TC03255

Appeal number: TC/2010/03421

VAT – whether face-value vouchers issued by appellant companies and paid for by patrons using debit and credit cards for use in payment for dancers' services in appellant companies' lap dancing clubs and subsequently redeemed by dancers dealings in credit guarantees or any other security and on redemption exempt from VAT– item 1 Group 5 Schedule 9 to VATA 1994 – yes – whether dealings in vouchers separate dealings in security for money – no - redemption of vouchers held to be ancillary part of overall composite taxable supply of performance facilitation services by appellants – appeals dismissed

FIRST-TIER TRIBUNAL
TAX CHAMBER

WILTONPARK LTD **Appellant**
SECRETS (PROMOTIONS) LTD
SECRETS (HOLBORN) LTD
SECRETS (EUSTON) LTD
SECRETS (ST KATHERINE'S) LTD
- and -
THE COMMISSIONERS FOR HER MAJESTY'S REVENUE & CUSTOMS **Respondents**

TRIBUNAL: JUDGE DAVID DEMACK
MARK BUFFERY

Sitting in public in London on 29 – 31 July 2013

Barrie Akin of counsel, instructed by Sanghvi Ruparelia chartered certified accountants of London, for the Appellant

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

DECISION

Introduction

1. Wiltonpark Ltd, Secrets (Promotions) Ltd, Secrets (Holborn) Ltd, Secrets (St Katherine's) Ltd, and Secrets (Euston) Ltd, the five companies whose appeals are before us, are all subsidiary companies of SL LH Holdings Ltd ("Holdings"), and form the Secrets group of companies. Each company operates what it describes as a licensed lap dancing or table dancing club in London where, amongst other things, dancers perform stage and table side dances for the entertainment of club patrons, who pay the dancers for their services. All the companies trade under the name or style of "Secrets". But that is not to say that they operate identically; they do not, but the differences in operation are minor and irrelevant to the decision we are required to make.

2. The appeals concern the correct treatment of transactions involving "Secrets money", i.e. vouchers issued by the Secrets companies which enable patrons to continue spending money in a club when they have run out of cash. Briefly stated, when a club patron has run out of cash but wishes to continue to spend money on entertainment and refreshments, he may use a debit or credit card to purchase from the relevant company, say, a £100 face-value voucher of Secrets money. The company charges him commission of 20% for that service, so that he pays £120 for the voucher. Assuming he applies the voucher in payment of a dancer's fees, at the end of the evening she applies to the company to redeem it. Its terms for doing so are that it pays her £80, and retains £20, i.e. it charges 20% for that service.

3. It is common ground that the 20% commission charged by the company for each Secrets money voucher to a patron is consideration for a taxable supply, see paras 2 and 4 of Schedule 10 to the Value Added Tax Act 1994 ("VATA"). It is also common ground that the 20% commission retained by the company on redeeming a voucher held by a dancer is consideration for a supply by the company to the dancer. The issue in the appeal is: what is the nature of that supply? Is it a taxable or exempt supply?

4. The Secrets companies claim to make supplies of a narrowly defined service to the dancer comprising "dealings in credit guarantees or any other security for money", and that such supplies fall within the exemption provided by Item 1, Group 5 of Schedule 9 to VATA (see para 52 below).

5. HMRC's primary contention is that Secrets money is not a security for money. Alternatively, they claim that the economic reality is that the Secrets companies are not dealing in securities for money, but are providing the dancers with a corporate supply of the opportunity and resources to supply their services to a wider market than would otherwise be available to them, and Secrets money is the means by which they can supply that market. HMRC maintain that such a supply may be characterised as performance facilitation services and is taxable.

6. There are two sets of appeals by the five appellant companies. The first set concerns claims all made on 14 July 2009 as follows:

Appellant	Return periods	Value of claim under s.80 VATA
Wiltonpark Ltd	05/06-05/09	£106,328
Secrets (Promotions) Ltd	05/06-05/09	£24,310
Secrets (Holborn) Ltd	05/06-05/09	£197,997
Secrets (Euston) Ltd	05/06-05/09	£110,552
Secrets (St Katherine's) Ltd	05/06-05/09	£67,793
Total		£506,980

7. HMRC rejected all five claims on 12 November 2009. The Appellant companies requested a review on 15 December 2009 and, on review, all the rejections were upheld. The tribunal directed that the five subsequent appeals the companies made against the refusal of the claims be consolidated.

8. HMRC understand that from 1 August 2009 to 30 November 2009, the appellant companies treated the relevant supplies as exempt. However, they were unable to obtain confirmation as to precisely how the supplies from 1 June 2009 to 31 July 2009 were treated. Consequently, they raised the following assessments on a best judgment basis:

Appellant	Return periods	Date Notification of Assessment	Value of Assessment
Wiltonpark Ltd	08/09 – 11/09	22 March 2013	£11.581
Secrets (Promotions) Ltd	08/09 – 11/09	22 March 2013	£4,424
Secrets (Holborn) Ltd	08/09 – 11/09	22 March 2013	£12,109
Secrets (Euston) Ltd	01/09	22 March 2013	£12,212
Secrets (St Katherine's) Ltd	11/09	22 March 2013	£1,953
Total			£42,278

9. Appeals against those assessments form the second set of appeals. On 22 July 2013, the Tribunal directed that the appeals against the assessments also be consolidated and that they be heard together with the earlier appeals.

10. The total VAT at stake under the joined appeals is therefore £549,258.

11. Mr Barrie Akin of counsel appeared for the five appellant companies. HMRC were represented by Miss Hui Ling McCarthy, also of counsel. They presented us with three bundles of copy documents, and a bundle of legislation and authorities.

