



VAT treatment of refunds made by manufacturers

Consultation document

Publication date: 31 May 2013

Closing date for comments: 31 August 2013

Subject of this consultation:	The VAT treatment of refunds paid by manufacturers directly to consumers.
Scope of this consultation:	To discover the extent to which manufacturers make such payments; to consider how UK law needs to change to accommodate them; what impact that may have and what administrative burdens it may give rise to.
Who should read this:	Manufacturers who pay rebates to consumers of their goods purchased through retailers.
Duration:	The consultation will start on 31 May 2013 and end on 31 August 2013.
Lead official:	Michael Kelly, HMRC.
How to respond or enquire about this consultation:	Responses to the consultation and queries about the content or scope of the consultation should be sent to: Michael Kelly, VAT Supply Team, HM Revenue & Customs, Room 3C/07, 100 Parliament Street, London SW1A 2BQ. Tel 0207 147 0305. Email: michael.kelly3@hmrc.gsi.gov.uk .
Additional ways to be involved:	As the number of businesses affected by this change is expected to be small, we are requesting written responses. However, if a meeting would be helpful, please contact Michael Kelly at the above address to discuss arrangements. Alternate format versions of this document are available on request. Please contact Michael Kelly at the above address.
After the consultation:	A response document will be published in the Autumn.
Getting to this stage:	UK law currently expressly allows a business in a direct relationship with a customer to adjust the VAT originally accounted for in the case of a post-supply adjustment to the consideration. It is silent on the position where a manufacturer, which has no direct relationship with the final consumer of its products, makes a post-supply payment.
Previous engagement:	None.

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1. Introduction

At Budget 2013 the Government announced its intention to legislate to allow manufacturers to adjust their VAT to take account of refunds they make to final consumers.

In this context the term 'refund' refers to a payment made by a manufacturer directly (or via a third party) to the customer of a retailer. These payments may be made for a number of reasons, for example:

- faulty products;
- damaged products;
- customer dissatisfaction.

Normally when a retailer sells goods to a customer, it is the retailer that refunds money to the customer if those goods are returned, or a retrospective reduction in price is agreed. Where the goods are subject to VAT, the retailer is entitled to make an adjustment under regulation 38 of the VAT Regulations 1995 ("regulation 38") and reclaim the VAT declared to HMRC on the original transaction. A VAT registered purchaser must make a similar adjustment to any VAT reclaimed on the goods.

However, sometimes the purchaser seeks a refund of some, or all, of the price paid for the goods from the manufacturer and not from the retailer. This might happen, for example, when there is a major fault in the goods. Regulation 38 does not explicitly address this situation.

The measure seeks to equalise the VAT treatment as far as possible and ensure that UK law expressly accords with EU law.

The legislation to implement this change will take effect in 2014.

This consultation seeks views on:

- the extent to which manufacturers make such refunds;
- the range of circumstances that may give rise to a refund;
- how the change should be implemented;
- what impact it may have and what administrative burdens it may give rise to.

2. Background

The European Court of Justice in the case of *Elida Gibbs (C-317/94)* held that a manufacturer was entitled to adjust its VAT to take account of refunds paid directly to

final consumers under a promotion scheme. In that case a consumer could send a coupon to the manufacturer and claim a cash refund of part of the price paid to the retailer.

HMRC had not interpreted the judgment as applying where the manufacturer made a refund in cases of, for example, faulty or damaged goods. In such cases the refund by the manufacturer was viewed as compensation or an ex gratia goodwill payment and thus outside the scope of VAT. Following representations, we have reviewed this interpretation of the law and we now accept that in certain situations the manufacturer is entitled to adjust the VAT it has accounted for when it makes a refund direct to the retailer's customer.

3. How the change will be made

Legislation

The change will be made by amending the Value Added Tax Regulations 1995 (1995/2518).

Objective

The objective of the change is to ensure that the net VAT accounted to HMRC on any given supply of goods is proportionate to the total consideration paid by the consumer for the goods, after adjusting for any refund made.

Question 1

Do you agree that this is the correct objective?

Scope and meaning of "refund"

The changes will only apply to the extent that the refund is related to the original purchase price paid by the consumer. Therefore payments that relate to compensation for a consequential loss or the amount of a refund that exceeds the total consideration paid for the goods will not be covered by the proposed change. In effect, the consumer has to be put in the position of never having purchased the product (i.e. they return the goods and receive a full refund of the purchase price) or, of having paid a lower price for the product (i.e. they retain the product and receive a partial refund of the purchase price).

The provision of a non-monetary credit such as the issue of a voucher by a manufacturer to a consumer would therefore not be covered by the definition of "refund" as this entails a discount against a future purchase rather than a reduction in the original consideration.

