NATIONAL INSURANCE CONTRIBUTIONS – school fees paid by company to school for the education of the sons of the directors of the company - whether payments in kind – no - whether the company discharged the parents' debt – yes - whether the liability was that of the company – no - appeal dismissed – SSCBA 1992 Ss 3 and 6(1); Social Security (Contributions) Regulations 1979 SI 1979 No. 591 Reg 19(1)(d)

THE SPECIAL COMMISSIONERS SpC 00294

ABLEWAY LIMITED

Appellant

- and -

THE COMMISSIONERS OF INLAND REVENUE

Respondents

SPECIAL COMMISSIONER: DR NUALA BRICE

Sitting in London on 19 September 2001

Mr B Whiffin ATII, FFA, of Messrs B W Whiffin & Co, Accountants and Registered Auditors, for the Appellant

Mr C Ward, HM Inspector of Taxes, for the Respondents

DECISION

The appeal

1. Ableway Limited (the Appellant) appeals against two Notices of Determination originally issued on 26 June 2000 and varied on 28 February 2001. The first varied notice was in the following form:

"1 That Ableway Ltd is liable to pay primary and secondary Class I contributions from 6 April 1995 to 5 April 1999 in respect of the earnings of Mr B Whiffin.

2. The amount that Ableway Ltd is liable to pay in respect of those earnings is £4,356.62.

3. The amount that Ableway Ltd has paid is £0.00.

1. The difference is due to Class I contributions on School fees."

2. The second varied notice was in exactly the same form save that, in paragraph 1, the name of Mrs J Berry appeared in the place of the name of Mr B Whiffin. Mrs Berry is the wife of Mr Whiffin.

The legislation

3 Section 6 of the Social Security Contributions and Benefits Act 1992 (the 1992) Act provides that national insurance contributions are payable where earnings are paid to or for the benefit of an earner. The relevant parts of section 6 provide:

"Liability for Class 1 contributions

6(1) Where in any tax week earnings are paid to or for the benefit of an earner over the age of 16 in respect of any one employment of his which is employed earner's employment-

(a) a primary Class I contribution shall be payable in accordance with this section and section 8 below if the amount paid exceeds the current primary threshold (or the prescribed equivalent); and

(b) a secondary Class I contribution shall be payable in accordance with this section and section 9 below if the amount paid exceeds the current secondary threshold (or the prescribed equivalent)."

4. Section 3 of the 1992 Act defines "earnings" and "earner" and the relevant parts of section 3 provide:

""Earnings" and "earner"

3(1) In this Part of this Act and Parts II to V below-

(a) "earnings" includes any remuneration or profit derived from an employment; and

(b) "earner" shall be construed accordingly."

5. Section 2 of the Social Security (Consequential Provisions) Act 1992 provided for the continuity of The Social Security (Contributions) Regulations 1979 SI 1979 No. 591. Regulation 19 provides that certain payments (including payments in kind) are excluded from the computation of earnings for the purposes of earnings-related contributions. The relevant parts of Regulation 19 provide:

"Payments to be disregarded

19(1) For the purposes of earnings–related contributions, there shall be excluded from the computation of a person's earnings in respect of any employed earner's employment any payment in so far as it is- …

(d) subject to paragraph (5) of this regulation, any payment in kind or by way of provision of board or lodging or of services or other facilities; …".

The issues

6. The Appellant paid fees to a school attended by the two sons of Mr Whiffin and Mrs Berry, the directors of the Appellant. The Inland Revenue argued that the payment of the school fees by the Appellant was remuneration or profit derived from the employment of Mr Whiffin and Mrs Berry within the meaning of section 3(1)(a) of the 1992 Act; that, accordingly, earnings had been paid to or for the benefit of earners in employed earners' employment within the meaning of section 6(1) of the 1992 Act; and that primary and secondary Class I contributions were therefore payable. The Appellant accepted that the payments for school fees were earnings within the meaning of section 3(1)(a) of the 1992 Act but argued that the payments were payments in kind within the meaning of Regulation 19(1)(d) and were therefore to be excluded from the computation of the earnings of Mr Whiffin and Mrs Berry for the purposes of earnings-related contributions. The parties agreed that the payments would not be payments in kind if the liability for the payments was that of Mr Whiffin and Mrs Berry (although discharged by the Appellant) and that the payments would be payments in kind if the liability were that of the Appellant.

