

Joint Tax CoE, HMRC and HMT VAT Meetings – Subject: IT Licences

Meetings between HMRC, HMT and the Tax Centre of Excellence are usually held bi-monthly or as often as required and the statement of purpose is to promote best practice and knowledge sharing within the Government Department (GD) sector in relation to CoE customer GDs – but where practicably possible, other GDs and executive agencies as well. The CoE works in partnership with HMRC and HMT on the impact of VAT changes and their applicability to the CoE.

At our joint meeting held on the 1st December we discussed Contracted-Out Heading 14 – IT Licences and the following principles were agreed in relation to the current HMRC COS14 guidance:

- Licences delivered electronically are deemed to be a supply of services and not goods and is within EU Implementation Regulations which were enacted in 2011; and
- where a physical package is purchased containing a voucher or code to be redeemed electronically then this is also a supply of services.
- A licence which is supplied as part of a fully managed IT service or is part of a dovetailed fully managed IT service - whether for bespoke or off-the-shelf software is VAT recoverable. (see examples a-d below)
- A licence which is not supplied as part of a fully managed IT service but is for **bespoke** software is VAT recoverable however a licence purchased for off-the-shelf software is not. (see examples e-i below)

What is a licence?

A licence is not a tangible good but a service and grants the use of intellectual property (the software) to the end user usually under an end user licence agreement. Nearly all software applications are licensed rather than sold. There are a variety of different types of software licenses. Some are based on the number of machines on which the licensed program can run whereas others are based on the number of users that can use the program; they vary and provide for software such as Office, upgrades to Windows, database systems and tools to manage infrastructure. A licence does not allow the transfer of the software to another user without express permission of the software owner, neither does it allow for alteration by the recipient without express permission. **As such in all licence cases the ownership of the intellectual property remains with the licence provider.**

The following examples and VAT treatment have been agreed:

Examples of a licence provided separately to the delivery of software or a fully managed service but where the licence is an integral part of the end to end fully managed IT provision / dovetail principle

- a) In this example the licence is supplied and invoiced separately but is all part of the same fully managed service. Company A Ltd supplies a fully managed IT service to a GD and also a bespoke software build. The licence to use the software and for subsequent maintenance, was purchased from a subsidiary of Company A Ltd. The licence is owned by the subsidiary and is invoiced separately to the rest of the fully managed service and is for the on-going

maintenance and access to the bespoke software. The licence is an integral part of the fully managed service because of the access to and use of the bespoke software and the software forms a composite supply of a fully managed IT system provided by Company A Ltd. The licence enables the GD system access and to carry out its daily business as well as ensuring all interfaces link up.

Agreed VAT recovery under H14. Reason – the licence dovetails into the fully managed IT service and is also relating to bespoke software.

- b) This example demonstrates where the GD has made the decision to take procurement of the licence in-house – though still delivered to the GD from an external provider with the rest of the fully managed IT service externally outsourced. Both are integral to each other.

An IT system allows the GD to link together and create an environment where historic systems can be interrogated. The licences are purchased by the GD from an external company, the licence allows access to this IT system / software by the GD's outsourced IT provider – Company B. Company B makes use of the licences (provided by the external licence provider) in their provision to the GD of a fully managed IT service. Although the GD allows Company B the use of the licenses in order for them to provide the fully managed IT service the risk of operating and managing the licenses does not rest with the GD but remains with Company B. The licence software is an integral part of the managed service provision. Previously under this example Company B delivered everything including sourcing the licences direct from the external licence provider without any involvement from the GD.

Agreed VAT recovery under H14. Reason – the licence dovetails into the fully managed IT service.

- c) This is an example of how a GD requires licences as part of the fully managed and serviced IT infrastructure in order to function and operate its 'standard' computer infrastructure.

Microsoft licences are purchased through a reseller not directly from Microsoft. These licences (supplying access to a multitude of different programs, operating systems, security, mail, maintenance and software updates) are integral to the delivery of the fully managed IT services via agreements with Company B who deliver the computer systems and infrastructure. Both the licenses and the infrastructure on their own are not operational. However when put together i.e. dovetailing they can then deliver the services and the GD can carry out its daily business.

Agreed VAT recovery under H14. Reasons the licence dovetails into the fully managed IT services as part of the delivery of the computer infrastructure and systems

- d) Oracle Licences

Oracle supply licences to a number of GDs for use of the Oracle ERP product which provides for use of financial, procurement and HR systems etc. These ERP systems are an integral part of a fully managed IT system and the purchase of licences directly from Oracle dovetail in with the other IT contracts which make up the end to end managed IT supply. Without the Oracle licenses the GDs cannot operate their systems.

Agreed VAT recovery under H14. Reasons –the licence dovetails into the fully managed IT service.

- e) A licence purchased for off-the-shelf software with the intended use of this software as-is (i.e. not part of a fully managed IT supply nor dovetailing).

Agreed VAT treatment is not recoverable. Reason – the licence / software does not meet H14 criteria.

- f) A licence is purchased for off-the-shelf software, however the GD has no intention to use this software in its current state but will have it significantly modified fulfilling the criteria of 'bespoke software' (the be-spoke work performed in-house).

Agreed VAT treatment – not recoverable, does not meet H14 criteria.

- g) The GD purchases the software and licence and using in-house expertise turns it into a bespoke application. The application is then maintained and supported (along with all the other IT applications) by the outsourced IT service provider and their charges will also cover patches, upgrades and technical support.

Agreed VAT treatment – the initial Purchase of software/licence is not VAT recoverable under H14. Reason – the original supply is for off the shelf software.

However, when the outsourced IT service provider starts to support the finished bespoke application (along with all the other software as part of its managed IT supply to the GD), then the ongoing costs for this are VAT recoverable as part of the supply of a fully managed IT system; H14 criteria is met.

- h) A variation of (f) – A licence is purchased for off-the-shelf software however the GD has no intention to use this software in its current state but to have it significantly modified fulfilling the criteria of 'bespoke software'. The be-spoke work is outsourced to either another provider or the same provider of the licence.

Agreed VAT treatment is VAT recoverable. Reason bespoking, meets the H14 criteria.

- i) Bespoke software is supplied to the GD and the GD purchases the licence for the use of this bespoke software either as part of the provision of the bespoke software or from a separate supplier. Note: This licence could be the original off-the-shelf licence that the Supplier purchased prior to the bespoke build.

Agreed VAT treatment is recoverable for either the original licence or specifically for the bespoke software once built. Reason bespoking meets the H14 criteria

If you have any questions on the above, please get in touch with your hub contact.