CHAPTER 34

AGENCY

Agency concerns an unusual relationship between the buyer and seller where an agent is usually the intermediary in the transaction.

An individual may act as an agent when buying or selling something on behalf of another party.

For VAT purposes the relationship can be rather complex and must be treated with care.

34.1 Introduction

There is no definition of ‘agent’ in the legislation. An agent is someone who acts for, or represents, someone else (the principal) in arranging supplies of goods and services. Supplies arranged by an agent are made by or to the principal represented. The principal cannot avoid any liability to account for VAT on supplies, or to pay VAT on purchases, by using an agent. However, whether or not a person is an agent for another person depends upon the actual arrangement between them and not simply upon the trading titles adopted. For example, ‘motor agents and distributors’ usually trade as principals and travel agents and employment agencies are not usually agents in all their activities. Solicitors and architects are normally principals but may occasionally arrange supplies as agents for their clients.

An agent/principal relationship exists if both parties agree that it does and the agent has agreed with the principal to act on his behalf in relation to the particular transaction concerned. The agreement may be written, oral or merely inferred from their general relationship and the way their business is conducted. Whatever form this relationship takes, the following conditions must be satisfied.

a. It must always be clearly established between the agent and principal, and acceptable to HMRC, that the agent is arranging transactions for the principal, rather than trading on his own account.

b. The agent must never be the owner of the goods or use any of the services bought or sold for the principal.

c. The agent must not alter the nature or value of any of the supplies made between the principal and third parties. VAT Notice 700, Para 22.2

In C & E Commrs v Johnson, QB [1980] Woolf J took agency as the ‘relationship which exists between two persons, one of whom expressly or impliedly consents that the other should represent him or act on his behalf and the other of whom similarly consents to represent the former or so to act’.
34.2 Agents and VAT

An agent will usually be involved in at least two separate supplies at any one time.

- The supply of own services to the principal for which the agent charges a fee or commission.
- The supply made between the principal and the third party.

The VAT liability on the supply of agent’s services will not necessarily be the same as the liability of the supply between the principal and the third party.

In determining whether an agent is liable to be registered for VAT, turnover includes the value of services to the principal and the value of any supplies which the agent is treated as making through acting in his own name.

34.3 Agents Acting in the Name of Their Principals (Disclosed agents)

An agent may only take a minor role in a transaction and simply introduce the principal to potential clients or suppliers. Alternatively, the agent may be more closely involved and receive/deliver goods, make/receive payment and possibly hold stocks of goods on behalf of the principal. However, provided that the invoicing for the supply is between the principal and the customer, the only VAT supply made by the agent is the provision of services to the principal.

Illustration 1

```
Customer  ↓  Agent  ↓
↑  Sale of Goods  ←  Agency Services  ←
    ←  Principal  ←
```

The agent has found a customer for the principal and has charged the principal a fee for doing so. The principal will then sell goods to the customer and raise an invoice for that sale of goods.

There are two suppliers for VAT purposes:

1. Sale of goods by principal to customer.
2. Agency services from agent to principal.

Each would be dealt with as separate supplies for VAT purposes.

34.4 Agents Acting in Their Own Name (Undisclosed Agents)

An agent may be empowered by a principal to enter into contracts with a third party on behalf of the principal. In such cases, particularly where the principal wishes to remain unnamed or undisclosed, the agent may receive and issue invoices in his own name for the supplies concerned. In such circumstances, although in commercial terms the transaction remains between the principal and third party, for VAT purposes special rules apply as set out below.
Goods

Where an agent acts in his own name in relation to a supply and either

a. goods are imported from outside the EC by a taxable person who supplies them as agent for a non-taxable person, or

b. goods are acquired from another EC country by a non-taxable person and a taxable person acts as agent in relation to the acquisition, and then supplies the goods as agent for that non-taxable person, or

c. where neither (a) nor (b) above applies in relation to a supply, goods are supplied through an agent

then the goods must be treated, as the case may be, as imported and supplied by the agent, acquired and supplied by the agent or supplied to and by the agent as principal. For these purposes, a person who is not resident in the UK and whose place (or principal place) of business is outside the UK may be treated as being a non-taxable person if as a result he will not be required to be registered under VATA 1994. VATA 1994, s.47(1)(2)(2A)

