

# Making Tax Digital for VAT

## (Lectures B1051/ B1052 – 13.44/ 12.48 minutes)

Digital reporting and record keeping for VAT, included in the pre-Budget Finance Bill 2017 updates the powers contained within Schedule 11, VAT Act 1994 (administration, collection and enforcement), allowing the introduction of Making Tax Digital for VAT. Draft Regulations and a Draft VAT Notice were published for consultation on 18 December 2017 with comments invited by 9<sup>th</sup> February 2018.

From 1 April 2019 businesses with a turnover in excess of the VAT threshold (£85,000) will have to:

- keep their records digitally for VAT, and
- provide VAT return information through MTD functional compatible software.

This requirement will remain, even if they fall below the threshold at a later date. It will only cease when they deregister for VAT.

Businesses with turnover below the VAT registration threshold can choose to stay on the current system for VAT or they may elect for the relevant exemption not to apply.

### *Exemptions*

The exemptions that already apply to electronic VAT returns will be extended to cover digital record keeping requirements and so includes a business:

- that is run entirely by practising members of a religious order whose beliefs are incompatible with the use of electronic communications;
- to whom an insolvency procedure applies;
- where it is not reasonably practicable to make a return using an electronic return system due to disability, age, remoteness of location or other reason.

Where HMRC commissioners refuse any of these exemptions, there is a right of appeal.

### *Functional compatible software*

This is software that is required to meet MTD requirements. It will be used to:

- keep records in a digital form as required by the regulations;
- preserve digital records in a digital form as required by the regulations;
- create a VAT return and provide HMRC with this information digitally;
- provide HMRC with VAT data on a voluntary basis;
- receive HMRC information via the Application Programme Interface (API) platform.

HMRC have said that they will provide a list of compatible software in due course which is likely to include all of the current software providers (Xero, QuickBooks, SAGE, FreeAgent, KashFlow). Businesses are not restricted to using just one piece of software. However where more than one piece of software is used, they must be digitally linked to ensure that HMRC receive what they need.

#### *HMRC VAT Notice Example 1*

A business uses one piece of accounting software (A) to record all sales and purchases and electronically transfers the totals into a spreadsheet (B) that it uses to calculate the return. The information is then sent to a piece of bridging software (C) that submits the return to HMRC.

Altogether the three pieces of software maintain the mandatory digital records, calculate the return and submit it to HMRC. The links between the three pieces of software must be digital for the set of software to be functional compatible

There will be a one year soft landing period for penalties where there are manual links between (A) and (B). After that, they must be automated. This soft landing approach does not exist for manual links between (B) and (C) which must be automated from day one.

#### *HMRC VAT Notice Example 2*

A business uses one piece of accounting software to record all sales and purchases, this software then calculates the return and submits it to HMRC. As well as the records in the accounting software the business uses a spreadsheet to keep track of a fleet of cars and work out its road fuel scale charges.

The adjustment is not required to be kept in digital format so the business can type the adjustment into its accounting software.

#### *HMRC VAT Notice Example 3*

A VAT group uses three different software packages to record the mandatory records for different parts of the group. Each piece of software calculates the amounts needed for the return from each part of the group. A common spreadsheet is used to compile the totals and create the return for the whole of the group. The information is then sent to a piece of bridging software, which submits the return to HMRC.

Altogether the five pieces of software maintain the mandatory digital records, calculate the return and submit it to HMRC. The links between the five pieces of software must be digital for the set of software to be functional compatible software.

#### *HMRC Agent's example (Addendum to the VAT Notice)*

In this example the client keeps their VAT records on a non-API enabled spreadsheet. The client emails the spreadsheet to their accountant who imports the data into their API enabled software, with any adjustments being filtered back to the spreadsheet. The accountant submits the VAT return from their API enabled software.

### *Digital record-keeping*

The regulations will specify the information a business needs to keep and preserve digitally, and will include designatory data such as business name, principal place of business, VAT registration number and details of any VAT accounting schemes used.

For each supply made, there must be a record of the time and value of the supply as well as the rate of VAT charged. Output value for the period must be split between standard rate, reduced rate, zero rate, exempt and outside the scope.

For supplies purchased, the business must record the time and value of each supply as well as any input tax claimed.

There is no real time requirement for MTD so data could be entered just before submitting a VAT return. Clients who are reluctant for whatever reason to move over to MTD, could task tax agents to do the work for them, handover over their manual cashbooks once a quarter and with the agent using their own software to meet the MTD record keeping and filing requirements. It should be noted that the accountants would have to enter each transaction into the software rather than totals.

Each VAT registered business must keep a VAT account providing the link between primary records and the VAT return; The VAT account will be used by the software to fill in and the taxpayer's VAT return and to calculate the VAT payable or repayable.

### *Retail schemes*

Retail scheme users will be permitted to record electronically sales transaction data based on daily gross takings, rather than recording individual sales.

### *Flat Rate Scheme*

Digital record keeping requirements for flat rate scheme users will mirror current record keeping requirements so scheme users will need to keep records of sales but the only records of purchases they must keep are those relating to capital goods with a VAT inclusive value of £2,000 or more.

### *VAT returns*

The return will be produced and submitted digitally; there will be no option to manually input numbers for businesses over the £85,000 threshold. The functional compatible software should be able to produce a VAT return from the digital records that have been created. The user will be able to check the return and then submit it digitally to HMRC on a quarterly basis, unless monthly or annual returns are being filed. There will be no requirement to change VAT quarters to align them with the accounting or tax year end.

For agents to be able to submit the returns on the taxpayer's behalf, they will obviously need to have access to the functional compatible software, either the client's software or their own.

For the time being there will be no change to statutory VAT return or payment dates.

### *Voluntary updates*

Taxpayers will have the option to voluntarily submit supplementary data. It seems likely that most will not use this facility and will stick with the standard nine-box return.

If HMRC make an enquiry into a VAT return, information will need to be supplied digitally but, until that point, no additional information needs to be submitted.

#### *VAT Return Example 1*

A business uses one piece of cloud based accounting software to record all sales and purchases. They provides access to their agent. The agent calculates the business partial exemption adjustment on a spreadsheet and enters this into the software. The software then calculates the return and submits it to HMRC.

As the records in the spreadsheet are not required digitally, the agent can type the adjustment into their accounting software. However a digital link would reduce the chance of errors.

#### *VAT Return Example 2*

A business uses one piece of accounting software to record all sales and purchases and transfers the totals into a spreadsheet. The business sends this spreadsheet to their agent, who uses it to calculate the return, ideally by importing data into compatible software. The information is then sent to a piece of bridging software that submits the return to HMRC.

The three pieces of software maintain the mandatory digital records, calculate the return and submit it to HMRC. The links between the three pieces of software must be digital for the set of software to be functional compatible software.

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