

# VAT treatment of free meals and transport for employees 1/14/21



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Both before and during the Covid-19 crisis, some companies have been providing their employees with free meals and transport between home and work for the sake of business continuity. This article explores the VAT implications of this practice.

## VAT rules

Taxpayers planning to provide their employees with free meals or transport should consider provisions of the VAT Act governing the deduction of input tax and the taxation of personal consumption.

The right to deduct input tax on goods and services acquired for making taxable supplies arises from a key principle of the VAT system.<sup>1</sup> We need to consider restrictions on input tax deduction imposed by section 100 of the VAT Act and in particular restrictions set by the Cabinet of Ministers<sup>2</sup> that deny the deduction of input tax on goods and services acquired for staff recreation, private needs (including transport services, fuel purchases and telecommunications), meals, health improvement, and entertainment. It is important to note that the right to deduct input tax is an integral part of the VAT system and cannot be restricted in principle. According to the case law of the Court of Justice of the European Union ("CJEU") any restriction on input tax deduction rights affects the tax burden and should be applied equally across the EU. Deviations are allowed only in cases specifically listed by the VAT Directive, which provides that input tax on expenses that are not closely linked to business, such as luxuries, amusements and entertainment, is not deductible.

The ban on the deduction of input tax on food or transport expenses under the Cabinet of Ministers' rules is essentially a declarative provision because each situation should be assessed according to whether the free service aims to promote the company's business or to satisfy private needs. So the right to deduct input tax on free meals or transport for employees is not denied in every case. The CJEU finds that accommodation, food, reception and entertainment expenses may be closely linked to the company's business needs and where those expenses are shown to represent costs of its taxable supplies, they should create input tax deduction rights.<sup>3</sup>

In addition to provisions allowing input tax deduction, we need to consider provisions that determine the taxation of personal consumption. VAT applies on a free transfer of assets usable in the taxpayer's business or on a free supply of services for the private needs of the taxpayer or his staff or on the use of the taxpayer's assets for non-business purposes if input tax on the goods or their components has been fully or partly deducted. This provision aims to ensure equality between the company's employees and any other person wishing to acquire the service, who would have to pay VAT on it. Whether free services should be charged to VAT depends on whether they aim to satisfy the private needs of the taxpayer or his staff (a non-business purpose) or to carry on business.

Clearly, in most cases the employer is not responsible for how an employee plans to commute. Yet in certain situations (e.g. the building trade, the cleaning trade and horticulture may involve work being done

at constantly changing addresses, something the employees could not even be aware of when being hired), the employer's attempts to keep employees from using public transport and other reasons related to the Covid-19 crisis may create a need to provide employees with transport services. The employee's private benefit from such services is merely subordinated to the company's business purpose.

Also, a meal during the lunch break is the employee's own choice and cost unless this free choice is strictly limited. The length of the lunch break, the location of the workplace, working evening and night shifts, unusual working hours, short breaks, employees' inability to return from lunch on time and other factors may create conditions for the taxpayer where providing the employee with free meals at the workplace is crucial for business continuity. In that case the employees' private benefit is not the primary one.

Thus, while in general the purpose of free food or transport services is to satisfy the private needs of staff, under certain conditions the risk a company faces when leaving the food or transport decision to the employees may be critical for the normal conduct of business. Clearly, employees receive a private benefit from free food or transport, but this should be treated as subordinated to the company's needs and purposes. The CJEU case law confirms this opinion: there are no restrictions on input tax deduction if the employee indirectly receives a private benefit from the acquired goods and services in addition to the benefit derived by the company.<sup>4</sup>

So employers that regularly or occasionally provide or plan to provide their employees with free food or transport should be able to explain their decision and the rationale behind it in order to retain input tax deduction rights or to avoid having to charge VAT on those free services.

Our upcoming articles will be dealing with certain aspects of personal income tax and corporate income tax.

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<sup>1</sup> Section 92 of the VAT Act

<sup>2</sup> The Cabinet of Ministers' Rule No. 17 of 3 January 2013, Application of Provisions of the Value Added Tax Act and Certain Requirements for Payment and Administration of Value Added Tax, paragraph 159

<sup>3</sup> CJEU ruling of 19 September 2000 on joint cases C-177/99 and 181/99

<sup>4</sup> CJEU ruling of 1997 on case C-258/95 and the Attorney General's findings of 11 December 2008 on case C-371/07