – showed that if Airbus did not accept a piece of work they would not pay for it, contrary to the case of an employee whose work - even if it was poor - which would be paid for. Reworking of designs fitted that pattern as Mr Fitzpatrick fulfilled his task as a professional designer delivering a quality service.

- The evidence showed that there was a varied work pattern, with different hours frequently being worked as

different issues arose to be dealt with; insofar as 'core hours' were covered, that was due to a need to co-ordinate with Airbus employees and not because Mr Fitzpatrick was a 9-5 worker. Work on site was not inconsistent with the independence of the worker.

56 For the Crown it was submitted:-

- Both the written contracts and the circumstances in which they were discharged must be considered in a two-stage process, first identifying the 'arrangements' and then the 'circumstances'.

- The evidence shows that the normal minimum of 35 hours a week worked by Mr Fitzpatrick, the allocation of specific tasks to him, the following of Airbus's instructions as to methods and systems of work, the scope of each task and the checks on work done which were made, all support a finding of the degree of control typical of an employed relationship. The appellant is wrong to say that *Morren* and the latitude it recognises in regard to control of skilled workers has not been followed in more recent decisions: it was for example cited with approval in *Market Investigations* and remains good law.

- Airbus's requirements were clearly for the personal services of Mr Fitzpatrick and the hypothetical contract would not contain a substitution clause, pointing strongly to employment.

- The 'irreducible minimum' in regard to mutuality of obligation was present in that work was always available for Mr Fitzpatrick and he was always paid for

it. The evidence showed the reality of mutual obligations, which would be imported into the notional contract.

- There was in reality no financial risk for MBF other than the costs of sickness and its only chance to increase profits was for Mr Fitzpatrick to work longer hours. Payment by the hour is more akin to a contract of service than to one for services. Negotiation of fees is no different to bargaining for wages.

- The equipment needed for the work performed was provided by Airbus, as an employer, and no equipment as such was provided by Mr Fitzpatrick; training at MBF's cost may be consistent with employment.

- The continuity of work throughout the appeal period leads to the conclusion that Mr Fitzpatrick was dependent for that time on one party as his employer.

- The right to terminate on 7 days' notice is characteristic of an employment contract.

- The evidence does not show that Mr Fitzpatrick was 'part and parcel' of Airbus's organisation but that factor carries little weight on its own.

- The likely mutual intention to avoid employment status in the notional contract is irrelevant in view of the other pointers to a contract of service, since the parties cannot change the objective effect of the contract they make simply by re-labelling it.

- No work was done for others and in view of the hours worked it was unlikely that any such work could have been done. There is therefore the reality of exclusivity

in the appeal period which is a relevant circumstance in establishing the notional contract; in any event, the factor is not determinative since many employees have more than one job.

- The contracts at levels 1 and 2 specified 'normal working hours' and quantities of hours for the work, while the level 3 contract was made also by reference to hours of work, which is not typical of an obligation under a contract for services: the notional contract would do the same, leading to a regime which was typical of employment. The same is true of the requirement for work to be done on location.

Conclusions

57 As a matter of overall impression, we are of the view that both the arrangements and the circumstances in which they took effect gave rise to the reality of a relationship - or a series of relationships during the appeal period - typical of that in a contract for services. Many factors, as might be expected, point in that direction in the various contracts.

58 Thus, even in the third level (Morson/Airbus) contract which at first sight looks like an agreement for the supply of casual staff who might be expected to be temporary employees, and which contains none of the explicit provision found in the level 1 and 2 contracts designed to establish clearly that they are contracts for services, there are features which mark it out as inappropriate for employees.

59 The first example of the third level contract provides for groups of persons to be supplied to Airbus, without making any distinction between them, and at hourly rates applicable to all the members of the group indifferently. There was no stated obligation for Airbus to offer a particular amount of work to any individual, and it is apparent that the total number of hours allocated to any group could be used up by its members unequally – one earning more than another because of a greater number of hours worked, consequent upon a greater volume of work allocated.

60 In the second example of this contract, there is the appearance of a set number of hours being allocated to Mr Fitzpatrick specifically, but it is apparent that this is in effect an accounting mechanism reflecting the different rates of hourly payment for each of the groups to which he was in turn allocated. And although Airbus had specifically chosen the persons to make up each group, vetting their CVs, and thus could be said to have required their personal services, there remains an absence of the mutuality of obligation needed for a contract of employment to exist.

61 Secondly, the right in third level contract to cancel without notice is characteristic of a contract for services but quite foreign to the world of employment, as is the provision for agreeing compensation in such an event. Each contracted worker was fundamentally insecure, having neither a specified rôle in the company nor a particular line of duty beyond what was for time being allocated by the permanent staff. Clause 13.1.3 on the remedying of breaches, clause 16 requiring legal liability insurance to be effected by Morson and clause 20 placing the responsibility on Morson of complying with various statutory obligations point in the same direction; it is hard to imagine an employee in the normal way being affected by such

terms. The fact that a form of contract intended for purchases of goods was pressed into service for another purpose is beside the point: this was the contract the parties made and it is the only one the tribunal can refer to.

62 Against such a background, the other terms of the third level contract which point to employment have less weight. They are consistent with a contract for services and are explained by the special needs of a very complex and commercially sensitive undertaking. They are: the selection of named individuals, payment by the hour, time recording, quality standard approvals, site working, and all intellectual property created and information involved vesting in Airbus.

63 The first and second level contracts are quite explicitly contracts for services and it is unnecessary to refer to them in any detail, so well known are the terms which typify such agreements and which they clearly contain. The only pointers to employment are the references to working normal or core hours, the differential rate in the first level contract for extra hours, the 7 day notice periods, the omission of the insurance obligation in the second level contract and the vesting of intellectual property rights in Airbus. As before, we do not see these provisions as altering the main character of the contracts and as being referable to the particular circumstances of the end-user.

64 Does the practical reality of working alter the conclusion which emerges from the contracts? In some respects, the evidence about this seems ambiguous: thus the negotiation of remuneration at various stages, the absence of any prospect of Mr Fitzpatrick actually sending a substitute, the degree of checking and approval of designs, the work allocation and coordination by the permanent team leaders, the broad similarity of working hours from one week to the next, the fact

of almost all work being done on site, the close integration with Airbus's own workers, all these could be interpreted either way. We are satisfied, however, that these factors should fairly be seen in the context of others which point to independence:

- Thus, the absence in reality of any thought that Mr Fitzpatrick might send a substitute to discharge his obligations is, as the authorities show, not inconsistent with his having been engaged as a professional man whose personal expertise was valued as might be that of an architect or surgeon. Against the background of MBF's well-established existence and its history of engagements with various end-users, Mr Fitzpatrick's status as a freelance specialist in his area is entirely credible.

- Both contractors and employees habitually negotiate and re-negotiate their remuneration whenever the chance presents itself. In the absence of any career structure for Mr Fitzpatrick, MBF's negotiation of fees for new work is typical of how an independent provider would proceed, whereas an employee would tend to look as much for re-grading or promotion as a means of improving remuneration and there is no evidence of such behaviour on Mr Fitzpatrick's part.

- The checking and approval required of design work was an inevitable necessity in a project in which every part was interdependent and was in addition subject to the approval of external authorities. This factor would have had to be present in respect of any work done for Airbus, as the special conditions as to quality approval in the third level contract testify, so that there may appear little difference between the position of employees and service providers: the difference came in

the absence of disciplinary or grievance procedures for the contractors, the fact of having to rectify errors at their own expense and their liability to be laid off without notice.

- Mr Fitzpatrick's design work had normally to be performed on site and with Airbus's equipment because there was no other sensible way to do it, given the nature of the overall project of building an aircraft; there are many other examples of an independent contractor's work being done on the client's site and with the client's equipment for the same sort of reasons: an electrician repairing a wiring circuit, a plumber adapting a drainage system, an engineer checking a safety installation on an oil rig, and so on. In the context, we do not see on-site working as a conclusive indicator of employment.

- Basic working or core hours needed, within reason, to be adhered to produce an efficient interface with Airbus's staff, but given the variations in them which in fact occurred, in particular with regard to Mr Fitzpatrick's starting and ending times in the day, the pattern of working does not seem to us to be typical of normal employee working habits.

- A further factor in this context which distances Mr Fitzpatrick's situation from that of employment is payment for each hour worked and weekly invoices being submitted reflecting that; being sent home without pay when the Airbus computers broke down is a logical extension in that context, as is the absence of sick or holiday pay, the range of employee benefits generally and universal employer-provided training for work-related needs.

65 Other considerations pointing to a contract for services can be seen. Thus, the evidence does not show that Mr Fitzpatrick was 'part and parcel' of Airbus's organisation in any but the most temporary and limited sense; the opportunity for other work to be undertaken simultaneously was there for Mr Fitzpatrick if he had chosen to limit his working hours for Airbus; the fact is established of differing payments following weekly invoicing; the financial fortunes of MBF vary depending on the work and remuneration available; MBF's had a repeated need to find new clients for Mr Fitzpatrick's skills; the parties' plain intention, shown both in the contracts and in practical ways, was not to create an employment relationship.

The notional contract

66 We find that the contract which the legislation requires us to hypothesise would be a contract in which Mr Fitzpatrick would not be regarded for the purposes of Parts I to V of the Social Security Contributions and Benefits Act 1992 as employed in employed earner's employment by Airbus, and one in which he would not be regarded for income tax purposes as an employee of Airbus. The appeals for the years 2003-04 and 2004-05 must therefore be allowed.

67 The appeals against HMRC's decision and determinations for the years 2001-02, 2002-03, 2005-06 and 2006-07 are allowed for the reasons indicated at paragraph 3 above.

Appeal rights

68 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: 5 January 2011

E C R Consulting Ltd v Revenue & Customs [2011] UKFTT 313 (TC) (11 May 2011)
INCOME TAX/CORPORATION TAX
Personal service companies (IR 35)

[2011] UKFTT 313 (TC)

TC01174

Appeal number TC/2010/1565

National Insurance - earnings of worker supplied by service company - provision of services through intermediary – Company contracting to provide computer services – whether, if arrangements had taken the form of a contract between the worker and the client, the worker would have been employed by the client under a contract of service – No – Appeal allowed- Social Security Contribution (Intermediaries) regulations 2000, SI 2000/727, reg 6 (1) (c).

FIRST-TIER TRIBUNAL

TAX

E C R CONSULTING LIMITED Appellant

- and -

THE COMMISSIONERS FOR HER MAJESTY'S

REVENUE AND CUSTOMS Respondents

TRIBUNAL: DAVID S PORTER (JUDGE)

ALBAN W HOLDEN (MEMBER)

Sitting in public at Albion House, Leeds on 17 and 18 February 2011

Matthew Boddington, a tax consultant, for the Appellant

Tony Burke, a tax inspector, instructed by the General Counsel and Solicitor to HM Revenue and Customs, for the Respondents

DECISION

1. E C R Consulting Ltd (ECR), appeals against the decision and determinations issued on 3 December 2007 in respect of liability to National Insurance Contributions (NIC) for the period 6 April 2002 to 27 March 2005 and liability to PAYE income tax for each of the years 2002/03, 2003/04, and 2004/05. The decision and determinations were made pursuant to what is commonly known as the IR35 legislation, and related to arrangements where ECR indirectly provided the services of its sole director and shareholder, Miss Richardson, to Vertex Data Services (VDS) during the relevant period.

Comment [DJ1]: A three year "tax grab"

2. The decision was made under Social Security Contributions (Intermediaries) regulations 2000, SI 2000/727 Regulation 6 (4) and the determination under Income Tax (Pay as You Earn) Regulations 2003, SI 2003/2682, Regulation 82

3. ECR did not provide Miss Richardson's service directly to VDS, but did so through arrangements with an agency company, Best People Ltd / Spring Technology. Miss Richardson is a highly skilled IT worker specialising in software development.

4. Mr Matthew Boddington, a tax consultant with Accountax Specialist Tax Advisers appeared on behalf of Miss Richardson and called her to give evidence. Mr Tony Burke, from the Appeals and Reviews Unit at Leeds, appeared for HMRC and called Miss Hilary Harrison, a compliance officer, Miss Linda Brown, a team leader employed by VDS, and Mr Graham Holmes, a senior manager at VDS to give evidence. All the witnesses gave evidence under oath and we were provided with agreed bundles.

5. We were referred to a substantial number of cases the principle ones being :-

- *Ready Mixed Concrete (South East) Ltd v Minister of Pensions and National Insurance* [1968] 2 QB 497
- *Mersey Docks and Harbour Board v Coggins & Griffiths (Liverpol) Ltd* [1946] UKHL 1
- *Hall (H M Inspector of Taxes) v Lorimer* [1992] 1 WLR 939 (CA)
- *Dragonfly Consultancy Limited v The Commissioners for her majesty's Revenue and Customs*[2008] EWHC 2113 (Ch)
- *Nethermere (St Neots) Limited v Gardiner* [1984] I.C.R. 612
- *Lime-it Ltd v Justin (office of the Board of Inland Revenue)*[2003] STC (SCD)15
- *Tilbury Consulting Ltd v Margaret Gittins (H M Inspector of Taxes)* [2003] SPC 3020

- *Market Investigations Limited v Minister of Social Security* [1969] 2 QB 173
- *Stoddart v Cawder Golf Club* [2001] EAT/87300
- *Express and Echo Publications Limited v Ernest Tanton* [1999] EATRF 98/0528/3

The LAW

6. Regulation 6 (1) of the Social security Contributions (Intermediaries) Regulations 2000, SI 2000/727 made under the Social Security Contributions and Benefits Act 1992 (the 1992 Act) provides:

'These regulations apply where-

a. an individual ("the worker") personally performs, or is under an obligation personally to perform, services for the purposes of a business carried on by another person ("the client"),

b. the performance of those services by the worker is carried out, not under a contract directly between the client and the worker, but under arrangements involving an intermediary, and

c. the circumstances are such that, had the arrangements taken the form of a contract between the worker and the client, the worker would have been regarded for the purposes of parts 1 to V of the 1992 Act as employed in employed earner's employment by the client.'

'Intermediary' is defined in Regulation 5 and it is common ground that ECR is an intermediary for this purpose. 'Employed earner's employment' is defined in section 2 (1) of the 1992 Act to include a person whom is gainfully employed under a contract of service (which is not further defined).The intermediary is treated as making, and the individual as receiving, a payment of deemed employment income calculated in accordance with the rules set out in the legislation in respect of which the intermediary has to account for PAYE and primary and secondary Class1 NIC.

7. The legislation calls for a two stage exercise. The first is to find the facts as they existed during the period covered by the decision. The facts to be found are those that serve to indentify the 'arrangements' involving the intermediary and the circumstances in which those arrangements existed and the nature of the services performed by the 'worker'. The second is to assume that the 'worker' (Miss Richardson) was contracted to perform the services to the client (VDS) and to determine, whether in the light of the facts, Miss Richardson would be regarded as VDS's employee. The burden of proof lies with ECR and the standard of poof is on the balance of probabilities

Comment [DJ2]: Really? This tells us that ECR are guilty until proved innocent?!

Worth noting perhaps?

The facts

8. The parties are as follows:

Vertex Data Science Ltd (the "Client")
Best People Ltd /Spring Technology (the 'Agency')

ECR Consulting Ltd (the "intermediary")
Miss Elaine Richardson (the "worker")

Miss Richardson has been in business since June 1993 after having been made redundant by her previous employers. She told us that she did not want to risk being made redundant again and decided to become self - employed. As her expertise was in complex computer consultancy, she formed a company to prevent personal liability if she were to be sued. She appears to have had a large number of contracts, some of which have, in the past, run for nearly a year with the same clients. The average period appears to have been about 6 months. Her contract with Jaguar Land Rover, for instance, appears to have run intermittently from 20.8.2008 to 12.6.2010. ECR has serviced up to 3 separate clients during the period 2002 – 2005; in 2006 and 2007 it serviced 2 separate clients. ECR has specialised computer equipment and an office. It promotes the company's services through a website (http:/www.ecr-consulting.demon.co.uk).The Website contains details of Miss Richardson's CV.

9. Late in 2001, Miss Richardson was asked by Best People Ltd (Best) whether she wished to provide computer services to VDS but she refused as she was involved with another contract. She indicated that she would be pleased to help in the future if they approached her again. In February 2002 Best approached her again to see if she could help with the implementation of the Accenture Customer 1 billing system (with which she was familiar) for TXU Energy. This meant moving the clients of TXU Energy from several mainframes at VDS's building into a new billing system. She told us that she was not interviewed for the position and assumed that VDS had checked her web site which contained her CV.

10. There was no direct contract between Miss Richardson and VDS. VDS had urgently required to find someone to help with the work and they had been approached by Best, who had suggested that they used ECR and Miss Richardson. VDS had been prepared to pay £600 per day for the services but insisted, in view of the very high daily fee, that should they terminate the contract with Best, they would not expect to pay a termination fee of the same order.

Comment [DJ3]: Interesting argument as to why she used Limited company.

Comment [DJ4]: This detail here is perhaps why she was considered to be in business on her own account. If she only ever had one client the story could be different.

Comment [DJ5]: Bringing her own skills to the table – shows a lack of control.

Comment [DJ6]: Key fact here.

11. This first contract between Best and ECR was for a period of 6 months from 6 March 2002 to 5 September 2002, but was extended by correspondence from 6 September 2002 to 27 December 2002. By a letter dated 18 October . Best terminated the contract on 18 November 2002. ECR did not employ Miss Richardson to work with Best or VDS again until 21 April 2003, a gap of 3 months. She had been apprehensive about working for VDS again after the early termination of the last contract. Best offered a rate of £300 per day to ECR for her services but she refused to work at that level. Eventually the rate was increased to £350 and she agreed to the work because of the poor state of the contracting market. The work involved converting all Powergen's customers onto one platform- the Accenture Customer 1 system.

12. The second contract ran from 22 April 2003 to 25 July 2003, but following correspondence was extended to run from 11 August 2003 to 7 November 2003; and then from 24 November 2003 to 23 February 2004.

13. Best was taken over by Spring Technology Staffing Services Limited (Spring) who entered into four further contracts with ECR for Miss Richardson services at a rate of £350 per day for the following periods:-

- 15 March 2004 to 21 May 2004
- 22 May 2004 to 20 August 2004
- 23 August 2004 to 19 November 2004
- 22 November 2004 to 18 February 2005. This contract was extended by correspondence on 3 occasions to cover the following periods:
- 21 February 2005 to 11 March 2005
- 14 March 2005 to 20 March 2005
- 21 March 2005 to 27 March 2005.

14. In November 2005 Mrs Hilary Harrison, an HMRC Employer Compliance officer, commenced a review of the business records of ERC. She subsequently entered into correspondence with ECR's agents, Lawspeed, about her findings. In April 2007, after concluding her enquiries, she sought the advice of a Status Inspector colleague, who considered the evidence provided by her and then informed Lawspeed that the IR35 legislation was applicable as regards Miss Richardson's work for VDS. Mrs Harrison could not advise as to the Status Inspector's thought process and he had not been called as a witness.

15. Lawspeed did not agree that the IR35 legislation applied and consequently Mrs Harrison arranged, in December 2007, for the issue of Regulation 80 Determinations to ECR to recover additional tax as under:

Comment [DJ7]:

This isn't how employees are hired. Although this does indicate some sort of rolling type arrangement.

Comment [DJ8]: Don't know what this is???? Guess it is a tax payment call.

Notice of Regulation 80 determination 2002/03 £8907.78

2003/04 £8710.00

2004/05 £9395.00

Total £27,012.78

She also arranged for the issue of a section 8 decision to recover Class 1 NIC of £24,539.74 for the period 6 April 2002 to 27 march 2005 (of which £7069.51 had already been paid).

The contracts

16. As indicated at paragraph 7 above, it is first necessary to consider the terms of the various contracts dealing with the employment. In this context there were three contracting parties. There are agreements between VDS and Best/Spring, and contracts between Best and ECR. The contracts between VDS and Best/Spring produced to the Tribunal were less than satisfactory as they were unsigned by either party and appear to be generic agreements provided by VDS as their "IT Procurement Services" contract. As it appears that the agreements have been acted on by the parties, we are treating the agreements as valid and determinative for the purposes of this appeal.

Comment [DJ9]:

1.Unsigned contracts are considered executed. Worth pointing out.

2.Shabby generic contracts, which don't reflect the arrangements are also considered live contracts – and are used by HMRC/Judges. So contractors shouldn't sign them. Warning!

17. The first contract between VDS and Best appears to be Version 1.0 (27.4.01) and provided that Best had to find a suitable contractor, which it sourced from ECR having seen Miss Richardson's CV on ECR's website. The contract provided that VDS would be charged within the appropriate bandwidths (as fixed by VDS presumably in agreement with Best) for the level of personnel required, which rate would be fixed for 12 months. The parties conceded that the rate paid by VDS to Best was different to that paid by Best to ECR. From the figures in the contract the difference appears to have been substantial. For example Appendix 4 rates run from £988 to £1400. The contract specifically named Miss Richardson to be the personnel for the purposes of the contract.

- Clause 4.3 states that Best will supply a contractor who "will perform to a standard consistent with the requirements specified by VDS, and that the contractor will be replaced within 3 working days if Best has been informed by VDS that the contractor was not satisfactory. It also provided as follows.

  "The Consultants who are unable to fulfil their duties to the standard required will be replaced by the Agency if required"…

- 4.6 payment of invoices would be in 30 days

- 4.10 Best is to indemnify VDS against all losses, liabilities, claims, costs and expenses and insure the same up to £2,000,000
- 4.15 VDS could terminate the contract on 4 weeks notice.

The second contract between Best and VDS appears to be Version 2.0 (1/4/2002). Again the contract is unsigned and it is agreed that for the purposes of this appeal the terms are the same as the earlier contract.

18. The six Contracts above between Best and ECR are all in the same format and provide that ECR is the supplier of the services, which will be performed by Miss Richardson, the personnel named in the schedule. The rate for the first contract was £600 per day, which is equivalent to £140,000 per annum allowing for weekends and holidays. The subsequent contracts were at £350 per day equivalent to £84,000 on a similar basis. The level of payment indicates that miss Richardson is clearly a knowledgeable computer expert capable of handling complex work.

