Real-time VAT collection (split payment method)

Indirect Tax

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Pitched at tackling fraud in relation to online business to consumer (B2C) sales involving overseas sellers, this consultation asks much broader questions about the feasibility of a real time VAT collection mechanism. Could this be HMRC testing the water for wider application in the future?

On 20 March 2017, HMRC published a call for evidence on changes to the way VAT is collected in relation to online shopping. This proposal leads on from recent Budget measures relating to sales by overseas businesses via online marketplaces and the Fulfilment House Due Diligence Scheme (FHDDS).

However, this consultation will be of wider interest to taxpayers, advisers and banks/payment service providers because it signals HMRC's interest in exploring a real time VAT collection mechanism which might then be rolled out to wider areas of VAT. Other countries have already introduced real time collection of VAT, including business to business invoice based transactions.

What is split payment?

The consultation introduces the split payment concept and seeks views and evidence on the technical feasibility of extracting VAT in real time using card payment technology and depositing it with HMRC. This is a fundamental shift in the way VAT is reported and collected.

Why is this being introduced?

HMRC report there has been a large increase in online shopping in the UK in recent years, with many goods sold to UK consumers by overseas sellers using online marketplaces. To satisfy consumer demand for rapid delivery, overseas sellers now routinely store their goods in the UK before a sale is made.

Under existing VAT law, when goods are in the UK at the point of sale the overseas sellers are required to register for VAT in the UK, regardless of the level of sales as there is no VAT registration threshold for overseas businesses. Typically, the sellers should charge and collect VAT and pay it over to HMRC in the usual way. HMRC say that many overseas sellers are not VAT registered – or if they are VAT registered, they are not always collecting the appropriate amount of VAT.

HMRC wish to explore solutions to address what they see as the three key factors within the current system that create this opportunity for non-compliance:

1. Businesses based in overseas jurisdictions, but with VAT obligations in the UK;
2. The time lag between the consumer paying for the goods and the business later remitting the VAT element to HMRC;
3. Where the VAT is paid by a UK customer to an overseas business which may or may not pay it over to HMRC in due course.

Views are also sought on the design principles that HMRC would be guided by in developing a split payment system.

Addressing the lack of clarity

The consultation is not entirely clear on precisely which types of sales the split payment method is aimed at. For example, it would seem to apply to sales where goods are already in the UK (as in the FHDDS) but also where goods are outside the UK when the sale is made, meaning it has a wider application than the fraud targeted by the FHDDS. HMRC are also silent on EU v Non-EU overseas businesses. Post Brexit, this distinction is presumably irrelevant but in the interim (and possibly transitional) period different VAT rules apply to those categories of suppliers and, until Brexit happens, EU law is applicable as usual.

Views are sought more on the technical feasibility of using payment technology in general and focusses less on the VAT principles involved when dealing with this particular issue of fraud and non-compliance. It feels like HMRC are testing the water about the concept of real time reporting and are using this particular VAT issue to introduce the idea.

Is this necessary now?

The consultation champions the instant success and effectiveness of existing and recently introduced powers to tackle this type of fraud with non-compliant businesses being removed from online marketplaces, joint and several liability notices issued and a tenfold increase in the number of online overseas businesses applying to register for VAT. We will ask how necessary this additional measure is in this area. Is it striking the right balance between combatting fraud and minimising complexity / administrative burden for taxpayers and HMRC? Especially at a time when businesses are being required to cope with the implications of Making Tax Digital and Brexit.

Determining the right amount of VAT

Determining how much VAT to deposit with HMRC could present quite a challenge. Some of the examples in the consultation around different VAT liabilities demonstrate the complexity of working out how much VAT to withhold / hive off. We wonder who would be responsible for determining the VAT liability of the goods sold and who would deal with errors, adjustments, refunds and be accountable for penalties?

To deposit the correct amount of VAT with HMRC in this supply chain, taxpayers need to either be told how much of the payment represents VAT or be provided with the information needed to determine how much VAT is included in the total payment. A third possibility is that taxpayers are simply told to withhold a fixed percentage of the payment e.g. one-sixth which represents VAT. This opens up the possibility of overpayments / underpayments and adjustments; the administration of which needs to be carefully considered.

The interaction with import VAT and custom duties (and the payment thereof) needs to be considered further. Particularly as the post-Brexit landscape is likely to mean all overseas goods will attract import VAT.

Next steps

We have been invited to a stakeholder meeting to discuss the proposals further and will respond to the consultation on the areas within our competence. Please respond directly to HMRC on the areas relating to payment technology. We welcome members' views or questions on the tax technical aspects and experience of split payments in other countries – please send them to technical@ciot.org.uk by Friday 9 June.

You can find the call for evidence on [GOV.UK].