12. We received oral evidence from two witnesses, Mr Stephen Less, a director and shareholder of Holdings, and Mr Jayant Sanghvi, a chartered certified accountant acting for Holdings and the appellant companies. From their evidence, and the documents before us, we make the findings of fact which follow.

The facts

13. By way of introduction, Mr Less explained that each of the appellant companies operates an individual business from rented premises, all the clubs being furnished similarly to give the same "feel" and general ambience. The basic pattern of business, including the issuing and redemption of Secrets money, the kinds of food and drink sold and their prices, and the way in which patrons and dancers are charged for entry to each club, are similar, but not identical. The terms on which dancers operate and the way in which they earn money from patrons are also very similar, but again not identical. For instance, patrons and dancers entry fees vary from club to club. We might add that patrons are almost invariably male.

14. Mr Less also explained, and we accept, that the dancers at Secrets clubs do not perform on a patron's lap, or on a table. They dance on a stage or close to where a patron is seated.

15. The Secrets group in fact consists of six companies, the five which have appealed and Secrets (Western) Ltd. The last mentioned, which operates from Covent Garden, started trading after the periods the subject of the appeals, so that its trading is irrelevant in the present context. Wiltonpark Ltd trades from Hammersmith, Secrets (Promotions) Ltd from Finchley, Secrets (Holborn) Ltd from Holborn, Secrets (St Katherine's) Ltd from East Smithfield, and Secrets (Euston) Ltd from Euston. Although the six companies form a group for certain purposes, they do not form a VAT group, each one being separately registered for VAT.

16. Each company holds a premises licence under the Licensing Act 2003 issued by the local authority responsible for the area in which it trades. Although the conditions imposed by the licences vary from authority to authority, it is a fundamental requirement of each licence that there is no sexual physical contact between a patron and a dancer. The licences permit the sale of alcohol, regulate opening hours, specify limitations to be observed by dancers, and deal with other requirements such as fire safety and other regulatory requirements.

17. The group has a code of conduct which all dancers at Secrets clubs must strictly observe. The relevant parts of it, as taken from its most recent version, take the following form:

"CODE OF CONDUCT FOR TABLE DANCERS

1. INTRODUCTION

As a Dancer attending Secrets you will be expected to conduct yourself in a mature manner, at all times. Your sincerity, courtesy, thoughtfulness and friendliness should create a positive atmosphere in which customers can relax, which should encourage them to return again and again. Every Dancer's behaviour and performance at Secrets is important.

. . .

6. OPENING TIMES

All Secrets venues open at 8.00pm with the exception of Secrets Holborn which opens at 7.30pm. Last orders are called at 3.00am …(All Secrets venues are closed on Sundays.)

. . .

9. DANCERS ENTRY FEES

Dancers must check in with the Dancer Co-ordinator when arriving and pay their entry fee. The payment, which varies from day to day, must be paid in full upon entry (see tariff).

. . .

11. DRESS CODE

The Dancers dress code is extremely important both for your and Secrets image. You are requested to wear long evening dresses and thin high-heeled shoes. Hair, make-up and jewellery should always be of the highest standard. Whilst you are in the public areas of Secrets, you must put your clothing back on immediately after each performance and remain clothed until your next performance begins.

. . .

16. STAGE AND TABLESIDE DANCING (NOT A CHARGE IMPOSED BY SECRETS)

It is customary for Dancers to expect to receive a customer's gratuity, per single track, of £10 for each topless dance and £20 for each fully nude dance. Dancers are requested to dance at the table where customers are seated. Dancers are also requested to promote themselves by performing their stage signature dance in order to make the customer more aware of each Dancer.

. . .

18. TABLE GRATUITY (NOT A CHARGE IMPOSED BY SECRETS)

If a customer invites you to the table, for any long period of time, you are advised to make it clear that whilst you are sitting with them, as their guest, it is the usual practice for a customer to offer a gratuity for table accompaniment. The Management (purely as a suggestion) suggests that you should receive £250

per hour or part thereof, for the time that you are seated with a customer at their table.

If the customer has agreed to give you a £250 gratuity for table company Secrets suggest that you give the customer value for money by including as many dances as they request.

19. YOUR GRATUITIES

It is the Dancer's responsibility to collect any gratuities that the customer may give for table, stage dancing or table company with a customer (see clause 18). If possible, the amount should be discussed or agreed with the customer, which can be received after or prior to the dance being performed. Secrets staff or management will not become involved in collecting any gratuities if the customer does not give the Dancer a gratuity.

. . .

21. SECRETS MONEY

In the event that customers are short of cash to tip the Dancer for her table or stage dance or for sitting at their table, Secrets Money is available for customers to acquire, via their credit/debit card or other currency. These can be exchanged at the end of the evening, via the Dancer Co-ordinator or Manager, for UK sterling, subject to the cashing up of the Secrets Money commission in force, at the time.

22. YOUR CONDUCT WHILE PERFORMING

Secrets is licensed by the Local Authority and certain Rules and Regulations apply. You, as a self employed person, operating in licensed premises, have to operate in accordance with the rules. Full rules are on display in the premises.

23. DEALING WITH CUSTOMERS

a. When speaking to a customer, you may not use language of a sexually graphic nature at any time.

b. Whilst within Secrets, you must never be in the company of a customer except in an area open to the public.

c. You may never give a customer your telephone number, address or other contact details.

d. As a general rule, you may never arrange to meet a customer outside Secrets.

24. LEAVING AND LEAVING EARLY

All Dancers are expected to remain in Secrets until closing time.