19. The contracts between Best and ECR provided at :

- 1 b) The Supplier (ECR) warrants that the Services shall be initially performed by such personnel named in the Schedule (in this case Miss Richardson). The Supplier may propose a replacement to perform the Services in substitution for the named personnel, but any such proposed substitute shall only be accepted if approved in writing by Best and the client.
- 2 c) At the end of the initial engagement Best shall be under no obligation whatsoever to offer further work to the Supplier and the Supplier shall be under no obligation whatsoever to accept any further work, if offered.
- 3 a) provides for indemnity from ECR to Best in similar terms to the VDS contract, and that ECR will indemnify Best against any income tax (whether PAYE or otherwise) or primary National Insurance Contributions…
- 4 b) invoices are to be raised against time sheets
- 5 c) Best are entitled to terminate the contract on 28 days notice or pay ECR in lieu of notice.

20. It appears that there was no contract between Miss Richardson and ECR, due to the fact she is the single shareholder and Director of the company. We take the view that the terms of the other contracts are relevant when considering the manner in which Miss Richardson worked at VDS. The contracts have been entered into by parties other than Miss Richardson. The other parties must have intended the tems of the contracts to be

Comment [DJ10]: Personal services – not good. !!

Comment [DJ11]:

Interesting this one. Level of payment is being used to indicate that someone is a highly knowledge expert – i.e. and cannot be controlled. Something we said in our whitepaper.

We should bring this up again. "How can highly knowledge experts be controlled?", "Why would a client pay someone a vast sums of money to tell them how to do a piece of work?"

Key point I reckon.

Comment [DJ12]: Buzzer goes off. Substitution is not an unfettered right, and is therefore not valid. HMRC will argue that the client is vetting the sub'.

Comment [DJ13]: Very good. No MOO.

enforceable. There have been numerous cases in the High Court, this Tribunal and the Employment Tribunal relating to the status of an individual's employment, all of which depended on the specific facts of the specific cases. We are bound by the High Court's decisions but not those of the Tribunal, although we are bound to consider them. In *Ready Mixed Concrete (South East) Ltd v Minister of Pensions and National Insurance* [1968] 2 QB 433 (*Ready Mixed*) MacKenna J listed three conditions for a contract of service to exist:

(1) 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

(2) 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 the other master

(3) The provisions of the contract are consistent with its being a contract of service

These conditions are fundamental to the creation of a contract of services and if any one of them cannot be met then the contract is not a contract of service.

21. Lawspeed wrote to HMRC on 6 July 2007 setting out in considerable detail the reasons why they considered Miss Richardson was not an employee. Mr Boddington has adopted those matters for the purposes of this appeal. The numerous cases identify the various matters which need to be considered, which overlap with those in Lawspeed's letter. We propose to use the headings in the letter and to indicate where Mr Burke, on behalf of HMRC, is in disagreement.

Substitution

22. Both of the contracts allowed for substitution. Mr Burke suggested that the contracts named Miss Richardson as the operative and the substitution clauses required VDS to consent to a substitute. As a result the service was personal to Miss Richardson and as the substitution clauses required the consent of both parties they were fettered and, as such, were not absolute in their terms. Mr Holmes, a senior manager at VDS, stated, in the meeting that HMRC had with him and Mrs Brown on 8 April 2010 that the use of contractors was a budgetary matter. Contractors were employed to control risk in relation to expenditure. This was evidenced by the need to pay £600 per day for Miss Richardson on the first contract reduced to £350 in the second. VDS needed to bring in appropriate people with the necessary skills on a short term basis to help out with various projects. Both Mrs Brown and Mr Holmes said that VDS would not have accepted a substitute. Given that VDS was prepared to employ Miss Richardson on a contract at £600 without ever having met her, we are satisfied that if she had been unable to attend through illness or had been unsatisfactory, VDS would have returned to Best/Spring under the substitution clause for them to supply another contractor with sufficient, skills, qualifications and experience. Miss Richardson confirmed that she could have sent other people to do the work as she knew of at least 6 others who were suitably qualified

Control

23. A working relationship which involves no control at all from a manager is unlikely to be classed as employment. Mrs Brown stated that she had overall control of Miss Richardson. We accept that she needed to advise Miss Richardson of the way in which VDS worked, although she accepted that VDS had no manuals or directions as to office procedures specifically for either the employees or the contractors. We do not accept, even with the qualifications she advised us of, that she was able to tell Miss Richardson how to do the work or the time she should expend in doing so. Miss Richardson produced to the Tribunal her internal time sheets for the time she worked on the project. These had been completed to comply with the European working directives, but bore no relationship to the time records kept by VDS. The records, prepared for the purposes of the agency contracts and invoices for Best, merely identified that she had worked for 37 ½ hours each week. Miss Richardson's time sheets reveal variations from 31 hours to 45 hours each week. From these time sheets it is clear that the hourly rate she was paid was based on 37 ½ week. If she worked longer or shorter hours she received no more money. The fact that she could work the hours she pleased clearly shows that she was not controlled by Mrs Brown in relation to her working practices.

Comment [DJ14]: Spot on.

Comment [DJ15]: That's a new one!!

Comment [DJ16]: Implies that daily rates are much better than hourly for IR35 purposes.

24. The two contracts, clauses 7(b) Best and 1.8 (Spring) provided that the agreements cannot be varied without the consent of Best/Spring, therefore VDS cannot be said to have daily control. Clauses 1(g) (Best) and 2.6 (Spring) indicate that Best/Spring is to decide the method of working and use its own skill and expertise to provide the services. VDS has no control over how the work is done nor when the services are to be performed save for obvious opening times of the offices and the fact that the work had to be carried out there. The fact that Miss Richardson was given a personal pass does not in our opinion make her an employee.

25. The IR Employment Status Manual states

> " …if working on large sites where access is limited to normal working hours, the worker is not going to be able to work as and when she or he pleases [and] the limitations put on when the work can be carried out tells us nothing about the status".

Mr Burke commented that *Ready Mixed* suggested that*:*

> *"* Control includes the power of deciding the thing to be done., the way in which it shall be done, the means employed in doing it, the time when and the place where it shall be done. It is the right of control not whether it is exercised".

Mrs Brown explained that she was the Design Team Leader at the time Miss Richardson was engaged to work for VDS and that Mr Holmes was her immediate Line Manager. The design team consisted of between 12 and 14 workers and included VDS employees. The project team moved from their original base in Manchester to its Bolton office. Miss Richardson was part of the design team that would produce a technical specification that

identified the changes required to the IT system. The VDS employees performed the same type of work as Miss Richardson. We accept that Mrs Brown had experience in the implementation of the system and that she was responsible for allocating and prioritising the work for the team. She told us that VDS operated a Peer Review system for the monitoring and maintenance of standards. We do not accept that these reviews were to ensure that Miss Richardson had dealt with the system correctly, but rather for the whole team to examine how the project was progressing with a view to resolving problems.

26. During her first contract, when she worked in Bolton, she had rented accommodation, and had had to continue the payments, although VDS had terminated the first contract earlier than was expected. It is unlikely that an employee would have been left with the liability to pay the additional rent. Mrs Brown indicated that all the individual on her team were engaged because of their professional experience and skill. Further, her own annual salary was on the region of £30,000 compared o Miss Richardson's initial pay which equated to £140,000. There has to be a sufficient degree of control exercisable, consistent with the contract of employment. We have decided that VDS did not have sufficient control.

Comment [DJ17]: HMRC were trying again to imply that testing/review mean that she was controlled.

This one really gets my goat up. It shows a clear lack of understanding of the IT development process.

This one is worth putting in a blog about this case. Maybe we can link it in to the poor cases of government trying to develop systems, and say that they clearly don't understand the software lifecycle!

Financial risk

26. Mr Burke suggested that Miss Richardson took no financial risk. She did not have to buy any equipment to carry out her work. The invoices were all paid on time so there was no risk of a bad debt. She had no opportunity to carry out any other work during the time she worked for VDS, so that there was no opportunity for her to make an additional profit. We do not accept that there was no financial risk. Given the amount that VDS was paying on all the contracts it would have been justified in suing Best, Best would then have sued ECR if there was negligence on the part of Miss Richardson. Clauses 3 (a) (Best) and 7.1 (a) (Spring) created an obligation to indemnify VDS. We note that consequential loss has not been excluded, so that the liability could have been substantial. If the contracts were not handled with the appropriate skill, the contracts could be terminated immediately. Clause 5 (e) (Best) and 9.3 (Spring). Miss Richardson advised us that ECR carried comprehensive insurance as the growing compensation culture increased the risk of being sued.

Comment [DJ18]: To by knowledge, no IT contractor has ever had to make a claim.

Opportunity to profit

27. In *Hall (H M Inspector of Taxes) v Lorimer* [1992] 1 WLR 939 (CA) Mummery J stated of somebody who is self-employed:

"He has the opportunity of profiting from being good at being a vision mixer. According to his reputation so there will be a demand for his services for which he will be able to charge accordingly. The more efficient he is at running the business of providing his services the greater his prospect of profit. "

Miss Richardson did, in fact, perform services for two other clients whilst working for VDS. These involved providing advice as to the most appropriate hardware and software required by the businesses, and the procurement, installation and set up of that equipment for them.

Personal factors

26. Miss Richardson provided the details of the contracts that ECR had had since starting in business in June 1993 referred to in paragraph 6 above. In *Hall (H M Inspector of Taxes) v Lorimer* [1992] 1 WLR 939 (CA) Mummery J stated:

> " If a skilled worker works for a number of clients throughout the year and has a business-like approach to obtaining his engagements (perhaps involving expenditure on office accommodation, office equipment, etc) this will point towards self-employment"

Mr Burke pointed out that all of the contracts named Miss Richardson as the operative. He considered that that meant that the contracts were personal to her and that this fulfilled the first of the conditions set out in *Ready Mixed.* Mr Holmes made it clear in the interview with HMRC on 8 April 2010 that the contractors were used as a budgetary measure and we are satisfied that VDS were not concerned who did the work so long as they were suitably qualified. They appear to have been content to leave the choice of operative to Best/Spring. We cannot therefore accept that the work was personal to Miss Richardson.

Comment [DJ19]: This is a very subtle argument.

The client did not engage the contractor personally, but the agency did.

27. Miss Richardson told us that she tended to take holidays when she was not working as she needed to provide a specialist service to the clients. She accepted that all the services had to be provided at VDS to tie in with their computer systems and, as the information was sensitive, VDS did not want information either taken off the site or downloaded on to her equipment at home.

In business on her own account.

28. In *Market Investigations Limited v Minister of Social Security* [1969] 2 QB Cook J said the test to be applied is;

> "Is the person, who has engaged himself to perform those services, performing them as a person in business on his own account? If the answer is Yes then the contract is a contract for services. If the answer to the question is No then the contract is a contract of services."

ECR is in business on its own account. Miss Richardson produced to the Tribunal copy business cards and company stationary. ECR operates from a dedicated business area at her home. It has company domain and website. ECR advertises its services and is a member of the PCG. It has retained reserves and invested in development and has over the years taken on fixed price work for a variety of clients.

Comment [DJ20]: I bet the PCG are delighted with this bit of PR!!

Comment [DJ21]: This has cropped up a few times.

Right of dismissal

29. By Clause 5 (e) of the Best agreement Best can terminate the contract with ECR if the services are not satisfactory. By (9.3 of the Best/ Spring) agreement Spring can terminate the contract with ECR "forthwith" for lack of performance. This is reflective of a commercial agreement and is an indicator of self-employment. Mr Burke suggested that a typical self-employment contract will come to an end on the completion of the work for which the contractor was engaged, whereas an employment contract usually contains provisions allowing one or other party to give notice of termination. A power to terminate an engagement for reason other than a serious breach of contract is indicative of a contract of employment. Miss Richardson had worked for VDS for a considerable length of time and the proposals in the contracts are at best neutral. We can not accept that terms in the contract are neutral, as VDS did terminate the first contract early, which effectively meant that Miss Richardson was no longer working.

Intention

30. Mr Burke suggested that intention is only relevant as a "tie breaker" in determining status (when indicators are evenly balanced). In the IR35 situation, it is not possible for the parties to have any intention over a hypothetical contract. Lawspeed have pointed out that in *Stoddart v Cawder Golf Club* [2001] EAT/87300 it was suggested

Comment [DJ22]:

This is a new one!!!

Why can't they use the original intentions from other contracts, or evidence?

> " Where persons intend to create a self-employment situation and the ingredients of such can be found, such as the method of payment, potential exposure to VAT and the lack of consent to be an employee, it is very difficult for any Tribunal to conclude that the contrary to what the parties had intended to achieve had resulted".

Clause 7 (c) (Best) and 1.2 (Spring) explicitly states that there is no intention to form an employment relationship. Mr Burke noted that clause 7.2(b) (Best/Spring) agreement with ECR provided that ECR would indemnify Best from any liability for income tax national insurance contributions and otherwise. In *Dragonfly Consultancy Limited v The Commissioners for her majesty's Revenue and Customs*[2008] EWHC 2113 (Ch) Henderson J said:

> " In the majority of cases, however, such statements will be of little, if any, assistance in characterising the relationship between the parties….If the actual contractual arrangements between the parties do include statements of intention, they should in my view be taken into account, and in a suitable case there may be material which

would justify the inclusion of such a statement in the hypothetical contract. Even then, however, the weight to be attached to such a hypothetical contract would in my view normally be minimal".

We consider that the contracts cannot be ignored and their intention can be consider when considering the terms of the hypothetical contract.

Mutual obligations

24. 31. The agreements indicate that no mutual obligation exists between VDS and ECR (Clause 2 (c) (Best) and 1.2 (Spring)) explicitly state that Best/Spring shall be under no obligation whatsoever to offer further work to ECR nor will ECR be under any obligation to accept any future work, if offered. Ditto 1.2 (Spring). Mr Burke suggests that under the terms of the hypothetical contract Miss Richardson would be required to provide her own work and skill in return for agreed pay. Thus the irreducible minimum of mutual obligations would be present in the hypothetical contract. We cannot accept that. As indicated earlier we believe that VDS was unconcerned as to who the contractor should be they were merely interested in obtaining a necessary skill for the shortest period of time as cheaply as possible. We do no accept that there was any mutuality of obligation.

Submissions

Mr Burke

Comment [DJ23]:

This is a very short summary of the HMRC arguments, which is s shame.

32. We do not propose to re-iterate matters which have already been considered when reviewing the evidence, but rather to record the principle matters which Mr Burke and Mr Boddington have raised in their final submissions to the Tribunal. Mr Burke submitted that Henderson J set out the reasons for IR35 in *Dragonfly Consultancy Limited v The Commissioners for her majesty's Revenue and Customs*[2008] EWHC 2113 (Ch) in the following terms:

> "The background to the IR35 legislation … is fully set out in the judgment of Robert Walker LJ in *R(Professional Contractors Group) v IRC*[2002] STC 165. In paragraph 51 of his judgment…he described the aims of both the tax and NIC provisions as being.. .. 'to ensure that individuals who ought to pay tax and NIC as employees cannot, by the assumption of a corporate structure, reduce and defer the liabilities imposed on employees by the United Kingdom's system of personal taxation' ".

The legislation requires the Tribunal to accept that the hypothetical contract that Miss Richardson is deemed to have entered into with VDS is one of employment. That, he submitted, is best achieved by 'painting a picture' [as suggested by Mummery J in *Hall (H M Inspector of Taxes) v Lorimer* [1992] 1 WLR 939 (CA)]. As a result it is necessary to give appropriate weight to each of the matters, which have been considered.

33. In that context he submitted that

- as Miss Richardson was named in the schedule to the agreements she was required to work for VDS in her personal capacity;
- she had worked for a considerable time with VDS
- and she had been paid on a monthly basis
- there was, therefore, a clear contract of employment with VDS

That proposition was further enhanced when it was realised that Miss Richardson had to work under the control of Mrs Brown in the Design Team. She was not free to come and go as she pleased and was required to work at VDS's premises. The suggestion that Best/Spring had the right to substitute another contractor for Miss Richardson was illusory. Best/Spring could only do that if VDS were dissatisfied with her performance and consented to the next contractor. In those circumstances the basis of the substitution was fettered and did not amount to a right to substitute at all. Such a right could not be incorporated in the hypothetical contract.

34. There was no prospect for her to make any further profit as she had to work full time for VDS. The agreement between Best and ECR required ECR to be responsible for paying the PAYE and NIC liabilities as would a contract of employment. In addition, Miss Richardson took no financial risks nor did she need to supply any of her own equipment to carry out the employment. In those regards, the terms of her hypothetical contract would be the same as the employees for VDS. She was, through the employment, part and parcel of the organisation and as a result the hypothetical contract would be one of employment and she would not have been engaged by VDS on a self-employed basis. The hypothetical contract incorporated the 3 prerequisites set out by MacKenna J in *Ready Mixed* and the assessment must be upheld.

Mr Boddington

35. Mr Boddington confirmed that the parties have agreed that for the purposes of this appeal there is no material difference between the test under the Tax legislation and the NIC legislation. The legislation does not assume what the nature of the contract is: it seeks to determine the type of contract the hypothetical contract would be either a contract of employment or a contract for services by reference to the 'circumstances' and ' arrangements'. This requires a hypothetical or notional contract to be inferred from those 'circumstances' and 'arrangements' as required by Regulation 6 (1) (c) of the NIC legislation and the equivalent tax legislation. He submitted that superficially it was difficult to tell the difference between the two types of contract. The work being done was similar to that carried out by the employees of VDS. It is necessary to consider the written contracts between the parties. There is no such contract between Miss Richardson and ECR. There were, however, contracts between ECR and Best/Spring and Best/Spring and VDS. The contract of 5 March 2002 between ECR and Best pre-dates the period of the assessment. The material parts of that contract should, therefore, be imported into the hypothetical contract.

Comment [DJ24]: Poor argument, since it was for different amounts, with breaks in the work.

Comment [DJ25]: She wasn't paid a monthly salary.

Comment [DJ26]: This is a weak argument. It only focuses on the "when" in control, which is not enough. The "how" is more key I think.

Comment [DJ27]: They have a valid point here.

Comment [DJ28]:

On it's own this is a poor argument. Many self employed people work full time for one client at a time.

Comment [DJ29]:

No, she didn't because she is a highly skilled "knowledge worker".

Comment [DJ30]: Evidence????

36. In *Express and Echo Publications Limited v Ernest Tanton* [1999] EATRF 98/0528/3 Peter Gibson LJ held that as Mr Tanton's contract had a specific provision to the effect that he could supply a substitute driver, the contract had to be one for services. As a result the case did not pass the irreducible minimum of mutual obligations as set out in *Ready Mixed*. The right to substitute means that the contract cannot be personal to the contractor. The agreements between Best/ Spring and VDS make provision for a substitute. The reality of the case is that VDS would have requested that Best/Spring should find a replacement for Miss Richardson, if the occasion arose. The substitution clause is still affective even if the consent of VDS is required. If Mr Burke is right and the clause is fettered it is still a clause which would not appear in a contract of services, but in a contract for services.

Comment [DJ31]: Weak argument. IR35 not a paper exercise etc. Matt is probably trying to imply intention to create contract for services here.

37. ECR was engaged for the performance of a specific project. There has never been any other obligation on Best/Spring or VDS to offer work to ECR or on ECR to accept such work. What occurred was the impact of market forces typical of the freelance contracting market place. It is a situation and a relationship that is typical of self-employment and atypical of an employer/employee relationship.

38. Clause 1(g) in the agreement between ECR and Best provided that ECR 'shall be expected to exercise a degree of control as to the method of the performance of the services'. It also provided that the contractor would use reasonable endeavours to see that VDS standards and methods were complied with. Mrs Brown exercised no real control over the way Miss Richardson carried out the contract. There appears to have been no employee policies, procedures or guidance available for any of the contractors. Miss Richardson was able to decline to work for VDS after the early termination of the first contract and was always free to do the same at any time. These rights are not normally found in a contract of services.

Comment [DJ32]: Key point here.

It's not like she was working for McDonalds and follow the company process manuals.

39. There was no provision in the agreements for holiday entitlement, holiday pay, sick pay, the provision of a vehicle, or a contribution to a pension fund. Most of these provisions would appear in a contract of service. Further the case of *Lime-it Ltd v Justin (office of the Board of Inland Revenue)*[2003] STC (SCD)15 and *Tilbury Consulting Ltd v Margaret Gittins (H M Inspector of Taxes)* [2003] SPC 3020 are similar to this appeal as they dealt with contractors in the computer industry and found that the contracts were contracts for services. In the circumstances the assessment should be dismissed and the appeal allowed

The decision

40. We have considered the facts and the law and have decided that Miss Richardson was employed under a contract for services. Miss Richardson decided to become self employed when she was made redundant and in 1993 set up ECR. We consider that given the level of responsibility she has taken over the years that it was prudent of her to operate under the protection of a limited company. We accept that that in itself would not prevent the hypothetical contract being a contract of services. We have however

considered the matter in the round and concluded that the hypothetical contract would be one for services for the following reasons:

a. Unlike many of the case we have been referred to, this case has two agencies- Best/Spring and ECR. Miss Richardson was not a party to the contract between VDS and Best/Spring. As submitted by Mr Boddington, we accept that, where the parties have entered into formal contracts, the terms of those contracts have to be imported into the hypothetical agreement between Miss Richardson and VDS.

b. The HMRC interview of 8 April 2010 clear shows that VDS used their contractors on the basis that they could obtain the best advice at the most reasonable price. VDS appear to have relied on Best/Spring to provide the contractors. It appears that it was immaterial who was appointed, so long as that person had the necessary skills. We do not accept that in reality the substitution clause was in any way fettered as suggested by Mr Burke. On that basis we are satisfied that the hypothetical contract would have to have a valid substitution clause, which could only be found in a contract for services.

c. VDS were prepared to negotiate the best price at the time, which in this case, was £600 for the first contract and almost half that amount for the second contract. The hypothetical contract would have to have a clause, which gave VDS the opportunity to fix the remuneration to be paid on their terms. It would not be possible to control an employees pay in that manner and a contract of service would make no such provision.

d. Whilst we accept that Mrs Brown represented VDS with regard to the management, we do not accept that she had any real control over the way in which Miss Richardson worked. It is unusual that VDS were content to accept invoices showing the work for the week as being 37.5 hours when it is clear from Miss Richardson's internal records that the hours she worked varied from week to week. That is consistent with a contract at an agreed price, which leaves the contractor to deliver the same as best he or she might. A contract of services would specify a 37.5 hours working week and would make no provision for the employee to provide variable cover without consent.

e. The termination provisions made it clear that there was no obligation on either party to employ the other or work for the other. This was demonstrated when Miss Richardson refused initially to work for VDS, also when VDS subsequently terminated the first contract prematurely. The hypothetical contract would have to make provision for this. This is not a provision that would be found in a contract of services.

