TC02267

Appeal number: TC/2011/01002

VALUE ADDED TAX — registration — whether appellants trading as single partnership or as two differently constituted partnerships — on the evidence, two separate partnerships — appeal allowed

FIRST-TIER TRIBUNAL
TAX CHAMBER

COLIN SUMMERS
CHRISTOPHER SUMMERS **Appellants**

- and –

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

TRIBUNAL: JUDGE COLIN BISHOPP
GORDON MARJORAM FCA

Sitting in public in Birmingham on 14 and 15 May 2012

Mr Mohammed Sarwar, counsel, for the appellants

Mrs Cheryl Payne-Dwyer for the respondents

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DECISION

Introduction

1. The issue in this appeal is whether there is a single partnership between the two appellants, or two distinct partnerships, one between the two appellants alone and the other between them and Mrs Tina Summers. The first appellant, Mr Colin Summers, is the father of the second appellant, Mr Christopher Summers. Mrs Tina Summers is the latter's wife. Although she has been treated in the course of these proceedings as if she were an appellant, there is no decision of HMRC which is directed to her and she is not, properly, an appellant. She did, however, play a major part in the relevant events. We trust that the appellants and Mrs Summers will not object if, in the interests of brevity and clarity, we refer to them by their forenames in what follows.

2. The background to the appeal is that the Commissioners maintain that there was a single partnership whose turnover crossed the registration threshold in November 2005, rendering it liable to register and account for VAT from 1 January 2006. Their decision to that effect, conveyed by letter of 19 August 2010, is the subject-matter of this appeal. If, instead, the appellants are correct in their claim that there were two separate and differently-constituted partnerships the Commissioners agree that the turnover of neither partnership exceeded the threshold and that the liability to register was not triggered. We are required at this stage to decide only the issue of principle, that is whether there was one partnership or two, leaving the parties to deal with the consequences which follow, particularly the amount of tax for which the appellants must account, if we should decide the appeal in the Commissioners' favour.

3. We had written statements but also heard oral evidence from all of the witnesses whose evidence we describe below, and were provided with copies of various documents. The appellants were represented by Mr Mohammed Sarwar of counsel, and the respondents by Mrs Cheryl Payne-Dwyer, an officer of HMRC.

4. In about 1993 Colin began trading on his own account, using the name "Super Whippy", his business consisting of the sale of ice cream from a van. In 1997 Christopher and he entered into partnership in the same business, now with the benefit of two vans. We understand there was no written partnership agreement but Colin's evidence, with which Christopher agreed, was that the trading profits and losses were to be shared equally, while Colin was to retain the goodwill of the business for his own benefit.

5. In 2005, Colin told us, the partnership needed to obtain a new van. He had £12,000 in savings, and was willing to sell a car to raise more cash, in the event about £3,000. Christopher, however, did not have any spare cash and they were a long way short of the £54,000 they needed to pay for the van. They could raise £15,000 by borrowing, but still lacked £24,000. They attempted to obtain investment from an outsider in exchange for a share of the business, but were unsuccessful. However Tina, who was in well-paid employment and had some savings, agreed to provide the remaining £24,000, and did so. The van was purchased, with the assistance of a hire purchase agreement to fund the £15,000 which needed to be borrowed, and became an asset of the business

6. A few months later, Colin and Christopher started another business, selling hot food and using the name "Full Monty Catering". They did so in partnership, the partners being only themselves. That business is still trading, as a partnership between Colin and Christopher. In 2010, however, the ice cream business was transferred to a company, Super Whippy Limited, in which all three of the appellants have shares.

7. The facts set out above are not in dispute. What is in issue is the basis on which Tina agreed to pay £24,000 towards the cost of the new van. As the parties agreed, the outcome of the appeal is dependent on our perception of the evidence relevant to that one issue.