Illustration 2

<table>
<thead>
<tr>
<th>Principal</th>
<th>Customer</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sale of Goods</td>
<td>↑ Agency</td>
</tr>
<tr>
<td>£100</td>
<td>↑ £20</td>
</tr>
<tr>
<td>← ← Agent ← ←</td>
<td>← ← Agent ← ←</td>
</tr>
<tr>
<td>→ →</td>
<td>→ →</td>
</tr>
<tr>
<td>↑ ↑ Goods</td>
<td>↓ ↓ £100</td>
</tr>
</tbody>
</table>

It is important to appreciate that the principal is still selling goods to the customer from a contractual perspective. For VAT purposes, however, the agent is treated as buying the goods from the principal and then selling them onto the customer.

The agent is still providing agency services to the principal.

In this particular situation there are three supplies to consider from a VAT perspective.

34.5 Accounting for VAT – Non-EC and Intra-EC supplies

In order to put the VAT treatment of UK undisclosed agents on the same footing as that for commissionaires elsewhere in the EC, an undisclosed agent who is involved in non-EC or intra-EC supplies is seen as taking a full part in the underlying supply of any goods. There is no separate supply of the agent’s own services to his principal and the commission retained is seen as subsumed in the value of the onward underlying supply. This treatment is for VAT purposes only and has no impact on the legal status of agents or the way in which they are treated for the purposes of other taxes or legislation.

Illustration

A UK undisclosed agent sells goods to final customer for £100. He retains £20 as commission and pays £80 back to his overseas principal. All figures are net of VAT.
If the goods are imported, the VAT value at importation is arrived at in the normal way. If the goods are acquired from a principal in another EC country, the VAT value at acquisition is £80 based on the value of the invoice raised by the principal to the agent. The agent must account for VAT on the acquisition.

The agent can recover import/acquisition VAT, subject to the normal rules. He then makes an onward supply in his own name to the customer for £100, and accounts for output tax. The commission of £20 is treated as subsumed in the value of the onward supply of the goods and is not treated as a separate supply of own services to the non-UK principal. Effectively the £20 commission is ignored and VAT is only accounted for on the £100 onward supply.

\[
\begin{array}{c|c|c}
\text{Principal} & \text{Agent} & \text{Customer} \\
\downarrow & \uparrow & \\
\text{£80} & \text{Goods} & \text{£100} \\
\text{↓} & \text{↑} & \text{↑} \\
\end{array}
\]

Cost incurred in the UK (e.g. warehousing and handling) can be treated as supplied to the agent who can recover the input tax on them (subject to the normal rules).

Business Brief 9/00 provides useful guidance.

### 34.6 Accounting for VAT – Domestic Supplies

Subject to below, there is an underlying supply between the principal and customer and a separate supply of agent's services to the principal. The agent reclaims input tax and must account for output tax on the supply of the goods but as the nature or value of the supply is unchanged the amount of input and output tax is normally the same. The deemed supplies to and by the agent are simultaneous and he cannot reclaim the input tax on the supply to him in one period but defer the time when he is required to account for output tax to a later period in which he invoices the supply made by him ([Metropolitan Borough of Wirral v C & E Comrs](https://www.gov.uk/government/cases/m-borough-of-wirral-v-c-e-commissioners)). The VAT liability of the supply of agent's services is not necessarily the same as the liability of the supply of goods.

However, if he wishes, an undisclosed agent may also adopt the VAT treatment set out above for non-EC and intra-EC supplies for his domestic transactions.

### 34.7 Services

Where an agent who acts in his own name arranges a supply of taxable services and both the agent and supplier are registered for VAT, HMRC may, if they think fit, treat the supply both as a supply to the agent and by the agent. VATA 1994, s 47(3).

**Accounting for VAT – International Supplies**

As before, in order to put the VAT treatment of UK undisclosed agents on the same footing as that for commissionaires elsewhere in the EC, where an agent is involved in international services the services are treated as supplied to the UK agent as though he was a principal and supplied on by him. The agent’s commission is seen as subsumed in the value of the onward supply and he is not
regarded as making a separate supply of his own services to the principal. This applies to services being supplied both to and from the UK.