. . .

27. HOUSE RULES

Dancers should also abide by the general house rules, which are applicable to the branch of Secrets where you are dancing. Any variation of these rules will be notified to you.

ZERO TOLERANCE GENERAL VIOLATIONS

The following is a list of violations, which, if contravened, may result in instant removal from Secrets.

28. RUDENESS TO ANY CUSTOMER

. . .

29. DISHONESTY

. . .

30. FIGHTING

. . .

31. INTENTIONAL MISUSE OR DESTRUCTION

Disclosure of any confidential company information

. . .

34. REPEATED FAILURE TO FOLLOW ANY ADVICE REGARDING YOUR PERFORMANCE OR BEHAVIOUR

. . .

37. GAMBLING

. . .

38. PROSTITUTION

. . .”

18. In his evidence, Mr Less added to a number of the points contained in the code of conduct, and we proceed to include those additions. He said that the companies 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.

19. Mr Less described a typical patron’s experience at a Secrets club from entry to departure in the following way. On entry he is met at the reception desk near to which is a cloakroom. He is required to pay an admission fee of up to £20 depending on the time of entry and the venue. Exceptionally, patrons who arrive early in the evening or have a complimentary admission voucher are admitted free of charge. If he wishes to deposit a coat or briefcase in the cloakroom, the patron is charged an extra fee and is provided with a receipt. It is common ground that entry fees and cloakroom charges are standard rated supplies for VAT purposes, and that each company has accounted for VAT on them.

20. Various notices are prominently displayed near each club entrance. They are intended to regulate the conduct of patrons and to explain to them what they should and should not do whilst on club premises. One such notice, entitled "Important Guidelines", is rehearsed in the Schedule to our decision.

21. In return for his admission fee a patron is entitled to remain on club premises until the club closes for the night, and to watch dancers perform on stage. Assuming he requires no additional services from a dancer or refreshments, he pays nothing more.

22. Each club provides waiter service to patrons. Waiters take orders for food and drink and sell Secrets money to patrons. Payment for refreshments and Secrets money can either be made in cash, or by means of a debit or credit card. If a patron wishes to purchase Secrets money the waiter completes a slip on which are set out the patron's name, the time and date of the transaction, the value and denominations of Secrets money bought, the commission charged by the company running the particular club, and the amount paid. The bar cashier issues the appropriate number and denomination of Secrets money vouchers and records their numbers on the slip. The patron acknowledges receipt of the vouchers by signing the slip. He is given a till receipt and a copy of the debit or credit card transaction slip produced by the transaction. The premises manager also signs the slip. (As we understand it, a similar process follows transactions in which a patron wishes to convert foreign currency into sterling).

23. Mr Less went on to explain the provisions made to ensure that patrons obtain what he described as "the full Secrets experience". Patrons are permitted to sit at tables in the general area of a club, but also may sit in what is known as the VIP area if they pay a cover charge of £10 and purchase a bottle of champagne.

24. Each club has a stage area on which the dancers perform. Dancers performances on stage are provided free of charge to patrons. The performances also serve as a form of advertising for the dancers, who earn their own fees from patrons for performing individual dances and for table company (see para 26 below). The club selects dancers for stage performances, and they are expected to perform in accordance with a prepared rota, except when engaged with a particular patron. The Secrets companies do not pay the dancers for stage performances, but if patrons wish they can show their own appreciation by paying the dancers.

25. If a patron invites a dancer to perform individual dances for him, assuming she agrees to do so, she performs near to the table of and solely for the patron extending the invitation, and not on stage. Negotiations of the terms leading to such performances are entirely a matter for discussion between dancer and patron. Although the Secrets companies suggest a "gratuity" for each music track danced, they have no knowledge of the terms of dance transactions, and do not assist in extracting payment from unwilling patrons.

26. Patrons may ask dancers to sit and converse with them. This is known as "table company". Again, the Secrets companies suggest a rate for the purpose, in this case based on time spent. But, once more, negotiations for the purpose are a matter for the

parties, and the companies play no part in resolving any dispute that may arise between them.

27. Mr Less claimed that, generally speaking, patrons prefer to pay for entertainment at Secrets venues by credit or debit card. He disclosed that all the Secrets companies take such cards, but that the dancers do not. Consequently, since the companies are not party to the contracts between patrons and dancers for the latters' services, patrons are effectively restricted to paying dancers in cash or by means of Secrets money.

28. Dancers are paid for their services either in cash or with Secrets money. As the companies play no part in negotiating transactions between patrons and dancers, they do not know how much the former pay in cash and how much in Secrets money. The companies acknowledge that some patrons prefer to pay in cash to avoid paying the 20% commission they charge for Secrets money.

29. The Secrets companies admit that occasionally patrons do leave a club to withdraw cash from nearby ATMs, but Mr Less explained that the group has never considered installing ATMs in its clubs mainly because many customers would be unable to withdraw from them enough cash for their needs given the limits imposed by card issuers and/or ATM providers. Limits for cash withdrawals from ATMs vary between £100 and £500 per day.

30. The appellant companies originally treated commission charged by them in excess of face value on issue of Secrets money and the amounts charged to dancers on redemption of Secrets money as consideration for VAT inclusive standard rated supplies and accounted for it to HMRC accordingly.

Secrets money.

31. Secrets money did not originally form part of the Secrets group's business model; patrons could only pay dancers in cash, although they could use credit cards to purchase refreshments. That had a limiting effect on the business; patrons unable to pay dancers were less inclined to stay to purchase refreshments. The group therefore introduced Secrets money. Initially it could only be used to tip or pay dancers. Use of it to pay for refreshments was first permitted in May 2006.

