

Quick Reference Guide

Changes to VAT rules to erode the benefits of salary sacrifice?

Much has already been written on the change of VAT rules on salary sacrifice, but as the implementation date of 1 January 2012 draws ever nearer, this bulletin is designed to serve as a timely reminder to employers to review their arrangements and ensure systems are in place to cope with the changes.

Although businesses have had some time to absorb the significance of this change of policy following HMRC's announcement at the end of July (Revenue & Customs Brief 28/11), employers should also make themselves aware of the temporary transitional concession announced in October that permits deferred implementation of the new rules for existing salary sacrifice arrangements that were already in place on or before 27 July 2011. Full details of the transitional arrangements in these circumstances can be found in Revenue & Customs Brief 36/11.

Background

Historically, HMRC made a distinction between salary sacrifice and deduction from salary in return for supplies of goods or services by the employer. It was accepted that salary sacrifice did not represent 'consideration' for a supply whereas deduction from salary was treated as payment in return for the benefits.

The decision in the Astra Zeneca case in the Court of Justice of the European Union (ref C-40/09) concluded that HMRC's approach on salary sacrifice was not supported in law and so had to be seen to constitute consideration for a taxable supply.

HMRC have clarified that, in their view, the decision does not affect interpretation of UK Direct Tax rules so the changes are restricted to VAT legislation. It should also be borne in mind that not all benefits provided under salary sacrifice schemes will now be automatically subject to VAT e.g. healthcare insurance and childcare vouchers. As these are VAT exempt, output VAT will not fall due on such schemes but any input tax incurred in connection with the making of these benefit provisions will be subject to the VAT partial exemption rules so may become non-deductible VAT.

Common situations likely to be affected

1. Face Value Vouchers

The Astra Zeneca case was concerned with vouchers and the judgment means that although any VAT charged on the cost of the acquisition of vouchers is claimable as input tax, output tax becomes due within the value of the consideration of the benefit once supplied on to employees after 1 January 2012.

2. Motor cars

Due to the 'blocking' of input tax on buying (100%) or leasing (50%) of motor cars, most businesses will be unaffected as no output tax is due on the provision of cars to employees. However, if a vehicle has not been subject to a restriction of input tax then output tax will be due on the value of the benefit attributed to making it available to staff.



3. Food and catering

(i) Provided free of charge

If this benefit is available to all staff then no VAT is due.

(ii) Payment by staff or deduction from salary

This has always been standard rated (catering) or zero rated (food) and remains unchanged.

(iii) Payment made by way of salary sacrifice

This becomes liable to output tax (catering) from 1 January 2012. Provision of zero rated food remains unchanged.

4. Childcare vouchers and healthcare insurance

As mentioned above, the supply of childcare vouchers and the provision of insurance are both exempt from VAT and will not therefore attract an output tax liability. However, under the partial exemption rules, any VAT connected with the cost of such benefits such as administration fees could become non-reclaimable and businesses should review their partial exemption status/methods.

5. Cycle to Work Scheme

From 1 January 2012, output tax will become due on the value of the salary foregone by the employee in exchange for the hire or loan of a bicycle but any input tax incurred by the employer on the acquisition of the bicycles will remain reclaimable. Output tax will also still be due on the disposal of any bicycles and HMRC will accept the valuation tables used for Direct Tax purposes to ease administration.

If you have not already reviewed your own salary sacrifice arrangements following this significant change, it is strongly recommended you do so without further delay. HMRC will almost certainly take the view that there is no excuse for not having adopted these changes, having given sufficient notice to do so.

If you feel that you need further guidance or assistance implementing changes to your accounting systems to accommodate the revised rules, please do not hesitate to contact Abbey Tax and ask for one of our VAT Consultants on **0870 166 6270 or email marketing@abbeytax.co.uk**