[2015] UKUT 0343 (TCC)

Appeal number: FTC/74/2014

VAT – whether face-value vouchers issued by appellant companies constitute 'any security for money' within Item 1 Group 5 Schedule 9 to VATA 1994 – yes – whether services supplied by clubs in return for commission charged on redemption of vouchers are services of dealing with security for money – no - redemption of vouchers held to be part of composite taxable supply of performance facilitation services by appellants – appeals dismissed

UPPER TRIBUNAL
TAX AND CHANCERY CHAMBER

WILTON PARK LTD
SECRETS (PROMOTIONS) LTD
SECRETS (HOLBORN) LTD
SECRETS (EUSTON) LTD
SECRETS (ST KATHERINE'S) LTD **Appellants**

- and -

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

TRIBUNAL: Mrs Justice Rose, President of the Upper Tribunal Tax and Chancery Chamber

Sitting in public at the Rolls Building London EC4 on 18, 19 and 20 May 2015

Andrew Hitchmough QC and Barrie Akin instructed by Matthew Arnold & Baldwin LLP for the Appellants

Hui Ling McCarthy instructed by the general counsel and solicitor for HM Revenue and Customs, for the Respondents

DECISION

1. The Appellants ('Secrets') appeal from the decision of the First-tier Tribunal (Judge Demack and Derek Speller FCA) dated 23 January 2014 ([2014] UKFTT 115 (TC)) ('the Decision'). The Tribunal dismissed Secrets' appeals against HMRC's assessment that certain commission Secrets charges in the course of its business is payment to it for taxable supplies for the purposes of paying VAT. Secrets contends that the supplies provided in return for the commission are exempt from VAT.

The facts

2. The facts are set out in some detail in the Decision. Each of the Appellants operates as a licensed lap dancing or table dancing club in London where drinks and refreshments are served and dancers perform for club patrons. The dancers are self-employed and pay a fee to gain entry to the club each night when they are booked to perform. The entry fee is about £80 though this varies from club to club and may be waived at the discretion of the person in charge of the club on the night. Dancers perform either to the general audience on a stage at the club or for particular customers close to the table where the customers are sitting. The dancers generally do not get paid anything for dances performed on the stage, though customers may give them a tip to show their appreciation. If a patron invites a dancer to perform a dance particularly for him at his table then she expects to be paid a 'gratuity' by the customer. The Secrets companies suggest to patrons that they should pay a gratuity for each dance performed at their table. The gratuity is either £10 or £20 per single music track. The clubs have no knowledge of the precise terms of the dancers' transactions with patrons and do not assist in enforcing payment by patrons.

3. If a customer invites the dancer to join him at his table for any long period of time, it is the usual practice for a customer to offer a gratuity for 'table company'. The club suggests that the dancer should receive £250 per hour or part thereof for the time that she is seated with customers at their table. If the customer has agreed to give the dancer a £250 gratuity for table company, the club suggests to the dancer that she includes as many dances as the customer requests during that time.

4. The issue that has generated this dispute arises from the way in which the dancer is paid for some of her work at the club. The customer can give the dancer cash for tips, dances or table company. But often the patrons run out of cash before the evening is over and wish to continue to spend money on entertainment and refreshments. The dancers do not themselves have the means to accept credit or debit card payments in return for their work at the club. In order therefore to enable customers to pay for things without cash, Secrets clubs have established what is called 'Secrets money'. At any point in the evening, the patron can use a debit or credit card to purchase from the waiters or bar staff at the club vouchers which constitute Secrets money. Secrets money vouchers are printed on coloured paper and are sequentially numbered. Each voucher has its value printed on it in both words and figures. Presently vouchers are issued in denominations of £10,

£20 and £250. In the period covered by the present appeals, each of the Appellant companies issued its own Secrets money and accounted for its issue and redemption, vouchers only being valid in the issuing club. The terms and conditions of issue have varied over time, as has the transferability of vouchers.

5. The face of each voucher reads as follows:

> "Secrets Money"
>
> [value of voucher in words]
>
> Secrets money may be used by the customer for the payment of drinks, food, service charge, entrance fees or tip the staff and dancers.
>
> Any change given will be in Secrets money.
>
> Further Secrets money may be obtained by credit/debit card or other currency by asking the manager or waiting staff.
> Terms and Conditions apply."

