[2022] UKFTT 00017 (TC)

TC 08370/V

FIRST-TIER TRIBUNAL
TAX CHAMBER

Appeal number: TC/2017/03541

VAT – supply of a room and services – whether exempt supply of land or standard-rated supply of services – appeal upheld

BETWEEN

ERROL WILLY SALONS LTD **Appellant**

-and-

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

TRIBUNAL: JUDGE ANNE FAIRPO
MRS SONIA GABLE

The hearing took place on 24 June 2021. The hearing took place on the Tribunal video hearing platform. A face to face hearing was not held because of restrictions arising from the pandemic.

Mr G Edwards CTA, for the Appellant

Ms Millward, litigator of HM Revenue and Customs' Solicitor's Office, for the Respondents

DECISION

Introduction

1. This is an appeal against a decision by HMRC to issue a VAT assessment in the sum of £18,649 on 17 February 2017. The assessment was issued under s73 Value Added Tax Act (VATA) 1994.

2. The issue to be determined is whether the Appellant (EWS) makes an exempt supply of a licence to occupy in respect of rooms used by beauticians, or whether that supply is a standard-rate supply of facilities and services.

Background

3. The EWS premises (as relevant to this case) consist of two floors. The ground floor and the front part of the first floor is used by EWS. The back part of the first floor consists of two rooms and a shower room. It is these two rooms which are the subject of this appeal. There is a door between the back and front parts of the first floor; this provides an emergency escape route and is not generally used. There are two staircases between the ground floor and the first floor; one staircase at the front of the premises is used by EWS to access the front area of the first floor, the other, behind a door towards the back of the premises, is used to access the back part of the first floor.

4. Each of the two rooms at the back of the first floor is, or has been in the past, used by a beautician. The rooms were created approximately 10-12 years ago, in a refit of the premises. A sink had been installed in each room for general use, and the rooms had been painted plain white. The rooms had not been created specifically for use by beauticians. Mr Willy had, for example, originally considered that a chiropractor might use one of the rooms.

5. Each beautician otherwise provides her own equipment, materials and other products including towels and is responsible for cleaning the space with her own products. The rooms were decorated by the beauticians, not EWS. The shower room on the first floor was available to the beauticians' customers, although this was very infrequently used. The beauticians also had access to the toilet and staff restroom on the premises.

6. During the period of the assessment, only one of the rooms (Room 2) was used by a beautician (K). EWS charged rent for the room, calculated as 40% of K's takings. The other room was subsequently rented out to another beautician (A), who has since ceased to use the space. The rent in respect of A's room had been calculated as 33.3% of her takings. The beauticians set their own prices and opening hours.

Characteristics of leasing or letting of immovable property

7. The characteristics of leasing or letting of immovable property with regard to VAT have been established in case law, particularly European case law. *Stichting 'Goed Wonen v Staatssecretaris van Financiën* (Case C-326/99) noted that (§55-56):

> "The fundamental characteristic of [a usufructuary right], which it has in common with leasing, lies in conferring on the person concerned, for an agreed period and for payment, the right to occupy property as if that person were the owner and to exclude any other person from enjoyment of such a right"

8. That is, there are four characteristics to be considered:

   (1) the arrangement must relate to a defined area of immovable property;

   (2) it must confer a right to occupy that property, to the exclusion of all others;

(3) for an agreed period; and

(4) for payment

9. HMRC agreed that the arrangements provided a defined area for the beautician (the room), although the beautician made use of more than just this space, but contended that there was no evidence to show that the other three characteristics were met, because:

(1) it was uncertain whether there was a right to exclude others from the area;

(2) there was no evidence that the right of occupation was for an agreed period;

(3) as rent was calculated as a percentage of turnover, the condition that payment must be given is not met.

10. The appellant contended that these characteristics were present, as indicated by leases entered into between EWS and each of the beauticians in December 2018. These leases included a landlord's covenant for quiet enjoyment of the property by the tenant subject to compliance with obligations, for a term of one year. It was contended that payment of a percentage of turnover should be regarded as the payment of rent.

11. Although the leases were not in place at the time of the assessment, the evidence given by Mr Willy as to arrangements at the time is consistent with the terms of the leases. His evidence was also that the rooms belonged to the beauticians and were theirs to do with as they chose: he did not know how the rooms had been decorated, for example. When shown photographs of the rooms he could only identify which room was used by which beautician by elimination, in that he recognised in one photograph a particular artwork which K's husband had painted and which K had shown him. We note that this was apparently by way of interest and not (for example) in order to obtain permission to hang the picture. As noted above, at the time that the rooms were set up, Mr Willy did not have any specific use in mind for the rooms; he had in fact thought that a chiropractor might use one of the rooms. We consider that this is inconsistent with any intention on the part of EWS to exercise particular control over the use of the rooms.