It is HMRC's view therefore that the manufacturer is not entitled to make an adjustment at the point at which the voucher is issued. Instead the manufacturer would be entitled to make any necessary adjustment following the *payment* by the manufacturer to the retailer following redemption, either in the form of:

- a reduction in output tax in the case of redeemed multi-purpose vouchers (these are covered by this consultation); or
- in the case of single purpose vouchers the recovery of input tax by the manufacturer on the supply to it by the retailer. Since this is an input tax adjustment, it is unaffected by this consultation.

So, where a manufacturer pays a retailer following redemption of a multi-purpose voucher, there is then a refund of the type covered in this consultation.

Question 2

Do you agree that the correct scope and meaning of "refund" is a payment that relates to the supply of the goods and not any other matters and that it must be a monetary refund or redeemed multi-purpose voucher?

Examples of what HMRC will accept as refunds

The following are examples of where HMRC accept that a refund within the meaning of the proposed changes can be made:

- faulty products;
- damaged products;
- where the customer is generally dissatisfied with a product rather than being able to demonstrate a fault or damage; and
- product recalls for safety, health or quality issues.

Question 3

Do you agree with the examples given above?

Question 4

As a manufacturer, to what extent have you made refunds in the above categories and are there any other examples that you think HMRC should consider to be refunds?

Examples of what HMRC will not accept as refunds

The following are examples of where HMRC do not accept that a refund within the meaning of the proposed changes can be made:

- payments to the extent that they exceed in value the total consideration paid by the consumer - if the consumer receives a refund in excess of the original

consideration, any excess is of a compensatory nature and outside the scope of VAT;

- amounts for consequential loss, for example damage to a carpet following a washing machine leak – such a payment is made in compensation for the damage/loss and not an adjustment to the consideration paid for the goods;
- the issue of vouchers (including face value vouchers) or other credit token redeemable against future purchases. A voucher or credit token does not represent a refund against the original consideration but is a discount offered against the purchase of future goods, which may not be taken up;
- payments to third parties to repair the goods and a free supply of parts to effect a repair - the test is whether the customer has received a refund against the consideration he or she paid for the goods and, if that is unaltered, then there is no adjustment to be made.
- payments to customers covering the cost of repairs the customer paid to third party repairers. This is "out-of-pocket" compensation to the consumer - the original cost of the goods remains unaltered.
- cases where the goods are repaired, exchanged or replaced without any refund of the purchase price.

Question 5

Do you agree that the examples given should not be classed as refunds and are there any other examples that you think that HMRC should consider not to be refunds?

Goods supplied under finance agreements

Often goods will be supplied under finance agreements, such as Hire Purchase, where the finance company has an interest in the goods supplied to the consumer. Depending on the terms of the individual agreement title in the goods may pass to the consumer at different times and different termination clauses and consequences may apply.

Under *Elida Gibbs* principles, the manufacturer's VAT may only be reduced to reflect the amounts actually paid by the consumer and this will be affected by the number of payments the consumer has paid under the finance agreement.

Question 6

How does the fact that the goods have been sold under a finance agreement affect your policy and procedures for making a refund direct to the consumer?

Input tax

Consumers that were entitled to an input tax deduction will be required to make a corresponding input tax adjustment. Partly exempt consumers will need to adjust the amount according to their method. The amount by which a customer is or is not required to adjust their VAT should not affect the treatment by the manufacturer

Question 7

Do you agree that this is the correct treatment of input tax?

Anything else?

Question 8

Do you have any comments or suggestions that have not already been covered?

4. Tax Impact Assessment

The table below sets out the Government's view on what the impact of the legislative changes will be. This section gives all interested parties the opportunity to comment on what impact the changes will have and to point out anything that may have been overlooked. In particular the Government invites comments from charities, small businesses or bodies representing their interests.

Summary of Impacts

Exchequer impact (£m)	2013-14	2014-15	2015-16	2016-17	2017-18
	Negligible	Negligible	Negligible	Negligible	Negligible
Economic impact	This measure is expected to have a negligible exchequer impact. Changes to the rules on refunds made by manufacturers will have a negligible effect per annum to the Budget 2014 forecast. This is an indicative estimate and remains subject to OBR scrutiny as part of their forecast process.				
Impact on individuals and households	There is no impact on individuals and households as this measure only affects the VAT treatment by a business.				
Equalities impacts	This proposal affects businesses and does not have an equality impact on any protected characteristic.				
Impact on businesses and Civil Society Organisations	This measure is expected to have a negligible impact on businesses and civil society organisations. Although this measure could in theory affect all UK VAT registered manufacturers, of which there are about 130,000, we believe cases of manufacturers repaying consumers directly are rare. At most there will be one-off compliance costs and admin burdens for manufacturers relating to familiarisation with the amended legislation which should only take a few minutes.				
Impact on HMRC or other public sector delivery organisations	Negligible.				
Other impacts	None.				

