Tackling VAT evasion via online marketplaces – fulfilment houses

Indirect Tax

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FB 2016 introduces a package of measures to combat abuse and non-compliance by overseas businesses that import goods for sale via online marketplaces. The measures will also affect all UK-based businesses that fulfil orders of imported goods and those involved in transporting them. HMRC is also consulting on a fulfilment house due diligence scheme – we seek your views.

Background

Budget 2016 announced measures to tackle VAT loss arising from overseas businesses failing to account for the tax on sales of goods into the UK using online marketplaces. The Treasury estimates this abuse accounts for between £1bn and £1.5bn of the total VAT gap and that implementing these measures will secure future revenues of £65m (2018-19) rising to £365m (2020-21). It is within the context of such high forecasts that these measures need to be examined.

Summary of measures

There are two measures in FB 2016, along with a consultation document:

1. FB 2016 Clause 112 amends HMRC's powers to direct overseas businesses that sell goods into the UK to appoint a VAT representative here to account for output tax and pay it to HMRC. The power will be enforced by making the representative jointly and severally liable for the VAT due
2. FB 2016 Clause 113 allows HMRC to hold the online marketplaces through which goods are sold jointly and severally liable for the VAT due. It is worth noting that the measures are not restricted to third-country businesses: they

include any non-UK established business, which raises issues of whether they are compatible with EU law.

3. HMRC consultation – proposing a due diligence scheme requiring fulfilment houses to register and undertake ‘fit and proper’ checks on the goods they fulfil. HMRC would have powers to remove or reject a fulfilment house’s approval to trade, with penalties and possibly criminal sanctions. HMRC acknowledges the scheme will place cost and administrative burdens on particular businesses (that will be defined) and seek to obtain the views of businesses affected.

Due diligence scheme – your views sought

The CIOT will respond to the consultation and our technical team requests your views (to indirecttax@ciot.org.uk). However, many of the 66 questions are aimed at affected businesses to find out more about the impact these measures may have. We recommend that members also provide the statistical information requested by HMRC because our response will concentrate on these areas:

- How goods arrive in the UK and what knowledge exists of the source and destination of the goods.
- The effectiveness of a narrow or wider definition of ‘fulfilment house’.
- Exclusions for small businesses.
- Proposed checks, record-keeping, burdens, benefits and sanctions.
- Suggested alternatives.

Effectiveness of the due diligence scheme

HMRC has proposed a definition of a fulfilment house as:

> *‘… a business that provides services of storage, breaking bulk, unpacking, re-packing and making (or arranging) subsequent delivery to its clients’ customers of goods imported from outside the EU which have been cleared for customs purposes’.*

There is a suggestion that this definition could be applied more widely to include businesses that fulfil their own orders to prevent the compliance rules being avoided.

The due diligence scheme aims to deter abuse in this sector by requiring key businesses in the supply chain to work only with legitimate and compliant suppliers. HMRC considers this a ‘necessary and proportionate response’ to the VAT at risk.

Respondents will no doubt wish to give particular attention to the likely effectiveness of the measures, which largely seek to use intermediaries to police the relevant transactions rather than HMRC holding to account those that are non-compliant. HMRC acknowledges this will increase administrative burdens and costs but wishes to minimise this as far as possible for legitimate businesses.

Conclusion

The consultation raises several issues. The scheme assumes that the fulfilment and transport parts of the supply chain are the best sources of information and requires those businesses to act as enforcers. However, another policy might be to consider taxing the sales of goods as the default option by directing the online marketplace to act as an undisclosed agent (using Article 28 PVD and s.47 VATA 1994). The effect would be a supply to and by the marketplace provider which would then account for VAT on the full sales price of the goods. Qualifying overseas businesses could opt out of this arrangement if they could prove they were compliant or not in business. The onus would then be on the overseas business to prove its compliance.

Since the government’s measures will not apply automatically (HMRC will serve a notice on the online marketplace), a question arises as to how HMRC will identify the businesses that will be required to comply with directions. The consultation also does not indicate how HMRC will prevent businesses simply closing down one identity and creating a new one.

Given the amounts involved, it is clear that measures are needed to prevent loss whether due to evasion or inadvertent non-compliance. The key question will be how to balance the effectiveness of such measures against the impact on legitimate business, particularly small and medium-sized businesses.