

Provision of clothing free of charge to staff

[French Connection Ltd](#)

This case concerns the provision of clothing free of charge to staff. Staff were provided with a clothing allowance for the particular season. They then chose items from French Connection's (FC) stock up to the amount of the allowance, which they were allowed to keep. Whilst these items were provided free of charge, where a member of staff left within 3 months of the start of that new season their pay would be reduced by 30% of the value of the allowance used. FC accounted for output VAT on these deductions from salary but not on the value of the clothes provided. HMRC considered that when the clothes were given to staff there was a supply for VAT purposes and assessed FC for undeclared output tax. The assessment was based on the cost to FC of the clothing provided to staff, less the output tax accounted for on the 30% charges and less amounts where the cost of the clothes to an employee who left was under £50 (i.e. the business gift limit). The taxpayer ran a number of arguments. The key points coming from the FTT are:

- 1) Business Purpose – The taxpayer essentially argued that the UK had not properly implemented Article 16 of the Directive because HMRC was seeking VAT on goods provided free of charge to employees, solely for the purpose of their employment. The FTT disagreed saying that reference to non-business was an 'or' condition. The clothing in question constituted goods forming part of the assets of the business and were disposed of free of charge. The FTT concluded that the clothes were provided for a business purpose, but in this analysis this was irrelevant for determining whether there was a supply of goods.
- 2) Uniform – The taxpayer argued that there were a number of Tribunal decisions, especially Zoo Clothing, which supported its interpretation that the supply of a uniform was not a supply of goods. The FTT agreed with HMRC that whether the clothes were uniform or not had little or no relevance to determining whether there was a supply of goods. For completeness, the FTT concluded that it considered the clothes were not 'uniforms'.
- 3) Business Gifts – The issue of business gifts arises on a number of occasions. The FTT concluded that, despite the fact the arrangements were contractual, this did not prevent them being gifts. However, the FTT again concluded that the fact they are business gifts has no bearing on whether there is a supply for VAT purposes; the only impact of the gift rules would be to exclude gifts that cost less than £50.

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- 4) Valuation of the supply – The taxpayer ran a number of arguments focused on the time and value of the supply. These centred on the fact that on certain occasions, when staff leave at a certain time, they are charged 30% of their allowance. The FTT concluded that the time of supply was correctly when the clothes were provided to staff. In relation to the subsequent charge, the FTT concluded that it could not be right that a supply was devalued in case the staff member were to leave in the future. The VAT accounted for on the 30% charge was deducted from the assessment, since, if VAT was due on the full cost amount when the goods were handed over free of charge, VAT could not also be due on the 30% charge when the staff member subsequently left. Finally, the taxpayer raised issues regarding the valuation of the clothes. However, as the FTT concluded that the time of supply was when the clothes were provided to staff, the value was that of the cost to FC.

The taxpayer's appeal was dismissed.

Comment

This case highlights the difference between the VAT treatment of 'freely given' goods and services. For small value items, goods are efficient because of the business gift rules. Any business purpose test is irrelevant as it is the disposal free of charge that triggers the deemed supply under Article 16 if the item is not of small value. For services, obtaining VAT recovery without any equivalent deemed output tax charge very much depends on business purpose tests, as highlighted by the on-going Associated Newspapers litigation, which is to be heard at the UT later this year.

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