

VAT Strategy: Input Tax deduction without a valid VAT invoice

Statement of Practice

March 2007



1. This Statement of Practice explains and clarifies HMRC's policy in respect of claims for input tax supported by invalid VAT invoices. It also explains why amendments were made to section 24(6)(a) and paragraph 4(1) of Schedule 11 to the Value Added Tax Act 1994 (VATA), and regulation 29(2) of the Value Added Tax Regulations 1995 to introduce new measures. These changes were effective from **16 April 2003** and apply to supplies made on or after this date. The statement of practice was first issued in July 2003 and has now been revised to provide clearer guidance and the updated legal position. This guidance does not apply to situations where HMRC may deny recovery of input tax for other reasons such as "abuse" of the right to deduct.

Why were changes needed?

2. These changes were made to address the increasing threat to VAT receipts by the use of invalid VAT invoices and are part of the Government's strategy to address fraud, avoidance and non-compliance in the VAT system. They are a proportionate and necessary response to a systematic and widespread attack on the VAT system, where the use of invalid VAT invoices is becoming an increasing pressure on revenue receipts, particularly in those business sectors involved in the supply of the goods listed at Appendix 3. In addition to the revenue loss, this has led to distortion of competition.

3. For the vast majority of business there will be no change, and for businesses trading within the targeted sectors the measure will only impact if you have an invalid invoice. If you are a VAT registered business, and you have been issued with an invoice that is invalid, you should be able to return to your supplier and ask them for a valid VAT invoice that complies with the legislation. If for some reason you cannot, this Statement of Practice sets out whether or not you may be entitled to input tax recovery. In most cases, provided businesses continue to undertake normal commercial checks to ensure their supplier and the supplies they receive are '*bona fide*' prior to

doing any trade, it is likely they will be able to satisfy HMRC that the input tax is deductible. .

The 'right to deduct' principles

4. The basic principle of EU and UK law underlying input tax recovery is that of neutrality. In practice, this means that any business that makes taxable supplies has the right to deduct the VAT incurred on goods or services that form a cost component of those supplies. EU and UK law also provides for rules governing the exercise of the right to deduct VAT. These fundamental VAT principles governing the recovery of VAT are not being changed.

5. A business has incurred input tax if the following conditions are met;

- there has actually been a supply of goods or services;
- that supply takes place in the UK;
- it is taxable at a positive rate of VAT;
- the supplier is a taxable person, i.e. someone either registered for VAT in the UK, or required to be registered;
- the supply is made to the person claiming the deduction;
- the recipient is a taxable person at the time the tax was incurred; and
- the recipient intends to use the goods or services for his business purposes.

6. If you are a taxable person, in order to exercise your basic right to deduct input tax, you must hold a **valid VAT invoice**. Without a valid VAT invoice, there is no right to deduct input tax. However, in the absence of such an invoice, you may still be able to make claims for input tax, but these claims are subject to HMRC's discretion. This of course assumes that a taxable supply has taken place. Where HMRC question the fact that an underlying supply has taken place, these provisions do not apply.

What legislative changes have been made?

7. The change to section 24(6)(a), VATA permits HMRC to consider evidence other than that contained in documents when exercising their discretion (paragraph 4(1) of schedule 11 is merely a consequential amendment to this change). Before this change, regulation 29(2) permitted HMRC to accept alternative **documentary** evidence to support input tax

deduction without a valid VAT invoice. The amendment to regulation 29(2) simply permits HMRC, in applying their discretion, to consider evidence other than just documents.

What constitutes a valid VAT invoice?

8. A valid VAT invoice is one that meets the full legal requirements as set out in regulations 13 & 14 of the Value Added Tax Regulations 1995 (Statutory Instrument 1995/2518). The contents of a valid VAT invoice should show the following information (as set out in regulation 14(1)):

- (a) an identifying number;
- (b) the time of the supply;
- (c) the date of the issue of the document;
- (d) the name, address and registration number of the supplier;
- (e) the name and address of the person to whom the goods or services are supplied;
- (f) [Omitted by SI 2003/3220, reg. 7(a)]
a description sufficient to identify the goods or services supplied(h) for each description, the quantity of the goods or the extent of the services, and the rate of VAT and the amount payable, excluding VAT, expressed in any currency
- (i) the gross total amount payable, excluding VAT, expressed in any currency
- (j) the rate of any cash discount offered;
- (k) [Omitted by SI 2003/3220, reg. 7(a).]
- (l) the total amount of VAT chargeable, expressed in sterling.
- (m) the Unit Price

A self-billed invoice is not a valid invoice unless the recipient meets the conditions for self-billing in Reg 13 (3A) and (3B). The conditions for self-billing are also set out in Notice 700/62- Self Billing.