7. Thus the issue for determination in the appeal was whether the liability for the payments of the school fees was that of Mr Whiffin and Mrs Berry (as argued by the Inland Revenue) or that of the Appellant (as argued by the Appellant).

The evidence

8. A bundle of documents was produced by the Appellant; another bundle was produced by the Inland Revenue; and a bundle of agreed documents was also produced. There was also a statement of agreed facts.

9. Oral evidence was given on behalf of the Appellant by: Miss June Coote, an Employer Compliance Officer with the Inland Revenue (National Insurance) at Colchester; Mr Richard Hart FCCA, a partner in the firm of Messrs B W Whiffin & Co and Company Secretary of the Appellant; Mr Phil Muskett an Officer of the Inland Revenue in Luton, Bedfordshire; Mr Muskett issued the original Notices of Determination; Mr Barry Whiffin, ATII, FFA, a partner in the firm of Messrs Whiffin & Co and a director of the Appellant; and Mr Alan Wilkinson, an Officer of the Inland Revenue; Mr Wilkinson issued the varied Notices of Determination.

10. Oral evidence was given on behalf of the Respondents by Mrs Janet Rix, the Bursar of the school.

The facts

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

12. Mr Whiffin is the senior partner of the firm of Messrs B W Whiffin & Co, Accountants and Registered Auditors, of 90, High Street, Colchester. Mrs Joanne Berry FCCA (his wife) is also a partner in the same firm and Mr Hart is the third partner. The Appellant supplies services ancillary to the partnership. During the tax years 1995/96 to 1998/99 inclusive Mr Whiffin and Mrs Berry were directors of the Appellant and its major shareholders and the registered office of the Appellant was at the home address of Mr Whiffin and Mrs Berry, namely New House, Worlds End Lane, Colchester In the relevant years Mr Whiffin and Mrs Berry were paid remuneration by the Appellant which was the subject of PAYE. The level of the remuneration was such that it was below the earnings limit so that no national insurance contributions were payable.

13. Mr Whiffin and Mrs Berry have two sons, one born in 1989 and one born in 1991. In 1991 they visited the school and were given two entry forms (one for each son) which they both signed on 2 May 1991. The completed forms provided various information about the two sons and, before the signatures, the following text appeared:

"We understand that if, without giving a full term's notice in writing, we cancel this entry after a firm place has been offered or remove our son from the school, we will be liable for a full term's fees in lieu of such notice."

14. The first entry form was in respect of the elder son and indicated that a place was required for him in September 1993. The second form was in respect of the younger son and indicated that a place was required for him in 1995.

15. In evidence which I accept Mrs Rix stated that when an entry form had been completed the school put the child on the list for the term of entry. If a place were available a letter was sent to the parents saying that their child had been entered for a stated term. The letter would ask for a deposit of £200 so that the place could be kept and the parents were asked to sign a confirmation confirming the entry. The copies of the two confirmations signed by Mr Whiffin and Mrs Berry were produced; these indicated that the cheque for deposit for the elder son was banked on 29 April 1992 and the cheque for the deposit for the younger son was banked on 25 February 1994. In 1992 and 1994 the address for Mr Whiffin and Mrs Berry was given as in Witham, Essex. Mr Whiffin accepted that he and Mrs Berry paid a deposit of £200 for each son.

16. The first invoice for school fees was addressed to Mr Whiffin and Mrs Berry but was returned to the school and it was re-addressed to the Appellant.

Subsequently, the invoices were sent to Mr Whiffin at New House, Worlds End Lane in an envelope addressed to him personally; the invoices themselves were addressed to the Appellant and were paid by the Appellant. The amount of the school fees was returned as a benefit in kind by the Appellant on a return of benefits and expenses and also returned by both Mr Whiffin and Mrs Berry on their personal income tax returns and income tax was paid on that basis.

17. At some time unknown, but after November 1996 and before January 2000, Mr Whiffin, in his capacity as a director of the Appellant, wrote to the school on notepaper headed with the name of the Appellant and the address of the firm at 90, High Street, Colchester. The letter was in the following terms:

"I am writing on behalf of the company to clarify the position that has existed for some time with regard to the provision of chargeable services by the school in respect of the above named pupils.

The company has contracted with the school for the provision of those services and the request that they be supplied to the above named pupils.

The company undertakes to meet all costs and fees properly chargeable by the school for all and any services provided for so long as the said [pupils] remain as pupils of the school. The company also acknowledges and accepts the terms and conditions of the school in respect of the provision of services and in particular the requirements for notice of withdrawal of a pupil from the school and any payment required by the school in lieu thereof.