6. Secrets money vouchers contain on their face no promise to pay the dancer or anyone else their value.

7. Secrets earn money from operating the Secrets money scheme in two ways. First, when the patron buys Secrets money, he pays an additional 20 per cent over the face value of the vouchers. Thus it costs the patron £120 to buy £100 worth of Secrets money or £300 to buy £250 worth. Secondly, if a dancer accepts Secrets money as payment for her work, she can redeem the Secrets money by presenting the vouchers to the club at the end of the evening. When she redeems the vouchers the dancer receives the face value less a commission retained by the club of 20 per cent of the face value of the Secrets money. Thus for every £100 worth of Secrets money vouchers used at the club, Secrets will receive an aggregate commission of £40. The 20 per cent commission on redemption of the voucher back into cash is charged regardless of how the voucher has been acquired by the dancer. Thus there was evidence before the tribunal that dancers redeemed vouchers on behalf of waiters or bar staff who has received them as tips or that they use the vouchers to settle debts between themselves. Also some clubs will allow patrons on occasion to change unused Secrets money back into cash at the end of the evening. In every case, a 20 per cent commission is deducted from the face value of the vouchers on encashment.

8. It is the nature of that 20 per cent commission charge that is the subject of the dispute between the Secrets and HMRC.

9. There is no contractual document entered into between the dancer and the club but there is a code of conduct with which the dancer must comply. This stipulates how she should dress and conduct herself with the customers. It also sets out the gratuities that the dancer can expect for table dances and table company. The

Tribunal noted other points arising from the evidence before it. The clubs do not prescribe any set pattern of working hours, or require dancers to work a minimum number of hours or nights each week. Nor do they require dancers to work exclusively for the Secrets group. A dancer may be "fined" for a breach of the rules laid down. There is no requirement that dancers must accept Secrets money in payment for their services. However, should they refuse to accept payment in that form, it does affect their earning potential, particularly towards the end of the evening because then they can only perform in exchange for cash. Dancers who come to the club to work are expected to stay until the club closes at about 3 am.

10. Some of the material included in the Code of Conduct for dancers about the payment for work at the club is also included in signs on the tables or posted on the walls of the club for the benefit of the patrons. The wording of the signs appears to differ from club to club and in some instances it is not clear whether the sign is drawing the patrons' attention to the fact that the dancer as well as the patron has to pay commission and therefore that the patron needs to give the dancer more vouchers if he wants to ensure that she receives the full £250. For example in one sign setting out 'Important Guidelines', the notice refers to table company and says "Suggested gratuity to the dancer is £250 if given in cash or cost to you £300 if via Secrets money'. This would not, in my view, alert the patron to the fact that the dancer also pays a 20 per cent commission on the Secrets money and so that of the £300 that the patron pays, she would get only £200. However the wording of the Holborn Club's sign is more ambiguous because it says "Most dancers usually receive, for table company by the hour, a gratuity of £250 if given in cash or £300 if given via secrets money (details below)". The 'details below' refer only to the 20 per cent surcharge paid by the patron – there is no reference to the fact that the bar staff and dancers lose a further 20 per cent if they are paid in Secrets money. I doubt that this would be read by patrons as suggesting that they should pay the dancer £300 in Secrets money to make up for the commission she has to pay.

11. Since customers pay for Secrets money with a credit or debit card, the club takes on no greater credit risk than any other retailer accepting a credit or debit card in exchange for goods or services. There is a risk that the customer will disown the item when it appears on his bill and that if the club does not act quickly enough when the credit card company raises the query, it will forfeit the payment through this 'chargeback'. The evidence before the Tribunal was that the Secrets companies are more exposed to the risk of chargebacks than most retailers because of the nature of their business. Patrons can on occasion spend far more than they intend to spend and are therefore more likely to raise 'spurious disputes' e.g. to explain to a spouse or employer the nature of a large item on a credit card statement. On occasion patrons have commenced proceedings against a group company seeking to recover amounts debited to their credit cards though they are not always successful. However, the aggregate of all chargebacks suffered by the appellant companies during the period 13/04/2006 – 21/04/2009 was £16,162.14. During the same period, approximately £22,510,399 of Secrets money was either used to buy food or drink or encashed by dancers. The proportion of chargebacks

the Secrets companies suffered in relation to sales of Secrets Money was less than 0.07%.

12. The main question for the Tribunal and the main question on this appeal is what service is provided by the club to the dancer in return for 20 per cent commission deducted from the Secrets money that she redeems at the end of the evening and whether that service is a taxable supply. Secrets argue that the service supplied by the club in return for the 20 per cent is an exempt supply falling within Item 1 of Group 5 of Schedule 9 to Value Added Tax Act 1994 ('Item 1'). That provision exempts a service which amounts to:

> "The issue, transfer or receipt of, or any dealing with, money, any security for money or any notes or order for the payment of money."

13. There is a note included in Group 1 of Schedule 9 which reads:

> "(4) This Group includes any supply by a person carrying on a credit card, charge card or similar payment card operation made in connection with that operation to a person who accepts the card used in the operation when presented to him in payment for goods or services."

