

Cross-border services – reverse charge (Lecture B1075 – 16.11 minutes)

Services – some basic principles

VAT is chargeable in the country where the supply takes place for VAT purposes. The only question is whether the supplier charges it directly, or whether the customer accounts for it locally (i.e. using reverse charge).

There are a number of possibilities.

1. If both supplier and customer are in the UK and the supply takes place in the UK for VAT purposes, the supplier charges the customer VAT in the normal way

If the supply takes place in a different country for VAT purposes (i.e. under a special rule), VAT would be accounted for in that country. If the customer has a business or fixed establishment in that country, it would have to account for the VAT under reverse charge.

If not, the supplier would have to register in the foreign country and charge the customer the foreign VAT.

2. If the supplier is in the UK but the customer is outside the UK, then if the place of the supply is the UK, the supplier must charge UK VAT.

If the supply takes place where the customer belongs, if the customer is a business customer, it must account for the VAT under the reverse charge. The supplier has no foreign VAT obligation in this situation. If the customer is not a business customer, the supplier must register for VAT in the country where the supply takes place and charge the customer appropriately.

If the service is electronic, or is a telecommunication or broadcasting service, the supplier can register with HMRC for its Mini One-Stop Shop (MOSS) service and file a special return to account for the foreign VAT with HMRC which will then pay the foreign tax authorities.

3. If the supplier is outside the UK (either inside or outside the EU, it does not matter) and the customer is a business customer in the UK and the place of supply is the UK, the customer must account for the VAT under the reverse charge procedure.

If VAT registered, the customer accounts for output VAT in Box 1 and then recovers this as appropriate in Box 4.

If not VAT-registered, the value of the services received count as turnover in calculating if the customer turnover has exceeded the registration limit. If it requires the customer to register then VAT will be reported on later supplies received after registration as above.

If the supplier is outside the UK and the customer is not a business customer then the supplier must register in the UK and charge the VAT if the place of supply is the UK.

These rules apply the same way across the EU so, for example, if you or your client supplies services where the place of supply is another EU country, and the customer is not a business customer in that country, you/your client must register for VAT (there isn't usually a turnover threshold in this situation) and charge the customer the appropriate amount of VAT in that country.

Example – B2B supply

A UK-based VAT registered management consultant raises a sales invoice to a Germany company for work carried out from its UK offices.

The sale is outside the scope of VAT – the place of supply is Germany. The supplier records the sale in Box 6 of its VAT return (outputs) and also includes it on a quarterly EC Sales List (calendar quarter basis).

If it is VAT registered, the German customer will apply the reverse charge and declare output tax (value of invoice multiplied by German rate of VAT i.e. 19%) and claim the same amount back as input tax assuming the business is not exempt or partly exempt and the service is not partly used for non-business or private purposes.

The customer also records the net amount of the invoice in both Box 6 and Box 7 (outputs and inputs) but nothing is entered in Boxes 8 and 9 because the sale is for services and not goods.

If the German company was not VAT registered in Germany, the supply is still B2B and the reverse charge would still apply. The German company would add the value of the service to its own taxable supplies to see if this pushed it over the VAT registration limit in Germany which would require it to register there.

Example – B2C supply

The management consultant from the previous example completes some work for a charity in, say, Italy that does not make business supplies and is not VAT registered.

This is a B2C sale covered by the general rule, so the supplier charges 20% UK VAT to the customer, even though the charity is based outside the UK.

Rationale for reverse charge

Cross-border reverse charging was introduced to try to create a level playing field between using domestic or foreign service-providers.

If a business could not recover all the VAT it was charged, it might be tempted to use a foreign supplier that would charge it a smaller rate of VAT than a domestic supplier.

Reverse charging the supply means that the same rate of VAT would apply (to a VAT registered customer) irrespective of where the supplier was located.

Example

A partially exempt business with an input recovery rate of 60% has received two tenders for professional services which will be performed in the UK:

1. From a UK supplier, who will charge £10,000 plus 20% VAT;
2. From a supplier in Luxembourg who will charge £10,000 but will not charge VAT.

If the business used the UK supplier it would be charged £12,000 in total, but would recover (60% x £2,000) £1,200 VAT, giving a net cost of £10,800.

If it used the Luxembourg based supplier, it would be charged £10,000 but would then have to account for £2,000 output VAT in box 1 of its VAT return. It would only be able to recover £1,200 input VAT in box 4, and so would pay HMRC £800 of net VAT, making its total cost £10,800 – the same as if it used the UK supplier.

Contributed by Malcolm Greenbaum