

United Kingdom

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AT A GLANCE

Name of the tax	Value Added Tax
Date introduced	1 April 1973
Date of membership in EU	1 January 1973
Administered by	Her Majesty's Revenue & Customs (HMRC)

VAT rates

Standard	20%
Reduced	5%
Other	Zero-rate (0%) and Exemption
VAT Number format	GB123 4567 89
VAT return periods	Quarterly although HMRC may require a monthly or yearly submission in certain circumstances
Thresholds registration	£85,000 (2017/18)

Recovery of VAT by a non-established business - Yes

HISTORY OF VAT

Value Added Tax (VAT) was introduced in the UK on 1 April 1973 by the Finance Act 1972 at a rate of 10%. Several other Acts have been released to amend the original, the most recent of which is the VATA 1994. This act provides the VAT framework but many of the details can be found in regulations provided by HMRC, who the government authorize to manage this tax. Since its introduction both its application and complexity have increased exponentially.

SCOPE OF VAT

A transaction is within the scope of UK VAT if it is a supply of goods or services that takes place in the UK and is made by a taxable person (an individual, firm or company who is registered for VAT). This supply should also be made in the course or furtherance of business in order to qualify for VAT.

REGISTRATION

A UK trader must register for VAT when the value of his taxable supplies exceeds £85,000 in any 12-month period. However, a business may choose to register for VAT even if it does not meet this threshold, allowing it to reclaim any input tax incurred in relation to taxable business activities.

From 1 December 2012, non-UK established businesses are obliged to register and account for VAT on their supplies irrespective of their value. The VAT registration threshold is £NIL in such circumstances.

This does not apply to distance selling. Distance selling occurs when a taxable person in one EU member state provides and delivers goods to customers in another member state, where that customer is not registered for VAT, e.g. when goods are ordered over the internet. In cases such as this the registration threshold is £70,000. This threshold is relevant with respect to sales in a calendar year (1 January - 31 December).

VAT RATES

There are currently 3 effective VAT rates in the UK;

- The standard rate of VAT (20%)
- The reduced rate (5%), e.g. domestic supplies of fuel and power, children's car seats and residential renovations, conversions and alterations.
- The zero-rate (0%), e.g. books, medicines and certain foods.

If a supply cannot be defined as being liable to the reduced or zero rate, or being exempt, it is by default a standard-rated supply.

PLACE OF SUPPLY RULES

Goods

Goods exported out of the UK to a non-EU country are treated as a UK supply for VAT purposes and attract the zero-rate of VAT. Conversely, goods imported into the UK from outside the EU will not be a UK supply. However, VAT will be due on the import for which the person named as importer is accountable. This VAT is recoverable subject to the normal rules of deduction.

When goods leave the UK for an EU customer this is known as a dispatch. The place of supply in instances of this nature is the UK and the dispatching business can zero-rate the supply provided two conditions are met.

- (1) The customer is VAT registered in another Member State;
- (2) The goods can be evidenced as being removed from the UK to another Member State. It does not need to be the same country as the VAT number used at (1)

If either of the above conditions are not met UK VAT should be charged at 20%.

Goods entering the UK from an EU supplier are known as acquisitions for UK VAT purposes. The place of supply is deemed to be the location of the supplier. However, if acquisitions exceeding £85,000 are made by a non-UK business, then it will be liable to be registered for VAT in the UK.

Services

Where services are supplied from one business to another, the place of supply is usually treated as being where the recipient belongs (B2B). Where the recipient of the relevant services is not a business, the supply is usually treated as being supplied in the country in which the supplier belongs (B2C).

This gives effect that services supplied from business to business are not UK VATable where the supplier is in the UK and customer in another country. The customer would account for VAT under the reverse charge principle.

Services supplied to consumers are usually taxed at 20% where the supplier is in the UK. This also applies to B2B supplies where the customer and supplier are both in the UK.

There are exceptions to these rules. For example, any services supplied in relation to land are treated as being supplied where the land is situated. Admission to or participation in events, meetings, conferences etc, the place of supply is treated as where the event takes place. This applies to both business and non-business customers.

TIME OF SUPPLY RULES

Allocating the correct tax point to a transaction is important to ensure that transactions are included in the correct period VAT return.

The time of supply and tax point is usually the earlier of; the date when the goods are removed (or made available to the customer), the date of payment for the goods, or the date a sales invoice is issued.

The relevant date for a supply of services is the earlier of when the service is completed, an invoice is raised, or payment received. For a continuous supply of services, the time of supply is considered as the earlier of invoice date and payment date.