12. On balance, we find that the terms of the leases in this regard did reflect the previous arrangements and that, therefore, there was a right to exclude others from the area. We note that the nature of the beautician's services included services such as personal waxing which were also such that a beautician would be unlikely to agree to the possibility of another person entering the room without permission.

13. There was no particular evidence as to the agreed period other than the lease, but the arrangement was explained to have been for monthly calculations and payments of rent. In such a case, we consider it reasonable to conclude that there was an agreement that the rooms were let for a defined period of one month before the lease was entered into, and that the arrangements were on a rolling month-to-month basis. There were no submissions that such a rolling rental period did not amount to a defined term.

14. We note HMRC's submissions that a percentage of turnover does not meet the condition that payment must be given for a defined area. These submissions were not expanded upon, and we find them somewhat surprising as turnover rents are not uncommon. Although there is, at least theoretically, a possibility that the tenant may not achieve any turnover during a particular period, which would result in no rent payment actually arising for that period, the lease does contain provisions for the payment of rent. HMRC's submissions would logically mean that a rent-free period would preclude the existence of a lease during the rent-free period as payment would not be received for that period.

15. As such, we consider that the four characteristics are present in this case and the arrangements are therefore not immediately precluded from being treated as a supply relating to land.

Effect of the services

16. Having established that the supply is not precluded from being a supply relating to an interest in land, it is necessary to consider the effect of the additional services provided.

17. The appellant considered that the question should be determined following the principles in *Card Protection Plan* (Case C-349/96) (CPP), which are:

(1) Every supply of a service must normally be regarded as distinct and independent.

(2) A supply which comprises a single service from an economic point of view should not be artificially split.

(3) The essential features of the transaction must be ascertained in order to determine whether the taxable person is supplying the customer, being a typical customer, with several distinct principal services or with a single service.

(4) There is a single supply in particular in cases where one or more elements are to be regarded as constituting the principal service, whilst one or more elements are to be regarded, by contrast, as ancillary services which share the tax treatment of the principal service.

(5) A service must be regarded as ancillary to a principal service if it does not constitute for customers an aim in itself, but a means of better enjoying the principal service supplied.

18. It was submitted that any services supplied were ancillary, enabling a better enjoyment of the room supplied, and did not constitute an aim in themselves. As such, the service should share the VAT exemption which applied to the letting.

19. In the alternative, if there was no principal supply, it was contended that the decision in *Levob Verzekeringen BV* (Case C41/04) established that (§22) "…where two or more elements are so closely linked that they form, objectively, a single indivisible economic supply, which it would be artificial to split" the "predominant element [of the supply] must be determined from the point of view of the typical consumer" (*Zamberk v Financní reditelství v Hradci Králové* (Case C-18/12) ("*Mesto*"), at §30).

20. HMRC submitted that the services supplied by the appellant were such that the arrangement should be regarded as the active exploitation of the rooms, adding significant value, so that it could not be regarded as meeting the conditions of a supply of land (citing *Blue Chip Hotels* [2017] UKUT 0204 (TCC); *Luc Varenne* (Case C-55/14)).

21. HMRC also contended that the decision in *Byrom and others (trading as Salon 24)* [2006] STC 992 ("*Byrom*") was relevant, setting out the principle that a single supply can consist of a bundle of elements, which are integral to each other, but where it cannot be said that one single element is predominant with all others being ancillary. In such a case, the overall supply should be properly classified according to the description which reflects the economic and social reality, which was that of a supply of services. HMRC submitted that, as in *Byrom*, the economic and social reality in this case was that the arrangement was a licence to trade from the premises and therefore should be standard-rated.

Discussion

22. The question here, in summary, is whether the provision of the additional services such as receptionist services, the availability of a toilet and staffroom, the display of posters in the

window, and the display of a price list on a website amounted to the provision of "significant added value" such that the supply can no longer be characterised as a "relatively passive" supply of land or, in the alternative, that the economic and social reality of the arrangement was not one of a supply of an interest in land.

23. Considering HMRC's submissions regarding the application of *Byrom*, we consider that the specific facts of Byrom are particularly important to the eventual decision. The case concerned a salon which rented rooms to masseuses. A masseuse paid for the use of a furnished room for a day, together with other services such as security and reception services which the masseuses were required to use. The salon dealt with cleaning of the space, including the provision of clean linens in the rooms, and laundry facilities were also provided for the masseuses to use. The salon would call the pool of masseuses if there was spare capacity, to see if one wanted to use a room at short notice at a reduced daily rate. The salon advertised the services in the local newspaper, as well as on their website. Customers would pay a fee to the salon as well as to the masseuse; the masseuse's fee was placed in a security box which was kept by the salon. The salon provided security services, including CCTV, which – for safety reasons – were considered to be an essential part of the service supplied to the masseuses by the salon. The cash handling by the salon was also considered to be essential for safety purposes.