9. A taxable person may issue either a less detailed tax invoice where the charge made for an individual supply is £250 or less including VAT, or a modified tax invoice with the agreement of customer. If this is the case, not all

of the above information is required. Information about less detailed and modified tax invoices can be found in Section 16.6 of Public Notice 700 (The VAT Guide). Copies can be obtained from the National Advice Service on 0845 010 9000 or downloaded from HMRC's web site at www.hmce.gov.uk.

What is an invalid VAT invoice?

10. An invoice that falls short of any of the requirements laid down in Reg 14(1) of SI 1995/2518 is an invalid invoice-see Paragraph 8 above. This includes situations where some or all of the details do not relate to the person/business that made the supply or the details shown are those of a company that has gone into liquidation **or is missing at the time the supply is made.**

What do I do if I have an invalid VAT invoice?

11. The simplest thing is to ask your supplier to issue a valid VAT invoice (suppliers are legally obliged to do this). HMRC If a taxable supply has taken place but a revised invoice cannot be obtained HMRC may apply their discretion to allow recovery of input tax.

How do I know I have an invalid VAT invoice?

12. The first step is to ensure that you hold an invoice that contains all the right information. It is difficult to spot an invalid invoice where a false name, address or VAT number has been used. HMRC have established a team who can confirm that supplied VAT registration details are current, valid and match information held by HMRC. This is **not** authorisation of a transaction with that VAT registration, but can help, along with other checks to verify the legitimacy of your supplier. Such information can be obtained by telephoning 01737 734 then 516, 577, 612 or 761.

Invalid Invoice and HMRC's Discretion.

A proper exercise of HMRC's discretion can only be undertaken when there is sufficient evidence to satisfy the Commissioners that a supply has taken place.

Where a supply has taken place, but the invoice to support this is invalid, the Commissioners may exercise their discretion and allow a claim for input tax credit.

For Supplies/transactions involving goods stated in Appendix 3 HMRC will need to be satisfied that:

- The supply as stated on the invoice did take place
- There is other evidence to show that the supply/transaction occurred
- The supply made is in furtherance of the trader's business
- The trader has undertaken normal commercial checks to establish the bona fide of the supply and supplier
- Normal commercial arrangements are in place- this can include payment arrangements and how the relationship between the supplier/buyer was established

What do I do if my checks indicate that a fraud exists?

15. If your checks indicate that there may be a fraud you should consider whether you wish to continue with the transaction. You may also wish to inform HMRC Confidential on 0800 595 000.

I have an invalid VAT invoice; can I still recover input tax?

16. Not automatically. However, HMRC may apply their discretion and still allow recovery.

How will HMRC apply their discretion?

17. For supplies of goods not listed at Appendix 3, claimants will need to be able to answer most of the questions at Appendix 2 satisfactorily. In most cases, this will be little more than providing alternative evidence to show that

the supply of goods or services has been made (this has always been HMRC's policy).

18. For supplies of goods listed at Appendix 3, claimants will be expected to be able to answer questions relating to the supply in question including all or nearly all of the questions at Appendix 2. In addition, they are likely to be asked further questions by HMRC in order to test whether they took reasonable care in respect of transactions to ensure that their supplier and the supply were 'bona fide'.

19. As long as the claimant can provide satisfactory answers to the questions at Appendix 2 and to any additional questions that may be asked, input tax deduction will be permitted.

