



VAT Reverse Charge in Construction Industry – March 2021

To tackle VAT fraud in the construction industry a domestic reverse charge will be introduced with effect from 1 March 2021.

What is a reverse charge?

The reverse charge is a mechanism for accounting for VAT whereby the customer charges themselves VAT, rather than the supplier charging VAT. The domestic reverse charge is commonly used to prevent missing trader fraud i.e. the supplier will charge VAT, be paid the VAT and then 'go missing' before they declare it to HMRC. As the reverse charge makes it the customer's responsibility to account for VAT there is no opportunity for the supplier to disappear without paying the VAT to HMRC.

When does this apply?

The reverse charge applies in the following situations (also see enclosed flowchart):

- 🔧 The supplier and customer are VAT registered in the UK
- 🔧 Payment for the supply is reported within the Construction Industry Scheme
- 🔧 The supply is subject to VAT at either the standard or reduced rate
- 🔧 The customer is not an end user or intermediary (further details below)

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As a VAT registered construction business, what does this mean for me?

It means you may no longer need to charge VAT to your customers or no longer be charged VAT by your suppliers. You will need to review your contracts with customers and suppliers to see whether they are impacted by the reverse charge.

The reverse charge only applies to services that are used to make an onward supply of construction services. This means that the new rules only apply to businesses that are supplying their construction services to another business who will sell on these construction services. It does not apply where the construction services are provided to an 'end user' of those services (i.e. supplied to a business that has commissioned the construction of a new building).

Additionally, companies buying construction services and re-supplying them to a connected or linked end user, without making material alterations to the supplies, are treated as if they are an end user and the reverse charge does not apply. These are referred to as intermediaries.

In both situations, the supplier should be notified of end user or intermediary status.



It does not apply to employment businesses supplying construction workers but does apply to labour only subcontractors. The key difference is who is responsible for the work undertaken. In the former, the responsibility of the work lies with the company requesting the workers but in the latter the business supplying the subcontractors is responsible.

How does it work in practice?

If you are supplying a service that meets all the criteria for the reverse charge, then you no longer charge VAT to your customers.

The sale should be reported in Box 6. Your invoices should include wording that makes it clear that the domestic reverse charge applies and that your customer is required to account for the VAT. Your invoice should also state how much VAT is due under the reverse charge, or the rate of VAT. The amount of VAT should not be included in the amount charged to your customer. Example wording includes:

“Reverse charge: VAT Act 1994 Section 55A applies”

“Reverse charge: S55A VATA 94 applies”

“Reverse charge: Customer to pay the VAT to HMRC”

The receipt of a qualifying service will need to have the reverse charge applied. The VAT due will be paid to HMRC in Box 1 and reclaimed in Box 4 (subject to the normal rules). The net value should be reported in Box 7. Most software providers are introducing a tax code for this.

What happens if there are multiple services and some are not covered by the reverse charge?

If the value of the reverse charge part of the supply is 5% or less of the value of the whole supply this can be disregarded, and normal VAT rules will apply. Over 5% and the reverse charge will apply to the whole value.

Additionally, if two parties have already had a reverse charge service between them on a construction site, for convenience they can both agree that any subsequent construction supplies on that site can be treated as reverse charge services.

What construction transactions does the domestic reverse charge cover?

This domestic reverse charge will only apply to supplies of building and construction services that are subject to VAT at the standard or reduced rates that also need to be reported under Construction Industry Scheme. These are referred to as ‘specified construction services’.

What are specified construction services?

Specified construction services include:

- ✎ Constructing, altering, repairing, extending, demolishing or dismantling buildings or structures (whether permanent or not), including offshore installation services
- ✎ Constructing, altering, repairing, extending, demolishing of any works forming, or planned to form, part of the land, including (in particular) walls, roadworks, power lines, electronic communications
- ✎ Equipment, aircraft runways, railways, inland waterways, docks and harbours
- ✎ Pipelines, reservoirs, water mains, wells, sewers, industrial plant and installations for purposes of land drainage, coast protection or defence
- ✎ Installing heating, lighting, air-conditioning, ventilation, power supply, drainage, sanitation, water
- ✎ Supply or fire protection systems in any building or structure
- ✎ Internal cleaning of buildings and structures, so far as carried out in the course of their construction, alteration, repair, extension or restoration
- ✎ Painting or decorating the inside or the external surfaces of any building or structure
- ✎ Services which form an integral part of, or are part of the preparation or completion of the services described above - including site clearance, earth-moving, excavation, tunnelling and boring, laying of foundations, erection of scaffolding, site restoration, landscaping and the provision of roadways and other access works.

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The reverse charge will also apply to materials supplied with those construction services. If a supply contains a mixture of specified and other construction services, it will be classed as a single supply of specified services and the domestic reverse charge will apply.

What supplies are excluded from the Reverse Charge?

