VAT update

August 2018

In this month's update we report on (1) HMRC's revised guidance on the VAT cost share exemption; (2) HMRC's consultation and plans to address VAT avoidance via offshore looping; and (3) making tax digital for VAT. We also comment on three recent cases involving (1) consideration of whether an expenses salary sacrifice scheme was an economic activity for VAT purposes; (2) whether VAT was payable by an employment agency on supply of non-employed temporary workers to clients; and (3) an early case management decision in the taxpayer's favour in a case where there is a dispute as to whether a taxpayer's bill payment services is subject to VAT.

News

Revenue and Customs Brief 10 – HMRC publishes its policy on the cost share exemption

On 31 July 2018, HMRC published "Revenue and Customs Brief 10 (2018): VAT – cost share exemption". The Brief explains HMRC's revised policy for identifying supplies made by costs sharing groups (CSGs). The revised guidance, which is set out in paragraphs CSE3850 to CSE3895 of the Cost Sharing Exemption (CSE) Manual, is due to take effect from 15 August 2018. more›

HMRC addresses offshore looping VAT avoidance

On 19 July 2018, HMRC published a consultation on draft legislation intended to address VAT avoidance via offshore looping, predominantly in the insurance sector. more›

VAT Notice 700/22: Making Tax Digital

On 13 July 2018, HMRC published "VAT Notice 700/22: Making Tax Digital for VAT", which provides guidance on digital record keeping and return requirements for Making Tax Digital for VAT. more›

Cases

Pertemps: Expenses salary sacrifice scheme not an economic activity for VAT purposes

In *Pertemps Limited v HMRC*, the First-tier Tribunal (FTT) has held that a salary sacrifice scheme providing travel and subsistence expenses to employees was not an economic activity for VAT purposes. more›

Adecco: VAT payable on supply of non-employed temporary workers

In *Adecco UK Limited and others v HMRC*, the Court of Appeal has confirmed that VAT was payable on the supply of non-employed temporary workers to clients. more›

Any comments or queries?

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About this update

The VAT update is published on the final Thursday of every month, and is written by members of RPC's Tax team.

We also publish a Tax update on the first Thursday of every month, and a weekly blog, RPC's Tax Take.

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Allpay: Application by HMRC to amend its Statement of Case

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Where a CSG has correctly used the previous guidance for "directly necessary" services, the previous guidance can continue to be used until 31 December 2018, to allow CSGs time to ensure correct records are kept.

A copy of the Brief can be viewed here.

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HMRC addresses offshore looping VAT avoidance

On 19 July 2018, HMRC published a consultation on draft legislation intended to address VAT avoidance via offshore looping, predominantly in the insurance sector.

Financial services providers are unable to reclaim VAT incurred on their costs as financial and insurance services are VAT exempt if supplied within the EU. This leads to companies forming arrangements with non-EU companies to export and resupply, or loop, those services back to UK consumers to reclaim the VAT incurred.

HMRC intends to prevent looping by restricting the application of Article 3 of the Value Added Tax (Input Tax) (Specified Supplies) Order 1999, to circumstances where the final consumer is not in the UK.

A copy of the explanatory memorandum can be viewed here.

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VAT Notice 700/22: Making Tax Digital

On 13 July 2018, HMRC published "VAT Notice 700/22: Making Tax Digital for VAT", which provides guidance on digital record keeping and return requirements for Making Tax Digital for VAT.

The rules will come into effect on the first VAT period after 1 April 2019.

VAT registered businesses whose taxable turnover exceeds the VAT registration threshold of £85,000 will be obliged to:

- maintain and preserve records in a digital form
- file VAT returns using functional compatible software, and
- communicate digitally with HMRC through the Application Programming Interface program.

Records that must be maintained in digital form include the time and value of supplies made and received, including those made and received by third party agents. The software will then be able to prepare the VAT returns before requiring confirmation that they are correct and can be sent to HMRC.

The Notice provides some useful examples illustrating how the rules will apply to businesses.

A copy of the Notice can be viewed here.

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Cases

Pertemps: Expenses salary sacrifice scheme not an economic activity for VAT purposes

In *Pertemps Limited v HMRC*[1], the First-tier Tribunal (FTT) has held that a salary sacrifice scheme providing travel and subsistence expenses to employees was not an economic activity for VAT purposes.

Background

Pertemps Limited (the taxpayer), was a recruitment agency which introduced a "Mobile Advantage Plan" (MAP) to provide eligible employees with travel and subsistence expenses by way of salary sacrifice. The employees were flexible employees engaged by the taxpayer on indefinite contracts of employment. The employees were offered the opportunity to participate in the MAP. Any employees who took part agreed to a wage reduction, in return for the taxpayer making the payment for expenses which was equal to the wage deduction.

