

# VAT Facts

2017/18



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## Registration

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**Standard rate** = 20% from 4 January 2011

**Registration threshold from 1 April 2017:** £85,000

**Deregistration threshold from 1 April 2017:** £83,000

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## VAT rates and types of supply

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There are three different VAT rates, and these are collectively called taxable supplies:

- 0% - zero rate, e.g. books, construction of new residential buildings, transport and charity advertising;
- 5% - reduced rate, e.g. children's car seats, energy saving materials and certain types of construction work;
- 20% - standard rate, i.e. most other supplies.

There are also:

- Supplies made outside the UK, which are not therefore subject to VAT but, had they been made in the UK, would have been taxable, which allows input tax recovery (see below);
  - Non business supplies, e.g. supplies made by a charity for no consideration;
  - Exempt supplies – on exempt supplies no VAT is charged, e.g. land transactions, finance, insurance and charities.
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## Implication on VAT recovery of costs and overheads

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VAT incurred on your purchases and expenditure is called input tax. Input tax can be reclaimed if it relates to:

- Taxable supplies made in the UK, excluding exempt supplies;
- Supplies outside the UK that would be taxable supplies if made in the UK.

Input tax cannot be reclaimed if it relates to:

- Non business supplies, e.g. charitable activities;
- Certain supplies that are excluded, e.g. entertaining and the purchase of motor cars;
- Exempt supplies, unless it is beneath the partial exemption de minimis limits (see below).

Input tax cannot be recovered if it relates to non business supplies. Firstly, you must identify non business input tax, which includes a proportion of VAT on overheads. After excluding input tax on non business supplies, you have to identify input tax on exempt supplies, which may be recovered if it is beneath specified limits. This is called partial exemption (see below).

What remains should be taxable input tax, which is recoverable.

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## Partial exemption

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Input VAT can be claimed only to the extent that it relates to a taxable supply, either directly or on an apportioned basis. Where residual input tax is substantial, anti-avoidance provisions to prevent distortion must be considered.

A business can be treated as fully taxable in any accounting period if its input VAT attributable to exempt supplies is:

- i) £625 or less per month on average; and
- ii) the VAT incurred on purchases relating to the making of exempt supplies is no more than 50% of the VAT on purchases for taxable and exempt supplies.

On 1 April 2010 a simplification was introduced. If your exempt input tax is less than either test 1 or 2 below you may, on your periodic VAT returns, recover all your exempt input tax as you go and perform the detailed calculation at the VAT year end; this is when you account for exempt input tax for the year in the usual way if you exceed the limits.

Test 1: total input tax of the business is no more than £625 per month on average, and the value of exempt supplies is no more than 50% of the value of all supplies; or

Test 2: total input tax of the business less input tax directly attributable to taxable supplies is no more than £625 per month on average, and the value of exempt supplies is no more than 50% of the value of all supplies.

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## Bad debts

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A business may reclaim output tax, as bad debt relief, on any debts that are unpaid after six months. However, businesses that have not paid their liability to suppliers within six months are required to repay HMRC any input tax that they have claimed.

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## Input tax on cars

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- Businesses can recover the VAT that they pay on the purchase of cars bought wholly for business purposes. This primarily benefits leasing companies. In these cases, they will have to charge VAT when they sell the car. If a car is purchased outright, including on hire purchase, then no VAT can be recovered unless it is used wholly for business purposes;
- A business that rents a car from a lessor who has reclaimed the input VAT can reclaim 50% of the VAT on the rental charge where there is both business and private use. If there is no business use, no input VAT can be recovered. If you recover only 50%, you do not have to account for VAT on the employee's private use.

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## VAT fuel scale charges

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VAT is chargeable on the private use of fuel and is based on the vehicle's CO<sub>2</sub> emissions. The tables are updated regularly and are on HMRC's website.

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## Accounting

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### When do you charge VAT?

This is called the tax point or time of supply and is the earliest date that the goods/services are supplied, an invoice is raised or payment is made/received. The date of the invoice becomes the tax point if the invoice is raised within 14 days of the basic tax point.

### Place of supply

The place of supply of services is the place where a service is treated as being supplied. This is the place where VAT (if any) is due. For example, the place of supply of accounting services from the UK to a **business customer** in France, is France and the recipient accounts for TVA, not the UK supplier.

### Annual accounting

Annual accounting (one annual VAT return) is available when turnover for next year is anticipated to be no more than £1,350,000. Nine interim payments are required, or three quarterly ones. You are required to leave the scheme when your taxable turnover has exceeded £1,600,000.

### Cash accounting

Cash accounting is available when taxable turnover is no more than £1,350,000. You are required to leave the scheme when your taxable turnover has exceeded £1,600,000.

### Flat-rate scheme

Businesses with VAT exclusive turnover of up to £150,000 are permitted to calculate their net tax by applying a percentage for their industry to their turnover. If your business income exceeds £230,000, you have to leave the scheme.

### Special schemes

Special schemes are also available; for example, second-hand goods, tour operators, retailers and motor traders.

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## Groups

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### Eligibility

Two or more corporate bodies are eligible to be treated as a VAT group if each has a fixed establishment in the UK. One of them must control the other, or one person control all of them, or two or more individuals **in partnership** control all of them.

