

HM Treasury: Online sales tax

Assessing an option to help rebalance taxation of the retail sector

Response by the Chartered Institute of Taxation

1 Executive Summary

- 1.1 The Chartered Institute of Taxation (CIOT) is the leading professional body in the UK for advisers dealing with all aspects of taxation. We are a charity and our primary purpose is to promote education in taxation with a key aim of achieving a more efficient and less complex tax system for all. We draw on the experience of our 19,500 members, and extensive volunteer network, in providing our response.
- 1.2 The CIOT's view is that an OST should not be introduced to fund relief to retail rates ('RRR'); we believe that designing a brand new tax in order to remedy perceived unfairness occurring in the business rates system is an inappropriate and disproportionate way of solving the issue. The Government should as a first step articulate what the issues are with Business Rates ('BR') that need addressing, bearing in mind the economic evidence which lies behind the statement in paragraph 1.11 of the consultation document that a decrease in BR for eligible high value retail properties may be simply offset by an increase in the landlord's rent, effectively reducing the RRR's effect, possibly to nil. It is surely not the government's intention in potentially introducing an OST to make retail premises more profitable for landlords by imposing increased costs on businesses and their consumers affected by an OST?
- 1.3 If the fundamental issue is a need for revenue, whether to fund Retail Rates Relief or more generally, the review of the extent of avoidance and evasion in the Business Rates system should be undertaken as mentioned in the outcome of the 2021 consultation. This would seem to make sense also in terms of the integrity of the tax system. Further, if for whatever reason it is felt necessary to burden businesses and their consumers to find the necessary revenues, the government should explore whether an existing tax (VAT being the obvious choice) can be modified for this purpose.
- 1.4 The complexity of introducing a tax that requires all transactions to be deemed in or out of its scope should not be underestimated. Although for many businesses this may be fairly straightforward, there will be a significant minority for which this will be a complex, costly and time-consuming exercise. It seems likely that it will also

distort consumer choices and business decisions and act as a break on technological progress which could deliver these more effectively.

- 1.5 Any OST, if it is introduced, should be applied uniformly, UK wide to reduce scope for further complexity. Its design should, as far as possible, mirror definitions and processes already embedded in VAT legislation to reduce confusion for businesses and their customers. This should include considering the government's social policy reasons for not having VAT (or a reduced amount) on certain supplies and considering if it is appropriate to impose a sales tax for such supplies.

2 About us

- 2.1 The CIOT is an educational charity, promoting education and study of the administration and practice of taxation. One of our key aims is to work for a better, more efficient, tax system for all affected by it – taxpayers, their advisers and the authorities. Our comments and recommendations on tax issues are made solely in order to achieve this aim; we are a non-party-political organisation.
- 2.2 The CIOT's work covers all aspects of taxation, including direct and indirect taxes and duties. Through our Low Incomes Tax Reform Group (LITRG), the CIOT has a particular focus on improving the tax system, including tax credits and benefits, for the unrepresented taxpayer.
- 2.3 The CIOT draws on our members' experience in private practice, commerce and industry, government and academia to improve tax administration and propose and explain how tax policy objectives can most effectively be achieved. We also link to, and draw on, similar leading professional tax bodies in other countries.
- 2.4 Our members have the practising title of 'Chartered Tax Adviser' and the designatory letters 'CTA', to represent the leading tax qualification.

3 Introduction

- 3.1 We refer to the consultation document: Online sales tax: Assessing an option to help rebalance taxation of the retail sector¹ published on 25 February 2022.
- 3.2 We welcome that the government is consulting in order to consider views for and against the introduction of a new online sales tax (OST) to rebalance the tax system, as this was a commitment made in the Business Rates Review², published October 2021. We also welcome that this is an early-stage consultation, and the assurances that no decisions have yet been taken whether to introduce an OST.
- 3.3 Our stated objectives for the tax system include:
 - A legislative process that translates policy intentions into statute accurately and effectively, without unintended consequences.

¹ <https://www.gov.uk/government/consultations/online-sales-tax-policy-consultation>

² https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/1028478/BRR_final.pdf

- Greater simplicity and clarity, so people can understand how much tax they should be paying and why.
- Greater certainty, so businesses and individuals can plan ahead with confidence.
- A fair balance between the powers of tax collectors and the rights of taxpayers (both represented and unrepresented).

Responsive and competent tax administration, with a minimum of bureaucracy.