32. Secrets money vouchers are produced on colour printed 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. 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."

33. Secrets money vouchers contain no promise to pay dancer holders or anyone else their value. Nevertheless dancers are able to redeem Secrets money by presenting vouchers to the company operating the club at which they dance, in which case they receive their face value less the company's 20% commission.

34. We earlier set out the basic terms on which the Secrets companies issue and redeem Secrets money (see para 3 above). At each club there are notices setting out the terms and conditions attaching to Secrets money. They take the following form:

"Secrets Money

Terms and Conditions

1. Secrets Money:-

a) Can be obtained via your credit/debit card or other currency.

b) Can be used for the payment of drinks, food, service charge, entrance fees and tipping staff and dancers. Any change will be given in Secrets Money.

c) Is only valid in the Secrets venue it was obtained.

d) Will be subject to a commission of 20% (Twenty percent) which will be added to the face value of the Secrets Money.

e) Once obtained is non-refundable.

2. If the Secrets Money is to be used on a day other than the day of issue, the Secrets Money must be validated before use.

The validation process (for security purposes) is as follows:-

a) You must present the Secrets Money for validation to the Manager on arrival at the SECRETS venue from which it was obtained.

b) SECRETS will then check that the Secrets Money has not been used before. Checking process may take up to 7 days.

c) You may be required to show proof of acquisition of the Secrets Money, including the credit/debit card and the receipt originally used to acquire the Secrets Money."

35. As the terms and conditions state, strictly speaking, Secrets money is not redeemable by patrons; they have no right to a refund. However, in exceptional circumstances it will be redeemed, e.g. as a goodwill gesture, again less the 20% commission. Any change provided to a patron is given in Secrets money.

36. It follows that the rights attaching to Secrets money vouchers vary depending on whether they are held by patrons or dancers.

The dancers

37. Mr Less described the dancers who work at Secrets clubs as being "mostly young presentable women who have their own unique way of dancing and entertaining customers". The Secrets group takes steps to ensure that all its dancers have the right to be in the UK, or are permitted to work here. All the dancers are self-employed but, so far the group is aware, none is registered for VAT.

38. The group recruits dancers through adverts in "The Stage" magazine, its website, and by word of mouth. It holds weekly auditions, and at any one time has approximately 500 dancers in its "pool". Dancers tend to work three nights a week on average.

39. Each dancer is charged a daily entrance fee to the club at which she is dancing. The amount thereof is determined by the Secrets employee at that club responsible for the welfare of the dancers, known as the housemother. In assessing the appropriate amount, she takes into account the venue concerned, the day of the week, the time at which the dancer arrives, and how busy the venue is that evening. By way of example, we were told that dancers at the Holborn club were required to pay £80 per night from October 2005 onwards. Although the house rules provide that the entrance fee must be paid in full on a dancer's entry to the club, it may in fact be paid in part at that stage with the balance being paid, either in cash or by the redemption of Secrets money (less the usual 20% charge), at the end of the evening.

40. We earlier observed that the Secrets group has no right to any part of a dancer's earnings, and does not know the extent of the earnings of individuals. It does not monitor how many dances a dancer has performed, whether she has been paid in cash or by the use of Secrets money, or require dancers to disclose their earnings.

41. Although the Secrets venues are primarily known as table or lap dancing clubs, the individual companies running them derive their income from entrance fees from both dancers and patrons, cloakroom charges, the sale of (mainly alcoholic) drinks and food, and commissions on Secrets money on acquisition from patrons and from dancers on redemption.

42. For security reasons, each group company redeems Secrets money dancers have received at the club immediately after close of business each night, and at no other

times. In order to redeem vouchers, dancers must tender them to the premises manager. He or she examines all those tendered and, assuming they are in order, accounts to a dancer for £80 of each £100 of their face value.

43. The group accepts that dancers use Secrets money to settle debts between themselves, and that dancers redeem Secrets money for bar staff who have been given it as tips by patrons. It takes no objection to their doing so.

Secrets money – the patron/club transaction

44. Mr Sanghvi claimed that the Secrets companies are not guaranteed payment where a patron has made payment for Secrets money by debit or credit card, even though they have obtained an authorisation code, saying that even if a company had cogent evidence that a patron was in fact present and participated in a transaction, a card issuer would apply a chargeback (i.e. void a transaction and deduct an amount credited to the company's bank account) if the patron supplied a signed declaration stating that he did not take part in the transaction. The most frequently used reason for a chargeback was that a patron had been "debited" with a transaction twice. Mr Sanghvi explained that in most instances of chargeback, the company concerned had been able to show that the cardholder had been present, or that he had entered into two different transactions at the same value. He expressed the belief 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. In two cases to which we were referred (one of which involved over £6,500), the company concerned had successfully defended such proceedings.

45. For the purpose of effecting credit and debit card sales of Secrets money and also sales of food and drink, each of the appellant companies has entered an agreement with both Streamline (a card processing service provided by WorldPay (UK) Limited on behalf of National Westminster Bank plc) and American Express ("Amex"). Under the agreements Streamline and Amex provide the appellant companies with merchant acquirer services.

46. The agreements with Streamline cover the use of all credit and debit cards (including VISA, MasterCard, Switch, Maestro and Electron). The agreements with Amex cover the use of Amex cards.

47. Under the terms of each agreement, Streamline and Amex charge a negotiated fee per credit or debit card transaction. The "floor limit" (below which transactions do not require authorisation) is set at zero, meaning that each company is required to obtain authorisation from Streamline and Amex in respect of every credit and debit card transaction before accepting the payment.