If the supply is to a business customer, the place of supply is where the customer belongs.

Where the agent’s customer is not a relevant business customer, the agent’s supply is treated as made where the underlying supply is made e.g. if the agent arranges a supply of legal services from a lawyer in Spain to a private individual in the UK, the place of supply will be Spain and Spanish VAT may be chargeable i.e. the UK customer cannot avoid VAT in Spain by using an agent to acquire the services.

**Accounting for VAT – Domestic Supplies**

Subject to below, there is an underlying supply between the principal and customer and a separate supply of agent’s services to the principal. The agent reclaims input tax and must account for output tax on the supply of the main services but as the nature or value of the supply is unchanged the amount of input and output tax is normally the same.

The deemed supplies to and by the agent are simultaneous and he cannot reclaim the input tax on the supply to him in one period but defer the time when he is required to account for output tax to a later period in which he invoices the supply made by him. The VAT liability of the supply of agent’s services is not necessarily the same as the liability of the supply of the main services.

However, if he wishes, an undisclosed agent may also adopt the VAT treatment set out above for international supplies of services for his domestic supplies.

### 34.8 Disbursements

Where a supplier incurs incidental costs (e.g. travelling expenses, postage, telephone) in the course of making the supply and charges these items separately on the invoice to the client, such costs must be included in the value when VAT is calculated. However, where amounts are paid to third parties as agent of a client, such payments may be treated as disbursements if all the following conditions are satisfied.

a. The agent acted for his client when paying the third party.

b. The client actually received and used the goods or services provided by the third party. This condition usually prevents the agent’s own travelling expenses, telephone bills, postage, etc being treated as disbursements for VAT purposes.

c. The client was responsible for paying the third party.

d. The client authorised the agent to make the payment on his behalf.

e. The client knew that the goods or services would be provided by a third party.

f. The agent’s outlay must be separately itemised when invoicing the client.

g. The agent must recover only the exact amount he paid to the third party.
h. The goods or services paid for must be clearly additional to the supplies made to the client.

If a payment qualifies as a disbursement, it can be treated in either of the following ways.

- The disbursement can be passed on to the client as a VAT-inclusive amount (if taxable) and excluded when calculating any VAT due on the main supply to the client. The agent cannot reclaim VAT on the supply (since no goods or services have been supplied to him). Unless the VAT invoice for the disbursement is addressed directly to the client, the client is also prevented from reclaiming input tax as he does not hold a valid invoice. Generally, therefore, it is only advantageous to treat a disbursement in this way if no VAT is chargeable on the supply by the third party or the client is not entitled to reclaim the VAT.

- If an agent does treat a payment as a disbursement in this way, he must keep evidence to enable him to show that he was entitled to exclude the payment from the value of his supply to his client. He must also be able to show that he did not reclaim input tax on the supply by the third party.

- The goods or services can be treated as supplied to and by the agent under 31.4 above. The agent can then reclaim the related input tax (subject to the normal rules) and charge VAT on the onward supply if appropriate. VAT Notice 700, Para 25.1

34.9 Principal or Agent?

There is a common theme running through a large number of VAT cases about:

- taxi firms;
- driving schools;
- hairdressers;
- escort agencies;

as well as other types of business. A customer receives a service directly from an individual worker, but it may not be clear whether the individual worker is providing the service as principal or as agent for an organisation or collective of other workers. Suppose the customer pays £100 for the service and the worker keeps £60 of it. This could represent:

- a supply by the worker to the customer for £100, and a supply by the organisation to the worker for £40;
- a supply by the organisation to the customer for £100 and a supply by the worker to the organisation for £60;
- a supply by the organisation to the customer for £40 and a supply by the worker to the customer for £60.

It is generally reasonably easy to identify the flow of cash in the transactions, but the flow of cash may not directly match the supplies. One person may receive the cash as agent for another.
The importance of the distinction lies in several different areas:

- just getting the VAT accounting right;
- measuring the turnover for registration tests;
- the amount of VAT charged in total to the customer, because often the individual worker will be below the registration threshold;
- the nature and liability of the supplies concerned.

