

Review



VAT's a sacrifice employers may have to make

We reported in our August 2010 Review (please click [here](#)) that the European Court of Justice had ruled in *Astra Zeneca UK Ltd v Commissioners for Her Majesty's Revenue and Customs Case C-40/09* that employers would have to account for VAT on retail vouchers provided to their employees under salary sacrifice arrangements because the supply of vouchers is treated as the supply of services to the employees for VAT purposes.

HM Revenue & Customs had not at that point issued any response to the decision but it has now published guidance on the approach it will take. The guidance states unsurprisingly that where the benefit provided under a salary sacrifice arrangement is subject to VAT, VAT will indeed be due from the employer on the value of the benefit.

This means that benefits such as retail vouchers and bicycles (under the Cycle to Work Scheme) provided through salary sacrifice arrangements will generate a VAT liability for employers. Benefits that are not otherwise subject to VAT (e.g. childcare vouchers) will not give rise to a VAT liability, although do note that it will no longer be possible to recover VAT paid by the employer on administration fees charged by a provider of childcare vouchers.

Timing of changes

There is some good news of sorts. HMRC has announced that these new rules for salary sacrifice arrangements will only apply from 1 January 2012 to allow employers time to change their VAT accounting processes. In addition, it has unveiled the transitional rules that will apply to existing arrangements. Salary sacrifice arrangements put in place before 28 July 2011 will continue to be free from VAT until the earliest of:

- the date on which an employee's fixed term agreement expires; or
- the date of an employee's annual salary/benefits review; or
- the date of any other review or renegotiation that changes the benefits of a salary sacrifice agreement or changes an employment contract.

Arrangements entered into on or after 28 July 2011 will be subject to the new VAT rules from 1 January 2012.

Next steps for employers

Employers affected by the changes need to decide whether they will pass on any VAT cost to their employees or bear the cost themselves. This decision will be affected by a number of factors. For example, employers will need to consider whether their existing salary sacrifice arrangements allow them to make additional deductions in respect of VAT if they do wish to pass on the cost to employees and, if they cannot, whether or not they wish to take the possibly difficult industrial relations step of amending their employees' terms of salary sacrifice in order to do so.

Employers should also review their VAT accounting processes. They will need to identify which of the benefits they provide under salary sacrifice will be subject to the new rules from 1 January 2012 and, therefore, which will generate a VAT liability.

If you would like any further information about anything set out in this alert please contact:

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