Comment [DJ33]: WOW!

The sub clause is valid. I guess this makes sense because the client did not ask for Miss Richardson, and the decision was up to the agency. Very interesting. The agency saved her bacon there.

Comment [DJ34]:

Varying amounts of pay indicate a lack of control. Key point.

Comment [DJ35]:

Working variable hours is apparently an indicator of self-employment. Bit odd – ask any permie!

Comment [DJ36]:

Very good. Key point. Correct termination clauses indicate lack of MOO.

f. In 'painting the picture' it is clear to us that ECR is a genuine business and therefore not a target of the IR35 legislation. The terms of the hypothetical contract would result in a contract for services.

The findings of fact and the application of the statutory assumptions to those findings do not support the decisions appealed against. We therefore allow the appeal. We make no order for costs as none have been requested.

41. 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.

TRIBUNAL JUDGE

RELEASE DATE: 11 May 2011

Dave's notes:

- Lack of control due to varying pay levels and lack of processes/procedures that she had to follow.
- Lack of personal service because the client did not request her specifically, and left the agency to find whoever they wanted. This is quite unusual for contractors – not to have an interview, and for a client to just say "Send me an XYZ skilled person." Substitution existed because the client did not request her personally. She got out on a subtle point here.
- Beware of accepted any contract – even if it is not signed.
- Having all the trappings of business (cards, website etc) can help a great deal.
- HMRC still try to argue that because a developers work goes through the software lifecycle into the quality department for code review, and user acceptance testing, this means there is control. What codswallop.
- Daily rates with variable hours appear to be much better than hourly rates.
- And here's the main thing from my point of view: Here we have a classic case where **what** the worker was hired to do is EXACTLY the same as the existing employees. The contractor was hired to bump up the team to meet deadlines etc. And yet this person passed IR35. Sort of blows holes in any potential business tests!!

TC01264

Appeal reference: TC/2009/12134

Income tax and NIC – IR35 legislation – worker supplied through intermediary – whether worker was an employee or a subcontractor – a subcontractor – appeal allowed

FIRST-TIER TRIBUNAL
TAX

MARLEN LTD **Appellant**

- and -

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

Tribunal: Lady Mitting (Judge)
Rayna Dean (Member)

Sitting in public in Birmingham on 10 January 2011 and 28 March 2011

Mr. Matthew Boddington and Ms. Nicola Smith of Accountax Consulting for the Appellant

Kelvin Shorte of HMRC for the Respondents

DECISION

1. Marlen Ltd has appealed against a decision that a series of engagements under which the services of a Mr. Gary Hughes were provided to JC Bamford Excavators Limited ("JCB") were subject to what is commonly known as IR35 legislation. Determinations were made in respect of National Insurance Contributions for the years ended 5 April 2003, 5 April 2004, 5 April 2005, 5 April 2006 and 5 April 2007. Similarly determinations were also made for income tax for the same years. The notices and determinations were made on 28 January 2009.

2. We heard oral evidence from Mr. Gary Hughes and the Appellant also put in an unchallenged witness statement from a Mr. Ken Walton, the international engineering manager for JCB. The Respondents called no oral evidence.

The legislation

3. Regulation 6(1) of the Social Security Contributions (Intermediaries) Regulations 2000 provides:

> "These Regulations apply where—
>
> (a) an individual ("the worker") personally performs, or is under an obligation personally to perform, services for the purposes of a business carried on by another person ("the client"),
>
> (b) the performance of those services by the worker is carried out, not under a contract directly between the client and the worker, but under arrangements involving an intermediary, and
>
> (c) the circumstances are such that, had the arrangements taken the form of a contract between the worker and the client, the worker would be regarded for the purposes of Parts I to V of the Contributions and Benefits Act [the Social Security Contributions and Benefits Act 1992] as employed in employed earner's employment by the client."

"Intermediary" is defined in Regulation 5 and it is common ground that the Appellant is an intermediary for this purpose.

4. Similar provisions applying for PAYE purposes are contained in Schedule 12 to the Finance Act 2000 and Part 2, Chapter 8 Income Tax (Earnings & Pensions) Act 2003.:

> "1—(1) This Schedule applies where—
>
> (a) an individual ("the worker") personally performs, or is under an obligation personally to perform, services for the purposes of a business carried on by another person ("the client"),

(b) the services are provided not under a contract directly between the client and the worker but under arrangements involving a third party ("the intermediary"), and

(c) the circumstances are such that, if the services were provided under a contract directly between the client and the worker, the worker would be regarded for income tax purposes as an employee of the client."

5. The approach to be taken by the Tribunal has been set out by His Honour Stephen Oliver QC in the IR35 case of *Tilbury Consulting Ltd v Gittins* [2004] STD (SCD) 72:

> "The legislation calls for a two stage exercise. The first is to find the facts as they existed during the period covered by the decision. The facts to be found are those that serve to identify the "arrangements" involving the intermediary and the circumstances in which those arrangements existed and the nature of the service performed by the "worker". The second is to assume that the worker was contracted to perform services to the client and to determine whether in the light of the facts as found (the worker) would be regarded as the (client's) employee."

6. The issue to be determined by the Tribunal therefore is whether, had the arrangements taken the form of a contract between Mr. Hughes and JCB, Mr. Hughes would have been regarded as employed by, ie an employee of, JCB.

The evidence

7. Marlen Ltd ("Marlen"), of which Mr. Hughes is the sole director and shareholder, was incorporated in 1989. It provides its clients through various agencies with the engineering, design and drafting services of Mr. Hughes. In 2002 Marlen registered with an agency, DDC Precisions Ltd ("DDC"), through which Mr. Hughes' services were supplied first to a company called Compact Products Ltd (a satellite of JCB) in Cheadle, Staffordshire, from April 2003 to January 2004, and then for JCB itself at its Rocester site from February 2004 to April 2007.

Contractual arrangements

8. There is no written contract between Mr. Hughes and Marlen.

9. In April 2003, JCB and DDC entered into an arrangement whereby DDC became the "sole preferred supplier to JCB for contract engineering resources". This arrangement was evidenced by a single-page agreement dated 5 March 2003 under which DDC was given two working weeks to fulfil each request from JCB. The requests from JCB were subject to a set of JCB's "Conditions of Purchase". This eight-page document was in no way personalised, referred to supplies of goods and services and contained no clauses of particular relevance to the determination of the issues before us. We were also referred to an Agreement between DDC and JCB dated 2 April 2007 (ie post-dating the periods under appeal). This Agreement sets out

very fully the terms and conditions governing the supply by DDC to JCB of contract personnel, but no evidence was given as to whether this was the first such contract or a replacement for earlier ones and we therefore cannot say whether the contractual terms set out would have been in force during the periods under appeal. We therefore take no account of the terms of this contract.

10. Each engagement which DDC procured for Mr. Hughes was offered by DDC to Mr. Hughes by way of a Purchase Order letter. This was in the form of a personal letter to Mr. Hughes from DDC beginning:

> "We have pleasure to advise the following purchase requirements referring to the above purchase order subject to the attached Terms and Conditions of Contract for Services."

The letter set out the description of the role as "engineering resource support" and the commencement and completion dates. The first engagement with Compact Products Limited was covered by four such contracts running from 31 March 2003 to 6 February 2004, the first three for three months each and the last one for four weeks. The second engagement with JCB was covered by nine contracts, again running continuously but for varying numbers of months. The evidence which we heard from Mr. Hughes, and supported by Mr. Walton in his witness statement, was that towards the end of each of the contract periods, Mr. Hughes would speak to Mr. Walton to see if he was to be offered a renewed contract. JCB was under no obligation to offer an extension or a further contract but given the volume of the work, a contract was on each occasion offered and accepted. Mr. Hughes would inform DDC who would then liaise with JCB and Mr. Hughes to generate the relevant paperwork. Mr. Walton stressed that Mr. Hughes would not expect further work from JCB automatically, which is why he continued to ask for work. Mr. Walton describes speaking to the contractors about a month before their project is to end to see if the contractor had anything else lined up or if they were clear for, say, another six months. He stressed that any arrangement had to be agreed with DDC.

11. The final contract with Compact Products Limited commenced on 5 January 2004 and was due to end on 5 February 2004. However, Mr. Hughes was given notice under that contract on Monday 20 January that his final working day and last paid day of work was to be Friday 25 January. The early termination was said to be as a result of a budget deficit at Compact Products. Mr. Hughes was then out of work for two weeks before being offered his first contract with JCB. Mr. Hughes terminated the engagement with JCB by serving one week's notice to take up a contract on higher pay with Rolls Royce.

12. We were referred to two written contracts between Marlen and DDC dated 6 – 8 February 2004 and 28 March 2004 respectively. The terms which are relevant to this case were in each version identical. These documents were headed "Terms and Conditions of Contract for Services" and were the terms and conditions referred to in the engagement letters. The relevant terms and conditions included the following:

- Marlen was obliged to complete the services provided within any agreed timescale and was to devote such time as might be necessary for the proper performance of the services.

- Marlen was obliged to perform the services with reasonable care and skill - rectification of unsatisfactory work being at Marlen's cost.

- Marlen was to provide DDC with progress reports.

- Marlen was to ensure that its personnel observed health and safety regulations at the premises where the services were being carried out.

- In case of illness or injury to Marlen personnel, Marlen was to report the matter to DDC. Marlen was obliged to provide a suitably qualified replacement, incurring any additional training costs.

- If DDC or the client considered any of Marlen's personnel unsuitable, there was provision for either an agreed replacement or termination of the contract.

- DDC undertook to make all reasonable efforts to arrange access to the client's premises and to make available information necessary for Marlen to carry out the services.

- The services were to be carried out at a location agreed between DDC and Marlen.

- DDC was to pay Marlen monthly.

- DDC was not obliged to offer future contracts to Marlen and Marlen was under no obligation to accept future contracts offered by DDC.

- Marlen was entitled to enter into contracts with other parties, other than the client provided by DDC.

- Nothing in the contract was to make Marlen and DDC partners or to make Marlen personnel employees of DDC.

- Marlen and its personnel were excluded from any right against DDC or the client in respect of employment protection legislation and benefits etc.

- The contract could be terminated by one week's notice.

- Marlen was obliged to carry its own public liability and professional indemnity insurance.

- There were the usual provisions about indemnity and intellectual property rights.

13. The documentation referred to above therefore sets out the contractual arrangements. The practical arrangements of Mr. Hughes' role and the circumstances of his engagement, we gleaned from the following :

1. Mr. Hughes' oral evidence
2. Mr. Hughes' witness statement
3. The unchallenged witness statement of Mr. Walton
4. The notes of an interview between Mr. Forster of HMRC and Mr. Walton dated 20 June 2008, annotated and agreed by Mr Walton
5. A written response dated 19 October 2007 from Mr. Hughes to HMRC answering various questions raised of him
6. A written response from Mr. Walton dated 21 May 2007 to HMRC answering various questions raised of him

We do not refer in detail to all of these documents but extract the relevant information and note the odd points of contradiction.

The nature of Mr. Hughes' work

14. The purchase orders from DDC to Mr. Hughes referred to the provision of engineering resource support, further defined as mechanical design engineering expertise or checking expertise. Mr. Walton said that Mr. Hughes would have been engaged for a specific contract. This accorded with Mr. Hughes' evidence that he would normally at any one time have been working on one particular project, for example the development of a machine to be marketed in Brazil which required an engine to be fitted, the parts of which had to be 60% locally sourced in Brazil. Mr. Hughes could however be asked by JCB management to drop whatever he was doing and attend to another job if an emergency arose which required attention or which requires a skill which he was thought to possess. In the main Mr. Hughes worked in the Development Department but agreed on occasion to work on projects within the Production Department. The evidence of Mr. Walton (paragraph 21, witness statement) and Mr. Hughes' oral evidence was that JCB used its contractors for two purposes. One was to provide a skill or an aptitude which the employees did not necessarily possess, or secondly to "smooth out overloads where resource requirements exceeded availability". This accorded very much with Mr. Hughes' oral evidence that he personally was not brought in to apply a specific skill or expertise which JCB did not already have in house. His evidence was that the employed senior design engineers would all have an equivalent degree of skill and expertise to his own, but his recruitment arose out of a shortage of such skilled manpower on specific projects.

Substitution

15. The evidence as to substitution was confused. The contract between Marlen and DDC clearly provides (paragraph 4.11) that the contractor (Mr. Hughes) is obliged to provide a suitably qualified replacement in the event that he is prevented by illness or injury from performing his services. Mr. Hughes, in his witness statement and in his oral evidence, confirmed this, saying that he had the right of substitution; where he acquired the substitute from was up to him, and if he could not find someone suitable he would then have approached DDC. Mr. Hughes would have paid the substitute direct. It is equally clear and indeed undisputed that Mr. Hughes never did appoint a substitute. There is in fact no evidence that Mr. Hughes was ever off through illness or injury or for a sufficient period for the need for a substitute ever to arise. Mr. Hughes was asked by Mrs. Dean if he had considered appointing a substitute when he terminated his contract, to which he replied that he had not as he then considered that the contract and all his obligations under it were at an end, the contract having been to provide Gary Hughes.

16. Mr. Walton's evidence is somewhat at variance with this arrangement. At paragraph 23 of his witness statement he sets out that JCB would give DDC its requirements. He would not have accepted a substitute from Mr. Hughes, but that if a situation had arisen where Mr. Hughes has been unable to provide the services then he, Mr. Walton, would have contacted DDC to provide someone else with the same skill set. Mr. Walton saw his contract as being with DDC to provide someone suitable to do the job. Further, in his interview with HMRC, Mr. Walton was asked if Mr. Hughes had been unable to attend personally whether he was obliged to offer a substitute. Mr. Walton replied "definitely not" and that no substitute had been provided in practice. He stated that Mr. Hughes had never offered a substitute and had he done so one would not have been accepted. He did however go on to say that if Mr. Hughes had been absent for a month or more, then Mr. Walton would have gone back to DDC for a replacement contractor. To be noted here is that when Mr. Walton was asked to sign the interview note, Mr. Walton added in the following manuscript note which we set out in full:

> "On this particular issue it may have more to do with Mr. Hughes' contract with DDC which I have not seen. Our arrangement is with DDC and they get the personnel and recommend candidates that they feel are suitable for JCB's requirements. If there is a long term absence then this would be a matter between DDC and Mr. Hughes to find a replacement."

17. Without the benefit of hearing and probing this in more depth with Mr. Walton, we take the view that Mr. Walton's note in fact probably solves the contradiction. As far as JCB was concerned, its arrangement was with DDC, to whom they would look to fulfil its needs. If JCB felt that the need for a substitute had arisen it would be to DDC whom they would go. However, as between DDC and Mr. Hughes, Mr. Hughes had taken on the contractual responsibility for finding and funding a replacement for himself. There is no evidence and no suggestion is made that Mr. Hughes was ever absent from work for long enough to justify the recruitment of a substitute. Again it should be noted that in paragraph 23 of his witness statement, Mr. Walton states that he never expected Mr. Hughes "to give his personal service to carry out the job". JCB would give DDC its requirements and would expect DDC to match them.

Mr. Hughes' hours of work and working arrangements

18. This is another area where there is an apparent conflict of evidence between what is set out on paper and what appears to have happened in practice. In Mr. Walton's written response of 21 May 2007, the question is asked "whether or not the hours of starting and finishing were fixed, and if so the daily times". Mr. Walton's response is that there were fixed hours Monday to Thursday, 8:30am to 5:00pm and on Friday 8:30am to 4:00pm with 30 minutes' lunch each day. The next question was whether the number of hours worked each day or days per week and whether or not the worker was free to vary them without permission. Mr. Walton's response was that "hours worked in accordance with above. Permission given to work the fixed shutdown". In his interview with HMRC, Mr. Walton refers to the working hours as being set in stone but does also refer to them as the "minimum hours required to fit in with employee's work times".

19. This in fact is in contradiction not only with Mr. Hughes' own evidence but also with Mr. Walton's description of what happened in practice. Mr. Hughes' evidence was that the employed staff's core working hours were indeed 8:30am to 5:00pm and he understood that he was expected to work a basic 39 hour week, but in practice this rarely happened. Such was the volume of work Mr. Hughes would almost invariably work a greater number of hours. Equally, he never worked fixed hours but would start work earlier - at around 7:30am – and would leave later. On Fridays (72 out of 90 in his first two years with JCB) he normally left at 2:00pm. This flexibility was something that was not open to the employees. First, Mr. Hughes told us that he could work whatever hours he wished without seeking permission, although he would as a matter of courtesy tell the management. Secondly, if any employee wanted an afternoon off he would be expected to not only obtain permission but also to make up the time.

20. There is documentary support for Mr. Hughes' evidence in various JCB-generated documents which we saw. These list Mr. Hughes' working hours in any given week and we note for example that in week ending 6 June 2004 he worked 34.5 hours; week ending 5 September 2004 he worked 44 hours; week ending 12 September 2004 30.5 hours; week ending 19 September 2004 42.5 hours and week ending 26 September 2004 42.5 hours.

21. In Mr. Walton's interview with HMRC he adds an additional manuscript note at the end as follows:

> "Mr. Hughes was a conscientious worker and as stated there was plenty of work so invariably he would come in early and go later than the fixed hours to ensure the work was done. On some days he would arrive later or leave earlier."

22. In his witness statement Mr. Walton repeats that when a project began JCB would tell DDC the general hours of work "although Gary was always in before me and left after me" (paragraph 19). We find as a fact that, in practice, Mr. Hughes did not work the fixed hours laid down for employees but hours of his own choosing, and

that he did so without having to seek permission but that he did as a matter of courtesy inform Mr. Walton or his project manager. It may well be that this arrangement worked and was allowed to work because it was clear to everyone that Mr. Hughes did not take advantage of this flexibility and in any event worked in excess of the core hours. It could have been that if a contractor had been found to be under-performing he would have been reined back into the set hours, but this was not the case with Mr. Hughes.

23. Mr. Hughes told us - and this was confirmed by Mr. Walton – that there were at least a couple of occasions when the computer servers broke down and the contractors were sent home, without pay, whereas the paid staff were not sent home.

24. JCB, being a manufacturing plant, had set holidays, one week in May and three in July / August when the whole manufacturing plant closed down and the entire paid staff, with the exception of the maintenance and security staff, took their holidays. This was inflexible and all employees took their holidays within the compulsory shutdown. The only flexibility within the system was that in reward for long service employees were given, on a staged basis, one day's extra holiday as a "service day". None of this applied to Mr. Hughes. He worked throughout the time the plant was closed down and took his holidays whilst the plant was operational. He did not have to seek permission but again would tell the management as a matter of courtesy. At no time was permission ever refused to Mr. Hughes to work the hours he wished or to take the holidays he wished.

25. It was the evidence of both Mr. Hughes and Mr. Walton that the contractors worked within teams with the employees. They sat with them and there was no physical demarcation between them. Mr. Hughes was provided with a desk, a computer, a phone line and email access, his email address being given g.hughes@jcb.com. The rest of Mr. Hughes' equipment he took in himself – a calculator, micrometer, a steel rule and a measuring tape. There was a stationery cupboard which he, as a contractor, was not allowed to access. Apart from a high-visibility jacket, Mr. Hughes, unlike employees, had to provide his own clothing – fleece, safety shoes, woolly hat and a waterproof jacket.

26. The JCB computer operating system used by Mr. Hughes could only be used on site and he would not be allowed to bring his own systems into work or take any work home. Contractors were not allowed, for security reasons, to work off-site, and indeed, as Mr. Walton pointed out in his statement, the way in which Mr. Hughes' drawings were moved in the server was so complex that it was for this purely practical reason that work could only be done on site.

27. The contractors received no induction. Mr. Walton stressed that unlike employees, they were given no training. The training given to employees was lengthy, as befitted the extremely complex operating systems being used, but the contractors were expected to have all the necessary skills and knowledge to be able to operate the system without training and to be able to work, again without training, to the company and statutory legal standards. The contractors accessed the buildings, as did the employees, by simple swipe card, this being part of the site security system.

There were a number of miscellaneous benefits which the employees enjoyed but which were denied to the contractors – free canteen meals; membership of the company social club; entry into the private medical and dental scheme and access to the on site doctor and nurse; subsidised use of the gym facilities; participation in the bonus scheme. Equally the contractors received none of the usual employment benefits of holiday pay, sick pay, or membership of the pension scheme. They were not covered by the company's grievance or disciplinary procedure but equally did not participate in the appraisal scheme.

Financial arrangements

28. Mr. Hughes at the commencement of his contracts would agree with DDC an hourly rate of pay, and he was throughout paid for the hours worked, nothing more, nothing less. He had no knowledge of the financial arrangement between JCB and DDC. Mr. Hughes maintained a weekly timesheet which he had signed off by JCB management at the end of each week. There was no occasion when the accuracy of his timesheets was challenged. The timesheet would be faxed through by Mr. Hughes to DDC who would then invoice JCB in accordance with the contractual arrangements within the two companies. As far as Mr. Hughes was concerned he would, on a monthly basis, generate his own invoice for the total number of hours worked, which he would submit to DDC, who paid him on receipt. He accepted in cross-examination that other than DDC refusing to pay him, he in fact ran no financial risk.

Supervision / control

29. This was another area where there was an apparent conflict of evidence. It was common ground between Mr. Hughes and Mr. Walton that at the outset of a job, Mr. Hughes would be briefed by the project or engineering manager. They would outline exactly what was being built, what Mr. Hughes' role was to be and what was expected of him. He would then use his own knowledge and skill to design his particular part, get it manufactured and ready for testing and development. In interview with HMRC, Mr. Walton stated that a contractor "would be under the control of the project leaders… who would brief the contractor". It should be noted however that this was in response to the specific question as to how Mr. Hughes would know what work JCB wished him to undertake.