14. The appeal before me therefore raises two questions. The first is whether the Secrets money vouchers are 'security for money' within the meaning of Item 1. The Tribunal decided that they were. The second question is whether the services provided by the clubs to the dancers in return for the 20 per cent commission falls within the exemption in Item 1 or whether they are a wider bundle of services which form a taxable supply. Secrets contend that the transaction between the dancer and the club pursuant to which the 20 per cent commission is paid is simply a dealing with a security for money and hence is an exempt supply. HMRC argue that the service comprises a package of 'performance facilitation services' provided to the dancer to enable her to exploit the opportunity to supply a wider market including non-cash customers. The Tribunal held that the services provided do not fall within Item 1 and are a taxable supply.

15. Before turning to those questions it is convenient to consider the principal case on which both sides relied in support of their submissions; the decision of the VAT Tribunal and of the High Court on appeal in *Kingfisher plc v Commissioners of Customs and Excise*. The decision at first instance was that of Sir Stephen Oliver QC in the VAT Tribunal (decision number 16332 of 5 October 1999) and on appeal the decision of Neuberger J reported at [2000] STC 992.

16. *Kingfisher* concerned a voucher scheme operated by Provident Personal Credit Ltd ('Provident') which supplied vouchers usually on credit to consumers. The vouchers enabled the consumers to buy goods from high street retailers who were members of the scheme, including shops in the Kingfisher retail group such as Woolworth. The consumer buying goods at Woolworth paid with the voucher instead of cash and the retailer presented the voucher to Provident which reimbursed it for the face value of the voucher less a commission of 10 per cent. A

dispute arose between Kingfisher and HM Customs and Excise as to the VAT treatment of the transaction. One of the issues was whether VAT was payable on the 10 per cent. This depended on what, if any, service that 10 per cent was consideration for and whether that service was a taxable standard rated supply.

17. The voucher in issue had written on it the face value e.g. £5 and a statement 'We authorize retailers with Provident Trading Accounts to charge our account to the sum shown'. Before the VAT Tribunal Kingfisher argued that Provident's supply to Kingfisher in return for the 10 per cent was a taxable supply consisting of publicising the retailers and causing them to have sales at a higher level than would otherwise have been the case. That was not an exempt supply within Item 1. HM Customs and Excise contended that the discount charged by Provident was consideration for a separate exempt supply by Provident to Woolworth because the supply was in all material respects equivalent to the services supplied by a credit card company to a retailer. Any additional benefit derived by the retailer from the arrangement with Provident was incidental to the main nature of the supply of services by Provident.

18. Sir Stephen identified two supplies. The presentation of the voucher by the consumer to the retailer discharged the consumer of his or her obligation to pay the shelf price of the goods. When the retailer presented the voucher to Provident, the second supply was made: 'Provident supplies the service of honouring the voucher for the discounted amount'. He considered the nature of the supply by Provident to the retailer and held that this was governed by the operating agreement which formed part of the scheme. He held:

> "The consideration given by Provident to Woolworth in return for Provident's entitlement to the agreed discount is Provident's service of "redeeming" the voucher, in pursuance of its undertaking, written on the voucher, to have its face value amount charged to its account."

19. He rejected the submission that Provident also supplied advertising and promotional activities in return for the discount. This was because the obligation on Woolworth to pay the discount only arose when the sale was complete between Woolworth and the consumer. Further there was nothing in the operating agreement that obliged Provident to supply the services of advertising and promotion. Nor was there any evidence that the advertising and promotion in fact supplied by Provident went any further than listing Woolworth as one of the retailers participating in the scheme.

20. Sir Stephen went on to find that the service provided by Provident could fairly be described as a supply consisting of the receipt or dealing with a 'security for money' within Item 1 of Group 5. He held that:

> 'The word "security" when used without qualification or in a context that demands a narrow or specific construction has a wide meaning. The voucher, when presented by the customer to the participating retailer, evidences Provident's obligation to meet the price for the goods purchased by the

customer to the extent of the face value of the Voucher(s). As such it is a security within the wide meaning of that word. Moreover Provident's services has similar features to the services supplied by credit card companies and credit cards are referred to in Note (4) to Group 5.'

21. He therefore held that the second supply by Provident to Woolworth was an exempt supply of services for a consideration equal to the discount. He referred to the earlier case of *Commissioners of Customs and Excise v Diners Club* [1989] STC 407 and held that although the Provident arrangement was less sophisticated than the credit card arrangements detailed in that case, the essence of the arrangement was the same.