- 3.4 BR are determined by a calculation based on the size, value and usage of the property. The consultation states that some respondents to the BR Review consider the retail sector to be unduly burdened by BR, as they occupy more higher-value town centre properties than businesses selling online from lower-value out-of-town properties/warehouses.
- 3.5 An OST would not be a full replacement for the income generated by BR. Instead, income raised via an OST would be used solely to fund RRR for eligible retailers in England, or via increased block grants to the devolved administrations.
- 3.6 The CIOT's view is that an OST should not be introduced to fund RRR. We do not believe that a brand new tax should be imposed on businesses to remedy issues of fairness arising within another tax. Whilst we can, in principle, support changes to the business rates system or possibly adjustments to another existing tax to fund RRR, the introduction of a new tax seems a disproportionate way of solving the issue.
- 3.7 The consultation document notes concerns in paragraph 1.11 that a decrease in BR for eligible high value retail properties may be simply offset by an increase in the landlord's rent. This potentially calls into question the whole concept of introducing OST on online sales in order to rebalance the tax burden away from physical premises: it would instead be introducing new burdens and distortions on businesses and their consumers in order to benefit landlords: this surely cannot be intended? Such a risk must be fully explored prior to any introduction of an OST. In introducing any proposals for new or amended taxes, whether to fund BR reform or to raise revenue, the government should clarify where it intends the burden to fall and why, in order to facilitate well-directed responses to consultation.
- 3.8 As the stated purpose of the OST is to fund RRR, rebalancing the tax system and promoting distributional fairness, one area to consider in this context is business rates avoidance and to what extent reducing avoidance (and evasion) could achieve these objectives. The outcome of the BR review³ states at paragraph 2.28 that BR avoidance will be reviewed in the future, with particular concerns around the misuse of Empty Property Relief. It is not yet known whether the anticipated BR revenues lost to avoidance and evasion are similar to the projected income from an OST; if they are, then these revenues could be used to fund RRR instead of an OST.
- 3.9 Many of our responses on the technical design of the OST mirror issues that had to be resolved in creating or maintaining the VAT system. Although the CIOT's preference would not be to introduce an OST, if some form of tax on online sales is to be taken forward, we recommend use of the existing VAT system is explored further.

³ https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/1028478/BRR_final.pdf

- 3.10 In principle it could be possible for this to be achieved by discretely increasing the VAT rate on specific supplies that would be within the scope of an OST by 1 or 2%. Therefore, businesses would not need to learn the rules of an entirely new tax and spend additional resources in its administration.
- 3.11 However, we recognise that the VAT return in its current format would not provide details of the relevant turnover for these specific supplies so may require:
- a new box on the VAT return to report the value of relevant sales, a move which would affect HMRC's systems and all VAT registered businesses (VAT accounting systems changes, MTD changes etc), or
 - a new supplementary declaration that provides the breakdown of turnover and VAT of affected sales; again, this would require changes to HMRC own systems and well as system changes for affected taxpayers, though these may be somewhat less than the changes required for an OST.
- 3.12 In spite of our view that a separate OST should not be introduced as presented, we have nevertheless provided feedback on the questions as if an OST in some form (flat fee or revenue based) will be taken forward.

4 Chapter Two: Scope

4.1 Question 1: Would you favour a tax for all 'remote' sales or just a subset of 'online' sales?

4.2 We consider that all 'remote' sales, rather than only online sales, should be within the scope of any OST as remote sales that are delivered directly to the customer also reduce the requirement for the customer to physically visit the High Street and go into a retail store.

4.3 We do not therefore consider the OECD's definition of an e-commerce transaction a suitable definition for the purposes of an OST.

4.4 Question 2: How should taxable sales be defined and what would the practical implications be?

4.5 The definition of taxable sales for OST (whether the OST is flat fee or revenue-based) could mirror relevant excerpts of the existing VAT legislation, eg scope, rate and supply in s.1 – 5 to the VAT Act 1994 (VATA94), though the OST legislation will need to define the products subject to OST and the exceptions.

4.6 The practical implications of defining taxable sales would be that impacted businesses would need to review the supplies they make and determine if each supply falls within the scope of the OST or not. This review must take place regardless of whether the OST is based on a flat-fee or revenue-based methodology. For some businesses with a mixture of in scope and out of scope sales, this may be a time consuming and complex exercise. Further, if an OST is only charged on end consumers, businesses who operate a high volume/low margin model with no relationship with end consumers may find it impossible to carry out any additional verification of the customers' status beyond what is self-declared.

4.7 Question 3: Are there transactions that would be particularly difficult to classify as either online or remote? What are these, and how should these be addressed?

4.8 For higher value products purchased online, a customer may have to subsequently visit the supplier premises for various reasons such as: to sign finance agreements, warranty agreements, provide proof of

identity, view a demonstration product etc though the product ordered remotely may still be delivered to them directly from the retailer's warehouse.