48. Under the general terms and conditions in place, Streamline and Amex are entitled to "chargeback" any amounts paid to an appellant company where those amounts are not settled by the patron's card issuer. The appellant companies are at risk of chargeback for a period of 18 months after a transaction has taken place.

49. 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. Consequently, the proportion of chargebacks the Secrets companies suffered in relation to sales of Secrets Money was less than 0.07%.

50. Where a patron chooses to pay for Secrets money by way of credit or debit card, the amount of the transaction is entered into a handheld terminal (rented from Streamline) by a waiter in the club conerned. The patron is required to verify the transaction by entering his personal identification number (PIN) using the terminal. The data passes from the handheld terminal, via a secure network provided, to either Streamline or Amex (depending on the type of card used) for the purpose of seeking authorisation for the transactions. Such authorisation is usually received in seconds. Streamline and Amex seek payment from the customer's card issuer bank and, once settlement has been confirmed, which inevitably takes more time, than elapses from the time of a particular transaction to a company redeeming Secrets money then transfers the funds to the relevant appellant company's bank account. The company concerned does not directly obtain the authorisation of the credit or debit card payment from the customer's card issuer bank, that authorisation being obtained by Streamline and Amex.

51. Both Streamline and Amex notify the individual appellant companies on a monthly basis of the amount of the transaction charges they owe and of the amount of the total transaction payments owed by them to the companies. In the case of Amex, the transaction charges are deducted from the total transaction payments to give a net figure. Streamline and Amex pay over the sums owed to the individual Secrets companies once the settlement amounts have been confirmed. Evidence was adduced, and we accept, that between 1 and 12 days elapsed between the date of a Secrets group transaction and the date on which it received credit in its bank accounts from Streamline and Amex during the period with which we are concerned.

The relevant legislation

52. At the time of the earlier transactions with which we are concerned, the relevant article in the Sixth VAT Directive was Article 13B. It provided (so far as is relevant):

> "Without prejudice to other Community provisions, Member states shall exempt the following under conditions which they shall lay down for the purpose of ensuring the correct straightforward application of the exemptions and of preventing any possible evasion, avoidance and abuse:
>
> . . .
>
> (d) the following transactions:

> . . .
>
> 2. the negotiation of or any dealings in credit guarantees or any other security for money and the management of credit guarantees by the person who is granting the credit;
>
> . . ."

53. From 1 January 2007, art.13B(d)2 was replaced (in identical form) by art. 135(1)(c) of the Principal VAT Directive.

54. The article was transposed into domestic legislation as Item 1 of Group 5 of Sch.9 to VATA 1994. It provides:

> "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."

Discussion, submissions and conclusion

55. In support of the appellant companies' claim that Secrets money is "any security or money" within Item 1 of Group 5 of Schedule 9 to VATA, Mr Akin relies on the definition of that phrase offered by the VAT tribunal in the appeal of *Dyrham Park Country Club v HMCE* (1978) Decision No 700. In that case, members of a country club were required to subscribe for loan notes (referred to in the decision as "Bonds") for £350 at a premium. The Bonds created an obligation on the company to repay the sum of £350 to the registered holder in the event of the company going into liquidation whilst he remained a member or within five years thereafter. The question for the Tribunal was whether the issue of the Bonds fell within the exemption provided by the predecessor legislation to item 1 of Group 5 of Schedule 9 to VATA, or whether it comprised another element of taxable club membership fees. In the context of the underlying lending arrangement, the Tribunal held that each Bond was a "security for money" because that phrase meant:

> "… a document under seal or under hand at a consideration containing a covenant, promise or undertaking to pay a sum of money."

56. The tribunal went on to say that the document had neither to be marketable, transferable or negotiable.

57. Mr Akin further relies on the following passage from the decision of the tribunal in *Kingfisher plc v HMCE* (1999) Decision No. 16332, where the tribunal was dealing with vouchers issued by Provident Financial Services to its customers and used by them to buy goods from Woolworths:

> "The service supplied by Provident in the second transaction can, I think, fairly be described as a supply consisting of the receipt or dealing with a 'security for money'. 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 service has similar features to the services supplied by credit card companies and credit cards are referred to in Note (4) to Group 5."

58. He maintains that use of the word "moreover" in the final sentence of that quotation is a clear indication that a service having features similar to those supplied by credit card companies reinforces the conclusion reached in that case because Note (4) to Group 5 says:

> "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 and services."

59. In approving the tribunal's conclusion, the High Court (see *Kingfisher plc v HMCE* [2000] STC 992 at paras 69 to 74) noted that Note (4) to Group 5 extends the exemption to credit card operators. Mr Akin submits that it must follow that a security for money can be issued without the issuer being a person within Note (4). Or to test it another way, he asks: where was the credit card or quasi-credit card operation in *Dyrham Park*?

60. He further contends that attempts to restrict the Group 5 exemption to financial institutions, or to bodies participating in the financial sector, have been rebuffed by the courts, see *Sparkassernes Datacenter v Skatteministeriet* [1997] STC 932 at para 38, *RCC v Axa UK plc* [2008] STC 209 at paras 69 to 73, and *National Exhibition Centre v HMRC* [2013] UKFTT 289 (TC) at para 64.

61. Mr Akin next submits that the statutory definition of a "security for money" does not require the issuer to bear any credit risk; it matters not that Secrets is not a credit card operator, financial institution or other body participating in the financial sector. He adds that it is noteworthy that, at the time covered by the five appeals, HMRC regarded vouchers as "security for money" at the point they could be exchanged for money (see Notice 701/49/09 at para 3.2). Nevertheless, if contrary to his contention we were to find that there was an element of credit risk on the Secrets companies' part, Mr Sanghvi's evidence showed that they suffered a significant exposure to credit risk after Secrets money had already been encashed.