24. In summary, in *Byrom*, the recipients of the supply were provided with a full furnished room at daily rates which included services aimed at ensuring their safety, as well as benefiting from active advertising. The services relating to safety in particular were considered to be essential supplies given the nature of the business. The decision concluded that the additional services were such that the payment was considered to be standard-rated, being for the overall package of services and not a relatively passive supply of property. The court concluded that the masseuses could not operate their businesses without the overall package and noted also that the additional services were not optional.

25. In this case, the arrangements between EWS and the beauticians are very different. The rooms are rented for (at least) a month at a time and are rented unfurnished: only a sink has been included in the room. HMRC contended that the fitting of a sink in the rooms indicated that they were intended to be used by beauticians specifically, closely linked to EWS's business. However, we consider that the provision of a sink is generic, and plumbing is generally regarded as a landlord's responsibility, rather than being something specific to beauticians.

26. The occupants supply their own equipment, including furniture and any necessary linens, and make their own arrangements for dealing with laundry away from the premises. There was no suggestion that EWS would actively seek clients for the beauticians, or otherwise actively work to increase their takings to any significant extent. The advertising provided (a poster displayed in the window in respect of K's business and a list of prices for K on the EWS website) is, we consider, similarly passive – there was no indication that EWS had incurred any specific cost in facilitating this advertising, in contrast to the newspaper adverts provided in *Byrom*. EWS did not advertise the beauticians' services within the salon itself, and Mr Willy's evidence was that he thought that the beauticians generally acquired their clients by word of mouth.

27. HMRC contended that the beauticians would benefit from proximity to the salon, as customers would book beautician services when they came for a haircut. However, Mr Willy's evidence was that there was very little cross-over between the salon customers and the beautician customers. This was not challenged and we consider that HMRC's assumption that a significant benefit was conferred in this way is not substantiated.

28. Although Mr Willy acknowledged that having the EWS receptionist take telephone bookings for K might make it easier for K to book in clients, it was clearly possible to operate the business without this service, as A did not use it and his evidence was that K in fact made most of her bookings personally. With regard to a reception service of 'meeting and greeting' clients, it appears to us that EWS would need to have some mechanism for identifying its own clients, given the common entrance for their business areas and the beauticians' business areas; EWS would also generally want to know why persons were entering the salon in any case. This would seem to necessarily involve generally 'meeting and greeting' any person entering the salon and Mr Willy's evidence was that the beauticians themselves undertook the more substantive greeting of clients.

29. The use of other reception services (marking clients as having arrived, for example) was not mandatory nor was it suggested that there was any specific need for such service in contrast to, for example, the safety considerations in *Byrom*. Mr Willy's evidence was that the beauticians largely dealt with this themselves and, as such, it is clearly not essential to the beautician's business that there be a separate reception service.

30. The receptionist dealing with payments for K was not stated to be for any essential purpose such as safety but, rather, for convenience. This was primarily EWS's convenience, as they would therefore have supporting details of her turnover for the purposes of calculating rent, although it was acknowledged that it might be convenient for K as well. It is clear from the arrangements with A, and now with K, that the beauticians can readily deal with payments on their own.

31. There was some discussion as to the level of rent paid by each of K and A, as this differed. However, Mr Willy's evidence was that this was due to negotiation by A and that the rent paid by K had not changed when she ceased to use the reception services. The suggestion that the rent was variable to reflect the involvement of the receptionist did not explain why the second beautician, A, had also rented her room on the basis of a turnover rent without making any particular use of the EWS receptionist.

32. It was noted that there were provisions in the EWS insurance policy which would cover the beauticians' services. Mr Willy's evidence was that this was not deliberate; his wife had made the insurance arrangements, but he did not think that the cover would have been specifically requested. He thought it might have been standard wording for insurance of hairdressing salons. The beauticians had been told that they needed to make their own insurance arrangements, and K's insurance policy, providing £3m of cover, was provided as evidence.

33. We consider that the access given to toilet facilities and a restroom is, similarly, a matter of expediency rather than something without which the beauticians could not operate.

34. Considering the services overall, the only services which would specifically enable the better enjoyment of the room itself were the services such as heat and light and, arguably, the access to the toilet facilities. We consider that the other services would assist with the conduct of the beautician's business generally, rather than the enjoyment of the room specifically.

35. Therefore, for the reasons set out above, we consider that the additional services were ancillary to the supply of the room and not a predominant part of the supply. The beauticians were not required to use those services and did not always do so. The provision of the services was clearly not essential to the business of either of the beauticians.

Conclusion

36. For the reasons set out above, we conclude that the arrangements were such that they should be characterised as a VAT-exempt relatively passive supply of land, as the services are not such as to change that character.

37. The appeal is therefore upheld.

Right to apply for permission to appeal

38. 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.

ANNE FAIRPO
TRIBUNAL JUDGE

Release date: 05 JANUARY 2022