**A1 Lofts Limited and A1 Loft Conversions**

The Tribunal recently overturned a piece of VAT planning implemented by a loft conversion company in an attempt to avoid charging and paying VAT on the principal supply. The VAT at stake was in the region of £1.2m for the periods July 2002 to November 2004.

The company's argument was that it provides ‘project management services’, the money for which it put in a client account. It was taken out of this account to pay project management fees on which the company paid VAT, and to pay the costs of the project. These costs were treated as disbursements. Some money was retained in the client account to cover the possible costs of claims under a ten-year guarantee. Such money would not be subject to VAT until much later when it was released to the project manager.

Although the contracts reflected the intended arrangements, it was clear from witnesses/clients that they did not believe they had individual contracts with each of the tradesmen. If there had been a problem they would have expected the company to put it right. As a result, the company was supplying the loft conversion service itself and was liable to output tax on all its receipts. This case was remitted back to the Tribunal by the High Court on the basis that the Tribunal misdirected itself.

The First Tier Tribunal have now confirmed that there is one supply of loft conversion services as principal.

### 34.10 Employment Status

For VAT purposes we need to be dealing with non-employee relationships when considering agent v principal issues. An “agent” must not be an employee of the “principal”. The agent and principal must be in business on their own account for any of the above provisions to apply.

The tax legislation itself does not tell us whether a person is employed or self-employed, so the distinction between the two is based on case law and on HMRC practice.

In the vast majority of instances it is obvious whether an individual is an employee or whether he is in business on his own account as a self-employed trader. However there is a considerable grey area in between the two.

**Determining employment status**

Recent court cases indicate there is **no single satisfactory test governing the question of whether a person is employed or self-employed**.
HMRC advice is to **consider all the factors** that are present in, or absent from, a particular case then **weigh those pointing to employment against those pointing to self-employment**. Having done that, a **picture will emerge** from which employment status can usually be ascertained.

The following is a list of the **factors to be taken into account** in determining whether a worker is employed or self-employed:

- Mutuality of obligation
- Right of control
- Provision of own equipment
- Right of substitution and engagement of helpers
- Financial risk
- Opportunity to profit
- Degree of integration into the organisation
- Right to terminate the contract
- The number of paymasters

This is by no means an exhaustive but it does include the most important criteria.

We shall examine each in turn.

**Mutuality of obligation**

Where an **engager is under an obligation to provide work** and the **worker is under a similar obligation to accept the work** and to perform the tasks delegated to him, this usually points to the relationship being one of employment.

If a worker is self-employed, he will have no guarantee of work and even if work is offered to him he is under no legal obligation to accept the work offered. Employees on the other hand are rarely allowed the freedom to refuse work allocated to them.

The existence of any mutual obligation between the parties will **usually be obvious from any service contract between the two parties**. Employees usually have an employment contract which sets out the terms and conditions under which they are to perform duties for their employer.

**Right of control**

In a typical employer/employee relationship, the **employee will exercise very little control over what he or she does on a day-to-day basis**. There is typically a master/servant relationship between an employer and an employee. An employer will typically tell an employee what to do, how to do it and when to do it by.

The fact that a worker may be told how to perform duties will usually be seen as a **strong pointer to employment**.

On the other hand, a **self-employed person will have far more control** over the jobs that he or she undertakes and the deadline for completion of those jobs.
However where the worker is an expert (for example a ship’s captain or a brain surgeon), the issue of control would probably not be seen as material. For example, take a brain surgeon who works for the NHS. Whilst performing the surgery, he is in total control over what he does, how he does it and how long he takes to complete the task. However, this does not mean that he is self employed and this is an unusual situation and the issue of control in this instance will therefore carry less weight.

**Provision of own equipment**

When considering whether a worker is employed or self-employed, HMRC will look at who provides the tools for the job in hand.

An employee is rarely responsible for providing his or her own equipment. When we turn up for work we expect our employers to provide us with a computer, a printer, a telephone and some stationery etc.

A self-employed person, on the other hand, will customarily be responsible for providing the necessary equipment to enable him to undertake the work offered.

**Right of substitution and engagement of helpers**

The ability to provide a substitute and/or engage helpers is something HMRC look at closely when deciding whether a worker is employed or self-employed.

An employee will have no freedom to send a substitute in his or her place if, for whatever reason, they are unable to perform their duties. Similarly an employee will rarely be allowed to engage the services of a helper or assistant.