62. Miss McCarthy submits that Secrets money falls outside the exemption provided for by item 1 of Group 5 because:

a. it is unclear from the wording of the EU Directive and EU case law that an instrument is not a "security for money" within the meaning of the exemption unless there is, at least, a lending or credit (guarantee) arrangement underpinning the transaction;

b. a mere obligation to pay money outside the context of the granting of credit or lending of money is insufficient. Thus the transactions at issue in the *Kingfisher* case can be distinguished from those in the present one;
c. the Secrets companies do not suffer a "significant exposure to credit risk" as a result of the chargebacks. Any credit risk suffered is *de minimis* and does not correlate to the fees they charge patrons and dancers to use Secrets money. The companies are in no different position from any retailer who accepts payment by credit or debit card;
d. HMRC's guidance relied on by the companies is not apt to cover Secrets money – but even if it is, the question of whether HMRC acted outside the scope of its own guidance is outside the Tribunal's jurisdiction.

63. Further, Miss McCarthy maintains, the credit risk to which the Secrets companies are exposed is not that of an ordinary retailer dealing with customers; Secrets money is purchased by patrons and redeemed by dancers. The companies have no recourse against dancers for recovering cash paid to them on redemption, and accordingly bear a risk both before and after encashment of Secrets money.

64. Looking at the economic reality, as suggested by the European Court of Justice ("the ECJ") in (Case C-53/09) *R&CC v Loyalty Management UK Ltd* [2010] STC 2651 at [39] ND and applied by the Supreme Court in *R&CC v Aimia Coalition Loyalty UK Ltd (formerly known as Loyalty Management UK Ltd)* [2013] UKSC 15, Miss McCarthy submits that since exemptions from VAT are to be strictly construed, only supplies which fall within the objective or aim of the exemption can qualify (see (Case C-348/87) *Stichting Uitvoering Financiële Acties v Staatssecretaris van Financiën* [1989] ECR 1737 at [12] and [13]). She observes that the purpose of the exemption in point in the appeal was explained by the ECJ in Case C-455/05 *Velvet & Steel Immobilien* at [24] as being:

> "… to alleviate the difficulties connected with determining the tax base and the amount of VAT deductible and to avoid an increase in the cost of consumer credit."

65. In *CEC v Electronic Data Systems Ltd* [2003] STC 688, reflecting a statement in [24] of C-231/07 and C-232/07 *Tierce Ladbroke SA and Derby SA v Belgian State*, the Court of Appeal held at [135] that in order to fall within the relevant finance exemption:

> "… the services provided by EDS 'must, viewed broadly, form a distinct whole, fulfilling in effect the specific, essential functions' of an exempt transaction".

66. Miss McCarthy maintains that the focus of art.135(1)(c) is on credit guarantees, that is to say the assumption of credit risk (i.e. transferring the risk of default), and contends that this is reflected by the use of the word "security" in the phrase "security for money". As Roskill LJ held in *C&EC v Guy Butler (International) Ltd* [1976] STC 254 at 258:

> "… the phrase 'any security for money' in item 1, the word 'security' is itself there undefined but would appear to be used in the ordinary sense, that is to say some instrument whereby the indebtedness of the borrower to the lender is by some means 'secured'."

67. In relation to Secrets attempt to align itself with the position of the vouchers issued by Provident in *Kingfisher*, Miss McCarthy submits that that case can readily be distinguished. Provident was a company providing credit facilities, including the sale of vouchers on credit to customers. Customers were able to use the vouchers to purchase goods from retailers (including Woolworth) who were members of the relevant Provident scheme without having to pay any cash to the retailer. In turn, the retailer would redeem the voucher from Provident for the cash amount of the voucher, less a discount of 10%. Provident was left to collect the money from the customers, pursuant to the terms of its credit agreement with the customers. Consequently, Provident bore the financial risk of customers defaulting – Woolworth and the other retailers in effect having transferred that credit risk for 10% of the value of the vouchers. Miss McCarthy maintains that to be quite different from the present case for, unlike Provident, the Secrets companies do not extend credit to their customers.

68. Whilst accepting that the Secrets companies from time to time suffer "chargebacks", Miss McCarthy submits that they merely reflect the instances where a patron queries his credit card bill: the evidence shows the "risk" borne by the Secrets companies to be minimal. From the point of view of financial risk, the Secrets companies are in no different a position to a retailer selling gift vouchers whose customers are able to buy using a credit or debit card. The risk of chargebacks differs from the assumption of a true credit risk – i.e. the risk that a customer will default on the payment altogether. In *Kingfisher*, Provident assumed this risk; here, the risk of default is not assumed by the Secrets companies, but by either the merchant acquirer or the card issuer.

69. Further accepting that VAT Notice 701/49/09 at para 3.2 refers to a face value voucher as becoming a security for money at the point at which it is presented to a third party to be exchanged for money, Miss McCarthy observes that it is expressly said to be in the context of retail schemes (such as that in *Kingfisher*). Such schemes involve a tripartite agreement between an issuer, a customer and a retailer (where the issuer collects payments from the customer in arrears). No such tripartite arrangement exists in the present case (dancers are not obliged to provide their services on the presentation of Secrets money) and the dancers cannot sensibly be considered to be "retailers" as that word is generally understood.