Nothing in our agreement shall affect the rights of the school as to the acceptance or otherwise of pupils. Nor shall this agreement have any effect or bearing on the statutory position of the school in respect of its relationship to pupils."

18. At some time unknown, but after November 1996 and before January 2000, Mr Whiffin and Mrs Berry wrote to the school from their address at New House, Worlds End Lane, in the following terms:

"We refer to the provision of chargeable services being provided to Ableway Ltd by the school in respect of the above pupils.

We the undersigned are the parents of the said [pupils] being the pupils to whom the services relate.

We jointly and severally give an undertaking that in the event of any sums payable by Ableway Ltd to the school in respect of the said [pupils] remaining unpaid after due date of payment we will settle in full any such outstanding debt on demand.

This undertaking shall be irrevocable, other than by joint agreement between us and the school, during the entire period during which the said [pupils] shall be pupils at the school or, in the event of any debt remaining outstanding subsequent to such period, until all amounts due to the school from Ableway Ltd have been paid in full."

19. On 17 December 1999 Miss Coote visited the Appellant for a routine visit. She received full co-operation from Mrs Berry. She asked permission to approach the

school and this was granted. She wrote to the school on 29 December 1999 and asked for the following information:

"1. Please can you confirm the arrangements that the school makes for the provision of education for your pupils? Please can you supply a copy of your enrolment forms?

2. Would it be your normal practice to contract with a parent/guardian of the child for the provision of education?

3. Can you please confirm that this is the case in respect of [named pupils} (parent Barry Whiffin)?

4. Can you please provide a copy of the contract and/or educational arrangements for the above children?"

20. Miss Coote sent a copy of her letter of 29 December 1999 to Mr Whiffen and on 6 January 2000 Mr Whiffin wrote to the headmaster. He referred to the letter of 29 December 1999 sent by Miss Coote and said:

"I would appreciate it if your reply were to simply send Miss Coote a copy of the letter from Ableway Ltd that I passed to you confirming that it sets out the arrangements with regard to the liability for payment of school fees for [names of sons]. I do not believe that the questions regarding the provisions for education are relevant."

21. In reply to her letter of 29 December 1999 Miss Coote received copies of the two entry forms signed on 2 May 1991, a copy of the undated letter from the Appellant to the school, and a copy of the undated letter from Mr Whiffin and Mrs Berry to the school. She concluded that, as Mr Whiffin and Mrs Berry had signed the enrolment forms, they were liable to pay the fees and that meant that there was a liability for national insurance contributions. Subsequently the Notices of Determination were issued against which the Appellant appeals.

The arguments for the Appellant

22. For the Appellant Mr Whiffin accepted that the payments of school fees were earnings within the meaning of section 3(1)(a) of the 1992 Act but argued that the payments were payments in kind within the meaning of Regulation 19(1)(d) of the 1979 Regulations. He also accepted that, if the liability for the payment of the school fees were that of himself and Mrs Berry, then contributions were payable but he argued that the liability for such payment was that of the Appellant. He argued that the school had entered into an agreement with the Appellant for the payment of fees; the contract was between the school and the Appellant; invoices had been sent to the Appellant; and the terms of the arrangement had been set out in the letters between the Appellant and the school. He accepted that he and Mrs Berry, as the parents of their two sons, had given a guarantee but argued that that was not the same as assuming a liability. As school fees were always payable in advance there was never any outstanding liability. He denied that the signature of the entry form created a liability; it merely amounted to an agreement to pay one term's fees if a child did not take up a place or left without notice; the effect was just to place the child on a waiting list but it was silent as to who was responsible for the payment of the fees. He distinguished Richardson v Worrall (1985) 58 TC 642 as that concerned income tax and he agreed that there was an income tax liability; however this appeal concerned national insurance contributions.

The arguments for the Inland Revenue

23. For the Inland Revenue Mr Ward argued that the liability for the school fees was the personal liability of Mr Whiffin and Mrs Berry. They had assumed that liability by signing the entry form. He cited Richardson v Worrall at 670B as authority for the view that the discharge by an employer of a pecuniary liability of an employee was not a payment in kind but was earnings.