- 4.9 The OST rules would need to determine whether a visit to the supplier's (or third party) premises, the reason for the visit to the premises, and/or its timing, bring the sale within the scope of an OST.
- 4.10 **Question 4: Should click and collect be exempted? If so, how?**
- 4.11 There are variations in what 'click and collect' means for different businesses, and paragraph 2.17 outlines several different variations. A decision must be made on whether the OST becomes due merely because the supply has been ordered online, or if the sale is outside the scope of the OST depending on the extent of the customer's interaction with the retail store where the supply is collected, and/or if the retail store would qualify for RRR.
- 4.12 For example, a consumer may order a weekly grocery shop online. The local supermarket employs staff to take a trolley around the store to collect the products (in place of the customer), and there are staff employed to operate the customer collection point. The customer collects the shopping at the pick-up point located on the same retail premises. As the products are already onsite in the retail store, store staff are used to stock the supermarket shelves, walk around the store to collect the online order in a trolley, operate the onsite collection point, and the same retail premises are used for the key criteria of the onsite collection by the customer, the retail property (that may be subject to high BR) and the staff employed there are integral requirements for the click and collect supply to proceed. There appears to be good argument to exclude such sales from an OST.
- 4.13 The above scenario appears to show the maximum involvement of the local retail store for a grocery shop with a customer onsite visit. There are further variations to this: the same grocery shop prepared by a local store could be delivered to the customer's home, so without an onsite customer visit, would the application of OST be triggered by the combination of online order and home delivery, irrespective of the order being prepared from the local store in the retail premises using local staff?
- 4.14 For other click and collect purchases, the products may be stored and packaged from a centralised out-of-town warehouse and the customer collects a parcel from the designated collection point; this could be onsite from the retailer supplying the product (local store) or another designated collection point run by a third party. This can be fairly common in order to obtain free delivery on a lower priced online order from a retailer (higher priced orders may switch to free home delivery after a certain threshold). For these deliveries to a collection point, there is lesser or no use of the retail premises, so it must be determined whether even a small use of the retail premises by a customer visit allows for an OST exemption, or if a delivery is made to a third-party collection point, does the fact that the customer must travel away from home to collect the order provide a basis for exemption?
- 4.15 Further, for the above scenarios, if the online order would be subject to the OST in principle, there is a further question around whether there is any impact in scope if the retail property used in the order would be eligible for RRR or not.
- 4.16 We would anticipate that having to determine to what extent the customer being required to attend a local store in an online order impacts the scope of the sale being within OST would require quite detailed legislation. The position on whether an OST is applicable to purchases made via physical retail premises (physical visit to store to view products with either an immediate instore online order or a follow up online order after leaving the physical retail premises) also need to be considered.

- 4.17 **Question 5: Should an OST be applied to all goods? Are any exemptions necessary? If so, what are these and why?**
- 4.18 There are governmental social policy reasons why certain supplies of goods are exempt from, or subject to a reduced or zero-rate of VAT (Schedules 7A, 8 and 9 to the VAT Act 1994). The government must consider whether online orders of such goods should also be exempt from an OST, to align the with those reasons, or whether the idea of rebalancing an element of the burden of BR onto outside-store sales should take priority. Note that any such exemptions will bring additional complexity to the design of the OST and to the legislation, although it would be helpful if they followed the VAT definitions.
- 4.19 Any OST should be applied UK wide, as having differing rules in the devolved countries would add a further layer of complexity and issues of where the liability arose would need to be considered. It is not currently clear how OST revenues raised could be appropriately allocated via the block grant. Consideration should be given as to whether the supply is subject to the OST if the goods are exported to a consumer located outside of the UK, as such sales would not typically be otherwise made in-store. Would the imposition of an OST then make British businesses less competitive with the global market?
- 4.20 **Question 6: How would a goods-only approach apply to takeaway food?**
- 4.21 For VAT purposes, the supply of take-away food can be complicated as you must determine whether the supply is 'in the course of catering'⁴ (services) or of food⁵ (goods); there are additional tests regarding 'premises' and whether the food is hot or cold. There can be further complications with VAT when third party delivery agents are used, depending on the contractual arrangements. It is an area of VAT that is complex and regularly litigated so incorporating conditions into an OST for takeaway food is likely to be complex.
- 4.22 If OST legislation was to broadly mirror relevant excerpts of the VAT legislation, the government must decide whether supplies deemed as services for VAT purposes would be treated as if they were goods for the purposes of applying an OST. Alternatively, the OST could bring a limited range of services within the scope of the OST, possibly based on the essential use of physical premises in the preparation. All this would be an added complication for businesses to an area of tax that is not straightforward and the difference would increase the likelihood of taxpayer errors.
- 4.23 **Question 7: Do you think that digital products should be included in an OST? How should a 'digital product' be defined?**
- 4.24 If equivalent digital products can be sold from a retail premises, then it would appear equitable to fall within the scope of an OST in the same way as goods, though if a supply is normally sold without the need for premises, then it is arguably not in competition with retail premises. For example, in a retail store there are a variety of gift cards on sale that can be redeemed for digital services, such as a contribution towards a streaming subscription or to spend on mobile phone apps. There are specific rules for VAT on vouchers⁶ so if digital services are included within an OST, similar rules must be considered for an OST.

⁴ <https://www.gov.uk/guidance/catering-takeaway-food-and-vat-notice-7091>

⁵ <https://www.gov.uk/guidance/food-products-and-vat-notice-70114>

⁶ <https://www.gov.uk/guidance/find-out-about-changes-to-vat-legislation-on-face-value-vouchers-vat-information-sheet-0918>

