

Agent or principal?

(Lecture B1140 – 13.39 minutes)

Introduction

Deals involving three parties can often be difficult to unravel as far as VAT is concerned. It is important to establish who is the agent and who is the principal, as the VAT treatment is different in each case.

It is important to consider two questions:

1. Contracts – according to contractual issues, which party is supplying or receiving services and to or from whom?
2. Commercial reality – what is the perception of the customer as far as the deal is concerned? Which party does the customer consider he is dealing with?

Hairdressers, taxi firms.....and others

There are many three-party arrangements in the modern world but there have been many tribunal cases over the years involving taxi firms, so this is a good trade to consider in order to establish the approach to adopt in deciding the agent or principal question.

Example

A taxi firm might have a number of account customers and use self-employed drivers to carry out the taxi rides. The taxi firm is usually VAT registered but not the drivers because the drivers tend to earn less than the compulsory annual VAT threshold of £85,000. In this situation, is the taxi firm acting as principal for VAT purposes i.e. output tax is due on the full value of the ride charged to the account customers, or just the commission it retains i.e. the difference between the full fare and the amount paid by the drivers?

Tribunal case - backdated registration

In the recent FTT case of Bryn Williams (TC6963), the taxpayer was not VAT registered because his net commission from account customers meant his income was below the compulsory registration threshold. But the tribunal and HMRC both agreed that he was acting as principal, and the higher sales figure meant that he should have registered for VAT in 2009, with output tax due on all sales made in that period.

It is worth noting the factors that made HMRC decide that Mr Williams was acting as principal: he negotiated the contracts with the customers as his own deal; the cars bore his business logo; he received the money direct from the customers and paid the drivers; there was a shared risk with bad debts, rather than the driver taking all of the bad debt; at the time of the customer booking a ride, Mr Williams did not know which driver would carry it out.

One of the reasons this issue is so important is because HMRC has the power to correct a late VAT registration by going back up to 20 years. It is only errors made on a past VAT return that are time capped at four years.

Internet trading

It is very common in the modern age for businesses to sell goods or services online through websites. The intention of the site is to bring together buyers and sellers but there can still be a challenge in some cases to establish if the customer is dealing with the website or the main supplier. This will obviously affect the total output tax payable by either the website or supplier, so it is important to be clear about the terms of the arrangement.

Example

Sally is VAT registered and owns a website which brings together theatre groups looking to hire props for a show with other groups who have a stock of props. The key point is that the website clearly states: "If you are unable to resolve any complaint with the owner of the goods, then contact us and we will raise it on your behalf." This is a clear indication that the main supply excludes the website owner – she is acting as an agent and receiving a commission payment only.

Tribunal case – online services

In the FTT case of All Answers Ltd (TC6845), the company supplied completed essays, coursework and dissertations to students studying for exams, the essays being written by academic experts in a particular subject, enabling the students to submit them to their course providers for assessment.

The VAT challenge came down to the classic question of "who is supplying what and to whom." Was the taxpayer acting as an agent in bringing together the author and the student i.e. where output tax is only payable on the 2/3 of the commission retained by the agency? Or was the commercial reality that the author was working as a subcontractor for the taxpayer, and the taxpayer was supplying a completed essay as principal to the student i.e. output tax is due on the full payment made by the student? The court agreed with the taxpayer that the company was acting as principal, with a disputed assessment for £904,168 therefore being correct.

This case highlights the important point that if there is a contradiction between the terms and conditions of a deal and the commercial reality of what is happening in practice, then the commercial facts always take precedence. But the best tip is that you should always check that the two issues are in tandem and do not contradict each other.

Tips for internet sites

As explained above, the economic and commercial reality of a deal always supersedes what is said on a contract or sales invoice. Here are important questions to consider if a website arrangement is in place:

- Do the buyers and sellers know each other's identity;
- Who do the customers consider they are dealing with when parting with money?
- What invoices are raised by the website owner and provider of the services?
- What evidence is there that the website host is only fulfilling an agency function?

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