Self-billing: is it a risk or opportunity?

Indirect Tax



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We consider the benefits of self-billing invoicing systems and whether the modern digital world means they should be considered by more business owners.

Key Points

What is the issue?

Self-billing systems are effective when the customer rather than the supplier knows the value of a supply of goods or services; e.g. for many supplies in the scrap metal trade. A self-billed document can save time and administration costs and hopefully lead to quicker payment for the supplier.

What does it mean to me?

A self-billing arrangement is a diversion from the usual system of a supplier issuing a tax invoice. Agreements must always be treated with full diligence because customers are issuing documents which give them an input tax entitlement, which is a high-risk outcome as far as HMRC is concerned.

What can I take away?

Suppliers and customers must regularly review self-billing agreements – and renew them if deadlines have passed – and customers should also check that suppliers have not deregistered.

There are many situations when a business supplies goods or services but relies on the customer to confirm the amount that can be charged at a particular time. As a practical example, think of a builder who invoices on a monthly basis for a regular contract and relies on their client's surveyor to confirm the value of measured work carried out by a particular date. Alternatively, think of an author who is paid on a word-count basis and is not sure how the publisher counts the words; e.g. are headlines, bylines and quotes included?

In some cases, it makes sense for the customer to issue the sales invoice on behalf of the supplier and – in VAT speak – this outcome is referred to as self-billing. The customer will include VAT on the self-billed invoice if appropriate and claim input tax; the supplier must declare output tax on the return that includes the tax point.

In this article, I will consider some practical issues of self-billing and also if more businesses should consider its adoption.

Key features

If a customer issues a self-billed invoice to a supplier, the supplier must not issue a tax invoice for the same supply. This is logical and a self-billing contract agreed between both parties – a condition of operating any self-billing system – must make this clear. If a supplier and customer agree to adopt self-billing, it will apply to all supplies; they cannot pick and choose.

A self-billing agreement must be signed before any invoices are issued and it must meet the following conditions:

- The supplier and customer both agree to adopt it, either signing an agreement on paper or electronically.
- HMRC has provided an example in its public notice which can be used or adapted (see HMRC Notice 700/62 s 8).
- The self-billed invoice issued by a customer is the only acceptable document for VAT purposes. It must always show the ‘tax point’; i.e. the date when the supplier must declare output tax to HMRC on their return. It must also include a clear reference to self-billing.
- All agreements must include a start and finish date, which might be for the duration of a particular contract or, more likely, be based on a 12-month or two-year fixed period. Both parties can agree to an extension but there must be written evidence of this in case of a query by HMRC.
  See VAT Regulations 1995 Reg 13(3).

Note: Self-billing does not require HMRC’s permission. However, an officer has the right to ask to see the agreement and, in a worst case scenario, could seek to disallow input tax claimed by the customer if the agreement is flawed.

VAT status of supplier

A customer must always know which of its suppliers are VAT registered so that 20% VAT can be added to the invoice value if the work carried out is standard rated, or 5% VAT if it is subject to the reduced rate. As explained above, the supplier will account for output tax on the return that includes the ‘tax point,’ unless it uses the cash accounting scheme (CAS) when the payment date is relevant.

I can imagine that many readers are shouting out: ‘How will the customer know if a supplier suddenly deregisters, perhaps because their annual taxable sales are less than the deregistration threshold of £88,000?’

The answer is that the customer should adopt a standard audit procedure to regularly confirm that suppliers are still registered. For example, a labour-only subcontractor is more likely to deregister than a large building business that employs ten workers and also supplies materials, so a risk-based approach should be adopted. If there is any doubt, then HMRC’s VAT number checker-service can be used (see tinyurl.com/bdz2avdd).

A supplier can refuse to accept a self-billing arrangement proposed by their customer but this might be unwise:

- If the customer knows the value of a supply rather than the supplier, it makes sense for the customer to drive the invoicing process (see ***Author Alice: paid by the word*****).**
- A self-billing system can speed up the payment process because the supplier does not need to contact the customer and ask: 'How much should we invoice you for?'
- There is a commercial risk that a customer will refuse to do business with a supplier that has rejected a self-billing proposal.
- Some industries adopt self-billing as the default position; e.g. scrap metal, clothing and waste recycling traders. It is often sensible to comply with industry norms.