70. In our judgment, Secrets money is a security for money. It clearly falls within the statutory definition provided by item I of Group 5 of Schedule 9 to VATA. We agree with Mr Akin that "security" has a wide meaning, and nothing within VATA 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. We accept as correct Mr Akin's submission that a security for money can be issued without the issuer being a person within Note (4) to Group 5. In so deciding, we have carefully considered Miss McCarthy's submissions, but are unable to accept

them. Accepting that there is a lack of clarity in the wording of the EU Directive and EU case law as to whether a lending or credit arrangement underpinning a transaction is required for an instrument to be classified as a "security for money", we are content to rely on the statutory words themselves without gloss for holding that Secrets money is a security for money. We do not accept that the present case can be distinguished from that of Kingfisher because in the present case there was a mere obligation to pay money. The fact that the Secrets companies suffer no significant exposure to credit risk as a result of their being the subject of chargebacks in our judgment is irrelevant.

71. Further, the cash paid out by Secrets companies on redemption of Secrets money by dancers will in all, or almost all, cases be paid prior to the companies receiving monies from Streamline and Amex. As we earlier found even the most prompt card companies take one working day to credit a company's business bank account with monies due in respect of debit and credit card transactions.

72. In relation to the nature of the supplies made by the Secrets companies, Mr Akin submits that the amount deducted on encashment of Secrets money is consideration for its encashment on redemption, and not for the provision of any other supply made to the dancers by Secrets group. He claims the evidence to show that dancers do supply consideration to companies within the group by paying an entry fee to a club, namely a supply of the right to enter the club and to have the opportunity to earn "gratuities" from patrons on the premises ("the entry supply"); there is a clear direct link between the entry fees and the opportunity to earn "gratuities".

73. Mr Akin further submits that there is no predictability that a "discounted supply" (i.e. that whereby a dancer receives less than the face value of a voucher on its redemption) will arise when a dancer is provided with the opportunity to earn gratuities from customers; a dancer is free to refuse Secrets money should she so wish e.g. by rejecting a patron's invitation to dance for him. He also observes that dancers are given cash by patrons, so that the discount they obtain on the encashment of Secrets money cannot bear any relation to cash that they receive from patrons, or to the totality of their earnings.

74. He further contends that there is no causality between what he describes as the discounted supply and the entry supply; dancers suffer the discount at the end of the evening based on encashment of Secrets money, and not on what they have earned in the course of the evening. Yet further, he maintains the Secrets companies cannot know whether Secrets money tendered by a dancer was earned by her or by someone else, or whether it was tendered as a gratuity.

75. Mr Akin also contends that since there are direct links between, on the one hand, the discount and the discount supply and, on the other hand, between the entry fees paid by the dancers and the entry supply, there is no justification in treating the discount as part of the consideration for the entry supply when any link between the discount and the entry supply is far more tenuous than the link between the discount and the discount supply.

76. He maintains the evidence to show that the purpose for which Secrets money is issued is to satisfy the requirements of patrons who have insufficient cash to pay dancers. It fulfils an identifiable economic function from the outset – providing patrons with a form of funding. He claims its encashment by the Secrets companies on tender by a dancer follows on from that funding transaction and that funding function cannot be disregarded when considering the nature of the supply for which the discount is consideration; the encashment of Secrets money follows on from that function, and accordingly it is naturally linked to it rather than to any other. Mr Akin submits that it is no answer to that argument that the Secrets group could have arranged its businesses so as to charge a direct commission on their earnings; the Secrets group is not obliged to conduct its business so as to maximise output tax, and the tribunal cannot rewrite the transactions to do so, *RBS Property Developments v CEC* (2002) Decision No. 17789. He therefore submits that the discount supply is an exempt supply, and the appeals should be allowed.

77. Even were we to reject HMRC's primary contention that Secrets money is not itself a "security for money" Miss McCarthy submits that it does not automatically follow that Secrets' companies' supplies to the dancers are "dealings in credit guarantees or any other security for money" within the meaning of the EU Directive. She maintains that consideration must be given to the context in which the relevant supply takes place. Miss McCarthy contends that the 20% charged by Secrets companies to the dancers is not merely consideration 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, but comprises an ancillary part of an overall package of services comprising a composite supply, which is taxable in nature.

78. In relation to its consideration of the context in which the relevant supply took place, Miss McCarthy submits that the ECJ judgment in the case of *Faaborg-Gelting Linien A/S v Finanzamt Flensburg* (Case C-231/94) is exactly analogous to the situation presently before the tribunal. That case dealt with the provision of food in a restaurant and at [11] to [14] the court said:

> "11. By its first question, the national court asks essentially whether restaurant transactions constitute supplies of goods within the meaning of Article 5 of the Sixth Directive, which, under Article 8(1)(b), are deemed to be carried out at the place where the goods are when the supply takes place, or whether they are supplies of services within the meaning of Article 6(1), which, under Article 9(1) of the directive, are deemed to be carried out at the place where the supplier has established his business.
>
> 12. In order to determine whether such transactions constitute supplies of goods or supplies of services, regard must be had to all the circumstances in which the transaction in question takes place in order to identify its characteristic features.
>
> 13. The supply of prepared food and drink for immediate consumption is the outcome of a series of services ranging from the cooking of the food to its

> physical service in a recipient, whilst at the same time an infrastructure is placed at the customer's disposal, including a dining room with appurtenances (cloak rooms, etc), furniture and crockery. People, whose occupation consists in carrying out restaurant transactions, will have to perform such tasks as laying the table, advising the customer and explaining the food and drink on the menu to him, serving at table and clearing the table after the food has been eaten.
>
> 14. Consequently, restaurant transactions are characterised by a cluster of features and acts, of which the provision of food is only one component and in which services largely predominate. They must therefore be regarded as supplies of services within the meaning of Article 6(1) of the Sixth Directive. The situation is different, however, where the transaction relates to 'take-away' food and is not coupled with services designed to enhance consumption on the spot in an appropriate setting."