- 4.25 For VAT purposes, digital services are also known as ‘electronically supplied services’ and definitions for digital services are provided in VAT legislation and guidance⁷. If such services have an equivalent available for purchase in a retail store, then these too may be subject to an OST.
- 4.26 **Question 8: How can the risk of value shifting from goods to services be reduced, for an OST that has services out of scope?**
- 4.27 HMRC ran a VAT & value shifting consultation⁸ in 2021 to which the CIOT responded⁹. The OST policy team may wish to engage with the value shifting team to discuss relevant value shifting examples and outcomes experienced by HMRC for VAT.
- 4.28 Value shifting has been experienced with other taxes, such as warranty insurance (VAT exempt) with white goods (standard VAT rate) and value shifting within Insurance Premium Tax. Value shifting has required specific legislation to counter avoidance.
- 4.29 To reduce the scope for error or manipulation, it may be necessary to introduce specific valuation provisions where goods and services are supplied together, and they are not all subject to an OST. The rules in section 19, and Schedule 6 to VATA may provide a basis for such provisions. Similarly, well-established VAT rules around concepts of single and multiple supplies, delivered goods etc, provide something of a blueprint for any OST.
- 4.30 **Question 9: Are there other ways you could foresee OST being avoided? How could this be defended against?**
- 4.31 As for question 8 above, the VAT and value shifting team in HMRC may have examples for VAT that could be relevant to an OST. The CIOT has not received feedback on any additional examples.
- 4.32 It is not clear how overseas sellers to UK consumers will be taxed, or if these sellers will be outside the scope of the regime, though there may be at an unfair advantage compared to UK sellers if they are not. If however the OST is due on online sales by overseas sellers to the UK, how will HMRC identify and register applicable businesses? Will they have to appoint an agent or tax representative? The CIOT is represented on HMRC’s Split Payment VAT forum (split payment still being in its infancy), and it could be possible for the split payment to also incorporate a flat rate OST if required, though we understand that any introduction of split payments for VAT is looking likely to be beyond 2026.
- 4.33 **Question 10: Do you think some or all categories of services listed above (including any digital services) should be included in the scope of an OST? Would you add any additional services?**
- 4.34 We do not have further examples.
- 4.35 **Question 11: To what extent do businesses currently distinguish between their sales of goods and services in business systems? On what basis do they currently make this distinction?**
- 4.36 This question is too broad for the CIOT to answer so businesses will be better placed to provide the required details.

⁷ <https://www.gov.uk/guidance/the-vat-rules-if-you-supply-digital-services-to-private-consumers>

⁸ <https://www.gov.uk/government/consultations/vat-and-value-shifting>

⁹ https://assets-eu-01.kc-usercontent.com/220a4c02-94bf-019b-9bac-51cdc7bf0d99/6acee604-c5e9-49a0-baa7-915172d3d4ca/210408_VAT_and_Value_Shifting_CIoT_comments.pdf

- 4.37 **Question 12: Do you agree that an OST should be designed to exclude B2B sales?**
- 4.38 Because an OST is a tax which will not be recoverable by businesses and given the need to avoid multiple layers of tax, we would support the OST being levied only on sales to final consumers, and excluding B2B transactions from its scope. If an OST is levied on B2B transactions, there is the risk that this irrecoverable tax will just cascade down by being embedded as part of the business' cost base (like irrecoverable VAT).
- 4.39 Distinguishing between B2C and B2B sales will however bring added complications to OST calculation and reporting, as businesses will have to evidence that customers who claim to be in business actually are. Whilst the CIOT would not support mandatory certification, HMRC should advise in guidance what evidence would be acceptable proof.
- 4.40 It may be worth exploring the use of 'presumptions', in a similar way to those which determine the place of supply for VAT purposes of telecommunications, broadcasting and electronic services.
- 4.41 **Question 13: Do you agree that an approach of removing all B2B transactions from scope would be preferable to applying the tax according to the individual transactions (eg according to the use of the item sold)?**
- 4.42 A broad-based rule such as excluding all B2B supplies from the scope of the tax would be administratively simpler than the more complicated position of determining the tax treatment at an individual transaction level, particularly for businesses with a large portfolio of products and customers.
- 4.43 However, there will inevitably be a temptation on behalf of business customers (particularly unincorporated businesses), who intend to use the products for private purposes, to purchase the item in their business capacity, thus avoiding the OST. However, the fact that the customer may then lose their rights under the Consumer Rights Act might dissuade that behaviour. It is also possible that somebody with a single account with a supplier may make an error in deeming the purchase to be business or personal, and the supplier would not be in the position to know.
- 4.44 **Question 14: What is your preference from the above or any alternative approaches to exclude B2B sales from an OST while limiting administrative burdens on business?**
- 4.45 Our preference would be to not have any compulsory certification. Suggestions for evidencing a business could be the supply of a valid VAT registration number, which for many businesses forms part of setting up a business customer in the reporting system. Alternatives for non-VAT registered customers could be its company number or an HMRC reference number that is not required to remain confidential. Any process which involves the use of HMRC registration numbers would require HMRC to issue them promptly, so that new or growing businesses are not disadvantaged because they can't provide evidence of business status due to HMRC delays. This still does not address the question of people buying in different capacities as we mention in our response to Question 13 above.
- 4.46 **Question 15: How do you think a business should be defined for the purposes of an OST?**
- 4.47 There are definitions of what a business is in VAT legislation; the definition of a business for OST should be the same as an existing tax definition, and it should be made clear which definition is being used for these purposes.
- 4.48 **Question 16: Are there other types of entities or transaction types which should be out of scope of an OST eg online sales by charities, public bodies or consumer to consumer transactions?**

- 4.49 For transparency, the CIOT is a charity making a limited number of online sales of goods and services so declares an interest, though it is likely that such sales would be below any OST annual threshold and allowance (if introduced).
- 4.50 Supplies by charities and public bodies can be complicated for VAT purposes with supplies being exempt from VAT, subject to a zero or reduced rate, non-business, or outside of the scope. A transactional OST on top of the varied VAT positions would bring added complication and cost for these entities. For public bodies, central government may need to increase their funding to offset the costs of an OST so this may render it ineffective. The CIOT would support public bodies and charities being outside the scope of the OST regime. The position must be also considered for charities' trading subsidiaries.
- 4.51 We would not support a consumer-to-consumer OST as these types of non-commercial transactions would be well below any threshold and allowance.