22. On appeal by Kingfisher, Neuberger J held that the tripartite relationship between Provident, Woolworth and the customer was close to the relationship between customer, retailer and a credit card company. He did not consider that any of the differences relied on by Kingfisher were sufficient to justify arriving at a different result from the result arrived at in the credit card company cases such as *Diners Club*. Although the 10 per cent commission was higher than that charged by credit card companies, this merely reflected the more risky credit profile of Provident's customers. The precise order in which the involvement of the various parties occurred did not amount to a difference in principle either. Kingfisher relied on the judgments of the EU Court of Justice in cases such as Case C-126/88 *Boots Co plc v Customs and Excise Comrs* [1990] ECR I-1235, [1996] STC 1359 and Case C-288/94 *Argos Distributors Ltd v Customs and Excise Comrs* [1996] ECR I-5311, [1996] STC 1359. In those cases the retailers issued their own vouchers granting discounts to consumers via third parties. The European Court held that the relevant transaction for VAT purposes was the discounted supply to the customer. Neuberger J distinguished those cases on the grounds that the retailer or supplier gave the discount direct to the customer and there was no question of a tripartite arrangement under which the customer paid full value to a third party which third party then paid a discounted rate to the retailer. Neuberger J said:

> '54. A problem with the analysis of the tripartite arrangement put forward by Kingfisher is that it effectively overlooks the fact that Provident is providing a service to Woolworth. The reality of the arrangement, as I see it, is that Woolworth is getting a benefit from Provident, and that benefit is not merely the payment of money: it is the right to be included in the scheme operated by Provident and the ability to redeem the vouchers. Without Provident's consent, Woolworth could not benefit from the scheme. It could not, for instance, advertise the fact that it was prepared to accept Provident's vouchers for purchase of goods in their stores, because Provident could simply refuse to pay Woolworth on presentation of any vouchers. In that connection, this case bears comparison with the credit card cases relied on by the commissioners.'

23. Neuberger J then dealt with a submission by Kingfisher that all they received in return for the 10 per cent discount was the payment of money. The commissioners had conceded that the payment of money by the customer as the consideration for

the supply of goods or services is not itself to be regarded either as a supply of goods or as a supply of services; it is not even an exempt supply. The judge accepted that no express obligations were imposed on Provident under the arrangements with Woolworth other than to pay the 90 per cent of the face value of the vouchers. However he rejected the submission that that was all that Provident supplied:

> '59. … The fact that Provident is providing the customer with a voucher in advance does not alter the fact that it is Provident taking the commercial risk, in the sense that it will almost always be providing the voucher on credit to the customer. Further, the retailer is obtaining benefits. First, it is able to sell goods to a customer who might otherwise not have the cash to purchase goods, or who might not purchase goods from the retailer if the retailer were not part of the scheme. Secondly, the retailer has relative certainty of payment from Provident, rather than having to take the risk of customer's credit, which is almost certain to be significantly less good than that of Provident.
>
> 60. The contention that there is no obligation on Provident in the Agreement, other than to pay money to Woolworth, appears to me to overlook the reality of the situation … Woolworth does not have to do anything under the agreement unless and until Provident includes it in the scheme, for instance by informing all who enter into the scheme that the vouchers may be used at Woolworth, thereby providing part of the service to Woolworth which, in my judgment, forms the basis of the arrangement between Provident and Woolworth in the context of analysing the relationship for VAT purposes. If Provident does not inform purchasers of vouchers that the vouchers can be used at Woolworth, so that, for instance, the list of retailers advertised by Provident as being in the scheme excludes Woolworth, then the vouchers will not be used at Woolworth, and Woolworth will neither profit from, nor be obliged to honour its obligations under, the agreement. It is only if Provident advertise to purchasers of the vouchers that Woolworth is included in the scheme that Woolworth will benefit from the scheme, and will therefore have to observe its obligations under the agreement.'

24. Neuberger J then turned to the question whether the supply he had identified was an exempt supply within Item 1 or not. He upheld the decision of the VAT Tribunal on this point as well. As a matter of ordinary language the transaction fell within the exemption since it involved the transfer or receipt of or dealing with security for money. He also considered that it was hard to avoid the conclusion that if the service provided by a credit card company to a retailer is exempt, so must be the service provided by Provident to Woolworth. He agreed with the VAT Tribunal's comment that the Provident voucher arrangements were less sophisticated than credit card arrangements. He noted too that --

> '74. … all Provident had to do in order to enable Woolworth to participate in the scheme and thereby to benefit by increasing its turnover, was to ensure that customer are informed that Woolworth is one of the participating retailers. Anything which Provident does beyond that, which happens to benefit

Woolworth is no more than incidental thereto: it would not merely be no part of Provident's contractual obligations, it would not even be a prerequisite to enabling Woolworth to participate in the scheme in practice.'