Exceptions to these rules occur when deposits are paid as this creates more than one tax point for a supply. These two tax points are calculated in the normal way in relation to the date the deposit is paid and the date the remaining balance is paid.

EXEMPTIONS

All exempt supplies in the UK are treated as non-taxable and therefore no input VAT incurred in relation to any of these supplies can be recovered. The value of any supplies of this nature should not be counted towards the VAT registration threshold for compulsory registration. Examples of exempt supplies include services relating to betting, gaming and lotteries, finance, insurance and some land transactions, for example; the rent on a property is usually exempt.

RECOVERY OF INPUT VAT

To allow a business to recover input VAT from HMRC a supply of goods or services must have taken place. The goods or services that have been supplied must have a direct link with a taxable transaction. The supply must have been made to a taxable person for a business purpose and VAT must have been correctly charged. Input VAT incurred is available for credit in the period in which it arises and is deducted from output tax owed in the same period. If the input tax for a given period is greater than output tax HMRC make a payment for the net amount.

Where a business makes both taxable and exempt sales the trader is required to identify what input tax relates exclusively to each type of supply. Input tax incurred solely in relation to taxable supplies is recoverable by normal means, and input tax relating to exempt supplies is non-recoverable.

There will be instances where input tax incurred cannot be attributed to either taxable or exempt supplies exclusively – this is “residual” input tax. Residual input tax must be apportioned to determine the extent to which it relates to taxable supplies.

Under a system previously known as the 8th VAT Directive refund system, a business that incurs VAT on costs in an EU member state where it is not registered and does not make supplies is entitled to recover VAT directly from that member state.

Non-EU businesses can reclaim UK VAT via the 13th directive provided that there is a reciprocal arrangement allowing a UK company to reclaim indirect taxes paid in that country. Input tax is blocked on items such as business entertainment costs or costs relating to any exempt supply.

COMPLIANCE OBLIGATIONS

HMRC have a general power that requires traders to keep certain records including; copies of all VAT invoices issued/received by the business, documentation relating to all imports and exports, documentation relating to all acquisitions and dispatches of goods; credit and debit notes and a VAT account. These records must be kept for a minimum of 6 years.

A VAT registered person should provide his customer with a VAT invoice within 30 days of the tax point of the supply. The invoice should contain the following information;

- 1) Invoice number;
- 2) Date of supply;
- 3) Invoice date;
- 4) Supplier's name, address and VAT registration number. If the supply has been made to a customer in another EU member state, the registration number must be prefixed e.g. GB;
- 5) Recipient's name, address and, if the recipient is another EU member state, it must show the recipient's VAT registration number in that member state;
- 6) Description and quantity of goods/services;
- 7) Amount being charged;
- 8) Rate of VAT applicable;
- 9) Total amount being charged;
- 10) Rate of discount, if offered
- 11) A reference to any schemes utilized.

A taxable person is expected to complete and submit his VAT return at the end of each VAT quarter, although traders can request to submit a return at the end of every month. The VAT return should denote the VAT element of all transactions that fall within the scope of UK VAT as well as any VAT relating to trade that takes place within the EU and tax on imported goods. An online return must be submitted within 7 days of the end of the month following the quarter end (for example, a 30 April return should be submitted by 7 June). Electronic payment is due on the same date although any payments made by direct debit will be allowed 3 extra days.

Where a VAT return is submitted late or a payment of VAT is made late, the trader is liable to a default surcharge. When the first default occurs, a default surcharge liability notice is issued, meaning that any default during the 12 months (surcharge period) after the first default will result in a percentage of unpaid tax being owed to HMRC in addition to the unpaid tax. The surcharge period is also extended to 12 months from the end of the quarter of the default.

The greater the number of defaults during the surcharge period, the greater the percentage of unpaid VAT payable to HMRC by the trader.

SPECIAL CASES

The period in which a trader must account for items is usually dictated by the tax point of the transaction. However, HMRC allow smaller businesses to disregard these rules and instead use the **Cash Accounting Scheme** to account for VAT. Under the rules of the scheme, movements through the cash book are taken into account; the date input tax paid & the date output tax received. This scheme allows traders automatic bad debt relief as they are only required to pay HMRC the VAT on the payments received, instead of paying in advance, before sales invoices may have been settled.