79. Miss McCarthy observes that it is not HMRC's case that the 20% charge to dancers represents further consideration for the right to enter the clubs, access the facilities and perform to customers in general (i.e. the "entry supply" claimed by Secrets). Rather their case is that the 20% 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.

80. In determining the nature of a supply, Miss McCarthy maintains that one must look for the essential features and purpose (objectively assessed) of a transaction and examine the commercial reality. Regard must always be had to the circumstances in which the transaction took place (*College of Estate Management v C&EC* [2005] STC 1597 at [29] and [30]). The mere fact that a constituent element is essential for completing an exempt transaction does not warrant the conclusion that the service which that element represents must be exempt ((Case C-2/95) *Sparekassernes Datacenter (SDC) v Skatteministeriet* [1997] STC 932, ECJ at [65]).

81. Miss McCarthy submits that Secrets is not merely providing the dancers with redemption or encashment services, it is also providing the dancers with access to the non-cash customer market and the facility to exploit that market because, unlike the arrangement in *Kingfisher*, the dancers are making their supplies not from their own premises using their own resources, but from Secrets' premises and using its' resources. When viewed from this perspective, she claims there is self-evidently a direct link between the 20% charge to the dancers and the package of services supplied by Secrets.

82. In *Kingfisher* at [74], Neuberger J observed that:

> "[74] … all that 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 customers were informed that Woolworth was one of the participating retailers. Anything with 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".

83. Miss McCarthy submits that to be quite different from the present case. Here, the relevant supply in return for the 20% charge is not "dealings …in security for money". Rather, it is one comprising a number of interwoven elements – the overarching supply being one which provides dancers with greater commercial opportunities and facilitates the dancers' exploitation of those opportunities.

84. In that connection, Miss McCarthy invites us further to consider and apply by analogy the decision in *Byrom and others (trading as Salon 24) v R&CC* [2006] STC 992 at 1009. In that case Warren J, at para 70, in dealing with a claim by the taxpayers that the hire of a room in a massage parlour by a masseuse was a separate exempt supply of land, said:

> "In my judgment, the over-arching single supply is not to be treated as a supply of a licence to occupy land. The description which reflects economic and social reality is a supply of massage parlour services, one element of which is the provision of the room … This is a case where the tax treatment of the supply is self-evident once it is established that the other services elements [including laundry facilities, credit-card services and advertising] are not ancillary to the provision of the licence."

85. Accordingly, even were we to hold Secrets money to be a "security for money", Miss McCarthy further submits that it does not automatically follow that Secrets supplies to the dancers fall within the scope of the financial services exemption (see *Tierce Ladbroke* at [23]). The composite supply by Secrets to the dancers is not one of "dealings in … security for money". Rather, the 20% charge is consideration for Secrets' provision of a single, taxable supply of performance facilitation services (so described) to the dancer. Redemption of the Secrets money itself comprises an ancillary part of the overall, composite supply.

86. Whichever way the transaction between Secrets and dancers is analysed, Miss McCarthy submits, it is not one that attracts the finance exemption. Accordingly, the appeals should be dismissed.

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.

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. It is plain to us that the Secrets companies' situations are analogous with those considered by the courts in the *Faaborg-Gelting* and *Byrom (Salon 24)* cases, and lead to the same conclusions as those to which the respective courts in those cases came. 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.

89. In so deciding, we have taken full account of the submissions of Mr Akin on the same point, but are unable to accept them.

90. 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.

DAVID DEMACK
TRIBUNAL JUDGE

RELEASE DATE: 23 January 2014

SECRETS

IMPORTANT GUIDELINES

FULLY NUDE TABLE DANCES

SUGGESTED GRATUITY TO THE DANCER FOR EVERY MUSIC TRACK PLAYED IS £20 IF GIVEN IN CASH OR COST TO YOU £24 IF VIA SECRETS MONEY

DANCERS TABLE COMPANY (INCLUDING DANCES) BY THE HOUR

SUGGESTED GRATUITY TO THE DANCER IS £250 IF GIVEN IN CASH OR COST TO YOU £300 IF VIA SECRETS MONEY.
NO CHARGE IS IMPOSED BY SECRETS FOR TABLE COMPANY

DANCERS GRATUITIES

ARE STRICTLY BETWEEN THE CUSTOMER AND DANCER AND ANY MONEY (INCLUDING SECRETS MONEY), GIVEN TO A DANCER SHOULD ONLY BE TO TIP THE DANCER FOR TABLE DANCING, STAGE PERFORMANCES OR TABLE COMPANY (AND FOR NO OTHER REASON).

SECRETS MONEY

AVAILABLE FROM WAITING OR BAR STAFF. VIA YOUR CREDIT/DEBIT CARD, IN £1, £20 AND £250 DENOMINATIONS (SUBJECT TO A 20% SURCHARGE), CAN BE USED TO TIP THE DANCERS FOR TABLE DANCING, STAGE PERFORMANCES, TABLE COMPANY OR PAY FOR DRINKS, FOOD, SERVICE CHARGE (OPTIONAL) OR TIP THE STAFF.

VIP LOUNGES

ENTRY IS GAINED BY A £10 PER PERSON COVER CHARGE AND A PURCHASE FROM THE VINTAGE CHAMPAGNE LIST.
SECRETS MONEY IS NOT A CONDITION OF ENTRY TO THE VIP LOUNGES.