30. We see Mr. Walton's evidence as being very much in line with Mr. Hughes' oral evidence, which was that the only form of real control exercised over his work was by Mr. Walton "overseeing the project and checking on progress". The way in which Mr. Hughes carried out the work and the priority which he gave to different aspects of it were not of concern to JCB but were a matter entirely for Mr. Hughes. Mr. Hughes likened Mr. Walton's role to that of a householder monitoring the progress of an extension being built by professional builders. That householder would be interested in the progress of the extension, would be ensuring it was running to time, but would have no input into how it was being built. Mr. Walton, according to Mr. Hughes, would not in any event have been able to exercise any practical control as he would not have the necessary degree of knowledge or skill or be able to access Mr. Hughes' computer, which was subject to a personal password. We believe

it may well be useful at this stage to incorporate within this decision three paragraphs of Mr. Walton's witness statement which in effect sum up on the position as Mr. Walton saw it:

> "17. At the beginning of a typical project the principle engineer would sit down with Gary and explain what needed doing. Gary would decide how to do the job using standard industry guidelines books of the material that were available and steel standards as only certain nuts and bolts can be used on JCB machines. For example if Gary would be require to maybe design a part of a digger arm this would not be the whole arm just a small part of it. How he actually designed it was for him to decide using his own skill and knowledge.
>
> […]
>
> 32. During the period Gary was working at JCB once Gary accepted the project it was down to Gary to break down the project requirements and design the different parts. There were different parts of machines to design and each guy had a different way of working. The total machine design would be an assembly of these different pieces of work which would all come together at the end.
>
> 33. There is no standard way of working as each individual uses his / her own calculations and method of working. How Gary got to the end result was down to him. None of the contractors have been taken on to do the total machine conceptual design work."

31. The conflict in evidence in fact comes between Mr. Hughes' oral evidence and what he wrote in response to questions from HMRC. The question he was asked was the frequency with which he had to report, to which he replied "daily discussions were held to discuss the progress of the project". He went on to say that he would provide technical details of the design. However he also went on to say that he was not monitored or controlled on the services provided, merely having to apply JCB and European standards.

32. Mr. Hughes was unable to explain why he had written that there was daily reporting as there just wasn't. Subject however to this, we do not see there is a major discrepancy. It is clear from Mr. Walton and from Mr. Hughes that the work to be done was handed down by the project manager who briefed Mr. Hughes, as indeed he would have to otherwise Mr. Hughes would not have known what he was expected to do. However beyond that, it was up to Mr. Hughes to carry out the work in the way which he saw fit. This is also supported by a manuscript note which Mr. Walton made to his interview with HMRC:

> "To clarify further how the work was handed out. After a brief with the project manager or engineering manager, Mr. Hughes would be left to get on with the work. The manager would oversee the project to check what progress was being done. The way the work was done was up to Mr. Hughes as long as he worked within the agreed deadlines and health and safety guidelines."

33. It was common ground between Mr. Walton and Mr. Hughes that although Mr. Hughes was engaged initially on a particular project, he was on occasion asked to move to other jobs and he never refused, although Mr. Hughes told us that in practice he could have done had he wished to. Mr. Walton clearly believed that he had the authority to reassign Mr. Hughes to any other project within his unit, and he was indeed asked on occasion by management to help solve any unexpected problem which might arise.

Case law

34. We were referred by the parties both orally and in their opening and supplementary closing skeleton arguments to a number of cases which have been the subject of analysis in many tribunal decisions. We do not propose to repeat that analysis here but would reassure both parties that we have considered all the passages in all the cases to which we were referred, and the mere fact that we do not repeat a reference in this decision does not indicate that it has been overlooked. The widely accepted approach to determining employment status, which was adopted here by both parties, can be found in the judgment of MacKenna J. in *Ready Mixed Concrete (South East) Ltd v Minister of Pensions and National Insurance* [1968] 2 QB 497 at 515:

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

35. In *Market Investigations Ltd v Minister of Social Security* [1969] 2 QB 173 Cooke J stated at (184-185):

> "… the fundamental test to be applied is this: "Is the person who has engaged himself to perform these services performing them as a person in business on his own account?" If the answer to that question is "yes," then the contract is a contract for services. If the answer is "no," then the contract is a contract of service. No exhaustive list has been compiled and perhaps no exhaustive list can be compiled of the considerations which are relevant in determining that question, nor can strict rules be laid down as to the relative weight which the various considerations should carry in particular cases. The most that can be said is that control will no doubt always have to be considered, although it can no longer be regarded as the sole determining factor; and that factors which may be of importance are such matters as whether the man performing the services provides his own equipment, whether he hires his own helpers, what degree of financial risk he takes, what degree of responsibility for investment and management he has, and whether and how far he has an opportunity of profiting from sound management in the performance of his task."

36. In *Hall v Lorimer* [1992] STC 599 Mummery J stated at (612) (in a passage approved by Nolan LJ – [1994] STC 23 at (29)):

> "In order to decide whether a person carries on business on his own account it is necessary to consider many different aspects of that person's work activity. This is not a mechanical exercise of running through items on a check list 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. The process involves painting a picture in each individual case. As Vinelott J said in *Walls v Sinnett (Inspector of Taxes)* [1986] STC 236 at 245: "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 of 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 may be compelling in one case in the light of the facts of that case may not be compelling in the context of another case"".

37. The need for mutuality of obligation and of control have been referred to as "the irreducible minimum" in any contract of employment.

Submissions

38. We now set out the advocates' arguments and our own considerations and conclusions on the various elements which go towards painting the picture in this case. Again, as in our reference to case law, we should say the advocates very helpfully made lengthy oral and written submissions. These have all been carefully considered and the fact that we have not expressly included in our decision any particular submission does not mean we have overlooked it.

Mutuality of obligation

39. Although Mr. Hughes' engagement with JCB lasted from 31 March 2003 to April 2007 (less the two-week period when he was out of work following the early termination of his contract with Compact Products), the engagement was made up of a number of short-term contracts. It was submitted by Mr. Shorte and accepted by Ms. Smith that there could be mutuality within the individual contracts despite there being no long-term or ongoing mutuality. This is clearly correct as JCB were under no obligation to continue to offer Mr. Hughes a further contract every time an existing one came to an end, but this does not affect the position under each individual contract.

40. In putting forward his own submission, Mr. Shorte adopted the summary of case law set out by Judge John Clarke in J and *Littlewood v Revenue & Customs* [2009] UKSPC 00733 at paragraphs 57 to 84. Mr. Shorte contended that the JCB recruitment process involved identifying the work to be done and the suitability of the individual contractor before a contract was offered to DDC. DDC accepted the work and supplied Marlen to do it. For each period of engagement there would have been an offer of work, an agreement to do that work and an agreement to pay for it. Mr. Shorte went on to contend that the hypothetical contract would contain a requirement to provide Mr. Hughes personal service; there would be consideration paid for the provision of that service and there would be a period of notice required to terminate the contract. Consequently, Mr. Shorte submitted, the irreducible minimum of obligation was present.

41. It was Ms. Smith's contention that there was no mutuality of obligation within any of the individual contracts. She cited the fact that Mr. Hughes was sent home when the computers were down; the early termination of the contract with Compact Products and Mr. Hughes' early termination of his final contract with JCB.

42. It appears to us that Ms. Smith is correct in her view. Mr. Shorte's submission that within each contract there was "an obligation on JCB to provide work, or at least to pay for it, and on Mr. Hughes to undertake the work" is not borne out by the facts. When the computers were down the employees remained in place and were paid, whereas Mr. Hughes was sent home, crucially, and this was accepted by Mr. Walton, unpaid. Both parties terminated a contract partway through. The contract with Compact Products was terminated because of a budget deficit. Mr. Hughes terminated his own contract with JCB when a better offer came up. In sending the contractors home when the computers were down, it appears to us that JCB demonstrated that it did not consider itself to be under any obligation to provide work or pay even after an offer had been made and accepted. Both parties demonstrated by their conduct in terminating contracts midway through their belief that these contracts could be terminated at any time without consequence. That this happened is not consistent with a relationship in which mutuality of obligations is present.

Control

43. Both advocates referred to the tribunal to the words of MacKenna J in *Ready Mixed Concrete* that control in this context means the power of deciding the thing to be done, the way in which it should be done, the means to be employed in doing it, the time when and the place where it shall be done.

44. It was Mr. Shorte's submission that Mr. Hughes was under a large degree of control. Mr. Shorte saw Mr. Hughes as a resource used by JCB as they saw fit – in reality no different from an employee. He pointed to Mr. Hughes' acceptance that he brought no particular skill not already possessed by the senior employees. He reminded us of Mr. Walton's view that Mr. Hughes was under the control of the project leaders and that by his own admission Mr. Hughes told us he had to report daily. Further, Mr. Hughes had accepted that he would take instructions from the senior designers who "were very clear what they wanted". Mr. Hughes had to carry

out his work in JCB's premises, not being allowed to take it home. Mr. Shore also referred us to Mr. Walton's initial statement that Mr. Hughes had to work fixed hours and that he could be reassigned to other projects. JCB, contended Mr. Shorte, defined what was to be done, where the work was to be done and the time within which it had to be completed. His progress was at all times monitored and such was the degree of control that it could only lead to the conclusion that this was a contract of service.

45. Ms. Smith, adopting the words of MacKenna J, stressed that the control had to be substantial enough to render the worker the servant of the master, and it was her submission that control to that degree did not exist here.

46. The degree of control that is exercised has to be looked at in the context of what is being done, what is being produced. There is no absolute standard which can be universally applied. Mr. Hughes was working on but one small part of a very much larger project. As Mr. Walton pointed out – "the total machine would be an assembly of these different pieces of work which would all come together at the end". They couldn't possibly "come together" if there was not a measure of control over precisely what Mr. Hughes was producing. His work had to be coordinated and fitted into the greater whole. Every part that was being produced for any particular machine was interdependent with every other part. Equally JCB would have time limits to meet – time limits which had to be passed down to their contractors and employees alike. Every single person employed and contracted had to work together to produce a specific machine within a specified timeframe. This could only be achieved by a reasonably rigorous direction and supervision by senior management. We believe that in reality, the degree of supervision and direction exercised over what Mr. Hughes was doing would be broadly similar to that exercised over all the other contractors and senior employees simply because the nature of the project demanded it. We got the impression that the senior employed designers worked in very much the same way as Mr. Hughes – being told what needed to be done and then left to use their skill and knowledge to design it. In summary therefore, when we look at "the thing to be done" and "the way in which it shall be done" we find that management dictated what had to be done, but the way in which he did it was very much down to Mr. Hughes, but having said that we believe that this would be no different from the way in which similarly qualified senior employees worked. This similarity extends to an examination of where the work had to be done. Mr. Hughes had no latitude in this. He could not work at home but had to work on site – the only practical place to carry out such work.

47. However, as McKenna J made clear, there are other aspects to control and it is in an examination of these that a clear distinction can be drawn between employees and contractors and as a contractor Mr. Hughes was subject to markedly less control than employees. No employee had Mr. Hughes' flexibility of working hours. In practice he came and went virtually as he wished, advising management only as a matter of courtesy. No employee had the ability to take a Friday afternoon off or work through the mandatory staff holidays when the plant was closed down. No employee could take holidays when he wished. Mr. Hughes went through no induction process and was not subject to appraisals. He was not subject to the company's disciplinary or grievance procedures. He was under a contractual

obligation to rectify errors at his own expense. Examining the question of control as a whole and putting together all the individual factors which make it up, we conclude that Mr. Hughes was not subject to the degree of control which would be necessary to constitute a contract of employment. The control to which he was subject was significantly less than that exercised over employees and demonstrates a clear distinction between the two.

48. We pause here to review our findings so far. We have considered two factors – mutuality of obligation and control. These are the two factors which make up the irreducible minimum required to demonstrate a contract of employment. Whilst we have found some evidence of control, that which does exist falls short of that which is required in the terms of the test propounded by MacKenna J. The picture in relation to mutuality is even clearer. It is our conclusion that there is no mutuality of obligation and the degree of control which would have been needed to establish a contract of employment just did not exist. The appeal therefore should succeed on this basis, but for the sake of completeness we go on to examine the remaining aspects of Mr. Hughes' working activities, thus enabling us at the conclusion to stand back and take an overview of the entire relationship.

Personal service / substitution

49. It was Mr. Shorte's submission that if there was no requirement for personal service there could not be a contract of service. He further submitted that in this case there was such a requirement. Ms Smith on the other hand submitted the evidence of the relationship between JCB and Mr. Hughes did not so demonstrate. In her view, JCB would have been satisfied with any qualified and skilled resource which DDC could provide to them.

50. As we have already indicated in paragraphs 15 to 17, the evidence on this point is not totally clear. Had the issue arisen in practice, it would have been a relatively straightforward matter of establishing what had taken place, but we do not have that advantage. The best and most objective evidence we have are the contracts and Mr. Walton's statements and these come together in paragraph 23 of Mr. Walton's statement, which we have summarised in paragraph 16 of this decision.

51. On balance it would seem to us that Mr. Hughes' personal services were not required. JCB wanted a job doing and they wanted it done by a skilled and properly qualified and competent designer. If it was not Mr. Hughes, no doubt DDC could have provided another. However, so ambiguous is the evidence and so untested the proposition that we do not feel this is a factor to which we can attribute much if any weight.

Financial risk

52. Mr. Shorte is correct in his assertion that Mr. Hughes has had no capital at risk, but he is not correct when he said that there was no possibility of Mr. Hughes making a loss on the contract. On the contrary, as was demonstrated in the contract with Compact Products, Mr. Hughes did carry a financial risk – the risk of termination

without compensation. Equally, Mr. Hughes, as we have seen, was sent home unpaid when the computers crashed. In both these instances, Mr. Hughes lost income and it was a risk which he bore and accepted as a contractor but would not have been borne by an employee. The risk, we accept, was not great in financial terms, but it did go beyond the risk of mere late payment of invoices which Mr. Shorte submitted was the only risk which Mr. Hughes carried.

53. There was also the contractual obligation on Mr. Hughes to put right at his own expense any defective workmanship. This was not a risk borne by employees.

54. Mr. Shorte submitted that the opposite side of financial risk was the opportunity to profit – the reason why a businessman will risk his capital. It was Mr. Shorte's contention that Mr. Hughes had no scope for increasing his profits and, as with employees, he was effectively on a fixed rate of pay. There is some strength in this argument. Certainly as Ms. Smith argued, it was open for Mr. Hughes to negotiate with DDC a higher hourly rate, but similarly presumably a senior employee of JCB could try and negotiate a better rate of remuneration for himself.

55. Looking overall at financial risk, there is evidence that Mr. Hughes carried some financial risk, albeit not great and this would if anything point towards a contract of services rather than employment.

The provision of equipment

56. Again this is a factor which could be consistent with either a contract of services or employment. JCB provided Mr. Hughes with his computer and software, but he provided his own calculator, steel rule and micrometer. Additionally Mr. Hughes had no access to the stationery cupboard, which was the preserve of the employees. We see this factor as effectively neutral, not giving any strong indicator either way.

Part and parcel

57. This is another of those aspects of the relationship where there is evidence which could support the existence of either a contract of service or a contract of services. As Mr. Shorte pointed out, Mr. Hughes was clearly integrated to a degree into the organisation. He was provided with a desk, not having to hot-desk, and worked alongside employees with whom, he accepted, he was working as part of a team. On the other hand he received none of the employee benefits to which we have referred in paragraph 27. True, he had an email address which on the face of it indicated that he was a part of JCB, but he signed off his emails describing himself as a "contractor".

58. There is clearly evidence that could be consistent with either a contract of employment or a contract of services. We treat this factor as neutral, not giving any strong indicator in either direction.

Intention of the parties

59. It was accepted by both advocates that the intention of both parties would have been to avoid employment and create self-employment. Equally it was accepted that there would not be an issue of actual intention because the contract is a fiction. The position is that in a borderline case intention can be critical, but we do not believe this to be such a case.

Summary

60. We have already summarised in paragraph 48 our views on the two principal issues of mutual obligation and control. In considering the remaining features we have also set out our views on each and what to us they revealed of the relationship between Mr. Hughes and JCB. In taking our overview, we make two preliminary points. First it is clear that Mr. Hughes was a member of a team and the team consisted of both employees and contractors. We do not believe this to be of any significance because not every member of a team has to have the same employment status. A team will be made up of a number of individuals who may bring identical skills or may bring different skills. They may all perform a similar role or their roles may be varied, and it does not follow that merely because they are part of a team their employment status has to be identical. It is not therefore indicative that Mr. Hughes had to be an employee merely because he was working in a team with employees. Secondly, Mr. Hughes, by his own admission, was brought in as a resource, in effect to make up numbers. He did not bring in a specific skill that the senior designers did not themselves have. They all possessed similar skills to Mr. Hughes but there were not enough of them, and therefore Mr. Hughes was brought in. We do not see that this is a relevant distinction to make. It does not matter whether Mr. Hughes is bringing in a skill which no employee already possesses or whether he is being brought in because JCB just did not have enough employees possessing the skill. What matter is the terms upon which he was taken on, and that is where we come back to the analysis of the working relationship.

61. In taking an overview of the relationship, feature by feature, a number of aspects are in effect neutral in that they don't give a particular indicator either way but could be consistent with either a contract of service or a contract of services. We would include within this category, for example, the monitoring of what Mr. Hughes was to be doing, where he was to be doing it, the provision of equipment and the fact that he worked as an integral part of a mixed team of employees and contractors. There were other aspects which gave a small but reasonably insignificant steer towards it being a contract of services, and we would include within this category the degree of financial risk. We did not find one single aspect which was consistent only with a contract of employment. On the contrary however we did find certain aspects which in our view were compelling indicators that our hypothetical contract would have been one of services. We would include here the fact that both JCB and Mr. Hughes treated the contracts as being capable of being terminated mid-way through with little notice and no payment in lieu; the flexibility which Mr. Hughes was allowed in his working hours and perhaps most importantly of all the fact that JCB, when the computers were down, merely sent Mr. Hughes home unpaid. This latter feature is one which we believe is only consistent with a contract of services, as witness the fact that none of the employees were similarly sent home.

62. For the reasons given above, the appeal is allowed in full.

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.

LADY MITTING
JUDGE

Release Date: 24 June 2011

TC01306

Appeal number TC/2009/15647

NATIONAL INSURANCE CONTRIBUTIONS – INCOME TAX (PAYE) – worker supplied through intermediaries – "IR 35" – whether worker would be employee if there were a contract between the worker and the client – no –Regulation 6, Social Security Contributions (Intermediaries) Regulations 2000 – s 48 Income Tax (Earnings and Pensions) Act 2003 – appeal allowed

FIRST-TIER TRIBUNAL

TAX

PRIMARY PATH LTD **Appellant**

- and -

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

TRIBUNAL: EDWARD SADLER (TRIBUNAL JUDGE)
NIGEL COLLARD

Sitting in public at 45 Bedford Square, London WC1 on 12 April 2011

Matthew Boddington, of Accountax Consulting, for the Appellant

David Lewis, of Her Majesty's Revenue and Customs, for the Respondents

DECISION

Introduction

1. This is an appeal by Primary Path Ltd ("the Appellant") in relation to what is commonly referred to as the IR 35 legislation. That legislation has effect so that a company which makes available to its client the services of an individual (usually the controlling shareholder of the company) can be liable both to pay National Insurance contributions and to a charge under the Pay As You Earn regulations in relation to earnings attributed to the individual in question if the circumstances of the arrangements are such that the individual would have been an employee of the client (rather than a self-employed independent contractor) had the client engaged the services of the individual directly.

2. As detailed below, the Appellant provided the services of Mr Philip Winfield ("Mr Winfield") to the Appellant's client, GlaxoSmithKline plc ("GSK") (through the services of agency companies) on two occasions during the period 4 June 2001 to 14 March 2003. The Commissioners for Her Majesty's Revenue and Customs ("the Commissioners") took the view that the circumstances of those arrangements were such that, had they taken the form of a contract between Mr Winfield and GSK, Mr Winfield would have been regarded as an employee of GSK. Accordingly, the Commissioners:

(1) Issued a Notice of Decision dated 5 October 2007 addressed to the Appellant pursuant to section 8 of the Social Security Contributions (Transfer of Functions, etc.) Act 1999 and Regulation 6(4) of the Social Security Contributions (Intermediaries) Regulations 2000 for the period 6 April 2001 to 5 August 2002 treating the Appellant as liable to pay primary and secondary Class 1 National Insurance contributions in respect of Mr Winfield's attributable earnings from the arrangements (rendering the Appellant liable to a net contribution, after credit for contributions paid, of £9,676.89); and

(2) Issued two Notices of Determination, each dated 5 October 2007, under Regulation 80 of the Income Tax (Pay As You Earn) Regulations 2003 for the tax years 2001/2002 and 2002/2003 requiring the Appellant to pay in total £15,420.84 in relation to the attributable earnings of Mr Winfield from the arrangements with GSK.

3. The Appellant appealed against both the Notice of Decision and the two Notices of Determination on 24 October 2007.

4. At the hearing before us the Appellant agreed that if its appeal were decided in favour of the Commissioners, then the Commissioners were entitled to require further National Insurance contributions, for the period up to 14 March 2003, which is the date on which the arrangements between the Appellant and GSK were terminated. Accordingly, we were asked to give our decision in principle as to liability, leaving it to the parties to agree the final amounts due should we dismiss the Appellant's appeal.

5. The issue we have to decide is whether, had Mr Winfield been engaged directly by GSK (rather than providing his services under the arrangements actually entered into), he would have been regarded as an employee of GSK or as an independent contractor providing his services. In our judgment, and for the reasons given below, had there been such an engagement, the nature of that engagement would have been that of an independent and self-employed contractor providing services to a contractor, and not that of an employee providing services to an employer under an employment contract. Therefore the special provisions (that is, the IR 35 legislation) relating to workers supplied through intermediaries are not applicable in this case. We therefore allow the Appellant's appeal against the Notice of Decision and the two Notices of Determination referred to above.

