

Escorts and agency services
Portman Escort Agency (19728)

Summary

In a case where an escort agency has been found to supply only introductory services and not full escort services, the Tribunal has held that determining the correct VAT treatment using a contractual analysis of the business model is insufficient if it fails to reflect the true reality of the way in which that business is conducted. This 'agency versus principal' debate will be of interest to any business that uses third parties to deliver some or all of its services to clients.

Background

The Appellant had been running the business of an escort agency since 1979 and was described as either providing girls to male customers to accompany those customers on dinner, theatre dancing dates etc. or as being in the business of effecting the introduction of girls to men whereupon the girls would then agree to go out on such dates.

The issue in this case is whether the Appellant was providing only an introductory service such that it was subject to VAT on its 'agency fees' only or whether it was supplying to customers the full service of providing escort girls (acting as principal).

This case concerns whether the Appellant was liable for VAT on the introductory or agency fees that it received or whether it was liable for significantly more VAT on the basis it was providing, as principal, the full service of providing escorts.

What makes this case somewhat unusual is that the terms of the one page contract between the escort agency and the escort would seem to be decisive in favour of the Appellant acting as principal. It required escorts to "provide the services of an Escort for clients of the Agency" and "provide her services to the Agency" in the capacity of an "independent contractor". However, the reality of the way business was conducted showed the contract to be little more than a sham.

The Tribunal was asked to consider whether the conduct of the parties was at such variance with the terms of the contract that the contract should not govern the VAT treatment of the Appellant.

The Appellant's key arguments were that, in fact and law, all it did was to make standard rated introduction supplies to its customers, citing Reed Personnel Services Limited [1995] STC 588 to support the fact that the contractual position is only the starting point when analysing the nature of the services for VAT purposes. The Appellant suggested that the question to be answered by the Tribunal was: "whether the girls or Portman supplied the escort services remunerated by the "tip" (that is the fee received by the girls)".

HMRC's main arguments centred around the terms of the written contract, stating that it clearly demonstrated that the Appellant was acting as principal in providing full escort services and that these contracts had been relied upon by the Department of Employment. As such, the contracts should not be dismissed as a sham. HMRC also argued that the advertising and guideline prices implied that the Appellant provided a unified service.

Judgment

The Tribunal allowed the appeal, concluding that the service rendered by the Appellant was a service of introductory 'agent' between escorts and customers.

It was found that the contract for providing escort services was made by the escort girl on each occasion when she agreed with the customer to provide a particular service in return for a fee that she would determine. The details of these contracts were entirely unknown to the Appellant.

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The appeal was allowed even though the Tribunal accepted that the contract assumed the Appellant was providing escort services as principal. This was because the Tribunal's approach was to "decide the VAT issue in a way that we think is realistic". As such, it was decided that the contract did not realistically reflect the reality that the Appellant performed an introductory service only and the escort services were rendered under a separate verbal contract in which the escorts agreed with the customers what they would do, where they would do it and how much they would charge.

This decision can be contrasted with that of the Tribunal in *Spearmint Rhino Ventures UK Ltd (19439)* where the dancing club was found to be acting as principal in supplying dancing services. The Tribunal also found in *F Di Resta and Miss D Di Resta (18641)* and *Stephen Paul Rudd trading as Duo's Sap and Sauna (16844)* that the establishment was acting as principal.

It should be noted that the agency was not introducing a part-time employee to customers but a self-employed contractor. That is different to the case of the introduction of an employee in which case the Working Time regulations might prohibit and agency contract.

Implications

The question of whether an agency / principal relationship exists is a potential issue for any business that uses third parties to provide some or all of their services to customers.

The decision in this case has upheld the continued approach of the Tribunal that where the reality of a situation is not truly reflected by the contract, all relevant factors must be examined to establish what is actually the case before the VAT treatment can be determined.

In addition, it is a fundamental principle that whether or not an agency relationship exists is a matter to be decided in accordance with the evidence. Both parties must know and accept what they are doing and in what capacity they are acting. This must also be supported by their actions.

In this case, the contract between the escort agency and the escort girls appeared to hold the escort agency as acting as principal. However, because the reality was that all parties involved did not regard the contracts as significant and they did not reflect the genuine contractual relations between the parties, the contract alone did not determine the VAT treatment. Instead, the Tribunal followed a more "realistic analysis" to conclude that the Appellant had acted as a disclosed agent and its liability was to account for VAT on the introductory fees it received and not the full value of the escort services provided to the customer.

The reason for the existence of the contracts appeared to be an effort to control or prevent prostitution and there was not the 'meeting of minds' necessary for the Tribunal to consider that both parties had entered into it with a clear idea and understanding of what its provisions meant.

In some cases, it may be possible for business to restructure their business model in order to achieve VAT efficiencies.