25. He therefore dismissed Kingfisher's appeal.

Are the vouchers 'security for money' within the meaning of Item 1

26. I can deal with this first issue quite shortly as I am entirely in agreement with the reasoning and conclusions of the Tribunal as set out in the Decision. The Tribunal held (paragraph 70) that 'security' in Item 1 has a wide meaning and that nothing within the VAT Act restricts such meaning. When presented for redemption by a dancer, a voucher clearly evidences, albeit implicitly, a Secrets company's obligation to meet the value stated on its face. They held that security for money can be issued without the issuer being a person within Note (4) to Group 5. The fact that Secrets suffer no significant exposure to credit risk as a result of their being the subject of chargebacks was irrelevant.

27. In my judgment, the voucher is given by the club patron to the dancer as an assurance to her that he has, by buying the Secrets money, made an arrangement with the club which means that she can confidently dance for him or provide table company without being paid by him in cash. This is because she knows, on taking the Secrets money, that she will be paid for her services at the end of the evening on redeeming the voucher. The voucher is given to the dancer by the patron precisely as a security for the money that the patron wants to pay her and which she will receive from the club when she redeems the voucher. It is well within the ordinary meaning of the words used in Item 1.

28. HMRC say that this is not a security for money because there is no extension of credit by the dancer, or even by the club, to the customer. However, I do not see that this is a necessary element and that was not part of the reasoning of either Sir Stephen Oliver or Neuberger J in *Kingfisher*.

29. HMRC sought to distinguish *Kingfisher* on the grounds that the judgments record that the Provident voucher had written on it that it authorised retailers with Provident Trading Accounts to charge their account to the sum shown. Here the Secrets money does not contain any such statement on its face. HMRC refer to the decision of the VAT Tribunal in *Dyrham Park Country Club Ltd v The Commissioners* [1978] VATTR 244 where the tribunal held that certain bonds issued by the club there were security for money, and defined that term as meaning 'a document under seal or under hand at a consideration containing a covenant, promise or undertaking to pay a sum of money'. Miss McCarthy, appearing for HMRC, argued that the Secrets vouchers do not contain any such promise. If a piece of paper without such a statement on it could be treated as security for money, then she said the term might be used to cover any item or token such as the tokens used by players in a game of Monopoly – something that does not look like a security for money at all.

30. This argument brings to mind the fictitious case of *Board of Revenue v Haddock* described by A P Herbert in *Misleading Cases in the Common Law* in which Albert Haddock tenders a cheque written on the side of a cow in payment of his income tax. Whether or not the fictitious judge in that case was right to hold that the cow could be a valid negotiable instrument, I consider that the Secrets money vouchers are securities for money even though they do not say on their face that the dancer is entitled to encash them. The Tribunal found that the club was under a legal obligation to redeem the vouchers when the dancer presented them. The Secrets money scheme depends on both patrons and dancers being confident that the vouchers can be used to pay the dancers what they earn. If the club refused to pay the dancer for the voucher, the Secrets money scheme would quickly collapse. I therefore uphold the Tribunal's conclusion that the vouchers are security for money. Since I have arrived at that conclusion I do not need to address Secrets' alternative submission that the vouchers are 'money equivalent'.

Is the service provided by Secrets in return for the 20 per cent commission a taxable supply?

31. The Tribunal noted (at paragraph 79) that it was not HMRC's case that the 20 per cent commission charged to dancers represents further consideration for the right to enter the clubs, to access the facilities and to perform to customers in general (i.e. the 'entry supply' claimed by Secrets). Rather their case was that the 20 per cent charge is consideration for access to a wider market than the dancers would otherwise have – namely the non-cash customer market – and, critically, for facilitating the dancers' exploitation of that market. They considered that the 20 per cent charged by Secrets to the dancers is not merely consideration for the encashment of the vouchers but for 'a package of performance facilitation services', namely the provision of the means by which the dancers can exploit the opportunity to make more supplies to a wider market (thereby increasing their turnover) by facilitating the dancers' performances to the non-cash customer base.

32. The Tribunal concluded as follows:

> "87. In our judgment, in VAT terms dancers are "retailers" in that they supply services to Secrets companies' patrons. However, they are severely limited in dealing with the matter in that they are only able to redeem the vouchers for services supplied to patrons in a specific location.
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> 88. Although considered individually, the VAT liability at each step of the process would appear to support the appellant companies' case, in our judgment the various steps which occur with regard to Secrets money cannot be separated in practice. … We accept the submissions of Miss McCarthy in respect of this aspect of the appeal in their entirety, and hold that there is a single supply of services by the Secrets companies to the dancers which is paid for by means of (1) entrance fees, and (2) the premium in Secrets money. It follows that we dismiss the appeals."

