

VAT and food - clearing the muddy waters!

(Lecture B1104 – 14.03 minutes)

The catering business is booming, with coffee shops, cafes, mobile catering units and restaurants continuing to flourish. An important issue to ensure profits are maximised is to correctly account for VAT on sales, recognising which supplies of food and drink qualify for zero-rating and those that are always standard rated.

Summary of basic rules

All supplies of food and drink consumed inside a catering establishment are standard rated. Cold food sold on a take away basis qualifies for zero-rating in many cases but there are exceptions where VAT is still payable e.g. sales of chocolate bars, crisps and fizzy drinks are all standard rated.

As a planning tip, the best approach is for your catering clients to work on the assumption that all sales are standard rated, and then specifically identify those sales of cold food and drink that qualify as zero-rated if consumed away from the premises. The challenge is to then ensure that all staff are aware of these opportunities for zero-rating. The zero-rated sales will need to be recorded separately, usually based on a multi-button till.

Defining 'the premises'

Before considering whether food is classed as hot or cold, it is important to understand the boundaries for a business as far as its premises are concerned. HMRC used to take the view that a whole site would be classed as 'premises' (e.g. a football ground) but that interpretation changed following the tribunal case of *Compass Contract Services UK Ltd* (CA[2006]STC1999).

It is now accepted that the premises only includes the specific area surrounding an establishment e.g. tables and chairs outside the café or a shared seating area inside a shopping centre which services the customers of a range of catering outlets (HMRC Notice 709/1, para 3.2).

A catering business that provides both on premises and take away food will need to recognise the 20% VAT difference on most cold food items for pricing purposes. Price lists should be clearly displayed so the customer is aware of the difference between take-away and on-site prices eg cheese roll (in) £2.40; cheese roll (take away) £2. The business might want to add a further charge to its 'in' prices to reflect the extra service involved e.g. £3 for cheese roll (in); £2 (take away).

Take-away food – the law

The legislation on VAT and take-away food served by cafes, sandwich bars, fish and chip shops and similar outlets is quite lengthy.

VATA1994, Sch 8, Group 1 makes an exception to zero-rating on food if it is 'a supply in the course of catering' – in other words, catering is standard rated.

Note 3 to this Group then confirms that catering includes 'any supply of hot food for consumption off those premises' i.e. take away food.

Note 3B then gives further detail about what is classed as 'hot food,' confirming it must be hot at the time it is sold i.e. either heated for that purpose, or kept hot after being heated, or provided to a customer in packaging that retains heat. Note 3B also captures supplies where the food is 'advertised or marketed in a way that indicates that it is supplied hot'.

It is important to ensure that clients do not incorrectly label food as hot when the reality might be that it is 'cooling down' after being taken out of the oven. If a product is promoted (marketed) as being hot, it will be subject to 20% VAT on take away sales but there is no problem with describing an item as 'freshly baked' (HMRC Notice 709/1, para 4.3, Test 5).

The definition of hot food – and recent tribunal case

Note 3C in the legislation confirms that food is deemed to be hot if it is served above the 'ambient air temperature' in the premises in question. It is deemed to be 'kept hot' (another phrase in Note 3B which requires a definition) if it is retained in such a way that it remains hot after it has been cooked i.e. the natural cooling process is thwarted.

The recent case of Pegasus (Manchester) Ltd (TC6382) related to an assessment for £114,122 covering a four-year period, in relation to take away sales of Afro/Caribbean food such as rice, wraps and curries, which the taxpayer claimed were zero-rated as cold food. HMRC claimed they were hot and therefore standard rated.

During preparation in a kitchen on site, the food under dispute was cooked to a temperature of 90/100C but it was then cooled in the kitchen in the pans in which it had been prepared, with a fan being used to assist the cooling process. Once cooled to 19/20C, it is placed in gastro norm containers which fit into the bain marie used in the retail unit (a bain marie is a water-based container powered by electricity). Food is kept in the bain marie for 1 to 1.5 hours, and the bain marie has an average temperature of 56C.

All parties agreed that the 'ambient room temperature' on the premises was 28C to 30C. This was quite high but accepted by HMRC because of the cooking going on from other units surrounding the client's trading area. The taxpayer claimed this was higher than the temperature of the food when it was served to customers, even though the bain marie had a temperature of 56C.

The judge dismissed the taxpayer's claim, agreeing with HMRC that the temperature of the bain marie must be reflected in the temperature of the food as well, the aim being so that it was served hot to the customer.

Exceptions to zero-rating

The legislation on the VAT liability of food is contained in VATA1994, Sch 8, Group 1. It confirms that 'food of a kind used for human consumption' is zero-rated but then contains exceptions to the zero-rating, followed by exceptions to the exceptions, and then exceptions to the exceptions to the exceptions. It is fair to say that the legislation will never win an award for 'plain English'.

But to summarise, here are some of the key items that are still standard rated when sold by a business on a take-away basis:

- Ice cream and similar products but excluding frozen yoghurt that's designed to be thawed before being eaten;
- Confectionery (chocolates, sweets and candies) apart from cakes and some biscuits e.g. a biscuit partly or wholly covered in chocolate is standard rated;
- Alcoholic beverages;
- Other beverages e.g. carbonated drinks such as lemonade and cola; mixers such as tonics and sodas, as well as fruit cordials, squash and bottled water;
- Hot drinks.

Note - it is sensible for your clients to refer to HMRC Notice 701/14 to ensure they are applying the correct VAT liability to their sales of food and drink. But don't forget that all food and drink sold for consumption on the premises of a business is always standard rated.

What is 'catering'?

We have established that food and drink sold on the premises of an establishment is always classed as catering, along with hot food and drink sold on a take-away basis. But other supplies of food and drink could still be classed as catering and therefore subject to VAT.

Example

Jean runs a café and has been asked to provide a finger buffet for 20 people for a local company. The buffet will consist of a range of sandwiches, cakes, sausage rolls and pork pies (all cold food), ready for consumption as soon as it arrives at the company's office. Should she charge VAT to her customer?

Catering is "a supply involving a significant element of service" – and HMRC take the view that food and drink supplied as part of a contract is classed as catering. It would be different if Jean turned up at the office of her customer and sold sandwiches to staff from a tray but a pre-ordered buffet is classed as catering (HMRC Notice 709/1, para 2.2.2).

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