The relevant legislation

6. The relevant provisions, as they relate to National Insurance contributions, are found in Regulation 6 of the Social Security Contributions (Intermediaries) Regulations 2000 (SI 2000 No. 727), and are as follows:

> *(1) These Regulations apply where –*
>
> *(a) an individual ("the worker") personally performs, or is under an obligation personally to perform, services for another person ("the client"),*
>
> *(b) the performance of those services by the worker is carried out, not under a contract directly between the client and the worker, but under arrangements involving an intermediary, and*
>
> *(c) the circumstances are such that, had the arrangements taken the form of a contract between the worker and the client, the worker would be regarded for the purposes of Parts I to V of the Contributions and Benefits Act as employed in employed earner's employment by the client.*
>
> *(2) Paragraph (1)(b) has effect irrespective of whether or not –*
>
> *(a) there exists a contract between the client and the worker, or*
>
> *(b) the worker is the holder of an office with the client.*
>
> *(3) Where these Regulations apply –*
>
> *(a) the worker is treated, for the purposes of Parts I to V of the Contributions and Benefits Act, and in relation to the amount deriving from relevant payments and relevant benefits that is calculated in accordance with regulation 7 ("the worker's attributable earnings"), as employed in employed earner's employment by the intermediary, and*
>
> *(b) the intermediary, whether or not he fulfils the conditions prescribed under section 1(6)(a) of the Contributions and Benefits Act for secondary contributors, is treated for those purposes as the secondary contributor in respect of the worker's attributable earnings,*
>
> *and Parts I to V of that Act have effect accordingly.*

(4) Any issue whether the circumstances are such as are mentioned in paragraph (1)(c) is an issue relating to contributions that is prescribed for the purposes of section 8(1)(m) of the Social Security Contributions (Transfer of Functions, etc) Act 1999 (decision by officer of the Board).

7. Regulation 7 of the Social Security Contributions (Intermediaries) Regulations 2000 sets out the way in which the amount of "the worker's attributable earnings" for any tax year is calculated. The calculation is a complex, nine-step, exercise. In this case the figures are not in dispute, and so we need not consider these provisions further.

8. In relation to the collection of income tax under the PAYE regulations, the charge to income tax is now found in Part 2 of Chapter 8 of the Income Tax (Earnings and Pensions) Act 2003 ("ITEPA 2003") (for the periods covered by this appeal the legislation was to be found in Schedule 12 to the Finance Act 2000, but nothing turns on that, so the parties were content to refer to the current form of the legislation). Section 49 ITEPA 2003 sets out the situation in which the income tax charge arises, and, so far as relevant to this case, is as follows:

(1) This Chapter applies where –

(a) an individual ("the worker") personally performs, or is under an obligation personally to perform, services for another person ("the client"),

(b) the services are provided not under a contract directly between the client and the worker but under arrangements involving a third party ("the intermediary"), and

(c) the circumstances are such that, if the services were provided under a contract directly between the client and the worker, the worker would be regarded for income tax purposes as an employee of the client.

(2) ...

(3) ...

(4) The circumstances referred to in subsection (1)(c) include the terms on which the services are provided, having regard to the terms of the contracts forming part of the arrangements under which the services are provided.

(5) ... .

9. Section 50 ITEPA 2003 treats the worker whose services are provided in this way as receiving earnings from an employment in respect of any payment or benefit he receives from the intermediary (other than a payment or benefit that is otherwise employment income), and the amount of such earnings is calculated under the provisions of sections 54 and 55 ITEPA 2003, in a complex eight-step process. Section 56 ITEPA 2003 applies the general taxing provisions (and in particular the PAYE provisions) in relation to the amounts treated as earnings from an employment, so that the intermediary is treated as the employer of the worker, and hence is brought within the PAYE provisions in respect of the deemed earnings of the worker. Regulation 80 of the Income Tax (Pay As You Earn) Regulations 2003 entitles the

Commissioners to determine, to the best of their judgment, the amount of any income tax which an employer has failed to pay to the Commissioners under those Regulations.

10. There is no dispute between the parties as to the construction of these various provisions. Nor is there any dispute as to the arrangements under which Mr Winfield ("the worker") performed services for GSK ("the client") under a contract with the Appellant ("the intermediary") – the point of difference between them is whether Mr Winfield would have been an employee of GSK had he been engaged directly by GSK. In arguing their respective cases the parties therefore referred to the extensive case law (in tax, employment law, and other jurisprudence) on the distinction between an employment contract and a contract for the services of an independent contractor.

11. One final point to note in relation to the legislation is the difference in the wording between the two hypothetical contracts predicated by, respectively, the NIC legislation and the income tax legislation. In the case of the NIC legislation the hypothetical contract is formulated by reference only to the arrangements entered into between worker, intermediary and client: in the case of the income tax legislation the hypothetical contract is not so strictly constrained – it is the contract which the client and worker would have entered into had they contracted directly for the services provided, having regard to the circumstances including the terms of the contracts comprising the arrangements under which the worker's services were made available to the client (see the case of *Dragonfly Consultancy Ltd v HMRC Commissioners* SpC 655 at paras. 32 to 34 and that case on appeal to the High Court, *Dragonfly Consultancy Ltd v HMRC Commissioners* STC 3030 at paras. 14 to 19). As is noted in the decision of Henderson J in the decision in that case in the High Court, in the great majority of cases an analysis of the two different hypothetical contracts to determine whether or not they are contracts of employment will lead to the same conclusion. In *Usetech Ltd v Young (HM Inspector of Taxes)* 2004 TC 811 Park J noted that the respective wordings of the provisions relating to National Insurance contributions and to income tax are not identical, but that both provisions have an identical meaning in that the hypothetical contract must be constructed from a consideration of all the circumstances – not simply by reference only to the terms of the actual contracts entered into by the various parties.

The evidence

12. We had in evidence before us three bundles of documents comprising correspondence between the Commissioners and the Appellant and its representatives; notes of meetings between the Commissioners and GSK and correspondence between those parties; contracts between agency companies and the Appellant for the provision of the services of Mr Winfield to GSK; contracts between GSK and the agency companies for the supply by the agency companies of the services of a consultant; time sheets completed by the Appellant in respect of the services of Mr Winfield supplied to GSK; and invoices rendered by the agency companies to GSK in respect of the services of Mr Winfield.

13. Mr Winfield gave evidence at the hearing for the Appellant. Mr Winfield had prepared a witness statement, and he was cross-examined by Mr Lewis, who represented the Commissioners at the hearing. For the Commissioners Mr Matthew Lamming gave evidence at the hearing. Mr Lamming has worked for GSK as an IT/business consultant for twenty years and for the period from April 2001 to August 2002 he was the project manager responsible for a team of ten workers engaged on a particular project for GSK. That team was a mix of employees of GSK and independent contractors engaged through agencies. Mr Winfield was engaged as a member of that team. Mr Lamming had prepared a witness statement, and he was cross-examined by Mr Boddington, who represented the Appellant at the hearing.

The findings of fact

14. There was no dispute between the parties as to the primary facts in this case. Our findings of the facts are set out in the following paragraphs 14 to 37.

15. The Appellant was incorporated in May 2000 and began trading in October 2000. The Appellant's business is the provision of services in the field of database software development, and in particular the development of software for the Oracle database. The Appellant's business address is Mr Winfield's home address, and the Appellant has an office with the usual office and business facilities and equipment at that address.

16. The Appellant's sole shareholder and director is Mr Philip Winfield. Mr Winfield is not an employee of the Appellant and has no contract with the Appellant for the supply of his services. For the periods relevant to this appeal the Appellant's business services were provided solely through the services of Mr Winfield. Mr Winfield's expertise is in the design and development of database software, and in particular interface software, that is, software which enables two or more different database systems to work together. He has a particular specialisation in database software in relation to medical, pharmaceutical and healthcare sectors.

17. In the period from 16 October 2000 to 1 June 2001 the Appellant entered into a sequence of contracts with different contract agencies for the supply of services to British Telecom. Thereafter the Appellant entered into the following contracts for the period from 4 June 2001 to 31 August 2004:

Contract with	End Client	Start Date	End Date
Abraxas	GSK	4 June 2001	21 December 2001
Abraxas	GSK	21 December 2001	29 March 2002
Abraxas	GSK	30 March 2002	26 April 2002
Galt Associates		1 May 2001	1 May 2003
Spring	GSK	26 November 2002	28 February 2003

Spring	GSK	3 March 2003	14 March 2003
Galt Associates		17 March 2003	29 August 2003
Galt Associates		1 August 2003	29 February 2004
Harvey Group		20 September 2003	
Galt Associates		1 March 2004	31 August 2004

18. The Appellant marketed its services through its website, through its membership of a professional body and by searching and responding to websites specialising in finding contract workers in the relevant specialist fields.

19. The first sequence of contracts to provide services to GSK (for the period from 4 June 2001 to 26 April 2002) was entered into through the agency of Abraxas plc. GSK approached Abraxas plc with details of the specification for the particular project it intended to carry out and its specifications for the contractors it required for the team for the project. GSK required the services of independent contractors to add particular skills to its existing employee team and to give flexibility in staffing the project – independent contractors were hired usually for the short-term and for a particular project, that is, for situations where GSK did not require the continuing services of an employee. Abraxas plc put forward candidates it thought met the specification, who would then be interviewed by GSK. Following interview GSK selected the candidates acceptable to it and the appropriate contracts were then entered into.

20. The contract between GSK and Abraxas plc is dated 1 February 2001 and is entitled "IT Agency Staff Agreement". It recites that GSK requires from time to time expert help in the performance and completion of various IT projects and that Abraxas plc has agreed to supply contract IT staff with the required knowledge and expertise. The principal provisions of the contract relevant to this appeal include the following:

(1) GSK engages Abraxas plc to provide Consultants to carry out the specified project. For these purposes "Consultants" are independent computer or other consultants who may be either employees or sub-contractors of Abraxas plc appointed for the purposes of the agreement. Abraxas plc agrees to provide a list of potential Consultants who meet the specification drawn up by GSK, and GSK then selects the Consultants it requires for the project. The selected individual Consultants are then identified in a schedule to be appended to the contract. GSK can reject a Consultant at any time, in which case Abraxas plc must provide a replacement;

(2) The contract has effect from 13 December 2000 and continues until terminated by either party on three months' notice;

(3) GSK agrees to provide each Consultant with instructions, facilities, equipment and access to enable the Consultant to perform his obligations as per the agreed specification;

(4) GSK agrees to monitor the Consultant's performance, agree weekly timesheets provided by the Consultant as to the work he has performed, and to pay invoices submitted by Abraxas plc based on submitted timesheets and applying the hourly rate identified in the agreed specification;

(5) GSK agrees to allow the Consultant to take holiday or time off to attend training courses provided that the Consultant gives GSK ten days' notice, and that such holiday or time off does not affect the project or delay it. If it is appropriate, Abraxas plc can offer a substitute to continue with the project during the Consultant's absence;

(6) More generally, Abraxas plc may at any time offer a substitute for the Consultant, provided that such substitute meets the agreed specification and is accepted by GSK;

(7) Abraxas plc is required to ensure that each Consultant has in place adequate professional indemnity insurance to a specified minimum level of cover;

(8) GSK may require Abraxas plc to terminate the engagement of any particular Consultant;

(9) Abraxas plc is required to conclude an agreement with each individual Consultant to reflect the terms of the GSK/Abraxas plc agreement. Such agreement must include a substitution clause in a form agreed by GSK;

(10) GSK accepts that each Consultant is in business on his own account and therefore may be engaged by other parties during the currency of the agreement and may work simultaneously for other clients, but Abraxas plc is required to ensure that nothing will prevent the Consultant from working to carry out the project to the agreed specification and timetable.

21. The contract between Abraxas plc and the Appellant whereby the services of Mr Winfield were made available to GSK is undated. It covers three periods: 4 June 2001 to 21 December 2001; 22 December 2001 to 29 March 2002; and 30 March 2002 to 26 April 2002. It specifies Mr Winfield as the "Nominated Individual" and GSK as the "Client". The principal provisions of the contract relevant to this appeal include the following:

(1) The relationship between the parties is one of independent suppliers, and no partnership or employer/employee relationship is created;

(2) The Appellant agrees that the Nominated Individual will be provided to undertake the services specified in the Works Schedule (which mirrors the project specification drawn up by GSK). The Appellant "may change or replace [the Nominated Individual] provided that Abraxas plc and GSK are satisfied that the proposed replacement possesses the necessary skills and expertise to carry out" the project;

(3) The Appellant is required to invoice Abraxas plc for fees calculated using the hourly rates specified in the Works Schedule, and when submitting its invoice the Appellant is also required to provide a progress report on the project;

(4) The Works Schedule includes a "work pattern", being a standard commitment of 37.5 hours per week or such other times as may be agreed with GSK;

(5) The Appellant is entitled to undertake other assignments during the period of the contract provided that there is no conflict of interest in relation to GSK;

(6) The Appellant is required to ensure that by its actions it is an "Independent External Expert", and not an employee of GSK or Abraxas plc. The Appellant acknowledges that it has no authority to commit or bind Abraxas plc or GSK;

(7) The contract between Abraxas plc and the Appellant may be terminated by Abraxas plc on four weeks' notice, or without notice in certain specified "default" circumstances.

22. The project undertaken by GSK for which it secured the services of the Appellant through the agency of Abraxas plc was the design and build of interface software to permit the web-based synchronising and joint operation of various medical dictionary and database systems created and used by GSK and also to synchronise GSK's dictionaries with certain external industry-wide specialist dictionary and database systems. The project required close liaison between GSK and a US company, Galt Associates. GSK had no employees with specialist knowledge in this field.

23. Before the Appellant was engaged for the project Mr Winfield had discussions with GSK personnel to discuss the nature of the services required by GSK and the scope and extent of the project, Mr Winfield's skills, his experience in the relevant fields, and his availability for the project and the required visits to the US.

24. Mr Winfield brought a unique skill set to the project team. GSK required those skills specifically and only for the project in question. When the Appellant was engaged it was given a broad remit by GSK in terms of completing that part of the project for which it was responsible. It was required to work within a timeframe which was part of the overall timetable for completion of the project. It was for the Appellant to determine how to carry out and manage its part of the project, and Mr Winfield discussed matters with the project manager and reported to the wider project team at progress meetings to ensure delivery in accordance with, and consistent with, the project as a whole. The initial – and critical – part of the Appellant's work comprised the preparation by Mr Winfield of a design document setting out its plan for the design and build of the specialist interface software. That design document was prepared with little input from GSK. It required the approval of a business analyst engaged (as an independent contractor) by GSK for the purposes of the project. Throughout the project there was little involvement with GSK employees in respect of the technical aspects of the work undertaken by the Appellant, but the work was in support of the project undertaken by the team as a whole and was checked against the standards, quality requirements and conduct of the project stipulated by GSK.

25. Mr Winfield could determine his own working hours. There was an expectation (but not a contractual requirement) that he would be available during the "core hours" of the working day. Normally he worked at GSK's premises. If he chose to work at

home he could do so provided the requirements of the project did not require his presence at GSK's premises. He required a GSK laptop computer in order to connect to GSK's network, but could copy information onto the Appellant's own laptop computer in order to work on the project at his home.

26. Mr Winfield was required to make a business trip to the US for the purposes of the project. The trip was made in the company of the GSK project manager and two others from the project team. The travel, accommodation and other arrangements for the trip were made on his behalf by GSK through its central facility and were at GSK's cost.

27. Mr Winfield's holidays were notified in advance to GSK. In fixing holiday dates Mr Winfield was mindful of the requirements of the project and of the Appellant's responsibilities towards the project, and also of the need to retain the goodwill of GSK for the sake of possible future contracts. There was never an issue between GSK and the Appellant as to Mr Winfield's holiday dates.

28. The situation did not arise where either the Appellant or GSK had to consider a temporary replacement or substitute for Mr Winfield. Since Mr Winfield had specialist skills required by GSK for the project such a substitution would have been feasible (and acceptable to GSK) only if the substitute had had comparable skills. On another (later) contract undertaken by the Appellant for a different client it had proved possible to find a substitute for Mr Winfield, and on a different occasion the Appellant had provided Mr Winfield as a substitute for another contractor.

29. GSK paid for the Appellant's services on the agreed contractual terms, that is, by reference solely to the number of hours worked by Mr Winfield and the stipulated hourly rate of payment. The average number of hours worked per week was stipulated in the contract, and any additional hours of work done which would have resulted in an increase in the weekly average would have required the approval of GSK, since the project had been budgeted by reference to the stipulated hours of work.

30. GSK made monthly payments to Abraxas plc, the party with whom it contracted, and in turn Abraxas plc made monthly payments to the Appellant, against delivery of invoices (supported by timesheets of Mr Winfield's hours worked) and progress reports. The payments made by Abraxas plc were between one week and six weeks after invoices were submitted by the Appellant.

31. GSK did not make any payment in respect of holiday or sickness or other absence on the part of Mr Winfield. There was no additional payment for overtime or unsocial hours worked. Nor did GSK make any payment or other provision in respect of bonus, pension, health insurance, training or other employee benefits which it made for its employees. Mr Winfield was entitled to use the GSK canteen and staff car parking facilities. Mr Winfield was not appraised in the course of the employee appraisal programme conducted by GSK.

32. The second sequence of contracts to provide services to GSK (for the period from 26 November 2002 to 14 March 2003) was entered into through the agency of Spring IT Personnel plc ("Spring"). There is a contract referred to as the UK Master Services Agreement between GSK (in this case a group company called GlaxoSmithKline Services Unlimited) and Spring whereby Spring agrees to provide Contingent Workers to GSK. There is also a contract between Spring and the Appellant whereby the Appellant agrees to provide services to GSK (as a client of Spring) for a specific assignment, summary terms of which are set out in a scheduled Assignment Summary, which stipulates the start and end dates, the rate per hour and the number of hours per week to be worked on average, and the termination notice period.

33. The general tenor of these contractual arrangements corresponds to that of the GSK/Abraxas plc/Appellant contractual arrangements, so that it is not necessary to set out those arrangements in detail. It is worth mentioning specifically that the contract between GSK and Spring contains a provision as to the relationship of the parties which specifies that Contingent Workers are not employees or sub-contractors of GSK and that GSK has no right to control the manner, means, or method by which Spring provides services under the contract, save that GSK is entitled to direct where and when the services are to be performed. There is a corresponding provision in the Spring/Appellant contract, reserving to the Appellant the right to determine the manner, means and methods required to ensure its services are performed to GSK's satisfaction, and reserving to GSK the right to direct the Appellant as to where and when such services are to be performed.

34. The work undertaken by the Appellant for GSK under this second sequence of contracts was less specialised (and payment was at a lower hourly rate). It related to the development of interface software for synchronisation with the Oracle database system, and was the initial stage of a larger programme being undertaken within GSK for implementing new systems. This work was for a different team within GSK. Mr Winfield worked with one other contractor for the contract period on discrete tasks within the larger project, and there was limited interaction with the project co-ordinator and the rest of the GSK team as to the technical aspects of the work.

35. In the course of working on the first GSK project Mr Winfield developed a relationship with Galt Associates and the Appellant began to work for them in the design of an integration and interface system for medical dictionaries and a Galt Associates proprietary application. Some of the initial work was carried out for them on a speculative basis contemporaneously with the work for GSK on the first project and fee-paid work continued between the two GSK assignments. During the second GSK project the Appellant submitted timesheets to Galt Associates showing at least 21.5 hours of work undertaken for Galt Associates (other records of the Appellant indicated 58 hours of work undertaken for Galt Associates during this period). After the completion of the second GSK project further assignments came from Galt Associates as its customers required interface systems and the Appellant then worked extensively for Galt Associates. Mr Winfield worked from his office at his home address when working on the assignments for Galt Associates. In the course of working for them he made a substantial number of business trips to the US, making his own travel arrangements and recovering the cost from Galt Associates.

36. Also at this time the Appellant worked (in co-operation with another specialist IT contractor) on the speculative development of a management system aimed at GP surgeries – this work began in the period between the two GSK projects and continued whilst the Appellant was engaged on the second GSK project. The Appellant also carried out some work for a German company at this time.

37. Throughout this period (from before the GSK contracts and beyond) the Appellant maintained employer's liability and professional indemnity insurance cover.

The parties' submissions

The Appellant's submissions

38. For the Appellant Mr Boddington submitted that the legislation requires a hypothetical contract to be inferred from the circumstances in which the arrangements have been made (in the present case) by the Appellant for Mr Winfield to work for GSK. To determine the nature of that hypothetical contract it is necessary to look first at the actual contracts entered into (in this case the contracts between the Appellant and the agencies Abraxas plc or Spring and then the contracts between those agencies and GSK); then at what actually happened on a day to day basis in terms of the way in which Mr Winfield performed his services for GSK, looking at the evidence of both Mr Winfield and GSK; and thirdly at the broader business circumstances and general *modus operandi* of the Appellant. Once the nature of that hypothetical contract is established from those different sets of facts it can be ascertained whether, by reference to the extensive case law on the subject, it is a contract for the services of an independent contractor or a contract of employment.

39. In the present case the actual contracts between the Appellant and the agencies and the agencies and GSK as client were consistent with the services of Mr Winfield being provided to GSK as those of an independent contractor: they were for a specific task and for a specific period; they were for the provision of a specific person, but with a right to substitute another with equivalent skills; they allowed, within limits, the worker to undertake work for other clients during the contract period; they took great care to provide that the worker should not be regarded as an employee of the client.

40. As for the day to day reality of the arrangements, Mr Winfield had a great deal of autonomy as to the way he carried out his work provided it fitted in to the overall workings of the project; he was clearly regarded by the client as someone engaged for the short-term and for a specific project and in that regard different from an employee of the client; he was paid on an hourly basis for work done; he enjoyed no employee benefits beyond the use of certain on-site facilities. Again, that is all indicative of a relationship between one contractor and another.

41. The broader business circumstances and context of the Appellant are also consistent with a relationship which is that of an independent contractor: the Appellant is a small specialist consultancy which seeks work in a variety of ways and

markets, sometimes working speculatively and seeking ways to manage overlapping commitments, invoicing for work done and taking the financial risk of delay or default on the part of the contractor.