33. Mr Hitchmough QC appearing for Secrets argued that the Tribunal erred in its approach to the issue of the scope of the service provided by Secrets to the dancer. The Tribunal erred, he submitted, by throwing all the factual background into the mix in order to identify the supply. This was contrary to the decision of the Supreme Court in *HMRC v Secret Hotels2 Ltd (formerly Med Hotels Ltd)* [2014] UKSC 16 ('*Secret Hotels2*'), decided in March 2014, after the Tribunal's ruling in this case. Mr Hitchmough contends that *Secret Hotels2* decides that in identifying what is supplied by the taxpayer, the court must look primarily at the contractual position. The court should consider the background facts only in order to perform a 'sense check' of the result derived from the contract. If that is right, then he submitted, the service provided by the clubs clearly falls within Item 1.

34. In the alternative, Secrets submit that if the clubs are providing a composite supply of services to the dancers, then the scope of those services is much more limited than the Tribunal found. Once one has correctly circumscribed the limits of that service, then Secrets argue that it is effectively the same service that Provident was providing to Kingfisher and that credit card companies are providing to retailers. The nature of that composite supply is such that it falls within Item 1 because the other benefits that the dancer obtains by being able to dance for non-cash customers for payment are merely incidental to the supply and not part of her contractual entitlement. The advantage she enjoys by accepting Secrets money is akin to the boost in sales that Woolworth achieved by being a member of the Provident scheme and is an incidental benefit rather than part of the services supplied.

35. HMRC argue that the Tribunal was right to find that the services provided in return for the 20 per cent commission was a composite supply of services which enable the dancer to gain access to the non-cash market available from the customers the club. They do not go so far as to say that one should treat the entry fee and the 20 per cent commission as one overall consideration for all the facilities provided at the club. That was not their submission before the Tribunal and it was not their primary submission on appeal because they do not need to go that far. However, their alternative submission is that if the Tribunal was right to treat all the money paid by the dancer during the course of the evening as one payment, then clearly the services she receives for that payment from the club are taxable supplies and cannot fall within Item 1.

Discussion

36. I do not accept that the Tribunal in this case erred in its approach to identifying the supply. *Secret Hotels2* is not authority for the proposition that Mr Hitchmough relied on. That case concerned the liability for VAT of a company which markets and arranges holiday accommodation through an on-line website. The outcome turned in part on the appropriate characterisation of the relationship between the company, the operators of the hotels, and the holiday-makers or their travel agents. The Principal VAT Directive laid down a special scheme for the VAT treatment of transactions carried out by travel agents if the travel agent dealt with customers in their own name using goods or services provided by other taxable

persons but not if they acted solely as intermediaries. The issue before the Supreme Court was, broadly, whether Morgan J had been right to approach the appeal before him on the basis that the court should start by assessing the effect of the totality of the contractual documentation, and only then ask whether that assessment was altered by the way in which Secret Hotels2 conducted its business. The Court of Appeal reversed his decision, holding that the tribunal had been right to weigh up the contractual documentation and the way in which Secret Hotels did business and come to a conclusion on that basis as to whether Secret Hotels2 operated as principal or agent.

37. Lord Neuberger, with whom the other Supreme Court Justices agreed, upheld Morgan J's approach. He said:

> "31. Where parties have entered into a written agreement which appears on its face to be intended to govern the relationship between them, then, in order to determine the legal and commercial nature of that relationship, it is necessary to interpret the agreement in order to identify the parties' respective rights and obligations, unless it is established that it constitutes a sham.
>
> 32. When interpreting an agreement, the court must have regard to the words used, to the provisions of the agreement as whole, to the surrounding circumstances in so far as they were known to both parties, and to commercial common sense. When deciding on the categorisation of a relationship governed by a written agreement, the label or labels which the parties have used to describe their relationship cannot be conclusive, and may often be of little weight. …"

38. Lord Neuberger then referred to the rules that apply when the court construes a contract governed by English law, noting that it is not generally permissible to take into account the subsequent behaviour or statements of the parties as an aid to interpreting their written agreement. The right starting point was to characterise the nature of the relationship between Secret Hotels2, the customer, and the hotel, in the light of the contractual documentation. One must next consider whether that characterisation can be said to represent the economic reality of the relationship in the light of any relevant facts. The final issue was the result of that characterisation so far as the relevant provisions in the Directive were concerned.