5 Chapter 3: Design

5.1 Question 17: Do you agree that an OST would be levied on vendors?

5.2 Yes, unless there are contractual reasons why a person in the supply chain becomes the 'deemed vendor' (eg undisclosed agent). The question of who bears the tax is a separate point and that the tax being levied on vendors does not preclude it being passed on to consumers through increased prices.

5.3 Question 18: How should different intermediaries that sell online on behalf of other businesses be treated with respect to an OST ie online marketplaces, franchises, auctioneers, agents and commissionaires?

5.4 In any supply chain, it must be determined who is the underlying supplier; for multi-party arrangements, the supplier is normally determined via the contractual arrangements.

5.5 The position for an OST for such intermediaries should largely mirror the similar rules for the VAT position.

5.6 For VAT, there are circumstances where third parties in the supply chain become joint and several liability for the VAT on supplies to consumers. It should be considered whether the OST will also be within the scope of this obligation.

5.7 Question 19: Are there situations in which it is not possible to distinguish the vendor from the intermediary, or in which the intermediary plays a crucial role in the sale? How should these be treated?

5.8 For VAT purposes, this can be the case for undisclosed agents and there is existing legislation and guidance¹⁰ for the VAT treatment of such sales, which could be broadly mirrored for an OST.

5.9 Question 20: Are there circumstances in which it would be appropriate for an intermediary to be liable for an OST, rather than the underlying seller? What are these?

5.10 See question 19.

5.11 Question 21: How would an OST define UK customers?

¹⁰ <https://www.gov.uk/hmrc-internal-manuals/vat-taxable-person/vtaxper35000>

- 5.12 There are existing definitions in VAT legislation and VAT guidance as to what constitutes a UK customer, and this can be different for goods and services. For simplicity, the OST rules should mirror these definitions as far as possible to reduce confusion.
- 5.13 **Question 22: Should UK-based intermediaries play a role in identifying taxable transactions or be made liable in some cases?**
- 5.14 If OST applies to a sale in a similar way to VAT, there could be differing OST obligations for the intermediaries, depending on the circumstances: disclosed agent/Undisclosed agent/Commissionaire. The VAT manual on taxable person: Agents sets out basic positions though in practice there are generally more complications to be considered.
- 5.15 Consideration is required on the OST position of administrators. There is legislation and guidance¹¹ published for VAT for this sector that could form the basis for the OST rules.
- 5.16 **Question 23: Would either a revenue or a flat fee approach have a greater distortive impact on consumer behaviour? What are the scope and design considerations that would lead to distortion caused by both models?**
- 5.17 The impact on customer behaviour is likely to depend, at least in part, on how visible the OST is to the consumer, and whether it affects the price they pay. The OST could be itemised on their online sales receipt as an additional tax charge and this may influence the customer to buy in-store rather than online, especially if a high-value item.
- 5.18 A flat fee OST could be distortive for low priced supplies, so the level of impact on customer behaviour may differ depending on the value of the supply, and again whether the tax is passed on. For example, ordering a single item for £1,000 with a flat fee OST of £2 may be largely disregarded by consumers or absorbed by the seller, whereas for an order of a few pounds, a flat fee of £2 may see consumers abandoning the online purchase.
- 5.19 **Question 24: Would either approach be particularly preferable? If so, why? Are there any preferences around scope (ie different exclusions or exemptions) which would make one of the approaches more preferable?**
- 5.20 We suspect that the businesses potentially in scope of an OST are better placed to answer this question.
- 5.21 **Question 25: Do you have experience to share of overseas' taxes on online sales using either model, or similar approaches not covered above?**
- 5.22 Although we did not receive feedback specifically on an online sales tax, it was noted that charging a tax on sales to the end consumer is similar to the USA's sales tax. In the international arena, there has been a move away from sales tax models with VAT being the preferred system for dealing with tax on consumption.
- 5.23 The USA's sales tax is charged on either the end consumer or to a business that will not make an onward supply of the purchase. The feedback received is that it administratively burdensome, particularly where reseller certification is required to evidence that the purchase may be made by a business on a tax-free basis. We would not recommend that certification be introduced for a UK OST.