On the other hand, if a self-employed person has contracted to do a job and is either sick or double-booked, that self-employed person will usually have the freedom to provide a substitute to complete the job in his place.

This was a crucial factor in the case of *Hall v Lorimer*. In this case the Court, after much deliberation, concluded that a vision mixer was a self-employed person largely because on a handful of occasions, he had been able to provide a substitute to fulfil particular contracts.

When looking at the right of substitution, HMRC will require evidence of occasions when a substitute has actually been used to fulfil a task. Therefore the presence in a contract of a clause which gives the worker the right to provide a substitute is not usually enough. The worker must clearly show that a substitute has in fact been engaged.

**Financial risk**

Individuals who risk their own money by (say) buying assets needed for the job, bearing the running costs and paying for overheads and materials, are almost certainly self-employed. Employees are not usually expected to risk their own capital.

An example of a financial risk is where a worker incurs significant amounts of expenditure on training in order to obtain the skills needed, which are then used in subsequent engagements. This can be treated as a pointer to self-employment if there is a real risk that the investment in training would not be recovered from income from future engagements.
Self-employed workers may also be required to **rectify unsatisfactory work in their own time** and at their own expense.

Financial risk could also take the form of quoting a fixed price for a job, with the consequent risk of bearing the additional costs if the job overruns. **The risk of making a loss is a very strong indicator of self-employment** and can be a decisive factor on its own.

**Opportunity to profit**

A person whose profit (or loss) depends on the capacity to reduce overheads and organise his work effectively is likely to be self-employed.

People who are paid by the job will often be in this position. For example, a person who quotes a fixed price may well be able to complete the task ahead of schedule or at a lower cost than originally envisaged.

**Degree of integration into the organisation**

Establishing whether a person becomes ‘part and parcel’ of the engager’s organisation can be a useful indicator.

**An employee will be integrated into the business of his employer.** For example, an employee will usually have his or her own desk, a designated computer with which to work, an e-mail address, a land line phone number, his or her own stationery, access to normal employee facilities such as the staff restaurant, and access to the employer premises (often by means of a security pass). Employees will also be allowed to join company pension schemes, receive invitations to staff functions such as Christmas parties and perhaps have a car parking space.

Contrast this with the position of a self-employed person, who will not be as integrated into an engager’s business, will not have a desk or a computer or access to the business premises without prior appointment and will not have the “employee type” benefits such as those described above.

**Right to terminate contract**

A right to terminate an engagement by giving notice of a specified length may be viewed as indicative of a contract of employment.

On the other hand a contract for the services of a self employed worker will usually end on the completion of the particular task.

**The number of paymasters**

A typical employee has one paymaster – he is paid by his employer and no-one else.

However, if a worker typically performs services for a number of different businesses, he is more likely to be self-employed.

**Summary**

HMRC has produced a guidance factsheet (ES/FS1) which summarises the issue of whether a worker is employed or self employed as follows:
If you answer “yes” to most of these questions you are likely to be employed:

- Do you have to do the work yourself?
- Can someone tell you where to work, when to work, how to work or what to do?
- Can someone move you from task to task?
- Do you have to work a set number of hours?
- Are you paid a regular wage or salary?
- Can you get overtime pay or bonus payments?
- Are you responsible for managing anyone else engaged by the person or company that you are working for?

If you answer “yes” to one or more of these questions you are likely to be self-employed:

- Can you hire someone to do the work, or take on helpers at your own expense?
- Can you decide where to provide the services of the job, when to work, how to work and what to do?
- Can you make a loss as well as a profit?
- Do you agree to do a job for a fixed price regardless of how long the job may take?

If you can’t answer “yes” to any of the above questions, you are still likely to be self-employed if you can answer “yes” to most of the following questions:

- Do you risk your own money?
- Do you provide the main items of equipment (not the tools that many employees provide for themselves) needed to do the job?
- Do you regularly work for a number of different people?
- Do you have to correct unsatisfactory work in your own time and at your own expense?

Note:

Factsheet ES/FS1 is reproduced in the Yellow Tolley Handbooks. You will find it in the section called “HMRC Codes of Practice & factsheets” in Part 2.