Reasons for decision

24. Richardson v Worrall (1985) concerned a credit card provided by an employer which was used by an employee for the purchase of petrol for private motoring. The employer paid the accounts presented by the credit card company and did not require reimbursement from the employee. Scott J held that the employee had incurred a personal liability to pay for the petrol which liability had been discharged by the employer through the credit card company and that the liability thus discharged was an emolument chargeable to tax under Schedule E. Scott J reviewed the authorities and, in the passage relied upon by Mr Ward at page 670B, said:

"There are, therefore, two principles established by these authorities which I must apply to the facts of the two cases before me. First, there is the principle that benefits in kind are not taxable unless they can, in one way or another, be turned by the taxpayer into money. If it is right to regard the credit card arrangements as the provision by the employers of a benefit in kind, namely, free petrol to the employees, then this is the principle that must be applied. Secondly, there is the principle that the discharge of an employee's debt represents money's worth received by the employee. If it is right to regard the credit card arrangements as the means by which the employees discharge their obligation to pay for the petrol they purchased, then the application of this principle must be considered."

25. Mr Whiffin distinguished this authority on the ground that it concerned income tax and not national insurance contributions. However, the same principles were followed in R v Department of Social Security, ex parte Overdrive Credit Card Ltd [1991] STC 129 which did concern national insurance contributions and where it was held that the right approach was to regard the discharge of an employee's debt as the equivalent of a payment in cash.

26. Accordingly I agree that the parties correctly identified the issue in the appeal as being whether the payment of the school fees by the Appellant was or was not the discharge of the debt of Mr Whiffin and Mrs Berry.

27. In considering that issue I first consider the oral evidence; then the contemporaneous documents; and finally the other documentary evidence.

28. The oral evidence of Mr Whiffin was that he did not enter into any agreement with the school when he signed the entry forms. At that time he could have applied to six schools. He said that he discussed the matter with the headmaster at the first visit in 1993 when the entry forms were signed or shortly after. He asked if the school would agree to supply its services to the Appellant. The headmaster had said that he was content so long as the parents gave an undertaking to guarantee the fees if the Appellant did not pay them. There was always a contract of care with the parents. If there were an agreement for a third party to pay the fees the headmaster would not accept an instruction from that third party about matters such as school trips.

29. The oral evidence of Mrs Rix was that the normal procedure was for prospective parents to ask the school for prospectus. If they then wished to see the school an appointment was made for them to visit the headmaster. It was part of her function to assess all the arrangements for the payment of fees, including scholarships and bursaries, and if special arrangements were made between parents and the headmaster she implemented them. If she were told that someone other than the parents was to be responsible for the fees she would send the invoice to that person but the liability remained that of the parents. If it ever became necessary to take legal action to recover fees that action would be taken against the parents, relying on the signed entry form and the signed deposit form. It was the obligation of the parents to cause the fees to be paid. She regarded the payment of fees by the Appellant in the same way as payment by a grandparent but remained firmly of the view that in such cases the ultimate liability remained with the parents.

30. Where the evidence of the witnesses conflicted I preferred the evidence of Mrs Rix. Mr Whiffin did not call the headmaster to give evidence of their conversations. Further, the documentary evidence supports the evidence of Mrs Rix.

31. As far as the contemporaneous documents were concerned these consisted of the two entry forms and the two signed confirmations sent with the deposits. All these documents are consistent with conclusion that the obligation to pay the fees was that of the parents. There is no indication on them that the obligation was that of the Appellant.

32. The other documentary evidence consists of the undated letter to the school from the Appellant and the undated guarantee letter from Mr Whiffin and Mrs Berry. Although these were received by the school (who sent them to Miss Coote) they were not acknowledged by the school. Further, there was no evidence about the date upon which they were sent. Mr Whiffin, who sent them, could not be precise although he said that they were not sent earlier than 1996. All that is known is that they had been passed to the headmaster prior to 6 January 2000, as they were referred to in Mr Whiffin's letter of that date, and they were in the school file as they were sent to Miss Coote. Even if they were sent in 1996 they cannot be best evidence of an arrangement which was claimed to exist from 1993. Indeed, if the arrangement had existed from 1993, it is difficult to see why the letters were required. In any event, the guarantee letter appears to evidence the obligations of the parents.

Decision

33. Having heard the evidence and seen the witnesses I conclude that the liability for the payments of the school fees was that of Mr Whiffin and Mrs Berry.

34. The appeal is, therefore, dismissed.

DR NUALA BRICE

SPECIAL COMMISSIONER

RELEASE DATE:

SC 3051/01

26.10.01