¹¹ <https://www.gov.uk/guidance/insolvency-and-vat-notice-70056>

- 5.24 **Question 26: What factors should be taken into consideration in setting an allowance? How would this differ for revenue and flat-fee models of an OST?**
- 5.25 See question 27 below.
- 5.26 **Question 27: What would be a reasonable OST threshold and allowance to set in order to protect small businesses while also making sure the OST generates sufficient tax revenues?**
- 5.27 The consultation documentation states that a threshold of £1-£2million of 'taxable' sales has been suggested by stakeholders; taxable referring to those sales that fall within the OST regime, rather than the business turnover itself (unless all sales are subject to the OST). This may mean that the business turnover is much larger than the threshold, though mainly with sales that are outside the scope of an OST.
- 5.28 We note that for VAT, HMRC has a VAT reporting simplification for smaller businesses, the annual accounting¹² scheme, which is for businesses with an annual taxable turnover of up to £1.35million. We would suggest that the OST threshold is no lower than the annual accounting threshold as it would seem at odds to be providing such administrative simplifications for VAT whilst at the same time bringing small businesses with a turnover of £1-1.35million into the OST regime. Ideally, there would still be some gap between the VAT annual accounting threshold and the minimum taxable sales for an OST, so our preference would be for the OST threshold to be nearer to, at or greater than the £2million annual taxable sales, irrespective of whether the OST is transactional or revenues based.
- 5.29 It is also worth noting that, if the threshold is based on 'taxable' sales, sellers will need to undertake many of the actions they would need to take as if they were in scope ie, determine sales in scope, identify and exclude B2B transactions etc. Consideration might be given to a higher turnover threshold alongside, or in place of, the 'taxable' sales threshold.
- 5.30 For a revenue-based OST, we would assume that the OST will still become payable to HMRC, even where the business does not make net profits in the annual accounts. If this is the case, this could increase the likelihood that the OST will be passed on to consumers, either embedded into the sales price or visible to the consumer as a separate charge.
- 5.31 In principle, we agree that an allowance could be available in addition to the OST threshold. However, it is not clear in the consultation document how this would not effectively be an increased annual threshold. Perhaps the allowance could have additional qualifying criteria including options not based on taxable sales eg, if you have a low amount though high valued number of transactions, you must reach a minimum annual number of qualifying transactions in addition to the annual OST threshold, though perhaps only up until a secondary threshold. If the business exceeds the annual threshold with low value high volume of sales, there could be a tapered additional allowance on annual sales up to a secondary threshold.
- 5.32 HMT would have to apply a taxable income modeller to determine the impact of any allowances in addition to the annual threshold; the CIOT is not able to calculate these figures.
- 5.33 **Question 28: Do you agree that an OST threshold or allowance should apply once to all businesses under common control?**

¹² <https://www.gov.uk/vat-annual-accounting-scheme/eligibility>

- 5.34 We do not necessarily agree with this statement. For VAT, businesses under common control may all be separately registered for VAT with independent VAT reporting, or they may form a VAT group and have a single VAT registration number that is applicable to all of the businesses.
- 5.35 Where businesses are under common control but independently registered for VAT and there is no artificiality in being separate, it would appear to be administratively complex to monitor the OST threshold and allowance conditions across several businesses under common control, who may have little or no associated supplies. This position would likely be more manageable for a VAT group, where all of the group's sales are reconciled into a single VAT declaration and there is a clearer oversight of the members' combined sales in a VAT return period.
- 5.36 There are VAT disaggregation rules¹³ regarding the artificial splitting of a business for the purposes of tax avoidance, which could be replicated in the legislation for an OST regime.
- 5.37 There is a similar common control rule for businesses liable to Digital Services Tax, though the threshold is much higher ie when the group's worldwide revenues from digital activities are more than £500 million and more than £25 million of these revenues are derived from UK users. Further, these this threshold test excludes the supply of goods entirely, which if where there are likely to be more difficulties in determining whether a supply is in scope of OST or not.
- 5.38 **Question 29: Do you agree the threshold or allowance would apply to individual businesses when they operate franchises or sell through online marketplaces?**
- 5.39 Yes.
- 5.40 **Question 30: Do you consider there to be strong arguments either for or against quarterly or annual reporting? If this hinges on any of the design options laid out in this consultation, please specify which options and why.**
- 5.41 Because an OST will require data to be captured at a transactional level (whether charged on a flat fee or revenues basis), it would seem appropriate to follow the reporting periods for other transactional taxes such as VAT, IPT etc where returns are typically required quarterly. It may also be necessary to allow or require more frequent reporting (eg for the largest businesses), and we have already recommended that smaller businesses using VAT annual accounting should be excluded.
- 5.42 **Question 31: Can you provide insight into the overall burden to administer all systems and processes required to support an OST? Do systems currently allow you to identify the features listed above; if so, please provide further details on how this distinction can be made.**
- 5.43 We have received feedback that it will be complex, possibly expensive and time consuming to adapt systems to account for a new OST.
- 5.44 Businesses would be better placed to provide feedback on the variety of systems used and their ability to identify relevant supplies.
- 5.45 VAT registered businesses are obliged to report VAT via Making Tax Digital (unless an exemption applies). HMRC will need to consider whether an OST will also be brought into the MTD regime and if so, when. The focus on MTD is currently on ITSA and we would not want to see an OST mandated until taxpayers have

¹³ <https://www.gov.uk/hmrc-internal-manuals/vat-single-entity-and-disaggregation-manual>

gone through the ITSA process. It will also be necessary to ensure that OST software is readily available, and compatible with other forms of MTD.