42. As to the case law, Mr Boddington referred to the "irreducible minimum" needed to create an employment contract as established in the authorities beginning with the case of *Ready Mixed Concrete (South East) Ltd v Minister of Pensions and National Insurance* 91968) 2 QB 497: the relationship between the parties must be that of mutual and personal obligation, that is, the provision of work by the employer and the doing of that work by the personal service rendered by the employee; there must be control of the worker by the employer to the extent consistent with a master and servant relationship; and all contractual provisions must be consistent with an employment contract.

43. As to the personal obligation, a right to send a substitute, which was available contractually to the Appellant, is inconsistent with the requirement for service to be a personal obligation: *Express Echo Publications v Tanton* [1999] IRLR 367; *Wright v Redrow Homes (Yorkshire) Ltd* [2004] 3 All ER 98; *Lime-IT v Commissioners of Inland Revenue* (2002 SpC). As to the mutuality of the obligation, for there to be a contract of employment there must be a continuing relationship under which the employer provides work to the employee (and continues to pay the employee if for any reason the work is not so provided) and the employee stands ready to carry out that work: *Propertycare Ltd v Gower* [2003] UKEAT 0547/03. In the present case this was not so: the Appellant was engaged to perform a specific project by a series of contracts which were renewed as the project progressed – there was no sense of the Appellant or Mr Winfield standing ready to carry out whatever tasks GSK required of them.

44. In relation to control, for a relationship to be that of employment, there must be a level of control which is more extensive than mere supervision or direction. Mr Winfield exercised considerable autonomy in how he worked, provided he fitted in with the development of the project as it proceeded. He had skills not otherwise available to GSK, and so no "employer" control could realistically be exercised over him – it was a "business to business" relationship.

45. As to the nature of the contractual provisions, that poses some difficulties where the contract under scrutiny is hypothetical. But in the Appellant's case it is clear that GSK sought to differentiate between its employees and those it wished to engage as independent contractors for the project, and the contractual documentation reflected that: GSK would not have entered into a contract of employment with Mr Winfield.

46. Looking beyond the "irreducible minimum" test of the *Ready Mixed Concrete* case, Mr Boddington referred to the test of whether the worker can be considered to be "in business on his own account": *Market Investigations Ltd v Minister of Social Scurity* [1968] 3 All ER 732, which looks at the degree of control exercised over the worker, the extent to which the worker is at financial risk, and the extent to which the worker benefits from investment in and management of his business. The Appellant was at financial risk in that it invoiced for the work done (and only for hours actually

worked) and was at risk of delay or default in payment on the part of either GSK or the intermediate agency. The Appellant managed its business by seeking out work opportunities as a specialist consultancy and running its affairs in a business manner – raising invoices, complying with its VAT obligations, managing "overlapping" contracts, undertaking speculative work, maintaining office premises at the home of Mr Winfield, maintaining appropriate insurance cover, ensuring Mr Winfield kept his skills up to date and his membership of the relevant professional bodies maintained, and keeping financial records.

47. Applying these various tests to the circumstances of the Appellant it is clear, in Mr Boddington's submission, that the hypothetical contract between Mr Winfield and GSK would be that of a self-employed freelance independent contractor, and not that of employer and employee.

The Commissioners' submissions

48. For the Commissioners, Mr Lewis largely accepted Mr Boddington's analysis of the way in which the hypothetical contract should be identified from the "circumstances" and "arrangements" comprising the actual relationships of the parties and the reality of the working relationship and conditions. He also agreed that the nature of the hypothetical contract must be analysed by reference to the tests which can be derived from the *Ready Mixed Concrete* and *Market Investigations* cases. Additionally, he referred to the case of *Hall v Lorimer* (1993) 66 TC 349, which makes it clear that the exercise is not a mechanical one of running through the items in a checklist, but of "painting a picture from the accumulation of detail", viewing the entirety of the arrangements in an informed and qualitative evaluation of the overall effect of the detail.

49. Where Mr Lewis differed from Mr Boddington was in his analysis of the evidence.

50. On the question of the extent and degree of control, the issue is whether there is a right to control, not whether in fact that control is exercised. That right of control must also be viewed in the context of the nature of the work and the worker – a skilled professional employee will not be subject to the same day-to-day control as an unskilled worker. The question is whether the "employer" has the power to decide what is to be done, the way in which it is to be done, the time when it is done and the place where it is done (see the *Ready Mixed Concrete* case and also *Dragonfly Consultancy Ltd v HMRC Commissioners* STC 3030). In the present case GSK had the right of control over what services had to be provided, and where and when those services had to be provided; work was allocated and monitored by GSK. GSK had sufficient rights of control to render the hypothetical contract one of employment.

51. As to the question of whether the Appellant could provide a substitute for Mr Winfield, Mr Lewis referred to the case of *Usetech Ltd v Young* (2004) 76 TC 811 and also to the decision of the Special Commissioner in the *Dragonfly Consultancy* case. The presence of a right to substitute in the hypothetical contract may be a pointer towards self-employment, but is not determinative of the matter. In the

Appellant's case Mr Winfield was specifically identified as the worker in the actual contractual documentation, and was hired for his specific skills. In practice he was engaged for the job and GSK, who had a veto right, would have been likely to resist any attempt by the Appellant or the agency to provide a substitute.

52. Mr Lewis referred to the concept of mutuality of obligation, referring to the cases of *Nethermere (St Neots) Ltd v Gardiner & Another* (1984) ICR 612, *Synaptek v Young* (2003) 75 TC 51, *Cornwall County Council v Prater* [2006] EWCA Civ 102, and *Dragonfly Consultancy*. He accepted that there must be an irreducible minimum of obligation on each side in order to create a contract of employment, but in his submission that went no further than an obligation on the worker to provide his work and skill and an obligation on the employer to pay for the work done. Those requirements were met in the Appellant's case.

53. As to other *indicia* as to the nature of the hypothetical contract, Mr Lewis argued that Mr Winfield was at little financial risk, and had little opportunity to increase his profit. He performed his services using equipment provided by GSK rather than his own equipment. The Appellant was paid on an hourly basis rather than by reference to a fee for the project undertaken. The termination rights in the contract were indicative of an employment arrangement (an independent contractor is usually engaged for a set period or to carry out a particular project: see *Morren v Swinton and Pendlebury Borough Council* (1965) 1 WLR 576). Mr Winfield was part of the team assembled by GSK (a mixture of employees and contracted workers) with similar working arrangements – he was effectively part and parcel of GSK's organisation: see the case of *Bank voor Handel en Scheepvaart NV v Administrator of Hungarian Property* 35 TC 311. Under the contractual arrangements Mr Winfield had a right to work for other contractors, but that was no more than a theoretical right, and in any event he was required to provide a minimum number of hours per week of service to GSK. Overall, there was little, if any, evidence to suggest that Mr Winfield could be regarded as a person in business on his own account: see the cases of *Market Investigations Ltd v Minister of Social Security* (1969) 2 QB 173 and *Lee Ting Sang v Chung Chi-Keung and Shun Shing Construction & Engineering Co Ltd* 2 AC 374.

54. Mr Lewis therefore submitted that the hypothetical contract between Mr Winfield and GSK which the IR 35 legislation required would, in the circumstances of the Appellant's arrangements with GSK, be one of employment, so that the disputed decisions made by the Commissioners rendering the Appellant liable to National Insurance contributions and PAYE liabilities should be upheld.

Decision and reasons for decision

55. In order to decide whether the relevant National Insurance contributions and income tax (PAYE) provisions apply to the Appellant in this case we are required to ascertain first what would be the terms of a hypothetical contract between Mr Winfield (the worker) and GSK (the client), and then to determine from the guidance in the cases whether such a contract would be a contract of employment or a contract for the supply of the services of an independent contractor.

The terms of the hypothetical contract between GSK and Mr Winfield

56. We are concerned with two sets of arrangements covering two periods of engagement: the first (through the agency of Abraxas plc) for the period from 4 June 2001 to 26 April 2002 (in itself a sequence of contracts for three contiguous periods, all those contracts being on the same terms); and the second (through the agency of Spring) for the period from 26 November 2002 to 14 March 2003 (a sequence of contracts for two contiguous periods, and again, all those contracts being on the same terms). As we have noted, the material contractual terms of the arrangements made through the Spring agency were, in their tenor, largely consistent with those made through the Abraxas plc agency, and the parties did not, in arguing their respective cases, significantly differentiate between the two. Where there are differences which we consider material to the terms of the hypothetical contract we have to construct, we identify those differences below.

57. We have noted at paragraph 11 above the discussion in recent cases as to the possible different bases for predicating the terms of the required hypothetical contract as appearing from the different language in the respective National Insurance and income tax provisions. The parties in this appeal made no issue of that point. The approach of Park J in the *Usetech Ltd* case is pragmatic. He said at paragraph 10, when comparing and contrasting the language of the respective provisions as they relate to the basis on which the hypothetical contract is to be predicated:

> "However, no-one has suggested to me, nor do I consider, that that or the other minor differences between the two statutory provisions affects this case or opens a possibility of the case being decided one way for NICs and another way for income tax and corporation tax."

He then went on to consider the terms of the hypothetical contract, in dealing with the question of whether it should include a right of substitution (which was one of the principal factors in that case) by reference to the wider circumstances including the conduct of the parties, and not simply the actual contractual terms (that is, by reference, in effect, to the approach inherent in the income tax provisions). We will follow that approach.

58. In this case, as with some others which have come before the tribunal, the exercise of constructing the hypothetical contract between the client and the worker is made more complicated by the interposition of an independent agency company between the appellant company and the client, so that in looking at the actual contractual terms governing the basis on which Mr Winfield's services were supplied to GSK in each of the contract periods it is necessary to look at the arrangements between GSK and the respective agency companies (Abraxas plc or Spring) and between those agency companies and the Appellant. In the present case the difficulties which this "two tier" situation may present are eased to an extent by the fact that there is a fair degree of consistency, or at least correspondence, of terms as between the "tiered" contracts.

59. Taking these points into account, the hypothetical contract between Mr Winfield and GSK would be on the following terms:

(1) The services of Mr Winfield are engaged for a series of fixed term contracts which may nevertheless be terminated before the expiry of the term by four weeks' notice.

We consider this to be the case because the Appellant has such arrangements in its contract with Abraxas plc, and notwithstanding that GSK can in the case of its agreement with Abraxas plc require the agency company to terminate the engagement of the worker, seemingly without notice. In the GSK/Spring agreement GSK must give thirty days' notice to terminate the engagement (Spring, in its contract with the Appellant, can terminate without notice if GSK exercises its termination right). In a "default" situation (misconduct or lack of performance) there can be summary termination.

(2) The services to be provided by Mr Winfield are specific and detailed.

In the first sequence of contracts (through the agency of Abraxas plc) the services relate to the development and testing of particular software programs and related database management and consultancy functions; in the case of the second sequence of contracts (through the agency of Spring) the nature of the services referred to in the documentation is general, but in fact Mr Winfield was engaged for the development of a specific interface software program.

(3) Mr Winfield is paid on the basis of a specified hourly rate for the number of hours actually worked: there is no payment in the case of absence for holidays, sickness or other causes. Over the contract period the average number of hours worked per week is set at 37.5, with scope to agree additional hours of work. Different hourly rates apply to the two respective sequences of contracts, to reflect the nature of the services provided and the market forces which influence fee or remuneration rates. Payment is made against invoices rendered with progress reports.

(4) Mr Winfield is not entitled to any pension or insurance benefits, benefits in kind, or bonus, share options or other incentive arrangements provided to actual employees of GSK.

(5) Mr Winfield must, in providing his services, co-operate with GSK and take account of its directions. Specifically, GSK has the right to direct Mr Winfield as to where and when and the timescale within which his services are to be performed, but Mr Winfield can at his discretion determine the manner, means and methods in or by which he performs the contracted services. On the days he works Mr Winfield is expected to be available during the "core hours" of the working day and to attend project team meetings, but otherwise he decides his working hours and whether he works in GSK's premises or at his office in his home.

(6) During his period of engagement Mr Winfield is entitled to undertake assignments for other contractors provided that there is no conflict with the interests of GSK and provided that there is no prejudice to the carrying out and completion of the GSK project.

This right is specifically provided in the arrangements for the first sequence of contracts and can be inferred in the case of the second sequence of contracts (during which Mr Winfield did in fact undertake work for other contractors).

(7) The contract is for the engagement of the services of Mr Winfield, but if Mr Winfield is not available for any reason he may propose a substitute for himself who may continue with the project during Mr Winfield's absence, provided that that substitute has comparable skills to those of Mr Winfield. GSK determines whether to accept such a substitute, depending on the appropriateness of the circumstances (including the proposed length of absence/substitution and the likely "learning curve" of any proposed substitute in terms of becoming familiar with the requirements of the project).

The arrangements for substitution in these terms are derived from the GSK/Abraxas plc contract and the Abraxas plc/Appellant contract. The second sequence of contracts (through the Spring agency) provide for a limited right of delegation under the GSK/Spring contract, and a right of replacement under the Spring/Appellant contract provided that GSK is satisfied that the proposed replacement has the necessary qualifications, skills and experience and is suitable to perform the services contracted for.

(8) There is no provision for training or other skills development for Mr Winfield other than a necessary and basic induction process. There is no provision for appraisal nor any grievance or similar employee rights procedures available to Mr Winfield.

(9) There is a requirement that Mr Winfield provides at his own cost public liability and professional indemnity insurance cover in the sum of not less than £1m (£250,000 in the case of the second sequence of contracts).

(10) The contract includes a declaration that Mr Winfield is not an employee of GSK.

The GSK/Spring contract provides that Contingent Workers shall not be employees or subcontractors of GSK, and the Spring/Appellant contract provides that the parties agree that their contract is a contract for services. There is no express provision on this matter in the GSK/Abraxas plc contract, but "Consultants" are stated to be independent consultants and GSK is expressed to have no responsibility for any payment of income tax or national insurance (with a corresponding indemnity from Abraxas plc) in relation to a Consultant. The Abraxas plc/Appellant contract contains an acknowledgement by the Appellant that the services supplied are those of an independent contractor.

The nature of the hypothetical contract: employment contract or contract for services

60. We now have to consider whether, having regard to the terms of this hypothetical contract, Mr Winfield is to be regarded as an employee of GSK or an independent contractor. In carrying out that task we note that in *Market Investigations Ltd v Minister of Social Security* it was stated that: "… the fundamental test to be applied is

this: 'Is the person who has engaged himself to perform these services performing them as a person in business on his own account?'"

61. It is clear from the cases that although there is a range of factors or *indicia* which might usefully be taken into account in ascertaining whether a contract is one of employment or one for the provision of services by an independent contractor, there is no simple formula or process which can be applied to determine, in any particular case, which factors are relevant or the weight or significance which is to be attributed to any factors which are considered to be relevant. In *Hall v Lorimer* Mummery J expressed the nature of the process in these terms (subsequently approved by Nolan LJ when that case reached the Court of Appeal):

> "In order to decide whether a person carries on business on his own account, it is necessary to consider many different aspects of that person's work activity. This is not a mechanical exercise of running through items on a check list 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 another.
>
> The process involves painting a picture in each individual case."

62. The essential factors – the "irreducible minimum" – which must be present if an employment contract is to exist were set out in the *Ready Mixed Concrete* case by MacKenna J in terms which have since been recognised as the helpful starting point for the analysis of the true nature of contracts in this difficult area:

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

63. The first of these conditions has evolved into two distinct factors: first, that there should be what has commonly been called "mutuality of obligation"; and second, that a defining feature of an employment contract is that the employee, and he alone, is the person whose services are to be provided.

64. The question of "mutuality of obligation" has led to discussion as to whether all that is required on the part of the employing party is that it should simply pay the remuneration contracted for, or whether a defining characteristic of an employment contract is that the employer is required to provide a flow of work and to continue to pay the contracted remuneration even if at times there is no work. The Special

Commissioner in the *Dragonfly Consultancy* case provides a helpful review of the cases which deal with the employer's obligation (see paragraphs 50 to 59), and reaches this conclusion: for a contract to exist there must, of course, be mutual obligations, but that obvious requirement is met if the "employee" is obliged to provide his labour and the "employer" is obliged to make payment for it; and that "an obligation on the employer to provide work or in the absence of available work, to pay, is not a precondition for the contract being one of employment, but its presence in some form…is a touchstone or a feature one would expect to find in an employment contract and where absence would call into question the existence of such a relationship."

65. Turning to the hypothetical contract between Mr Winfield and GSK, there is an obligation for GSK to pay Mr Winfield for the work he has done in terms of payment at the agreed rate for each hour of work as invoiced. There is no obligation beyond that. It appear that there was an expectation that there would be, on average, 37.5 hours of work each week – in the Abraxas plx/Appellant contract it is expressed in these terms: "Work Pattern: the standard commitment is 37.5 hours per week or such other times as may be mutually agreed with [GSK]" – and no doubt in a substantial, well-planned, carefully budgeted and well-executed project such as that undertaken by GSK, that expectation had a sound basis. But the essence of the arrangement was that Mr Winfield was paid only for the hours he worked, and should at any time his strand of work within the overall project have suffered a hiatus for any reason, we cannot see that he had any contractual basis for demanding other work or payment whilst he waited for his work to resume. Nor is there anything to suggest that GSK had it in mind to offer work beyond the specific project for which Mr Winfield's services were engaged. This feature of his hypothetical contract we see as calling into question whether it is an employment contract – it is a feature which is more indicative of a contract for services.

66. It is convenient here to deal with a related point, which concerns the nature of the contractual remuneration. Mr Lewis made the point that hourly pay is an indication of employment in that an independent contractor customarily charges a specified fee for the carrying out of a particular task. We do not agree. For a highly-skilled specialist such as Mr Winfield we would expect an employment contract to remunerate him on a specified salary pro rated for each month. In the context of professional skills, remuneration by reference to hours worked at an hourly rate is, in the present world, a feature (although not necessarily the only feature) of the fee charging structure of professional service firms (and, for that matter, plumbers, electricians and other skilled technicians and craftsmen). Therefore, in so far as the nature of the remuneration in Mr Winfield's hypothetical contract points in any direction, it does so away from employment.

67. The second limb of MacKenna J's first condition relates to the personal nature of the "employee's" obligations. He said this by way of expansion of the point: "The servant must be obliged to provide his own work and skill. Freedom to do a job either by one's own hands or by another's is inconsistent with a contract of service though a limited or occasional power of delegation may not be."

68. The question of the ability of the person providing the services to supply someone in his place, and its relevance in determining the nature of the contract is reviewed in the *Usetech Ltd* case and also by the Special Commissioner in the *Dragonfly Consultancy* case. The conclusion reached in those cases is that if there is a general and unqualified right for the person providing the services to send along a substitute in his place, as in the *Express Echo Publications* case, then that is incompatible with the personal service nature of an employment contract, and determines the matter. Something less than that in terms of what the parties have agreed to by way of an ability to provide a substitute is unlikely in itself to be determinative of the question, but will nevertheless be a pointer away from an employment contract.

69. We agree with that: putting it baldly, no employment contract envisages that the employee will send along someone else in his stead to perform the duties he has been engaged to perform. Therefore any contract which has at least some recognition that the provider of the services can supply a substitute in certain circumstances must seriously be considered as being a contract other than for employment.

70. In Mr Winfield's case it is clear that his specific services were engaged by GSK in that his name, qualifications and experience were supplied to GSK by the agency company (initially, Abraxas plc and later Spring), he was interviewed by GSK, and he is named as the consultant to be provided to them. Mr Winfield had specialist skills which were required to make up the skills set put together by GSK in the team it was assembling for a particular project (this was more so for the first sequence of contracts). As matters transpired during the contract periods the question of substitution did not arise – Mr Winfield was able to fulfil the contract terms himself, and his only periods of absence (on holiday) were arranged to the satisfaction of himself and of GSK without any disruption to the project. There was some speculation on the part of both Mr Lamming of GSK and Mr Winfield as to how the question of substitution might have been dealt with had it arisen, but as mere speculation we did not find that to be helpful. Mr Winfield gave instances of other engagements he had undertaken where he had provided a substitute and where he had substituted for another contractor, which is some indication that the practice can be a feature of the business in which he works, and that therefore there is some foundation in practice for including substitution provisions in engagement contracts.

71. What is clear is that in the present case the contracts between the parties (that is, both "tiers" of contracts) contemplate the possibility of substitution. As we mention at paragraph 59(7) above, this is more specifically dealt with in the first sequence of contracts entered into through the Abraxas plc agency. Those provisions do not give the Appellant the right to substitute another consultant for Mr Winfield, but a substitute may be offered, and although GSK has the right to refuse to accept that substitute, there is a framework within which GSK is required to consider whether the circumstances are appropriate for a substitution to be made, of which a key feature is (not unexpectedly) whether the person substituted meets the specification by reference to which the original consultant was appointed. The hypothetical contract must reflect the terms of the actual contracts in this regard.

72. We do not regard a substitution clause in these terms to be determinative of the matter in the sense that it must lead us to conclude that the hypothetical contract between GSK and Mr Winfield cannot be an employment contract. But in the exercise of weighing up all the features and factors we consider that such a clause tilts the balance in that exercise away from employment.

73. MacKenna J's second condition relates to the degree of control which the "employer" has over the "employee". In amplification of this point the judge said this:

> "Control includes the power of deciding the thing to be done, the way in which it shall be done, the means to be employed in doing it, the time when and the place where it shall be done. All these aspects of control must be considered in deciding whether the right exists in a sufficient degree to make one party the master and the other his servant. The right need not be unrestricted."

74. The question of control – or the degree of control which points to a situation of employment – is problematic in the case of a person who is engaged for his specialist skills. The "master" himself may well not have the skills or experience to give specific direction to the "servant", and in the case of *Morren v Swinton and Pendlebury Borough Council* Lord Parker CJ said: "…clearly superintendence and control cannot be the decisive test when one is dealing with a professional man, or a man of some particular skill and experience." In such a case one must look to more general questions of the level of supervision.