39. Lord Neuberger considered the contractual terms and concluded that Secret Hotels2 was acting as agent and not as principal. He then considered the factors that had caused the tribunal and the Court of Appeal to arrive at the opposite conclusion. He held that those factors, even taken together, were not inconsistent with, and therefore could not undermine, the existence and nature of the agency arrangement. He held therefore that Morgan J had been right to overturn the decision of the tribunal.

40. The situation in the present case is very different from the situation in *Secret Hotels2*. Here there are no contractual documents purporting to set out

comprehensively the rights and duties of the club and the dancer. The dancers do not sign any agreement when they start to work at Secrets or on entering the premises on any particular night. In the absence of comprehensive contractual documents, those rights and duties have to be drawn from such documentation that does exist together with the way the clubs conduct their business. The key fact in this dispute – the 20 per cent rate of commission – is not actually contained in any document since the Code of Conduct refers only to the rate in force at the club from time to time. I do not read the Decision as finding that the sole obligation owed by the club to the dancer (beyond the right to enter the club in return for the entrance fee) is the obligation to redeem the voucher. Such a conclusion flies in the face of the reality whereby both the club and the dancers are in effect operating their respective businesses on the same premises. They are dependent on each other for success and profitability. If a dancer enters the premises and refuses to comply with the code of conduct she can be 'fined'. If the dancer paid her entrance fee but was prevented by the club from dancing at tables or from accepting Secrets money she would have good reason to complain. The way that the Tribunal approached its task here was consistent with the underlying principles of contract law. Their approach was also consistent with the principle referred to by Lord Neuberger in *Secret Hotels2* that taxable persons are generally free to structure their transactions in a way which minimises their tax burden. I reject the submission that the Tribunal's approach in this case has now been shown to be wrong by the judgment in *Secret Hotels2*.

41. If the Tribunal were right to consider rights and obligations beyond the pure encashment of the voucher, was their decision inconsistent with the two decisions in *Kingfisher*? Mr Hitchmough contends that any benefit enjoyed by the dancer in being able to sell services to non-cash customers is a benefit which arises incidentally as a result of the Secrets deciding to offer Secrets money within the club. Secrets money was introduced to encourage the patrons to stay at the club ordering more refreshment after they have run out of cash. The dancer may enjoy a benefit from this but this is not something she is contracting for and it is not something for which she pays the 20 per cent commission. All she receives for the additional 20 per cent commission is the encashment of the voucher. This view is supported, Mr Hitchmough submits by the fact, as found by the Tribunal, that some of the vouchers redeemed by the dancers were in fact given to waiters or barmen as tips or were received from another dancer in settlement of some transaction between them. As regards those vouchers, there can be no question of the dancer receiving 'performance facilitation services' for the 20 per cent deduction she pays on redemption – all she receives is the encashment service either on her own behalf or on behalf of someone else.

42. In my judgment, the *Kingfisher* case establishes that when a voucher is redeemed of the kind in issue here, there is more than the encashment that is being provided. It is, at the least, the whole voucher system. I agree with Miss McCarthy's submission that *Kingfisher* and *Diners Club* show that the scope of the supply in the case of a credit card scheme, and schemes akin to a credit card scheme is determined not just by looking at the final step in the transaction, namely the presentation of the voucher for payment but at the whole scheme, including giving

the retailer access to the customers it could otherwise access. As Neuberger J said in *Kingfisher* the benefit that Woolworth derived from Provident was not merely the payment of money: it was the right to be included in the scheme operated by Provident and the ability to redeem the vouchers. Without Provident's consent, Woolworth could not benefit from the scheme. It could not, for instance, advertise the fact that it was prepared to accept Provident's vouchers for purchase of goods in their stores. Similarly in the present case, the benefit that the dancer derives from the Secrets money is the right to be included in the scheme which the clubs set up for patrons to be able to pay for entertainment at the club even though they have no cash. Without the club's role in operating the Secrets money scheme, the dancer would not be able to accept the invitation of non-cash customers to dance at their table or provide them with table company.

43. The next question is, if the services provided go beyond the encashment of the voucher at the end of the evening, what is the precise scope of the composite service? That must be established before one can consider whether the nature of the service is that of an exempt service or not. Mr Hitchmough argues that if I find that the service provided for the 20 per cent commission is a composite service and not just the pure encashment of the voucher, then the elements of the composite service are no more than were provided by the credit card company in *Diners Club* or by Provident in *Kingfisher*. In both those cases the court held that the service provided was an exempt service because it could not be distinguished from the service provided by a credit card company to a retailer.

