

HMRC consultation: Combating VAT fraud on the provision of labour in the construction sector

Indirect Tax

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HMRC's consultation, announced at Spring Budget 2017, sought views from stakeholders on proposed policy options to prevent supply chain fraud in supplies of labour provision within the construction sector. The call for evidence closed on 9 June 2017 and HMRC has been collating the feedback.

As set out in [Angela Fearnside's article](#) in *Tax Adviser* in May 2017, HMRC is experiencing organised fraud in the construction sector with organised crime groups artificially extending the supply chains with the intention of failing to pay VAT and making incorrect income tax deductions.

Due to the domestic reverse charge being effective at tackling VAT fraud in other sectors, in its recent consultation, HMRC sought feedback on extending the measure to the construction sector.

Representatives from the CIOT met with HMRC Policy officers last month to discuss the practical complexities of the proposed measure. The CIOT welcomes anti-fraud measures to combat tax evasion, and supports HMRC taking action to tackle fraud in this sector.

Who may be affected?

When implemented, the reverse charge would apply to standard and reduced rate construction services supplied in business to business transactions where the parties are registered for both VAT and the Construction Industry Scheme. The VAT liability for construction services supplied to unregistered consumers will not be affected, i.e. the supplier will remain responsible for charging any applicable VAT.

It should be noted that when businesses not ordinarily trading in the construction sector carry out building works of over £1million, they must also register for CIS as 'deemed contractors'. In principle, this could mean that deemed contractor is responsible for determining the VAT liability of the construction project.

Where the VAT liability of the project is simple and the deemed contractor is able to fully recover the VAT incurred, this does not appear to be an onerous change. However, for deemed contractors that have a mixed liability project, who are partially exempt (e.g. health, education, charity sectors) or both, the reverse charge calculation could be problematic and costly as well as raising their risks of penalties.

Issues discussed

HMRC had received feedback from industry that it could be simpler for those businesses obliged to account for CIS deductions, to also apply the reverse charge for VAT purposes.

We discussed the point that deemed contractors would face an increased burden and penalty risk in terms of costs and resource to determine the VAT liability for mixed rate projects, and the input VAT recovery position

in partial exemption and capital goods scheme calculations. We would like HMRC to keep the deemed contractor outside of the anti-fraud measure.

The CIOT also raised the point that the measure may increase the likelihood of VAT liability errors for small construction businesses at the start of the supply chain who will be dealing with another VAT liability as well as their usual standard, reduced and zero rated supply work. The type of fraud being targeted by this measure is not in this part of the supply chain but it would be small businesses disproportionately affected by the changes.

Our feedback will be considered within the consultation process. The implementation date for the change has not yet been decided.