The evidence

8. The appellants' case is that on 17 April 2005 agreement was reached between them and Tina that Tina would inject the £24,000 they required into the business and, in return, would receive a 25% share of it. It was also agreed that, since they were to continue working in the business while (it was then assumed) Tina would not, Colin and Christopher were to receive preferential shares, described as a wage, before the profits were divided. The agreement was reduced to writing, prepared by a friend of Christopher's, Mr Richard Steward, who happened to have called at Christopher's and Tina's home and who was using their computer while the discussions took place. The agreement reads as follows:

> "MEMORANDUM OF UNDERSTANDING
>
> I, Mr Colin Summers of [address] hereby agree that if Mrs T L Summers of [address] injects £24,000 in my business in order to purchase a van I will give her 25% share of my business. Me and my son work full time in the business and therefore are entitled to a wage, which I agree to be £6,000 each. In order to avoid any doubt she will only get share of the profits after our wages are paid. If in the future we change our legal entity from being a partnership to a Limited Company, Mrs T L Summers will be given 25% shares of the company."

9. Colin signed the agreement, above the date of 17 April 2005, and Christopher added his signature as a witness. Tina did not sign it. We shall return to this document later.

10. Colin, Christopher and Tina, as well as Mr Steward, gave evidence about the preparation and signature of the document, and their evidence was consistent. Mr Steward explained that he was not a party to the conversation about the new arrangements, and merely typed what Tina and Colin dictated to him. He then printed a single copy. He had not signed the agreement as a witness as he had not been asked to do so, but he was present, and watched, when Colin and Christopher signed it. Tina added that she needed some persuasion before she agreed to contribute the £24,000 and the "memorandum of understanding" was prepared and signed for her peace of mind. She did not see the need for a more formal document prepared by solicitors since this was a family business, but did want some record of the agreement and thought this sufficient. She did not see any need to sign it herself; all she wanted was a written record of the basis on which she had paid the £24,000. After it had been signed she put the agreement with her other papers, although when she came to look for it some time later she could not find it. We shall explain later how it came to be discovered.

11. On 19 April 2005 Tina transferred £24,000 from her personal savings to the account of the vehicle builders from whom the van was to be obtained. There was clear documentary evidence of that payment, and, although HMRC initially had some doubts, it is not now disputed that it was made. The van was delivered soon afterwards.

12. A point on which HMRC place some emphasis is that Colin and Christopher had already paid a deposit of £12,000 to the vehicle builders when the memorandum of understanding was signed—in fact they had done so in January 2005. The receipt for that deposit records that it was non-returnable, because the work on building the new van started once it was received by the builders. We agree that this is a matter of some significance, to which we shall return.

13. The appellants' evidence was that the ice cream business did not prosper, despite the acquisition of the new van and despite the fact that, contrary to expectations, Tina felt obliged to assist by herself working in the business in order, as she saw it, to protect her investment. Her evidence was that she had expected to see some return on her £24,000 within two years, and she was plainly disappointed that it had not materialised. It was, we gather, because of the low profits earned from the ice cream trade that the appellants decided to start the catering business.

14. In 2008 HMRC opened an enquiry into the partnership tax return submitted by Colin and Christopher in respect of the year to 5 April 2007. The enquiry led to a meeting on 2 December 2008, at which Colin, Christopher, their accountant Mr Liaqat Ali Khan and an HMRC officer, Mr Gary Paine, were present. We were provided with an undisputed note of the meeting, prepared by Mr Paine. The note relates mainly to the income tax enquiry, and only a small part of it has any bearing on this appeal. The note shows that Colin and Christopher explained that there were two partnerships, one selling ice cream and the other hot food, and that they regarded them as distinct. However, Tina is mentioned only in the context of her having helped out in the ice cream business on occasions, mainly at the weekends because of her employment elsewhere, and of her having kept records of the takings figures of each business. Mrs Payne-Dwyer emphasised the absence from the note of any suggestion that Tina was a partner in the ice cream business.

15. We should also mention a letter of 11 August 2009 written by Mr Khan to Mr Paine in the course of the income tax enquiry. It includes the sentence "Mrs Summers [*ie* Tina] paid £24,000 direct to the garage from her bank account (Advice Confirmation enclosed) in order to assist her husband." There is no suggestion in this letter, too, that Tina had become a partner in the ice cream business.