6 Chapter Four: Impacts

6.1 **Question 32: On balance, what would the impact be of an OST with business rates reductions on the scale described above, including on retailers that operate both online and offline?**

6.2 We have not received specific feedback on this question so retailers will be better placed to respond to this question.

6.3 **Question 33: Do the potential revenues from such a tax justify the additional administration that it would require of businesses, as well as the design complexities detailed in the previous sections?**

6.4 Irrespective of the tax raised, if it is anticipated to largely be used for funding increased rents for retailers then it becomes ineffective. As set out in paragraphs 1.2-1.3 this risk must be explored fully by the OST policy team.

6.5 We would like to see a comparison of the possible revenues of an adjusted VAT system (as suggested in para 4.3) compared to the anticipated OST revenues (which of themselves appear relatively modest). Further the exercise to identify avoidance and evasion in the BR review should be undertaken to see if the BR gap is similar to the anticipated OST revenues.

6.6 Introducing a new tax would bring complexities to taxpayers. It is not ideal to have VAT rules and OST rules applied to every sale. Though VAT was introduced as a 'simple' tax, the requirement to consider the VAT liability position on every sale and every purchase can make it a really complicated tax to administer, and for more complicated businesses with mixed portfolios of supplies, this would only be further compounded by an OST.

6.7 **Question 34: To what extent do you think an OST would impact innovation, efficiency and productivity?**

6.8 There could be some impact on investment / R&D for some businesses, particularly small businesses with tight margins and low-price elasticity. There may be some consideration given to how a new product or supply delivery could be adjusted to ensure it remains outside the scope of the tax. That said, there a risk that businesses might curtail their online sales if they become subject to an OST if they are nearing the threshold, thus affecting business growth. If there is a low threshold, smaller businesses could be put off selling online because of the additional tax / compliance obligations.

6.9 There would be upfront impacts on efficiency and productivity for most businesses affected by the OST rules. This includes the time taken to understand the rules (which may require the assistance of an outsourced tax specialist), review of the products to determine whether they are within the scope of an OST, updates to reporting/delivery systems, staff training and possible staff recruitment. Post implementation there will be additional responsibility of the administration and compliance of the tax.

6.10 **Question 35: To what extend do you believe that an OST would impact consumers' behaviour in favour of in-store retail?**

6.11 We believe that some combination of economic analysts and the retail sector is best placed to comment on consumer behaviour.

- 6.12 **Question 36: How do you expect online retail to evolve in the coming decade and how should an OST take account of these?**
- 6.13 Whilst economic analysts and the retail sector itself are likely best placed to answer this question, we note that there have been difficulties for businesses in determining the VAT liability of new innovative supplies which do not fit easily into the existing VAT rules, and we consider that an OST would be in a similar position. In such cases where the VAT liability position cannot be determined, the business has the option of making a submission to HMRC's non-statutory clearance team¹⁴. However, this can be a time-consuming and costly exercise for both the business and HMRC. Further, if HMRC deems that the supply can be dealt with under current legislation and guidance, it can be a frustrating exercise for both parties as HMRC may not provide a ruling upon which reliance can be placed and HMRC may not be able to provide a full explanation of the position.
- 6.14 If an OST was introduced, we anticipate that HMRC would have to issue similar non-statutory clearances to taxpayers where they are unsure whether evolving business models and/or supplies are in or out of scope of the OST.
- 6.15 **Question 37: What is the evidence for the degree of pass-through of the cost of an OST to consumers? To what extent will this vary depending on the type and value of the goods sold?**
- 6.16 We would anticipate that costs related to an OST, whether transactional or revenue based, would all/mostly be borne by the end consumer by means of increased prices.
- 6.17 We received feedback that some businesses who are subject to the Digital Sales Tax ('DST') have made an additional charge on invoices to customers to recoup the additional taxation costs. This is in spite of the DST not operating as a transactional tax. If an OST was introduced, we would anticipate that the position would be similar, whether it was itemised on an invoice or merely embedded into the price of the product(s) being supplied.
- 6.18 In the new Plastic Packaging Tax legislation, provision is made in legislation for the adjustment of pricing in contracts, so that the supplier can vary the price due to PPT (unless there is a pre-existing agreement preventing this). This evidences the general expectation that additional taxation costs for specific supplies are anticipated to be passed on to the customer. The CIOT has received feedback and direct member queries asking about the VAT position for this type of PPT recharge which evidences that pass-through for PPT occurs.
- 6.19 **Question 38: Do you have any data which would support the Government in making an assessment of the incidence of the tax or its distributional impacts?**
- 6.20 No.
- 6.21 **Question 39: In your assessment, what would be the distributional impact of an OST? Are there particular groups who are likely to be worse affected than others? How would this change if an OST were applied as a flat-fee per transaction (or some other similar metric) versus a percentage of firms' revenue from online sales?**
- 6.22 The introduction of new taxes impacts is difficult for smaller businesses who may not be represented by a tax agent, whereas larger businesses may have in-house tax specialists or engage outsourced specialist advice. HMRC may also find smaller businesses 'hard to reach' in terms of distributing educational material to raise

¹⁴ <https://www.gov.uk/guidance/non-statutory-clearance-service-guidance>

awareness of the new obligations. Businesses might still be considered 'small' even with turnover exceeding £1m.