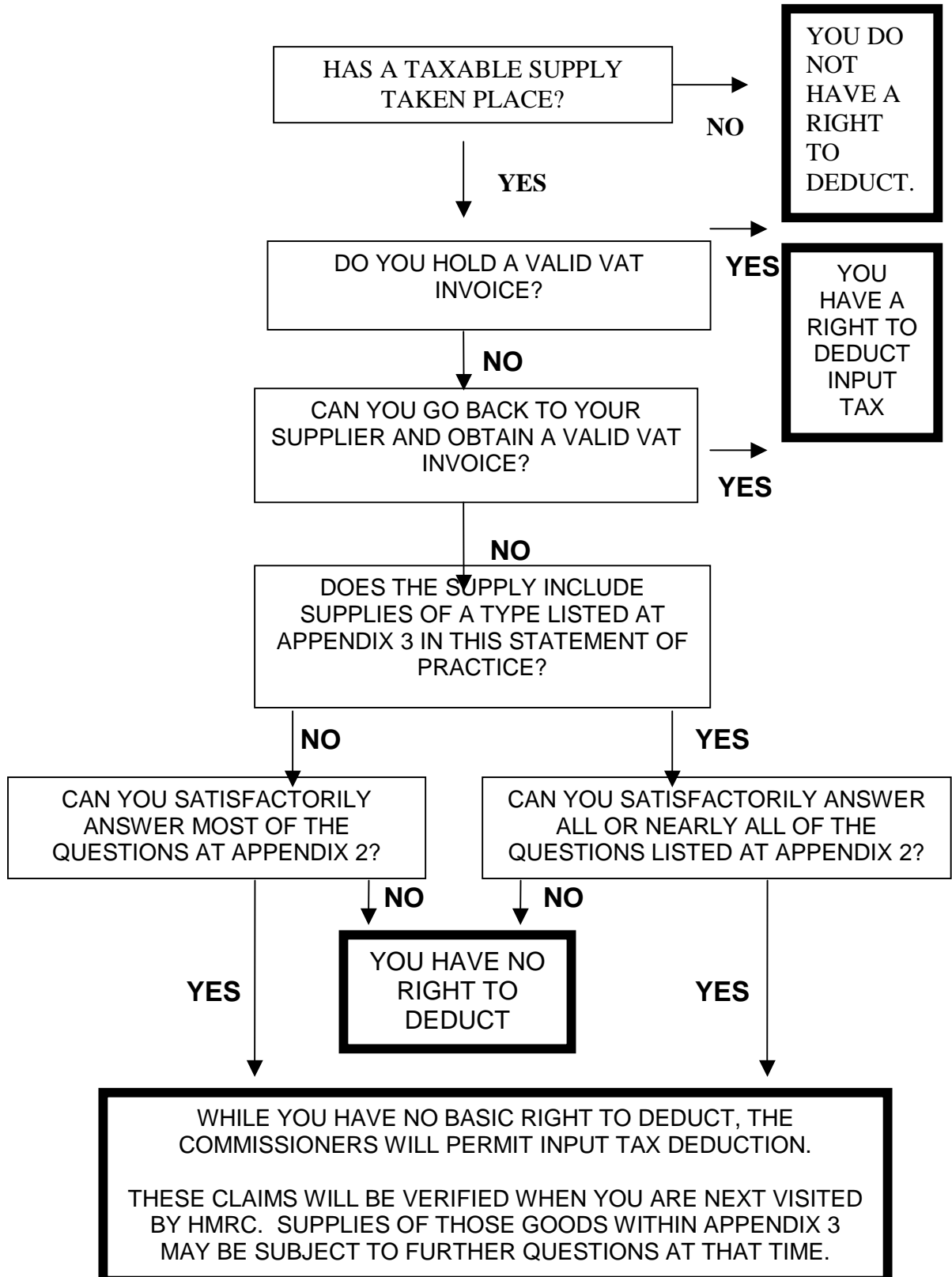
20. Decisions on when to disallow VAT claims will only be made after an independent central review of the case has been carried out.

Can I appeal against HMRC's decision?

21. If HMRC refuse to allow deduction of input tax under this Statement of Practice, unsuccessful claimants can first ask for a reconsideration of the decision. Should that be unsuccessful, they will then be able to appeal against HMRC's decision to the VAT & Duties Tribunal.

Appendix 1

Decision Flowchart



Appendix 2

Questions* to determine whether there is a right to deduct in the absence of a valid VAT invoice

1. Do you have alternative documentary evidence other than an invoice (e.g. supplier statement)?
2. Do you have evidence of receipt of a taxable supply on which VAT has been charged?
3. Do you have evidence of payment?
4. Do you have evidence of how the goods/services have been consumed within your business or their onward supply?
5. How did you know that the supplier existed?
6. How was your relationship with the supplier established? For example:
 - How was contact made?
 - Do you know where the supplier operates from (have you been there)?
 - How do you contact them?
 - How do you know they can supply the goods or services?
 - If goods, how do you know the goods are not stolen?
 - How do you return faulty supplies?

*This list is not exhaustive and additional questions may be asked in individual circumstances

Appendix 3

Supplies of goods subject to widespread fraud and abuse

- a) **Computers and any other equipment**, including parts, accessories and software, made or adapted for use in connection with computers or computer systems.
- b) **Telephones and any other equipment**, including parts and accessories, made or adapted for use in connection with telephones or telecommunications.
- c) **Alcohol** - those alcoholic liquors liable to excise duty, which are defined by section 1 of the Alcoholic Liquor Duties Act 1979 or in any regulations made under that Act (e.g. spirits, wines and fortified wines, made-wines, beer, cider and perry).
- d) **Oils** - all oils that are held out for sale as road fuel.