16. The income tax enquiry led Mr Paine to the view that Colin and Christopher should probably have registered for VAT but, since he was not a VAT officer himself, he passed on such information as he had to Mr Anthony Hardie, who is and was such an officer. In November 2009 Mr Hardie sent a VAT Enquiry Questionnaire to Colin and Christopher. It was not immediately returned and on 22 February 2010 Mr Hardie wrote to them again, indicating that the partnership tax returns suggested that they should be registered for VAT, with effect from 1 January 2006. That date was based upon an analysis of the takings figures of the two businesses which had been furnished in the course of the income tax enquiry. He also indicated that, in the absence of a reply, compulsory registration would follow.

17. On 1 March 2010 two questionnaires were returned to Mr Hardie. The first related to Full Monty Catering, named Colin and Christopher as the partners and stated that Christopher was "in charge of this business". The form was signed by Colin, and was accompanied by a table of monthly turnover figures which, if correct and to be taken alone, showed that the business remained below the registration threshold. The second questionnaire related to "C + C M Summers (Super Whippy)". "M" is Christopher's middle initial. The form named the partners as Colin and Christopher, and identified Colin as the partner "in charge for this business". It too was signed by Colin and accompanied by turnover figures which, again on the assumption that they were correct and could be taken alone, showed that the business remained below the registration threshold. We should add that the figures supplied were consistent with those provided in connection with the income tax enquiry.

18. Mr Hardie concluded from the manner in which the forms had been completed that there was a single partnership between Colin and Christopher, albeit there were two distinct business activities, that the turnover of the two activities should be aggregated and that, since the aggregate turnover did exceed the registration threshold, at that time £68,000, the partnership was obliged to register, and in fact should have been registered, as he previously thought, from 1 January 2006; nothing in the answers furnished cast doubt on the date he had determined from his analysis of the turnover figures which had already been submitted. On 2 March 2010 he wrote to Colin and Christopher, inviting them to complete a registration application, while at the same time indicating that if they did not do so, compulsory registration would follow. Mr Hardie's evidence to us was that, at this stage, he had seen nothing at all to suggest that Tina was a partner in either business.

19. On 4 March 2010 Mr Khan wrote to Mr Hardie. He had evidently not yet seen Mr Hardie's letter to Colin and Christopher of 2 March, and was instead responding to the letter of 22 February. His letter addressed an argument that Mr Hardie had not made, and on which HMRC do not rely, that the two businesses were closely bound (see the Value Added Tax Act 1994, Sch 1, para 1A), but he added that whereas the partners in Full Monty Catering were Colin and Christopher alone, Tina had joined them in the Super Whippy business in April 2005 when, he said, she injected capital of £24,000 towards the purchase of the new van and became what he called a "sleeping partner". What he meant, as he explained more fully in his oral evidence to us, was that the profits of the business had not yet been sufficient to entitle her to a share, since the first £12,000 of profit was devoted to payment of the "wages" due to Colin and Christopher.

20. Mr Hardie told us that he could not, at this stage, link the payment made to the documents relating to the purchase of the van, but as we have said HMRC do now accept that Tina made the payment. However, Mr Hardie was unwilling to take Mr Khan's assertion that she became a partner in the business at face value, since it did not correspond to the questionnaires completed and signed by Colin, nor to the information given to Mr Paine at the December 2008 meeting, which Mr Khan had attended, and where, as he thought, no suggestion was made that Tina had become a partner. He checked that point with Mr Paine, and was told that the note accurately represented what he had been told, and that Tina was not shown as a partner on the partnership income tax returns. In addition, Mr Paine furnished him with copies of the financial statements, prepared separately for each business, for the period ended 31 March 2007 which had been provided to Mr Paine in the course of the income tax enquiry. Copies of

those statements were produced to us, and each shows the partners as Colin and Christopher; Tina's name does not appear anywhere on them. The statements consist only of income and expenditure accounts; there are no balance sheets, and hence no record of Tina's capital injection and likewise no indication of whether it has been treated as a partner's capital, or in some other way.