75. In the present case there is little in the first sequence of contracts relating to the question of control. There is provision in the Abraxas plc/GSK contract requiring GSK to "provide the Consultant with sufficient instructions and facilities or access to facilities and equipment…to enable the Consultant to adequately perform his/her obligations under the Specification", and there is also provision that "[GSK] shall be responsible for monitoring the Consultant's performance of the Specification and for reporting any shortcomings to [Abraxas plc]." Neither of these provisions is dealing with the nature or extent of the supervision by GSK of the consultant's work.

76. In the second sequence of contracts (those made through the Spring agency) there is explicit provision (see paragraph 33 above) – GSK can direct where and when the worker's services are to be performed, but not the manner, means or method by which they are performed.

77. As to the evidence from Mr Winfield and Mr Lamming as to what actually happened (at least in the case of the first sequence of contracts), it was clear that Mr Winfield had responsibility for delivering his part of the project by applying the skills and experience for which he had been engaged, and that he was required by GSK to exercise that responsibility by carrying out his work in a way which fitted in with the requirements of the project on which the team was working – both as to timing and as to the technical compatibility of the work (see paragraph 24 above).

78. All in all we consider that there was a minimum supervision of Mr Winfield on the part of GSK – he was hired for his expertise to be part of a team for a particular project, and subject only to such supervision and direction as was necessary for and in the course of the management of the project as a whole he was left to do the work as he saw fit. The level of control or supervision exercised did not go beyond that which one would expect in the hiring of an independent contractor. Whilst we take note that the question of control should not be given too much significance in the case of a specialist worker, in so far as it is brought into the balance in this case it points away from a contract of employment.

79. MacKenna J's third condition in determining whether a contract is an employment contract is that the other terms of the contract should be consistent with its being an employment contract. In this context we refer to the following matters which the parties brought to our attention:

(1) Mr Winfield was not entitled to pension or other benefits or to participate in bonus or share incentive plans which GSK offered to its actual employees, nor was he entitled to training, the benefits of appraisal, or the sort of employee protection procedures now customarily incorporated into employment contracts. This demonstrates that GSK did not want to treat Mr Winfield in the way it treated its employees and as such it is an indication of the way in which they regarded the relationship. In itself, the absence of such benefits in the hypothetical contract does not give a particular indication as to the true nature of that contract – an employment contract is not required to include such benefits.

(2) A related point is the term in the hypothetical contract, derived from the actual contracts (see paragraph 59(10) above), that the relationship is not that of employer and employee. The issue is the true nature of the contract as seen from its terms and the way in which those terms were in fact given effect to, not what the parties considered the true nature of the contract to be. Despite the emphasis given to this point by Mr Boddington as an expression of the intention of the parties, we think that we should give only marginal weight to this point.

(3) The hypothetical contract is for a stipulated period but can be terminated, without cause, by a specified period of notice. We agree with Mr Lewis that this is a pointer towards a contract of employment, although in a contract for services, such as a retainer for a particular period, an early termination procedure may well be included in the terms to deal with the situation where for any reason the arrangement needs to be brought to an early conclusion.

(4) The hypothetical contract requires Mr Winfield to provide a specified level of public liability and professional indemnity insurance cover. We consider that this points towards a contract for services rather than an employment contract. As a factor it does not go to the heart of the issue as to the true nature of the contract, and therefore is certainly not determinative of that issue. But in an employment relationship it is generally the employer who is expected to bear the risks of such liability to third parties and to provide at its cost the insurance against such liability (although there are some professionally-qualified employees – for example in the medical field – who will provide their own insurance cover).

(5) The hypothetical contract provides that Mr Winfield may undertake assignments for other parties, subject to certain constraints which protect the interests of GSK and its need for the project to be completed to plan. This was a right which Mr Winfield exercised, especially in relation to the second sequence of contracts, when he undertook work for Galt Associates and also some speculative work for other parties when engaged to work for GSK. We return to this issue below, when considering whether or not Mr Winfield could be said to be carrying on business on his own account. For the present we observe that such a term in the contract is an indicator of the relationship being that of independent contractor, and not that of employer/employee.

80. The parties referred us to two other areas of enquiry based on case law, outside the immediate scope of the "irreducible minimum" conditions of an employment contract laid out in the *Ready Mixed Concrete* case. The first is the question of whether the worker carries the financial risk normally associated with being self-employed. The second (perhaps not entirely unrelated) is whether the worker can be regarded as carrying on business on his own account as one would expect to find if he were self-employed.

81. As to the question of financial risk, the general proposition is that a person who is self-employed carries the risks associated with running a business whereas an employee runs no risk other than that his employer will become insolvent owing him his wages or salary or that the employer will for some business reason make the employee redundant because a particular business operation has ceased or been reduced. Mr Boddington argued that the Appellant was bearing financial risk in a number of ways which would not be the case were Mr Winfield an employee of GSK: there was the risk of default by either GSK or the relevant agency company in paying the Appellant's invoices (and the fact that payment was irregular, at least as compared with a monthly salary payment); there was the risk of changes in the hourly rates (evidenced by the fact that the Appellant was able to negotiate only a reduced rate for the second sequence of contracts); there was the risk of sickness or other absence which resulted in loss of income; and there was the uncertainty as to the net return to the Appellant when it had to take account of its overhead and other costs such as insurance, keeping the skills of Mr Winfield up to date and maintaining membership of professional bodies, equipping and running the small office maintained in Mr Winfield's home, and marketing costs. Mr Lewis argued that the Appellant had invested minimal capital in the business, that in reality there was no way for the Appellant to increase its profits other than by having Mr Winfield work longer hours, that all the equipment required for Mr Winfield's work was provided by GSK, and that the risk of default in payment was very small.

82. We are of the view that the Appellant was exposed to financial risk in a manner and to an extent that Mr Winfield would not have been exposed to had he been an employee. Those risks are essentially the risks which are run by a self-employed worker. It is a definite pointer towards Mr Winfield being regarded as such in the assessment of his status which we are required to make.

83. Even more telling in that regard is the position if we apply the test as to whether the Appellant can be said to be providing services in business on its own account – if so, the case is one of a contract for services. As we have mentioned, this test was first formulated in the *Market Investigations Ltd* case. It looks not just to financial risk and the opportunity to create profit, but also to the wider business conduct of the person concerned and the context in which his activities are planned and carried out. It requires us in the present case to look beyond the immediate arrangements with GSK to the way in which the Appellant sought and obtained and conducted business.

84. The evidence of Mr Winfield is compelling in this regard:

(1) The Appellant actively sought out engagements by promoting itself through its website and by monitoring the websites of those who may have been seeking the expertise it has to offer.

(2) In the course of the first sequence of contracts with GSK the Appellant, through Mr Winfield, worked to secure business contacts with Galt Associates, a party involved in the GSK project, and carried out some work for them on a speculative basis: those contacts and that speculative work yielded a lengthy engagement for the Appellant once the GSK project was over and which continued concurrently with the second GSK project. (The extent of that concurrent work was not clear from the evidence – spreadsheets supplied by the Appellant to the Commissioners in the course of their enquiries indicated some fifty-eight hours of work for Galt Associates whilst the Appellant was engaged by GSK under the second sequence of contracts, but copy invoices related only to 21 hours of such work. In either event it was a material concurrent engagement.) That connection with Galt Associates resulted in further extensive work once the second GSK engagement was completed.

(3) In the period between the two GSK engagements, and whilst engaged by Galt Associates, the Appellant worked on speculative developments of at least two software products (in one case with another specialist computer software contractor) and some of that work continued during the period of the second GSK engagement, all with a view to maintaining or increasing a stream of fee income.

85. All this points firmly towards the conclusion that the Appellant was in business on its own account and that the services which it performed – including those it performed for GSK under the sequences of contracts which are the focus of this case – were performed in the course of that business.

86. If we stand back from the detail to view the overall picture, and make an informed, considered, qualitative appreciation of the whole as we are encouraged to do by *Hall v Lorimer*, we are clear that the picture we have of the relationship between GSK and Mr Winfield is one of an independent and self-employed contractor, and not that of employer and employee. This is the case not only by reason of the terms of the hypothetical contract we are required to construct for the purposes of the relevant legislation, where, as we have set out, the preponderance of factor or *indicia* point to this conclusion, but also in answer to the question of whether the services which were performed by the Appellant through Mr Winfield were performed as a person in business on its own account.

87. We therefore allow the Appellant's appeal.

Right to apply for permission to appeal

88. 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.

EDWARD SADLER

TRIBUNAL JUDGE
RELEASE DATE: 6 July 2011

Authorities referred to in skeletons and not referred to in the decision:

McManus v Griffiths (1997) 70 TC 218
Secretary of State for Employment v McMeechan (1997) IRLR 353
Netherlane Ltd v York (Officer of the Board of Inland Revenue) (2005) STC (SCD) 305
F S Consulting Ltd v McCaul (Inspector of Taxes) (2002) SPC 305
Global Plant Ltd v Secretary of State for Social Services (1971) 1 QB 139
Massey v Crown Life Insurance Co (1978) IRLR 31
Alternative Book Company Ltd v HMRC Commissioners SpC 685
Island Consultants Ltd v HMRC Commissioners SpC 618
Byrne Brothers (Farmwork) Ltd v Baird (2002) IRLR 96
Future On Line v Foulds (HM Inspector of Taxes) 76 TC 590
Montgomery v Johnson Underwood [2001] EWCA Civ 318
Stevedoring & Haulage Services Ltd v Fuller and others [2001] EWCA Civ 651
Tilbury Consulting Ltd v Gittins (HM Inspector of Taxes (No 2) [2004] STC (SCD) 72
Sherburn Aero Club Ltd v HMRC Commissioners [2009] UKFTT 65
MBF Design Services Ltd v HMRC Commissioners [2011] UKFTT 35

First-tier Tribunal (Tax)

JLJ Services Ltd v Revenue & Customs [2011] UKFTT 766 (TC) (28 November 2011)
INCOME TAX/CORPORATION TAX
Personal service companies (IR 35)

[2011] UKFTT 766 (TC)

TC01603

Income tax and National Insurance Contributions - IR35 case involving a company indirectly contracting to provide the services of an IT specialist to Allianz - change in the relationship after a period - Appeal allowed in part

FIRST-TIER TRIBUNAL Reference no: TC/2009/15078

TAX

JLJ SERVICES LIMITED

Appellant

-and-

THE COMMISSIONERS FOR HER MAJESTY'S REVENUE AND CUSTOMS

Respondents

Tribunal: HOWARD M. NOWLAN (Tribunal Judge)
ANDREW PERRIN F.C.A.

Sitting in public at Vintry House in Bristol on 24 and 25 October 2011

Neil Awbery of Clearsky Accounting on behalf of the Appellant
David Lewis, Higher Officer of HMRC, on behalf of the Respondents

DECISION

Introduction

1. This was a case of the type, usually referred to as an IR35 case, where the issue before us was whether Mr. John Spencer ("Mr. Spencer"), an IT specialist, would have been regarded as an employee of Allianz Cornhill Management Services Ltd ("Allianz"), had he rendered services to that company under a direct contract between himself and Allianz. As it was, he was employed by the Appellant, his own company, albeit that there was no written employment contract between himself and the Appellant; the Appellant then contracted to provide his services to Highams Recruitment Limited ("Highams"), Highams essentially being his and the Appellant's agent; whereupon finally Highams contracted to provide Mr. Spencer's services to the ultimate client, namely Allianz.

2. The tax and duty in dispute were PAYE income tax and National Insurance Contributions, both employer and employee Case I contributions. The dispute spanned from the tax year 2000/2001 to 2007/2008, and the total claimed amounts were £91,443.48 in tax, £61,268.35 in NIC, and interest of £48,048.46. It was accepted by HMRC that if the appeal was dismissed, such that the analysis was that Mr. Spencer should be regarded as always having been an employee, then tax already paid by the Appellant in Corporation Tax would be refundable, provided at least that earlier periods were still open for adjustment. Insofar as Mr. Spencer had received some salary and dividends from the Appellant, then tax already paid in respect of salary and dividends would also be deducted against the gross figures just mentioned. We were not concerned with the detailed figures, though it appeared that the net liability, for which the Appellant alone would have been directly liable was roughly £141,000. Whilst there is no direct relevance to this fact so far as this appeal and our decision are concerned, we were also told that by the time the Appellant had paid for the costs of the appeal, its retained funds would be only about £2000.

3. Our decision is that it is realistic to conclude that Mr. Spencer's notional status, either as an independent contractor or an employee of Allianz, actually changed during the period. The precise point at which the change occurred is not easy to define, but at the end of December 2003 there were various indications that the relationship did then change. Our decision is accordingly that in the early period, prior to the end of 2003, Mr. Spencer would not have been regarded as an employee, but that from the start of 2004 onwards, he would have been regarded as an employee. We will of course explain the reasoning for our conclusions for the periods on each side of that dividing line.

The evidence

4. Evidence was given before us by Mr. Spencer, and by two employees of Allianz, namely Karen Ballard and Mick Devereux, who gave evidence on behalf of the Respondents. There was no material dispute in relation to the evidence, and we will summarise the evidence in recording the facts below. We will also mention minor differences of emphasis, but nothing derogates from the fact that we were entirely satisfied that all three witnesses were describing aspects of the relationship in a broadly similar manner and all were entirely honest and trustworthy.

The law

5. The terms of the relevant legislation for income tax and NIC purposes is broadly the same. The current income tax wording, found in section 49 of the Income Tax (Earnings and Pensions) Act 2003 provides that:

> *"49(1). This Chapter applies* (i.e. meaning, in the circumstances of this case, that the Appellant would be treated as having paid employment income of a calculated amount to Mr. Spencer) *where:-*
>
> > *(a) an individual ("the worker") personally performs, or is under an obligation personally to perform, services [for another person] ("the client"),*
> > *(b) the services are provided not under a contract directly between the client and the worker but under arrangements involving a third party ("the intermediary"), and*
> > *(c) the circumstances are such that, if the services were provided under a contract directly between the client and the worker, the worker would be regarded for income tax purposes as an employee of the client.*
>
> ……
>
> *(4) The circumstances referred to in subsection (1)(c) include the terms on which the services are provided, having regard to the terms of the contracts forming part of the*

arrangements under which the services are provided."

6. We consider it unnecessary to quote the broadly similar NIC wording. The most material minor difference is that for NIC purposes there is not the same direction to consider the "circumstances" relevant to the notional direct relationship by *"including the terms on which the services are* [actually provided under the actual contracts]", in the manner referred to for income tax purposes by section 49(4), just quoted. Since however, neither party advanced any point in relation to any perceived difference in the wording for the different tax and duties, and since indeed section 49(4) only tells one to include the terms of the actual contracts amongst the circumstances to be taken into account in applying section 49(1)(c), and we conclude in this case that other general factors are of far more significance than the formal terms of the existing contracts, we will ignore any difference between the two forms of wording.

7. The sole question of principle for us, therefore, is whether, had Mr. Spencer performed his services for Allianz under a direct contract between himself and Allianz, he would have been treated as an employee or as an independent contractor.

The background

8. At the date of the hearing, Mr. Spencer, now 66 years of age, had been retired since 2007. He had clearly had a very long career in Information Technology ("IT"), and must have been one of the early computer specialists. We were told that from 1963 to 1991 (27 years) he had worked for STC, being made redundant in 1991. There is then some significance to the fact that he was unemployed for a 2-year period, trying but failing to gain replacement employment. In order to secure work he signed up with a firm specialising in finding placements for IT specialists, namely Highams. We understand that in 1993 and 1994, he was contracted to supply services to Highams, who made his services available first to Texas Instruments in Bedford for 14 months, and then to BAE systems for 2 months.

9. In 1994, there was again a period (of 4 months) when Mr. Spencer was out of work. It was also at this time that he formed his company, the present Appellant, with a view to the company providing his services to Highams, and Highams then on-providing the services to ultimate clients. We did not ascertain precisely why the Appellant was formed, and it may have in part been formed because Mr. Spencer might have gathered, or Highams might have suggested to him, that there would be some tax savings, and in particular NIC savings if the Appellant only paid on a modest proportion of its service fee income as salary to Mr. Spencer, paying Corporation Tax at the small companies' rate on the balance and paying out the after-tax income as dividends to Mr. Spencer. It seems, however, equally or more likely that the driver for the formation of the Appellant was an

insistence by Highams that he form a company and provide his services through the company. The explanation for this suggestion is that, prior to the introduction of the IR 35 legislation, Highams would very likely have had a concern that if it continued with a direct contract with Mr. Spencer, and HMRC contended that Highams was then Mr. Spencer's employer, Highams itself would be exposed to the risk of PAYE and NIC liabilities by continuing with a direct contract with Mr. Spencer, and contending that that relationship was not one of employment. The interposition of the Appellant would insulate Highams from this risk. There was no specific evidence that this was the explanation for the formation of the Appellant, but we were certainly told that all similar work procurement agencies like Highams all insisted that their "casual" workers form a company, and that it was thus that company and not the underlying individual that contracted to supply services to the "work-placement" company. It very much sounded as if Mr. Spencer had found that he was unable to obtain full-time employment, similar to his original STC work, and unable to obtain work through agencies unless he formed the company that he did form.

10. From 1994 to 2000, Highams found work for the Appellant and Mr. Spencer with six different ultimate clients, the two shortest engagements being for 3 months, and the two longest for 18 months. There were 3-month gaps, with no available work, between the last three of those engagements.

The work for Allianz

11. After a 3-month gap without work, Highams obtained a 6-month engagement for the Appellant and Mr. Spencer with Allianz, the German insurer that had taken over Cornhill, at their Guildford offices. This engagement commenced in May

2000. Allianz were particularly keen to engage someone very quickly to undertake a project geared to installing and writing programmes for systems referred to as Unix systems. The reason for needing to engage someone quickly was because the person who had previously been doing the work was leaving, and Allianz particularly wanted the replacement to be able to attend handover sessions with the predecessor. Accordingly the Appellant and Mr. Spencer were essentially given the engagement following a telephone interview. Mr. Spencer was at the time living in Harlow, a journey round the M25 from Guildford, which was why, once he had convinced the relevant people at Allianz that his speciality was indeed everything to do with Unix systems, he was engaged without a face-to-face interview and with a view to starting the project immediately. We were certainly convinced that Mr. Spencer seemed to be a very knowledgeable expert in relation to his particular field of installing and writing programmes for Unix systems, and can well believe that he would have immediately struck those at Allianz as well able to deal with their requirements.

12. Although we were shown written contracts between the Appellant and Highams and Highams and Allianz, those contracts all commenced at a slightly later date, and nobody now had copies of the contracts that operated for the initial engagement. We were told, however, that the initial contracts were very similar to the later contracts that we were shown.

13. In relation to contractual arrangements, we should mention the following points. Firstly, Allianz entrusted all its requirements for procuring computer specialists to a firm called Omni Recruitment ("Omni"). Omni dealt with securing both employees for Allianz, and, where appropriate, contract workers as well. We were told that it was not clear whether Mr. Spencer's services were provided via a chain of contracts, namely the unwritten employment contract between Mr. Spencer and the Appellant, the contract between the Appellant and Highams, an unseen contract between Highams and Omni, and then finally one between Omni and Allianz. That actually seems wrong to us since we were shown an actual written contract between Highams and Allianz, with no reference to any interposition of Omni. We assume therefore that Omni was simply acting as Allianz' agent.

14. The wording of the two written contracts that we were shown, namely the ones between the Appellant and Highams, and between Highams and Allianz were virtually identical, and were in particular identical in relation to various of the terms that were drawn to our attention. We will deal with them below but in summary those terms were the terms relating to the Appellant having a qualified right to provide a substitute worker for Mr. Spencer, the terms in relation to "control", and the terms in relation to hours of work and termination. At present we will simply record that there seemed to be every indication that the Allianz/Highams contract was the one that initially governed the terms; it seemed that the Highams/Appellant contract had then been drafted to match and mirror the terms of the Allianz contract; and it also seemed virtually certain that the initial Allianz/Highams contract would have been a general one in use for any contract workers working through "their companies", that might be engaged by Allianz, though Omni.

15. We have already mentioned that the first engagement was for a 6-month period, and in a schedule given to us of the dates for the various contract extensions and projects within each extension period, the project required to be done in that first

period was referred to as "Upgrade systems". In the period between commencement in May 2000 and 31 December 2003, the pattern of engagements and agreed extensions was fairly similar. With the sole exception of one 10-month extension, all of the later extensions were for short periods, one for 1month, two for 2 months, three for 3 months and two for 4 months. Most but not all of those contract extensions gave an indication of the particular project to be undertaken, and the name of the manager within Allianz for whom the project was essentially being done.

16. By contrast to the position prior to the end of December 2003, the position thereafter (until the last few months before the very end of the overall engagement in 2007), was that the contract extensions were for 12-month periods, and no project descriptions were given thereafter. We were also told that at the end of December 2003, Allianz sought to engage Mr. Spencer on an indefinite basis. There was slight confusion as to whether he was actually offered employee status, and if he was he definitely said that he declined that. He was certainly offered an indefinite appointment, and whether he actually declined that or not, as we have just indicated the contract extensions were for the entire years of 2004, 2005 and 2006, and there was no mention of identified projects against those extensions.

The particular terms of the contracts, and surrounding evidence in relation to each particular term

17. We will now summarise the terms of the two contracts in relation to the points material to the dispute, and then add the evidence of the parties in relation to each.

Substitution

18. The Appellant's representative placed considerable reliance on the clauses of each contract that sought to entitle the supplier to send a substitute worker, in place of Mr. Spencer. The relevant wording of the contract between the Appellant and Highams was that:

> *"3.1.5. The services shall be performed by the Contractor. However, the Company may send a substitute of equal experience and ability to perform the Services as set out in the Schedule. In the event of a change, the Company and/or the Contractor shall submit to Highams the names of suitably qualified substitutes and shall permit the Client an opportunity to interview such proposed substitutes."*

Whilst we are not at this point giving our own view on the proper interpretation and the relevance of this clause, we should just refer to two obvious ambiguities. Firstly, it was not clear what would happen if the Appellant proposed a substitute with the requisite "experience and ability", but Highams, and indirectly under the other contract Allianz, did not approve of the offered substitute at the interview. Could Allianz reject such a substitute? Secondly the defined term "Contractor" was also somewhat curious. We accept that where we were shown letter agreements extending or rolling over one contract to the next period, Mr. Spencer was generally identified as "the Contractor". However the contract itself defined the "Contractor" as "the individual undertaking the specified services on behalf of the Company". On one interpretation, that indicated that even Mr. Spencer was not identified as the

relevant supplier. We accept that this was never even advanced in argument, and as we have said, the renewal schedules did generally identify the ultimate supplier as Mr. Spencer.