- 6.23 Any introduction of a new tax, or new tax reporting processes, creates costs for businesses; this will be the case whether an OST is flat-fee or revenues-based. Whilst this can be very difficult for small businesses in terms of cost and resource time, it can also bring significant costs to larger businesses too, particularly for bespoke upgrades to reporting systems, which usually have to be outsourced to software contractors and then there is the cost of staff training or having to recruit new staff to deal with specific taxes. The CIOT is aware that some large businesses have had to recruit staff to specifically deal with Plastic Packaging Tax, or new staff to deal with customs duty/import/export burdens after the UK left the EU. For smaller businesses that cannot afford new staff, they would have to add responsibilities to the existing tax team or bear the cost of outsourcing to a tax adviser.
- 6.24 Where the cost of an OST is passed onto consumers, this would disproportionately impact lower income households, unless adjustments were made to relevant benefits, pensions or tax credits to offset increased price of the tax. If benefits were increased to mitigate the impact of the OST, the largest impact would be to consumers with incomes that are marginally above the threshold for governmental support.
- 6.25 For certain retail supplies, there are currently exemptions from VAT (Schedule 9 to the VAT Act 1994) or a zero/reduced rate of VAT (Schedules 7A and 8 to the VAT Act 1994) that applies for social policy reasons. It would seem at odds for an OST to be applied to sales that already have existing exemptions/reductions from VAT due to government social policy reasons (although conversely, granting exemptions undermines the declared 'rebalancing' purpose of OST). VAT Notice 701/7¹⁵ - *Reliefs from VAT for disabled and older people* provides just some of the examples of consumers who would be impacted by an OST charged on VAT-relieved supplies. Where consumers use online shopping due to reasons of (but not limited to) age, disability or lack of public transport, they may have no choice but to bear the cost of the pass-through of an OST.
- 6.26 It would seem sensible to relieve supplies qualifying for VAT exemption or a reduction to the standard rate for social policy reasons to also be exempt from the portfolio of supplies subject to an OST, though it may bring some unintended complexity, as such supplies are often litigated for VAT liability purposes.
- 6.27 **Question 40: What environmental impact might an OST have? How would its design affect an OST's environmental impact?**
- 6.28 The sole reason for having an OST is to fund RRR and rebalance the BR burden on high street bricks and mortar retailers compared to online retailers who can occupy cheaper out-of-town commercial properties, thereby increasing the (likely carbon-intensive) journeys of consumers to the 'high street'. There are no aims for an OST to either change customer behaviour to a less polluting way to shop nor impact businesses' net zero strategies: it may achieve the reverse. A thorough review of the likely net impact should be undertaken if this proposal is to proceed.
- 6.29 The main carbon emissions for retail and online sales are likely to come from property, transport (commercial and/or consumer) and waste from packaging.

¹⁵ <https://www.gov.uk/guidance/reliefs-from-vat-for-disabled-and-older-people-notice-7017>

- 6.30 The government's ten point plan¹⁶ sets out aims for greener buildings (point 7) and the shift to zero emission vehicles (point 4), and it is unclear to what extent, if any, the design of an OST could impact the emissions without embedding environmental aims into the design from the outset.
- 6.31 There are many live projects that are considering environmental impacts; for instance, for retail transport, the Department of Transport has ongoing work on the decarbonisation of road/rail freight and focus on reducing emissions for 'last mile logistics' for the deliveries of goods. This project is far better placed to know the environmental impact of transport on the retail market, so the policy team for the OST project could engage with DoT to explore the impact of an OST.
- 6.32 As many businesses are implementing carbon neutral and net zero strategies, the level of emissions produced in a bricks-and-mortar based retail business compared to an online retailer with a warehouse and customer delivery business model are constantly changing with the aim of decreasing emission levels year on year or within specified timeframes. It seems unlikely that an OST, which should only be funding RRR, will have any or negligible impact on carbon emissions. However, the OST policy team should explore whether the OST taxes the more polluting or less polluting way of purchasing retail products. From a green agenda perspective, it would seem odd to be taxing the less polluting way of buying retail products.
- 6.33 In respect of waste created by packaging in the retail market, the government has recently introduced a new tax, Plastic Packaging Tax, to encourage the use of recycled plastic in packaging products. Retailers and consumers will also face a new environmental charge on purchases, the Deposit Return Scheme. This will be introduced in Scotland in August 2023 and is anticipated to be implemented in the other UK countries, possibly in 2025. The VAT liability position on the DRS is still the subject of ongoing negotiations between the UK and Scottish governments and stakeholders have been raising concerns with the complications on the VAT position. A transactional OST would further complicate the position though may not specifically impact the carbon emissions position.

7 Acknowledgement of submission

- 7.1 We would be grateful if you could acknowledge safe receipt of this submission, and ensure that the Chartered Institute of Taxation is included in the List of Respondents when any outcome of the consultation is published.

The Chartered Institute of Taxation

19 May 2022

¹⁶

https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/936567/10_POINT_PLAN_BOOKLET.pdf