Note: Many supplies made by subcontractors to contractors in the construction industry could be subject to the reverse charge; i.e. the customer accounts for output tax and the supplier is not paid VAT. The principle of reverse charge accounting extends to self-billed documents in the same way as VAT invoices issued by a supplier.

Author Alice: paid by the word

Alice writes lifestyle articles for Bovian Publisher Ltd and is paid 15p per word plus VAT. It is likely that only the editor will know the exact word count, so a self-billing arrangement should be more efficient and save time. Alice also receives a royalty payment based on the number of times her articles are read online; again, the amount payable will be known by the publisher and not herself.

Note: The accounting staff at Bovian should regularly check that Alice is VAT registered, at least annually.

Case law

Many VAT enthusiasts will remember the long-running case of *GB Housley Ltd* [2016) EWCA Civ 1299 about whether the absence of a valid self-billing agreement for a scrap metal business gave HMRC the power to disallow input tax claimed by the

company. If so, should HMRC have accepted alternative evidence to support the claim, as allowed by the Value Added Tax Regulations 1995 Reg 29? See HMRC's VAT Input Tax manual VIT31200.

The First-Tier Tribunal supported the taxpayer. The Upper Tribunal agreed with HMRC but the Court of Appeal discharged HMRC's assessment because the department did not use its discretion to consider alternative documents. Overall, the taxpayer was probably fortunate to win the case but the clear message is that all self-billing conditions should be met to avoid a possible challenge from HMRC.

The risk of issuing self-billed invoices to a supplier that has deregistered was highlighted in the case of *Taygroup Ltd* [2013] UKFTT 336. The company claimed input tax on some supplies made by unregistered suppliers, and the tribunal agreed with HMRC that the company had not acted diligently to ensure that all self-billing conditions were met and that the agreements were renewed after 12 months.

To share another tale, a business issued self-billed invoices for services supplied by a sole trader and was then told by HMRC on a compliance visit that the supplier had deregistered two years earlier and that input tax could not be claimed on these supplies. A bit of Hercules Poirot investigating revealed that the sole trader had incorporated his business and the limited company had registered for VAT with a new number. See ***Top tip: use HMRC's self-billing agreement.***

Top tip: use HMRC's self-billing agreement

A tip for customers is to use HMRC's recommended self-billing agreement, which includes the following clause:

'The self-billee agrees … to notify the customer immediately if they change their VAT registration number; cease to be VAT registered; or sell their business or part of their business.'

If a supplier fails to meet this condition, they should accept that they have caused a problem and repay VAT incorrectly paid by a customer; i.e. to contra the input tax wrongly claimed by the customer. (See VAT Notice 700/62, para 3.1.)

What are the risks?

The tribunal cases highlight the main risk of self-billing for a customer; i.e. not being aware that a supplier has deregistered and is no longer a taxable person.

The main risk for a supplier is to wrongly think that customers decide the rate of VAT to charge on a job and that this should be accepted. It shouldn’t; it is always the responsibility of the supplier to charge the correct rate.

To share a tale, I used to act for a flooring business and the company had a big job with a building contractor to fit wood flooring to a new building. The contractor issued self-billed invoices to my client and zero-rated them on the basis that the owner of the building was a care home and it qualified as a new building to be used for a ‘relevant residential purpose’ and the building supplies were therefore zero-rated. The contractor provided a copy of the VAT certificate issued by the care home to support the zero-rating. The correct outcome is that only services supplied by the contractor to the care home operator are zero-rated; all supplies made by subcontractors to a contractor are standard rated. It took about six months for the contractor to accept this argument!

The risks to a supplier are less if all sales are subject to the same rate of VAT – such as a scrap metal business – rather than an industry where the liability can get complicated.

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