19. Mr. Spencer's evidence was that he attached some importance to this clause, in that if he was ill or unable for some period to do the work, were he able to offer a substitute, this would protect his company's continuing ability to retain its contract, and the connection to Allianz, and thus give him a better chance of resuming work.

20. Mr. Spencer admitted that the Appellant had no other employees, and certainly none that could meet the requirements for acting as a substitute. He did, however, say that during his career he had made many contacts, and that he knew of two people who did have the requisite experience to fulfil the substitute role.

21. The Respondents' witnesses did not dispute that if Mr. Spencer was unable, through illness or some other reason, to do the work, and the Appellant offered a substitute of whom they approved

during interview, they would accept that substitute. They certainly indicated however that they would have a discretion in the interview process as to whether to accept the substitute. They also said that they would equally look to their normal supplier, Omni, to provide a replacement worker, and that it would take any substitute three weeks to be of any use, since the substitute would have to learn much about Allianz's existing procedures and systems. Mr. Devereux also said in evidence that he was unaware of the existence of the substitution clause. It was then pointed out to him that, in earlier interviews with HMRC, he had revealed that he had been aware of it, and had expressed some view in relation to it. We did not treat Mr. Devereux's statement in evidence that he was unaware of the clause as indicating that he was giving dishonest evidence. We rather took it to exhibit a realistic businessman's contempt for a clause that he probably found irrelevant, a view somewhat in line with the one that we will reach in explaining our decision below.

Control

22. Two clauses of the Appellant's contract with Highams related to "rights of control", though their emphasis was principally on regulations and health and safety matters. They read as follows:

> *"3.1.6. while on the Client site, to comply with all lawful and reasonable directions of the Client with regard to health and safety issues and rules pertaining to the management of the building and will conform to the Client's normal codes of staff and security practice;*
>
> *3,1,7. the Services shall be performed in compliance with all applicable laws, enactments, orders, regulations and other similar instruments (including but not limited to applicable health and safety legislation);"*

23. The general evidence in relation to Allianz's right of control over Mr. Spencer was very much as one would obviously expect in the relevant circumstances. In other words, Allianz would decide on the next project to which Mr. Spencer would be assigned, and there would then be discussion as to how long that project would be

likely to take, and what further support from Allianz's employees Mr. Spencer would need in order to complete the project. Since it was manifest that Mr. Spencer was an expert in his field, and Allianz conceded that there was nobody in their own organisation who would know in detail how Mr. Spencer was then approaching his task, and whether he was pursuing it in the best manner, there would be little intervention with the day-to-day work that Mr. Spencer would then be doing. Obviously Allianz would enquire about progress, particularly if a project was over-running the expected period assigned for completion of the project. Furthermore, Allianz also said that it had the right, if some emergency arose, to require Mr. Spencer to pause in work on a particular project if some other matter needed to be attended to first. The example given was that, since Allianz was quoted on the New York Stock Exchange, there could be occasions when US filings had to be made within some deadline and this might require Mr. Spencer to give his attention to ensuring that the programmes enabled people to marshal the required information for the US filings, only then resuming the earlier project when this urgency had been attended to.

24. There was a slight, and understandable, difference in the evidence as to whether Mr. Spencer's performance was assessed, and whether in other words he was subjected to "quality control". Mr. Spencer indicated that there was no quality control at Allianz, at least of the type that he had been used to at STC. In contrast the Allianz witnesses said that there was some quality control. A relevant overall summary seems to us to be that it is not surprising that when Mr. Spencer had worked for a major computer company such as STC, a one-time affiliate of the US's ITT, the entire business would have been filled with computer experts and there would have been extensive quality control. By contrast at Allianz there would have been sufficient quality control for the management to derive confidence that Mr. Spencer was well able to accomplish the projects assigned to him, but nobody in the company would have had the detailed knowledge of Mr. Spencer's field of expertise to judge whether in every respect he was tackling his projects in the best way.

Working hours, lack of employee benefits and termination terms

25. The contracts themselves were strangely silent about working hours, though the renewal schedules generally indicated the hours to be worked by Mr. Spencer. When he was working five days a week, that is in the period up to his home move from Harlow to Somerset in mid-2004, the renewal letters generally indicated that he was to work for 37 ½ hours a week. After the move, he worked a three-day week from Tuesday to Thursday, and was generally expected to work for 22 ½ hours a week.

26. In reality the position was reasonably flexible. The Appellant billed Highams, and Highams billed Allianz for hours actually worked. If Mr. Spencer worked slightly more hours or fewer hours than the target 37 ½ and 22 ½ he simply billed for the hours worked. Alternatively, and if more sensible, if he worked a few hours short in one week, he might make them up in the following week or following weeks. Mr. Spencer could not simply increase his earnings by working significantly longer hours, and billing for them, without discussing matters with the relevant managers. During the total period when Mr. Spencer was working for Allianz, Allianz introduced a time sheet system under which its own employees were required to fill in time sheets, and allocate their time to particular matters and projects for cost-control

purposes. Mr. Spencer was required to participate in this system, along with the company's general employees, but the remuneration due to the Appellant was still entirely governed by the invoices submitted by the Appellant to Highams.

27. Mr. Spencer was not required to "clock-in" as employees were required to do though he generally worked for normal working hours. On occasions, when a project required that he work when the computers were not being used by the normal staff, he would then work out of normal hours. In a practical common sense manner, such matters would simply be discussed and agreed with the relevant managers in the business.

28. Mr. Spencer almost always worked at the Guildford offices of Allianz. He occasionally worked at a disaster recovery site that the company had near Heathrow, and once attended

meetings in Bristol. He always worked on the company's computers, for computer security reasons, and could not attach his own laptop computer to the company's systems. He did virtually no work at home, though occasionally took telephone calls, and might download information at home on his laptop that he might find of use in performing his services.

29. Since the Appellant billed Highams, and indirectly Allianz, simply for hours worked, there was the familiar position for contract workers that Mr. Spencer was not given paid holidays or payment when off work through illness. He also enjoyed no pension rights, and was not given any of the fringe benefits given to normal staff. He paid for meals even, we were told, the Christmas lunch, when other staff enjoyed certain benefits in this regard. He did not have a company car, and although he occasionally travelled as a passenger in a company pool car, he never drove one. It was even the case that if Mr. Spencer used his own car on Allianz business, he was not reimbursed for any costs. Needless to say, the Appellant's hourly charging rate was higher than the rate that Mr. Spencer might have commanded had he been an ordinary employee, and had he enjoyed the ordinary employee benefits of paid holidays, paid sick-leave etc.

30. There were no written terms that governed when Mr. Spencer might actually take holidays. As a courtesy he always agreed absences for holidays in advance, and generally at times when work projects made absence less disruptive.

31. Either party could terminate the contract with four week's notice. Obviously the contract could also be terminated immediately for gross misconduct etc., and somewhat oddly, although the contracts at both levels could not be terminated in the event of short illness, they could be terminated for any illness for a period of more than two weeks. In the seven years during which Mr. Spencer worked with Allianz, he was in fact never ill.

The parties' intentions

32. Both contracts contained an identical clause, indicating that "any Contractor supplied by [the Appellant] shall not be deemed to be an employee, agent or partner of Highams or the Client."

Other relevant evidence

33. We will now summarise a few more matters revealed in evidence that were not directly related to any terms of the contracts.

The German parent company's requirements in relation to employee numbers

34. We were told that Allianz itself had an extraneous reason for preferring to engage Mr. Spencer as a contract worker, rather than as an employee, certainly in the period after 2003, when Mr. Spencer dropped down to working on a part-time basis. This was because Allianz's German parent company laid down internal rules for the numbers of strict staff members who could be engaged in

particular areas of the business, and when 1 ½ staff members were designated as permitted for a particular area in which Mr. Spencer was working, it was highly convenient that, as a contract worker, he could be excluded from the headcount.

Other contract workers

35. We were told that, during the period when Mr. Spencer worked for Allianz, he was certainly not the only worker engaged on a contract basis. No evidence was given in relation to the other such workers, but we were certainly told that even today, at the date of the hearing, Allianz had a number of contract workers working for it, generally on a very short-term basis, and that so far as Allianz was concerned, it had not heard that any were being challenged under the IR 35 legislation. We repeat that no evidence was actually given about this, but the expectation that short-term workers of a particular category would not be challenged under the IR 35 legislation does seem realistic to us, and it forms part of the decision that we have reached.

The "own business" test, financial risk and the provision of tools

36. In view of the fact that one of the pointers in favour of saying that a worker is a contract worker rather than an employee is the feature of the worker having his own business, and financial risk, we should record the following evidence. It was accepted that Mr. Spencer worked almost entirely with "tools" provided by Allianz. The only business or financial risk referred to was the risk that even if Allianz paid Highams, Highams might become insolvent, such that the Appellant would not be paid for hours worked by Mr. Spencer.

The contentions of the parties

37. Cases of this nature are very familiar, and it is unnecessary to record the contentions of the respective parties in detail. The pointers towards employment and against employment are all well known. We simply add that both parties treated as their starting point the three tests laid down by MacKenna J in the case of *Ready Mixed Concrete (South-East) Ltd v. Minister of Pensions and National Insurance* [1968] 2 QB 497. Those three tests are the provision of work on a personal basis, the "engager" having sufficient rights of control to make the engager "master", and the other provisions of the contract being consistent with the contract being one of service. The Appellant's representative placed particular emphasis on the feature that the substitution clause indicated that the contract was not one for the

provision of personal service, but one where the Appellant could provide an alternate to render the services.

Our decision

38. The case law authorities in relation to this subject have placed emphasis on a number of tests, and we will start by commenting on each test, and the relevance that it has in relation to this case. Those tests are:

- the feature of personal service;
- the degree of control;
- the consistency of other terms;
- the issue of whether the provider of services has his own business, and
- the slightly nebulous issue of "mutuality of undertakings".

The issue of personal service and the significance of the substitution clause

39. We stop short of saying that the substitution clause in this case was a complete "sham". We accept that if the Appellant had notified Highams, and indirectly Allianz, that Mr. Spencer was going to be unwell, or absent, for a long period for some reason, but that the Appellant had managed to engage a suitable substitute, and that substitute passed Allianz's interview test with flying colours, then it is indeed possible that the Appellant could have continued to bill for the services of the replacement.

40. That, however, is the extent of the reality of the substitution clause. It is perfectly obvious that, as with all similar contracts drafted to seek to sustain non-employee status, the clause was inserted to achieve the desired tax purpose, and it has virtually no bearing on our approach to the decision in this case. The reasons why we consider it to be irrelevant are as follows:

- Although the clause that we have quoted was ambiguous, in that it did not make it clear whether Allianz could reject an offered substitute, said to be experienced etc, if that substitute failed the interview test, it was pointless to provide for an interview if Allianz could not reject an offered substitute. We accordingly conclude that the substitution right was certainly not an unfettered right. The authorities make it clear that such a fettered right is of only modest significance.
- Substitution should be considered in at least two contexts. In a case where substitution is a reality, it is perfectly possible that a substitute might be offered just on an isolated day. Take the case of a company offering a driver to drive a firm's office cars, with the clause that Mr. X would generally be provided, but that in his absence another of the firm's available drivers would be provided, it would then be clear that this contract was not a contract for the personal service of Mr. X. In the present case, it is inconceivable that the Appellant could have sent a substitute on this basis, when Allianz has indicated that it would take a replacement three weeks to be of any use. This means that the only context in which substitution could be a conceivable reality is where Mr. Spencer was going to be absent for a long period.

- There seems, however, little reality to the proposition that the Appellant might have even been able to offer a replacement where Mr. Spencer would be unavailable for a long period. It had no other employees. Even if Mr. Spencer knew of two people who might be suitable, there could be no knowing whether either might be available. In all probability they would have existing engagements, or be working or living miles away. In the

improbable scenario that one might have been available, it is far from clear that such a person could have, or would have wished to provide services indirectly by entering into some contract with the Appellant.

- In seven years, no substitute was ever offered, because it was never relevant, and it was perfectly clear that Allianz was interested in the qualifications and the individual suitability of Mr. Spencer, and would have been equally interested in the personal suitability of any replacement.

41. It seems to us that the substitution clause was one of the type always inserted in cases of this nature, having very little reality and that it should play virtually no part in influencing our decision.

The degree of "control"

42. When a worker is engaged on a part-time basis, engaged to undertake a particular project, the project is unique and not one that the engager would need undertaken repeatedly, and is one where the person engaged alone has the expertise to implement the task, we consider that the degree of control to be exercised is very modest. We accept here that in the early period when Mr. Spencer was engaged for his first single project, and even when he was re-engaged for defined projects, it is realistic to say that the control over his work was limited. Of course Allianz could say what it wanted done, and what the project was. Of course Alliance could divert Mr. Spencer to something that was suddenly urgent if some US filing requirement required urgent attention for a short period on some different work. But whilst Mr. Spencer was undertaking the project for which he was specifically engaged, we consider that he was using his expertise in a manner that could not be controlled in the sense of "how" he did his work. The control was therefore limited.

43. At the end of 2003, if not before, it became clear that Allianz wanted Mr. Spencer's services permanently. It no longer engaged him for projects. It either offered him employment, or permanent engagement, and even if he rejected that, he was thereafter engaged on an annual basis. In other words he became one of Allianz's key computer experts, available for work that was likely to be available indefinitely. He certainly ceased to be engaged just for identified projects. By breaking the link with projects, and indicating that Mr. Spencer would work generally within the organization, we consider that from 2004 onwards, there was more reality to control.

The supplier's own business

44. There are three features that we should consider in relation to the issue of whether Mr. Spencer would have been considered to be undertaking "his own business" on the notional direct contract with Allianz that we are required to assume.

In our view he fails on the first two, but there is something to be said in relation to the third.

45. The first respect in which Mr. Spencer would fail the "own business" test is that when engaged, he had no opportunity to make more or less profit according to how efficiently he

worked, how he managed to minimise and control costs, and manage the cost of tools, assistants etc that would be involved if he was conducting a business in the ordinary sense. Mr. Spencer was simply paid for hours worked.

46. It was suggested that since he might suffer financial loss if Highams went bankrupt, this was a financial loss that supported the "own business" case. We do not agree. The sort of financial risk that sustains the business case is the loss, or the diminished profit that results from costs not being controlled, or a project being undertaken on an inefficient basis when a price has been quoted for a project, rather than the supplier being paid on an hourly basis.

47. We do consider, however, that in one respect there was some reality to the contention that Mr. Spencer should be considered to have been conducting his own business. This was not raised in argument, but it still appears to us to have some degree of reality.

48. When Mr. Spencer was made redundant by STC, he sought replacement employment and for two years he was unemployed. He then concluded that he was only likely to obtain work through agencies, and the work that he did obtain was all short-term project work. It very much seems to us that he had a particular skill to exploit and market (that of setting up Unix systems and writing programs for them), but that that was not a service for which companies engaging him expected to need his services on an indefinite basis. They had short-term projects. They wanted Mr. Spencer for the project, but then foresaw no continuing role for him. Therefore he was exploiting a specific skill that he had, for which different clients had short-term demands, and he did indeed take the risk that there would be very significant periods during which he would have no work. Totalling up the periods during which Mr. Spencer did not work, following his redundancy at STC, there were periods of 24, 4, and three periods of 3 months without work (namely 40 months).

49. We consider that there is a distinction to be made between someone in the situation Mr. Spencer was in, in the period from 1993 to 2003, and the situation of many other part-time employees. If a seaside hotel engages someone to be a waiter in the summer season, that person works in exactly the same way as all other waiters, entirely under the control of the management, and it would be quite unrealistic to say that the waiter was exercising a special skill, rendered to different clients, in some continuing business of being a waiter. Mr. Spencer did appear, however, to have a somewhat "niche" specialty skill that he could only exploit on a part-time basis that clients would only want for the duration of the projects, and in a very modest respect we consider that would have given some modest support to his "own business" case, had he been engaged directly by Allianz, at the time when he was engaged for specific projects.

The "mutuality of undertakings" test

50. There is considerable case law in relation to this test, progressively indicating that the test is

of diminished importance, or that it is indeed nearly meaningless. Some case law relates to the situation of "umbrella contracts" between separate periods of admitted employment, and it is far from clear to us that the "mutuality of undertaking" test is of much assistance to us in this case.

51. There is a feature in this case where the phrase "mutuality of undertakings" has some resonance. A touchstone of being an employee is the hope and expectation that there will be some relationship of faithfulness between employer and employee. In other words, the employer will generally endeavour to keep staff employed even when work is short. Contract workers will be dispensed with first. Employees will commonly have several "employee benefits", and in particular pension rights. With short term engagements, none of this will be relevant with contract workers. Particularly in the early period, with the first and few following projects, we accept that Mr. Spencer never knew whether the various contracts would be renewed. He had been used to short-term engagements with worrying gaps between most of them, and would certainly not have felt confident that he had been taken on, with some hope or prospect of being engaged, and looked after, as a valued employee of Allianz.

The German motivation to engage contract workers rather than employees

52. We referred, in paragraph 34 above, to the rather curious way in which Allianz had some motive for engaging people as contract workers, to circumvent the limitation on employees for particular projects laid down by its German parent company. No evidence was given to the effect that this practice was deliberately undertaken in wholly unrealistic circumstances, but we nevertheless record the obvious point. This fact tends to indicate that, for irrelevant reasons, Allianz might have had a temptation to regard people as not being employees, when in reality they had all the hallmarks of being employees. Thus, to some degree, this factor tends to undermine the feature that Allianz allegedly regarded it as realistic to engage, or rather to continue to engage, Mr. Spencer indirectly for a very long period, purely as a contract worker.

The parties' intentions

53. We attach very little or no importance to the protestation by the parties to the contracts that they regarded Mr. Spencer as not being an employee. Quite apart from the fact that we must address a notional contractual situation that was not the one that the actual parties were in fact considering, their opinion on what is a matter of realistic construction of the overall facts is of very minor significance.

The distinction that we draw in this case

54. Our decision is that in testing whether Mr. Spencer would or would not have ranked as an employee at the point in mid-2000 when we must first address the key question, posed by the notion that he had a direct contract with Allianz, the answer is that he would have been a contract worker, and not an employee.

55. The type of situation, where we consider the contract worker analysis to be realistic is the one where:

- an individual has a particular area of expertise;
- that area of expertise is one that he has found has not enabled him to gain full time employment;
- the explanation for not gaining full-time employment is that the area of expertise is likely to be one that various companies might need, but not on an indefinite basis, but rather simply to complete a particular project;
- the type of work for which the worker is engaged is likely to be work outside the core work of the business.
- the individual has only been able to gain work through rendering his specialist expertise available through placement agents;
- the past pattern of work has confirmed all the above points of short engagements with different companies, and many unwanted gaps between engagements;
- the area of expertise is likely to be one where the client would indicate the project to be done, and the hoped-for time frame for completion of the project, but would not expect to be able to supervise or "control" the worker in any way, simply because the expert would be engaged to do something outside the expertise or competence of the company; and
- the company engaging the individual, engaging him for a project, would consider it quite inappropriate to provide holiday pay, pension benefit, and the other normal incidents of employment because they would all be inappropriate for such contract workers.

56. When the Appellant first indirectly entered into contracts with Allianz, we consider not only that all the above criteria were satisfied, but we take note of the fact that the fact pattern from the recent past would have rendered it very unrealistic (had the IR 35 rules then been in force) for HMRC to have contended that Mr. Spencer would have been an employee of VAI, the company for which he worked for 3 months (with a 3-month gap both before that engagement, and also after it and before the Allianz engagement). The past pattern seems to us to have been entirely consistent with the factors that we have just indicated seem to us to make "contract" status realistic.

57. We also note that shortly after the contracts were entered into in mid-2000, and indeed even at the time of the hearing, Allianz confirmed that it had engaged, and was now engaging, some workers on a contract basis, without regarding them as employees. Obviously we were given no evidence in relation to these cases, albeit that we were told that there had been no indication of any challenge by HMRC other than in the case of Mr. Spencer. Where, however, the criteria that we have summarised at paragraph 55 were satisfied, then it seems to us that non-employee status would have been perfectly realistic.

58. The situation altogether changes, however, certainly by the point in late 2003, when Allianz offered Mr. Spencer either employment, or indefinite engagement, and when in any event the parties moved to a pattern of annual renewals on a non-project basis. It seems perfectly evident to us that from that date onwards, Allianz regarded Mr. Spencer as someone who they wished to engage and retain indefinitely, and when

Mr. Spencer continued to work for Allianz, and accepted yearly contract extensions, it seems realistic to say that his status must have changed. He would by then plainly not satisfy many of the tests included in the bullet points in paragraph 55 above. He was engaged on an entirely personal basis. The substitution argument was basically irrelevant "window-dressing". If he was to be engaged indefinitely on a non-project basis, it seems likely that he was proving useful in numerous respects in relation to computers and IT, and no longer just undertaking his defined projects. So the "control" argument becomes stronger. And fundamentally Allianz wants to engage him as a permanent member of the team.

59. Our decision is accordingly that initially it would not have been appropriate to classify the notional relationship as one of employment. Certainly from January 2004, it would have been appropriate to regard the notional relationship as one of employment. We put the dividing line at 31 December 2003 because it was at that time that he was offered indefinite work, and it was from that date that renewals were agreed on an annual basis, and from which no further reference was made to particular projects.

60. We consider that it is possible that we have put the dividing-line in the wrong place, and that if we have done, the change-over to notional employee status would in fact have taken place well before 31 December 2003. We still consider, however, that the reason underlying the point in the last sentence of paragraph 59 is cogent, and we confirm that as the date when the status changed.

61. This Appeal is accordingly allowed in part.

Right of Appeal

62. 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.

HOWARD M. NOWLAN (Tribunal Judge)

Released: **28 November 2011**

URL: *http://www.bailii.org/uk/cases/UKFTT/TC/2011/TC01603.html*