Question 9

Do you agree that the proposed change will have no impacts other than those set out above? If not, what additional impacts do you think will result from the proposed change?

5. Summary of questions

From section 3

Objective

Question 1

Do you agree that this is the correct objective?

Scope and meaning of "refund"

Question 2

Do you agree that the correct scope and meaning of "refund" is a payment that relates to the supply of the goods and not any other matters and that it must be a monetary refund or redeemed multi-purpose voucher?

Examples of what HMRC will accept as refunds

Question 3

Do you agree with the examples given?

Question 4

As a manufacturer to what extent have you made refunds in the above categories and are there any other examples that you think HMRC should consider to be refunds?

Examples of what HMRC will not accept as refunds

Question 5

Do you agree that the examples given should not be classed as refunds and are there any other examples that you think that HMRC should consider not to be refunds?

Goods supplied under finance agreements

Question 6

How does the fact that the goods have been sold under a finance agreement affect your policy and procedures for making a refund direct to the consumer?

Input tax

Question 7

Do you agree that this is the correct treatment of input tax?

Anything else?

Question 8

Do you have any comments or suggestions that have not already been covered?

From section 4 – Tax Impact Assessment

Question 9

Do you agree that the proposed change will have no impacts other than those set out above? If not, what additional impacts do you think will result from the proposed change?

6. The Consultation Process

This consultation is being conducted in line with the Tax Consultation Framework. There are 5 stages to tax policy development:

- Stage 1 Setting out objectives and identifying options.
- Stage 2 Determining the best option and developing a framework for implementation including detailed policy design.
- Stage 3 Drafting legislation to effect the proposed change.
- Stage 4 Implementing and monitoring the change.
- Stage 5 Reviewing and evaluating the change.

This consultation is taking place during stage 1 of the process. The purpose of the consultation is to seek views on the proposal in order to confirm, as far as possible, that it will achieve the intended policy effect with no unintended effects.

How to respond

A summary of the questions in this consultation is included at chapter 6.

Responses should be sent by 31 August 2013, by email to michael.kelly3@hmrc.gsi.gov.uk, or by post to:

Michael Kelly,
VAT Supply Team,
HM Revenue & Customs,
Room 3C/07,
100 Parliament Street,
London SW1A 2BQ.

Or by fax to 0207 147 0097

Telephone enquiries 0207 147 0305 (from a text phone prefix this number with 18001)

Paper copies of this document or copies in Welsh and alternative formats (large print, audio and Braille) may be obtained free of charge from the above address. This document can also be accessed from the HMRC Internet site at <http://www.hmrc.gov.uk/consultations/index.htm>. All responses will be acknowledged, but it will not be possible to give substantive replies to individual representations.

When responding please say if you are a business, individual or representative body. In the case of representative bodies please provide information on the number and nature of people you represent.

Confidentiality

Information provided in response to this consultation, including personal information, may be published or disclosed in accordance with the access to information regimes. These are primarily the Freedom of Information Act 2000 (FOIA), the Data Protection Act 1998 (DPA) and the Environmental Information Regulations 2004.

If you want the information that you provide to be treated as confidential, please be aware that, under the FOIA, there is a statutory Code of Practice with which public authorities must comply and which deals with, amongst other things, obligations of confidence. In view of this it would be helpful if you could explain to us why you regard the information you have provided as confidential. If we receive a request for disclosure of the information we will take full account of your explanation, but we cannot give an assurance that confidentiality can be maintained in all circumstances. An automatic confidentiality disclaimer generated by your IT system will not, of itself, be regarded as binding on HM Revenue and Customs (HMRC).

HMRC will process your personal data in accordance with the DPA and in the majority of circumstances this will mean that your personal data will not be disclosed to third parties.

Consultation Principles

This consultation is being run in accordance with the Government's Consultation Principles.

The Consultation Principles are available on the Cabinet Office website:
<http://www.cabinetoffice.gov.uk/resource-library/consultation-principles-guidance>

If you have any comments or complaints about the consultation process please contact:

Amy Burgess, Consultation Coordinator, Budget Team, HM Revenue & Customs, 100 Parliament Street, London, SW1A 2BQ.

Email: hmrc-consultation.co-ordinator@hmrc.gsi.gov.uk

Please do not send responses to the consultation to this address.