



HM Revenue
& Customs

VAT: reverse charge for construction services

Who is likely to be affected?

Businesses involved in buying and selling construction services. It does not apply to zero-rated supplies of construction services.

General description of the measure

HMRC is conducting a technical consultation on the draft secondary legislation for a VAT reverse charge on certain construction services. This technical consultation will last for 6 weeks. The final version of the legislation will be published in October 2018, and will come into effect on 1 October 2019.

The measure will, for certain supplies of construction services ('specified services'), mean that the customer will be liable to account to HMRC for the VAT in respect of those purchases rather than the supplier (the 'reverse charge'). The reverse charge will apply through the supply chain up to the point where the customer receiving the supply is no longer a business that makes supplies of specified services. Also excluded from the reverse charge will be businesses that supply specified services to a connected party within a corporate group structure.

In these circumstances, the supplies in question will then revert to normal VAT accounting rules.

The reverse charge will include goods where those goods are supplied with the specified services.

Policy objective

This is an anti-fraud measure which removes the opportunity for fraudsters to charge VAT and then go missing before paying it over to the Exchequer.

Background to the measure

VAT fraud in construction sector labour supply chains presents a significant risk to the Exchequer. Organised criminal gangs fraudulently take over, or create new, shell companies to steal VAT whilst operating alongside actual construction services. This is commonly referred to as 'missing trader' fraud.

The government announced a consultation at Spring Budget 2017 to address this and published a summary of responses in December 2017. It also announced at Autumn Budget 2017 that the Government would be taking forward the measure and that there will be a technical consultation on the draft legislation in Spring 2018 with final legislation and guidance published by October 2018, a year before the legislation becomes effective on 1 October 2019.

The aim of this technical consultation on the draft secondary legislation is to test whether the scope and definitions are understood and achieve their objective, and that our estimates on the impacts below are reasonable.

Detailed proposal

Operative date

The final version of the secondary legislation will be published in October 2018. The reverse charge will apply to supplies of specified services on or after 1 October 2019.

Current law

Section 1(2) of the VAT Act 1994 (VATA) makes the supplier liable for any VAT on supplies of goods or services.

Under section 4 of VATA, VAT is charged on the supply of goods and services where they are made in the UK by a taxable person in the course or furtherance of their business. The rate of VAT charged on the supply of construction and building services can be 20%, 5% or 0% depending on the type of building the construction services are being carried out on. The legislation in the VAT Act 1994 that describes the rate of VAT for construction and building is Groups 6 and 7 to Schedule 7A and Group 6 to Schedule 8.

Section 55A of VATA provides that the recipient of a supply must account for the VAT due on supplies of a kind specified in an order made by the Treasury.

Proposed revisions

The introduction of a reverse charge does not change the liability of the supply of the specified services. What does change is the way in which the VAT on those supplies is accounted for. Rather than the supplier charging and accounting for the VAT, the recipient of those supplies accounts for the VAT.

Section 55A of the VAT Act 1994 provides the power for the introduction of a reverse charge by means of secondary legislation. This secondary legislation will come into effect on 1 October 2019 and will apply to supplies of specified services from that date. This includes the goods supplied with those services.

The types of construction services covered by the reverse charge are defined in the draft secondary legislation. These are based on the definition of 'construction operations' used in the Construction Industry Scheme (CIS) under section 74 of the Finance Act 2004.

The draft legislation excludes certain types of supplies of services. This is also based on CIS definitions under section 74 of the Finance Act 2004.

The draft legislation also excludes supplies of specified services that are made to customers who are not construction businesses such as a high street retailer. Also excluded are supplies of specified services where the supplier and customer are connected in a particular way, and for supplies between landlords and tenants. The meaning of connected is defined in the legislation and only applies where the customer is not a construction business and the supplier is part of that customer's corporate group. These exclusions are defined in the draft legislation as excepted supplies. Unlike for CIS, there will be no deemed contractor provisions whereby purchases become subject to reverse charge because the purchaser buys a certain amount of such purchases in a given period.

Where a VAT-registered business receives a supply of specified services (which are not excepted supplies) from another VAT-registered business on or after 1 October 2019, it accounts for that VAT amount through its VAT return instead of paying the VAT amount to its supplier. It will be able to reclaim that VAT amount as input tax, subject to the normal rules. The supplier will need to issue a VAT invoice that indicates the supplies are subject to the reverse charge.

Summary of impacts

Exchequer impact (£m)

2017 to 2018	2018 to 2019	2019 to 2020	2020 to 2021	2021 to 2022	2022 to 2023
-	-	+90	+135	+105	+75

These figures are set out in Table 2.1 of Autumn Budget 2017 as 'Construction supply chain VAT fraud: introduce reverse charge' and have been certified by the Office for Budget Responsibility. More details can be found in the policy costings document published alongside Autumn Budget 2017.

Economic impact

This measure is not expected to have any significant macroeconomic impacts.

Impact on individuals, households and families

This measure has no impact on individuals as it only affects businesses. This measure is not expected to impact on family formation, stability or breakdown but some small family owned businesses may incur additional costs to help them understand the changes, adapt their VAT systems and be able to calculate the reverse charge due.

Equalities impacts

It is not anticipated that there will be impacts on groups sharing protected characteristics.

Impact on business including civil society organisations

The reverse charge will help level the playing field for businesses by ensuring that VAT fraud is removed from supply chains. This measure will impact on around 100,000 to 150,000 businesses in the construction and building sector. The impact on business administrative burdens is expected to be significant. One-off costs include: familiarisation with the new rules and adapting VAT accounting systems and processes to enable reverse charge supplies to be calculated and reported. On-going costs include: calculating the reverse charge, keeping records of all reverse charge supplies, checking purchases are correctly treated, and reporting reverse charge supplies on VAT returns.

The reverse charge will impact on small and micro businesses, particularly in respect of loss of cash flow where VAT is no longer charged. Some businesses use the VAT they collect from customers as working capital before they pay it over to HMRC. During the consultation process and since the Autumn Budget 2017 announcement, HMRC has been working with trade associations and federations that represent small businesses in the construction and building sector. This will continue as HMRC develops the legislation and guidance in order to ensure that the changes and impacts are fully understood by all those in this sector. The small business impact is the main reason why there is a long lead in time for the measure.

Support, including guidance, will be available for all businesses who could be affected by the reverse charge during the one year lead in period. Once the reverse charge comes into effect, HMRC will also operate a light touch on genuine mistakes and penalties for a 6 month period.

There is no impact on civil society organisations.

Operational impact (£m) (HMRC or other)

HMRC will incur [initial] operational costs currently estimated at less than £1m but in the longer term compliance resources are expected to remain roughly the same. HMRC will need to ensure the reverse charge is being applied correctly.

Other impacts

Other impacts have been considered and none have been identified.

Monitoring and evaluation

This measure will be kept under review through communication with affected taxpayer groups.

Further advice

If you have any questions about this change, please contact Nick Chambers on 03000 585662 or email: nick.chambers@hmrc.gsi.gov.uk.

Declaration

Mel Stride MP, Financial Secretary to the Treasury has read this tax information and impact note and is satisfied that, given the available evidence, it represents a reasonable view of the likely costs, benefits and impacts of the measure.