To benefit from the MAP, expenses had to be "incurred wholly, exclusively and necessarily" in the performance of the duties of employment. Travel expenses were included so long as they were not "ordinary commuting" expenses to a "permanent" workplace. A workplace became permanent if the employee attended for a period of work lasting more than 24 months. Only employees who operated outside of a permanent workplace were eligible for the MAP.

HMRC argued that the MAP attracted VAT as it was a supply of service for the purposes of Article 2(1)(c), Council Directive 2006/112/EC (the VAT Directive).

The taxpayer appealed.

FTT decision

The appeal was allowed.

The issue for the FTT to determine was whether the MAP was a supply of services for consideration by the taxpayer to participating employees.

In considering this issue, the FTT followed the two-stage analysis set out in *Wakefield College v HMRC*[2]: (1) whether there was a supply by a taxable person; and (2) whether that taxable person carried on an economic activity.

Was there a supply?

The FTT concluded that there was a legal relationship between the taxpayer and the employee. The legal relationship involved a reciprocal performance whereby the employee agreed to forgo remuneration in exchange for the MAP. As such, there was a valid supply of services pursuant to Article 2 of the VAT Directive.

Was an economic activity carried on?

In considering whether the taxpayer carried on an economic activity pursuant to Article 9 of the VAT Directive, the FTT noted that *Wakefield* confirmed that there must be a broad enquiry taking into account all of the circumstances in which the services are supplied. The essential test is whether the supply was made for the purpose of obtaining income on a continuing basis.

1. [2018] UKFTT 0369 (TC).
2. [2018] EWCA Civ 952.

The FTT concluded that, despite resulting in an increase of profits as employment costs were reduced, the MAP did not provide an income stream to the taxpayer. Only the taxpayer could operate the MAP, so it was not a service that could be provided by a third party.

The principal supply was the supply by the employees of their labour in consideration for the remuneration and benefits provided by the taxpayer. However, in distinguishing *Astrazeneca UK Limited v HMRC*[3], the FTT held that the supply was ancillary to the fundamental elements of the employment relationship and not separate services outside a normal employment relationship.

The FTT therefore held that although the operation of the MAP was a supply pursuant to Article 2, it was not in itself an economic activity. The operation of the MAP was not therefore a supply subject to VAT.

Comment
This decision provides a useful analysis on when an activity constitutes an "economic activity" for VAT purposes. Although consideration of this question will be fact specific, the decision provides helpful clarification for businesses regarding the VAT treatment of salary sacrifice schemes involving expenses for employees who do not work in a permanent place of work and incur expenditure wholly, exclusively and necessarily for the purpose of performing their employment role. Businesses operating similar schemes should review their arrangements to ensure that the VAT treatment is correct.

A copy of the decision can be viewed here.

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Adecco: VAT payable on supply of non-employed temporary workers

In *Adecco UK Limited and others v HMRC*[4], the Court of Appeal has confirmed that VAT was payable on the supply of non-employed temporary workers to clients.

Background
Adecco UK Limited (the taxpayer), is an employment agency supplying its clients (the clients) with temporary staff, including non-employed temporary staff. These workers are not employed by the taxpayer but may be introduced to its clients to undertake assignments. During such assignments, there is no contractual relationship between the client and the worker.

The taxpayer and the clients enter into a contract, which is the same regardless of whether the worker is employed, not employed or contracted. The client is obliged to pay the taxpayer a fee for the work carried out by the worker.

The taxpayer and the temporary worker enter into a contract whereby the taxpayer is the employer and remunerates the worker.

The taxpayer attempted to reclaim overpaid VAT in respect of the non-employed workers' remuneration paid by the client following the decision in *Reed Employment Ltd v Revenue and Customs Commissioners*[5].

The taxpayer argued that it only introduced the non-employed workers to its clients and the workers (rather than it) provided the services to the clients.

HMRC refused the claim and the taxpayer appealed.

3. (Case C-40/09).
4. [2018] EWCA Civ 1794.
5. [2011] UKFTT 200 (TC).

Both the First-tier Tribunal and the Upper Tribunal (UT) rejected the taxpayer's argument that it was merely supplying introductory and ancillary services to its clients. Both tribunals concluded that the taxpayer supplied the non-employed temporary workers in return for payment and it was liable to account for the VAT on the fees charged.

The taxpayer appealed to the Court of Appeal.

Court of Appeal judgment
The appeal was dismissed.

The issue for the Court of Appeal to determine was whether the workers' fees charged by the taxpayer in relation to non-employed temporary workers was subject to VAT. To determine this, the Court considered whether the taxpayer or the non-employed workers, supplied services to the clients.

The Court concluded that no contract existed between the temporary workers and the clients, thus the workers did not provide their services under any such contract. Instead, the contracts existed between the taxpayer and the workers and taxpayer and the clients. The workers were under the control of the taxpayer rather than the clients.