A further scheme which allows businesses to lessen the burden of VAT is the **Annual Accounting Scheme**. Utilizing this scheme allows small and medium sized business to submit one VAT return a year, two months after year-end, and to pay VAT on an annual basis. Estimated payments are made during the year and final balance is settled at the end. Either 90% of the previous year's VAT liability is paid in 9 installments or as an alternative, the trader may choose to make 3

payments of 25% of the previous year's VAT liability. To qualify for the scheme, the taxable supplies of the trader must not exceed £1.35 million per annum.

Small businesses are also able to utilize the **flat-rate scheme** if the business' taxable turnover will not exceed £150,000 net in the next 12 months. In the normal way of accounting for VAT, payments to HMRC from the VAT return are measured by outputs less inputs. Under the flat-rate scheme a business does not change the way that it invoices customers and the same costs would be incurred by the business. However, when completing the VAT return, no input tax can be reclaimed. The output tax is calculated by multiplying VAT inclusive income by a flat-rate percentage. Each category of business has a specified flat-rate percentage and once a trader has established which category they belong to, the relevant percentage is applied to tax inclusive turnover to calculate the amount of VAT due. A 1% reduction applies to newly registered businesses using the flat-rate scheme for its first 12-month period. There are strict record keeping and accounting requirements.

The **Second-Hand Goods Scheme** exists for traders who buy their goods from unregistered members of the public and re-sell to other members of the public. It allows these traders to only account for VAT on the gross profits they have made as opposed to paying VAT on purchases and charging VAT on sales. The gross profit is VAT inclusive and so for standard rated goods the VAT fraction would be 1/6th. The utilization of this scheme brings many record keeping requirements with which the trader must stay compliant.

The **Tour Operators' Margin Scheme (TOMS)** is a special scheme that applies to businesses which buy in and re-sell travel, accommodation etc. TOMS may apply to tour operators, hoteliers who buy coach passenger transport and coach operators who buy in hotel accommodation. The scheme allows VAT to be accounted for on travel supplies without businesses having to register and account for VAT in every country in which the services and goods are enjoyed. Output tax is only payable within the scheme based on the margin of the supplies and input tax cannot be reclaimed on any margin supplies but can be reclaimed on any general overhead items.

RIGHTS OF THE TAX PAYER AND THE VAT AUTHORITIES

HMRC enforces compliance with the VAT legislation by the following means;

- HMRC have the powers to obtain information and documentation with the power to inspect premises if they are reasonably required to do so in order to check that person's tax position.
- A registered trader can expect their first control visit within 3 years of registration. Control visits can vary in duration depending on the perceived risk factor and the size and complexity of the business. The primary objective of the visit is to ensure that VAT is being accounted for correctly. If VAT is found to be due then a Control Officer will raise an assessment.
- Assessments are issued where a VAT return has not been submitted or has been submitted with errors resulting in VAT owed to HMRC not being paid. HMRC must consider fairly all material supplied by the trader and must base a decision on what has been provided. They must be made by the later of;
 - I. Two years after the end of the prescribed accounting period in question; or

- II. One year after evidence justifying the raising of an assessment comes to light. This rule is subject to a four year cap.

If a trader disputes the raising of an assessment by HMRC they have 2 options;

1. A taxpayer can request a review, asking HMRC to reconsider their decision. If this review is unsuccessful an appeal.
2. A trader can appeal directly to the First-tier tribunal whether a review has initially been requested or not. An appeal must be made within 30 days of the date of the disputed HMRC decision/assessment and can only be made in respect to certain matters. A trader is unable to appeal any decision/assessment if he has outstanding VAT returns or any outstanding liability.

EU DECLARATIONS

When a UK business acquires and dispatches goods within the EU, additional paperwork is required to be submitted. An Intrastat (or Supplementary Statistical Declaration (SSD)) is required for dispatches if the total value within a year exceeds £250,000. For arrivals, an Intrastat is required when total annual value exceeds £1,500,000. They must be completed and submitted electronically on a monthly basis within 21 days of the end of the relevant month. Nil returns need not be submitted.

An EC Sales List (ESL or ECSL) is required in order to record goods or services (with no UK VAT charge under the place of supply rules) sold to a VAT-registered business in another EU member state.

A business selling goods to other EU member states will automatically be sent an ESL if he has submitted an intrastat declaration. A business supplying services to EU customers, will be responsible for obtaining an ESL from HMRC themselves by the due dates.

Where a business sells goods to customers located within the EU with a quarterly value exceeding £35,000, a monthly EC Sales Lists is mandatory. Any value of sales below this threshold will require a quarterly ESL submission.