The following are not included within the definition of construction services:

- ✎ Drilling for, or extracting, oil or natural gas
- ✎ Extracting minerals (using underground or surface working) and tunnelling, boring, or construction of underground works, for this purpose
- ✎ Manufacturing building or engineering components or equipment, materials, plant or machinery, or delivering any of these to site
- ✎ Manufacturing components for heating, lighting, air-conditioning, ventilation, power supply, drainage, sanitation, water supply or fire protection systems, or delivering any of these to site
- ✎ The professional work of architects or surveyors, or of building, engineering, interior or exterior decoration and landscape consultants
- ✎ Making, installing and repairing art works such as sculptures, murals and other items that are purely artistic
- ✎ Signwriting and erecting, installing and repairing signboards and advertisements

- ✎ Installing seating, blinds and shutters
- ✎ Installing security systems, including burglar alarms, closed circuit television and public address systems.

How should building contractors prepare for this change?

Businesses that supply or receive construction services need to understand how they may be impacted by this change. They should be identifying instances where they supply services to other businesses in the construction sector (rather than to a consumer of those services) or receive them for the purposes of selling them on. If they do operate in this way, they need to determine whether the services are included within the list of specified construction services above.

Suppliers that no longer charge VAT on their services could find themselves in a VAT repayment situation and want to move from quarterly to monthly VAT returns.

For further information please contact our VAT partner:



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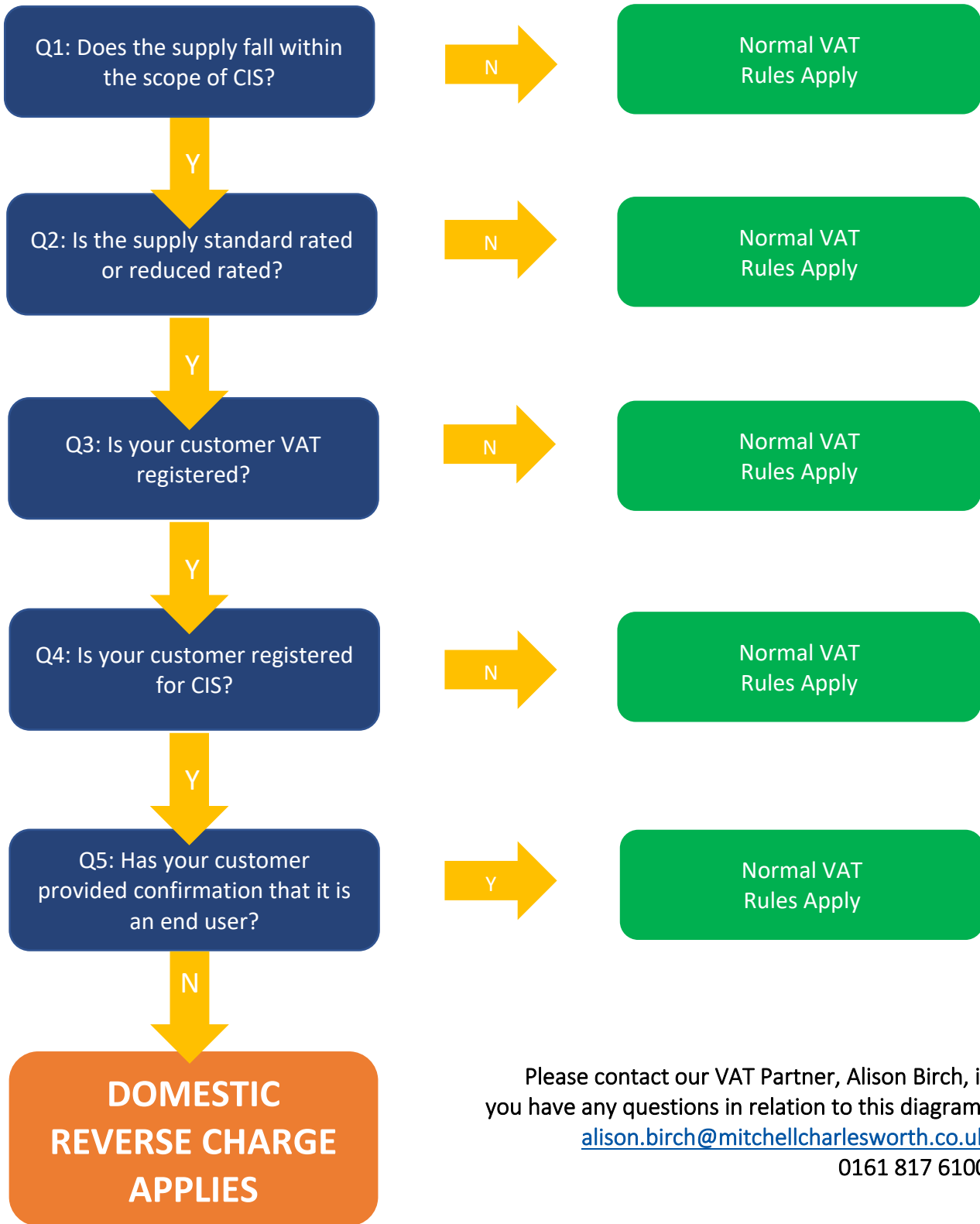
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Use this flowchart to see how you would decide whether to apply normal VAT rules, or apply the domestic reverse charge.

Do not use it for services supplied by employment businesses.



Please contact our VAT Partner, Alison Birch, if you have any questions in relation to this diagram:
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