21. During the course of the hearing Mr Khan produced a copy of a letter he wrote to Tina on 26 April 2005. It is described in its heading as a letter of engagement, and is in a standard form for such a letter. Mr Khan's evidence was that the writing of the letter coincided with Tina's becoming a partner in the ice cream business, although it makes no mention of her having done so. He had, he said, learnt that Tina had become a partner through a telephone call from Colin, and it was this call which prompted the letter of engagement. Unfortunately, however, Mr Khan did not make proper file notes, nor take other steps, to ensure that future partnership returns and accounts correctly reflected the change in the composition of the partnership, and it was this failure, coupled with the fact that the profits of the business were not sufficient to entitle Tina to a share, he said, which led to the later preparation of incorrect documents. He went on to add that the note prepared by Mr Paine of the meeting in December 2008, which he accepted to be accurate, made no mention of Tina's having become a partner since the identities of the partners had not been discussed, and he had not thought to raise the point himself.

22. We mentioned above that although Tina recalled placing the memorandum of understanding with her other papers, she was unable later to find it. The evidence we heard from Miss Farzana Ali, an employee of Mr Khan, was that in January 2011, while she was searching through documents held by the practice relating to the ice cream business, in particular in respect of the purchase of the new van, she came across the memorandum, which she realised was an important document, and she immediately gave it to Mr Khan.

Discussion

23. We begin by making the point that it has long been established that the burden of displacing a tax assessment lies on the taxpayer, largely because the relevant facts are, or should be, within his own knowledge. Although we are not required in this decision to deal with the assessment, its validity depends on the underlying question which is before us, namely whether there was a partnership between Colin, Christopher and Tina, and it follows that the burden of establishing that there was such a partnership falls upon them.

24. The definition of a partnership is to be found in s 1(1) of the Partnership Act 1890:

> "Partnership is the relation which subsists between persons carrying on business in common with a view of profit."

25. It can be seen that the definition is both short and simple. A written partnership agreement may extend to many pages and deal with a multitude of different matters, but there is no requirement, in statute or elsewhere, for any measure of complexity, nor indeed for a partnership agreement to be in writing. All that is required is that the partners carry on a business in common, with a view to profit.

26. The appellants in this case are not helped by many of the documents they produced, or which were produced on their behalf. While we recognise Mr Khan's acceptance of his own culpability in respect of the accounting documents and the partnership returns, we are bound to say that some parts of his evidence stretched credulity. In addition, though we do not doubt the truth of what Miss Ali told us, her discovery of the missing document seems rather convenient. We were also left with no cogent explanation, indeed one might say no explanation at all, from Colin and Christopher of their having committed themselves to the purchase of the new van before their finance was in place and, moreover, neither had a clear idea of whether the profits which they could realistically expect to earn once it had been acquired would justify the purchase.

27. Pausing there, it is unsurprising that HMRC were somewhat sceptical about the claim that there were two partnerships and, were what we have set out above the only evidence before us, we would almost certainly concluded that there was only one.

28. We should also make the point that the memorandum of understanding, as any lawyer would immediately appreciate, could not create a partnership. If one assumes, as is the appellants' case, that there was a subsisting partnership between Colin and Christopher, it was not possible for Colin alone to admit Tina as an additional partner. But in our view the legal ineffectiveness of the document, by itself, does not matter: provided we are satisfied from the remaining evidence that there was an agreement between Colin, Christopher and Tina that in return for a capital injection of £24,000 she was to become a partner with them the deficiencies in the memorandum can properly be disregarded. It is significant in this context, if we believe their evidence about the creation of the document, that Colin and Christopher were present at the time it was signed and that Christopher also signed it, even if as a witness, but with (as he told us) his agreement to what was proposed.

29. The decisive evidence was, in our view, that of Mr Steward and, more importantly still, of Tina herself. We did not form any impression that Mr Steward's evidence was the invention which HMRC's case (that the memorandum was not genuine) implies, and we accept what he told us. Tina too struck us as a truthful witness. We accept in particular that, without some form of protection, she would not have paid what we have no doubt she considered to be a significant sum of money towards the purchase of the new van. Thus despite its deficiencies we are satisfied that the memorandum of understanding was intended to create a partnership between Colin, Christopher and Tina, that there was an oral agreement to that effect even if the memorandum did not properly implement it and, albeit she did not in the event receive any return, that Tina was indeed admitted as a partner in the ice cream business. It is common ground that she was not a partner in the catering business. There were accordingly two discrete, differently-constituted partnerships and it follows that the appeal must be allowed.

30. 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.

COLIN BISHOPP
CHAMBER PRESIDENT

RELEASE DATE: 17 September 2012