### **Intra VAT group supplies**

Intra VAT group supplies are normally disregarded for VAT purposes. In cases of deliberate avoidance, HMRC may direct that:

- Intra VAT group supplies are liable to VAT;
- An associated company is to be treated as part of the VAT group;
- A member of the VAT group is to be treated as removed from the VAT group.

### **Holding companies**

Input tax on professional fees incurred in connection with the acquisition and disposal of shares in a subsidiary is recoverable in so far as the company incurring the cost is fully taxable; otherwise, partial exemption restrictions will apply.

Currently, a company that makes no taxable supplies in its own name, e.g. a non trading holding company or insurance company, can be included within a VAT group.

### **Applications**

An application for a company to join or leave a VAT group is effective from the day it is received by HMRC, or such other time as is agreed.

Additional anti-avoidance provisions apply where third parties receive the majority of economic benefits and the group is not fully taxable.

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### **VAT schemes – avoiding or saving VAT**

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The use of VAT mitigation schemes has to be disclosed within 30 days of the due date for submission of the returns. It is important to take advice if you believe you might be affected.

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### **Property**

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#### **Option to tax**

- An option to tax at the standard rate of VAT is available to those persons who make otherwise exempt supplies of land and buildings, other than dwellings and relevant charitable or residential buildings or a pitch for a residential caravan or facilities for the mooring of a residential houseboat;
- All options are revocable after 20 years. An option is also revocable within six months of notification to HMRC, subject to meeting certain conditions. All the forms are on the HMRC website under VAT 1614.

#### **Capital goods scheme**

Where the cost of a building or works to a building is £250,000 or more and VAT has been incurred, then any amount of exempt use within ten years of completion will give rise to an adjustment under the capital goods scheme. In

certain situations, the option to tax is not effective for land or buildings, including those that are, or will become, covered by the capital goods scheme either by the grantor or the recipient and will be used other than for a fully taxable business.

Input VAT initially claimed on IT equipment costing £50,000 shall be adjusted in accordance with the fluctuations in the taxable person's recovery rate, over 5 years.

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## Trade with EU

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There are special procedures and returns for trade with other EU states. The main requirements are:

- A quarterly EU sales list is required for goods supplied to other member states where the value in the current and previous four quarters does not exceed £35,000. Monthly lists are required where the limit is exceeded;
- Quarterly EU sales lists are required for services supplied to business customers in other EU states who account for VAT under the reverse charge;
- A monthly intrastat form is required both for arrivals and dispatches over the cumulate threshold, which is £250,000 for dispatches and £1,500,000 for arrivals. The forms are due electronically by the 21st of the following month;
- Goods and many services sold to an EU trader are zero-rated where the VAT number of the customer is shown on the supplier's sales invoice;
- VAT on goods acquired from the EU is self-assessed but recovered subject to the normal rules. Businesses selling by mail order to private customers must register in the customer's member state if the relevant requisition threshold is reached;
- If trade involves three countries it may be necessary to register in other member states.

Businesses that incur VAT in an EU state in which they are not VAT registered, may be able to recover the VAT under the 8th Directive if they are based elsewhere in the EU, or under the 13th Directive if they are based outside the EU.

The above does not take into account any changes that may occur following the vote to leave the EU on 23rd June.

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## Errors and penalties

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Errors that are up to the greater of £10,000 or 1% of turnover, subject to an upper limit of £50,000, can be adjusted on your subsequent tax return. Larger errors must be separately notified on Form VAT 652 or by letter.

If you correct an error that is under these limits on your next VAT return, due to the penalty regime mentioned below, you should consider whether to notify HMRC that you have made an error and corrected it on the next return.

### Penalty regime

On 1 April 2008 a new system for penalties was introduced that is linked to the reasons why the errors have occurred, and linked to potential lost revenue and the culpability of the trader.

This system applies in the same way to most taxes.

Under this system, if you send in a document that contains a mistake, HMRC will charge a penalty if the error is:

- Because of a lack of 'reasonable care';
- Deliberate - such as intentionally sending incorrect information;
- Deliberate and concealed - such as intentionally sending incorrect information and taking steps to hide the error.

The penalties are geared to the "potential lost revenue" (PLR). The table shows how the penalties relate to your culpability.

Penalised behaviour	Maximum penalty, without disclosure, based on PLR	Minimum penalty, with prompted disclosure, based on PLR	Minimum penalty, with unprompted disclosure, based on PLR
<b>Careless</b>	30%	15%	Nil
<b>Deliberate but not concealed</b>	70%	35%	20%
<b>Deliberate and concealed</b>	100%	50%	30%

There is also the concept of a suspended penalty but only for the "careless" category. HMRC mentions, as an example, a tennis club that sold its land to the local authority but omitted to disclose the gain on its tax return. They say that such a penalty cannot be suspended because the club is unlikely to have future gains.

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### Failure to pay VAT or submit a return

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Currently, there is a default surcharge system where penalties do not bear a direct relationship with the offence. A leading case is due to be heard, which may determine whether the system is fair.

A fact sheet of this type is, by necessity, of a brief and summarised nature. Kingston Smith LLP cannot accept liability for any losses incurred as a result of reliance thereon. Professional advice should be sought for more detailed information on specific technical points. Minimal reference to the VAT implications on construction, land and property has been made due to its extensive nature: greater detail is considered inappropriate for a fact sheet of this type. All information was correct at the time of going to press: March 2017.

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