In the Court's view, the taxpayer did not merely perform administrative functions. It held rights to terminate and suspend employment and remained responsible for paying the workers on its own behalf even if the client did not pay the taxpayer or decided to reject the temporary worker.

The Court noted the UT's point that the contract between the taxpayer and a temporary worker proceeded on the basis that unauthorised absence could breach the obligations owed by the taxpayer to the end clients.

The fees charged to clients were not split into workers' remuneration and commission for itself and instead, clients were charged one single sum.

The Court considered that as a matter of contract and of economic reality, the services were supplied to the clients rather than the taxpayer.

Accordingly, the taxpayer was liable to account for the VAT on the total fees charged to its clients. The Court held that the taxpayer had supplied the services of its non-employed workers to its clients and that their salaries did form part of its supply for VAT purposes.

Comment
In providing helpful guidance regarding the VAT treatment of supplies of this nature the Court said that *Reed Employment* had been wrongly decided. The VAT liability of other employment agencies will need to be carefully considered and a thorough review of all relevant contracts might be appropriate.

A copy of the judgment can be viewed here.

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Allpay: Application by HMRC to amend its Statement of Case

In *Allpay Limited v HMRC*[6], the First-tier Tribunal (FTT) has dismissed HMRC's application to amend its Statement of Case to plead a new legal issue and awarded the taxpayer its costs.

Background

Allpay Ltd (the taxpayer), provided bill payment services and treated this as exempt from VAT. On 21 January 2016, HMRC issued a decision that the taxpayer's bill payment services were subject to VAT and the taxpayer appealed the decision.

Article 135(1)(d) of the Principle VAT Directive 2006/112/EC, provides for a VAT exemption if the following two conditions are met:

(a) the services are "transactions … concerning … payments"; and

(b) the services are not "debt collection" services.

In its Statement of Case, which it provided on 6 December 2016, HMRC alleged that the services were of debt collection only.

On 17 November 2017, HMRC wrote to the taxpayer and asked whether it would withdraw its appeal on the basis of the 2016 decision by the Court of Justice of the European Union in *Bookit*[7] and the application of that decision by the FTT in *Paypoint v HMRC*[8]. In *Paypoint*, the FTT found that services which consisted of providing a system of payment collection was not exempt from VAT.

In light of these two cases, HMRC argued that the services were not "transactions … concerning … payments", under Article 135(1)(d) (the Payment Services issue).

The taxpayer refused to withdraw its appeal and pointed out that the Payment Services issue had not been pleaded in HMRC's Statement of Case. Although HMRC did not accept that it was not pleaded or that it required to be pleaded, it applied to the FTT for permission to amend its Statement of Case to include a pleading that the taxpayer's services were not "transactions … concerning … payments". HMRC claimed that the application to amend was only made out of an abundance of caution.

The taxpayer opposed the application.

FTT decision

HMRC's application to amend its Statement of Case was dismissed.

The FTT considered Rule 25 of the Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules 2009, and confirmed that HMRC's Statement of Case should set out its position in respect of its case in sufficient detail to enable a taxpayer to properly prepare its case for hearing.

The FTT first asked what was the issue in the case based on the existing Notice of Appeal and Statement of Case. The issue was whether the taxpayer's bill payments services were exempt as they were not debt collection services.

The FTT found that even though the onus of proof in respect of the Payment Services issue was on the taxpayer, it did not have to discharge this burden unless HMRC included in its Statement of Case an allegation that the services were not "transactions … concerning … payments".

6. [2018] UKFTT 0273 (TC).
7. [2017] EUECJ C-607/14.
8. [2017] UKFTT 424.

The taxpayer had averred in its Notice of Appeal that its services were payment services within Article 135(1)(d) and HMRC's failure to challenge that in its Statement of Case must be taken as acceptance of it.

The FTT then considered whether HMRC should be allowed to introduce into the appeal proceedings the Payment Services issue by amending its Statement of Case. The FTT considered that it would only be fair to permit an amendment that satisfies Rule 25 and in its view HMRC's amendment did not satisfy Rule 25, as it was too vague. HMRC had failed to set out, either legally or factually, why it considered the taxpayer's services not to be payment services. In the view of the FTT, to allow such an amendment would lead to trial by ambush.

The FTT therefore dismissed HMRC's application to amend its Statement of Case. Significantly, the FTT also awarded costs against HMRC on the basis that it was unreasonable for HMRC to apply to amend its Statement of Case without properly explaining what its amended case was to be.

Comment

This decision is a timely reminder to HMRC that it has to properly plead its case in sufficient detail in its Statement of Case to enable the taxpayer to fully understand the basis of HMRC's position.

Increasingly, there is a tendency on the part of HMRC to seek to change its legal arguments after it has served its Statement of Case. In appropriate cases, taxpayers should challenge any attempt by HMRC to introduce new arguments at a late stage in the appeal proceedings.

A copy of the decision can be viewed here.

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