44. However, there is a significant difference between the Secrets voucher scheme and the credit card service or the Provident vouchers service. In a credit card scheme, the retailer provides the goods to the consumer who presents the voucher at the retailer's premises without any further assistance from the issuer of the vouchers or credit card. The retailer is solely responsible for providing the infrastructure, ambiance etc to attract the consumers to come and spend their vouchers in its stores. In the present case, the retailer, that is the dancer, cannot provide the service for which she receives the voucher from the patron without the facilities of the club. It is the club which attracts the patrons and provides them and her with the facilities needed for her to perform table dances and offer table company to non-cash customers. For the dancer to make money from non-cash customers she not only needs the Secrets money scheme but the rest of the facilities that are provided by the club to her and to the patrons as the environment in which she can earn money.

45. It is necessary then to consider whether these services provided to the dancer by the club when she performs dances etc for non-cash customers should be regarded as distinct and independent supplies or are, together with the encashment of the vouchers at the end of the evening, so closely linked that they form a single indivisible economic supply which it would be artificial to split. That formulation of the test comes from the decision of the Upper Tribunal in *Honourable Society of Middle Temple v RCC* [2013] UKUT 250 (TCC), [2013] STC 1998. The Upper Tribunal held that when considering whether it would be artificial to split the different services, one must look at the supply from the point of view of a typical

customer to see if the customer would regard the different elements as inseparable and indispensable. They also held that it was irrelevant that in other circumstances, the different elements can be or are supplied separately by a third party. I was also referred to the decision of *Byrom and others (trading as Salon 24) v RCC* [2006] EWHC 111 (Ch) where Warren J was considering the supply of services to a masseuse including the licence to occupy the room where the masseuse could operate her business. The judge held that the taxpayer had provided a range of services to the masseuse including bed linen, towels and washing facilities. He held that the description of the services which reflected economic and social reality was a supply of massage parlour services, one element of which was the provision of the room.

46. It is true that the dancer does not have to accept Secrets money and that she pays separately for entrance to the club. However it was not suggested that there are many, if any, dancers who refuse to accept Secrets vouchers and it is difficult to see why any dancer would choose to limit her earning ability in this way. Looking at the matter from her point of view, she will only agree to accept Secrets money if she makes use of the rest of the club's facilities to perform dances for non-cash customers. The club provides a bundle of services to the dancer all of which are important for her to be able to make the best use of the facilities at the club to earn her living. It is artificial to split the Secrets vouchers scheme from the other services provided by the club to the dancer to be able to provide dances and table company to non-cash patrons.

47. Further, I agree with HMRC's submission that the size of the commission is an indication that the dancer is paying for much more than encashment or for the narrow composite service of access to the Secrets money scheme. As discussed earlier, the clubs are not taking on a credit risk on behalf of the dancer because they are paid by credit card for the vouchers. In *Kingfisher* Neuberger J considered whether a commission of 10 per cent charged by Provident was likely to reflect payment for the limited scope of services that HMRC contended was the totality of what was provided. He held that it was because of the more risky credit profile of Provident's customers. I agree that the 20 per cent charge reflects the fact that the dancer cannot provide her services to the non-cash customers without the much wider bundle of facilities and services provided by the clubs to create the environment in which the dancer can earn the Secrets money. That is what she is paying for.

48. This conclusion is not undermined by the fact that the vouchers are also redeemed by dancers on behalf of waiters or in settlement of a debt owed to her by another dancer. That is not the purpose for which the scheme is operated. Clearly the 20 per cent commission has to be charged on those encashments too because it would be too difficult to police a differential commission rate since the club does not monitor how many dances the dancer performs during the evening.

49. I therefore hold that the 20 per cent commission payment charged by the club on redeeming the Secrets money is a payment in return for services which go significantly beyond the simple receipt or dealing with security for money for the

purposes of Item 1. The services provided can accurately be described as the provision of the means whereby the dancers can exploit the opportunity to make more supplies to a wider market thereby increasing their turnover by facilitating the dancers' performances to the non-cash customer base.

50. Finally, looking at the nature of the services provided they are in my judgment clearly taxable supplies and not exempt supplies. They go significantly beyond what is described in Item 1.

51. I do not consider it is necessary for me to consider whether the Tribunal went further than it needed to in referring in paragraph 88 to the supply to the dancers comprising a bundle of services supplied in return for both the entrance fee and the 20 per cent commission. Even if one disregards the entrance fee and looks only at the 20 per cent commission, the services supplied in return for that payment constitute, in economic reality, a taxable and not an exempt supply.

52. In the light of the findings set out above, I dismiss Secrets' appeal.

TRIBUNAL JUDGE:

Mrs Justice Rose, President of the Upper Tribunal (Tax and Chancery Chamber)

RELEASE DATE: 1 July 2015