A Clear Vision Guide – January 2023

Your Guide to VAT

CLEAR VISION
accountancy · consultancy

Disclaimer

The information contained in this guide has been extracted from HMRC VAT online guidance and produced in summary form for general awareness.

Specific VAT issues should always be confirmed with an accountant.

Contents

What is VAT?

Value Added Tax (VAT) is the tax you pay in the UK when you buy goods or services. It is tax on goods and services consumed in the UK.

The standard rate of VAT in the UK is currently 20%.

There are different rates of VAT for different goods and services:

- Reduced rate – 5%
- Zero rate – 0%
- No VAT is charged on goods or services that are: exempt from VAT
  outside the scope of the UK VAT system

See the Government's guide to VAT and rules and procedures.

Which rate to use

If you are unsure of the VAT rate to use, check on the HMRC website.

What does exempt mean?

There are several types of exempt income including:

- Insurance, finance and credit
- Education and training
- Fundraising events by charities
- Subscriptions to membership organisations
- Selling, leasing and letting of commercial land and buildings – this exemption can be waived.

These items are exempt from VAT so are not taxable. You do not include sales of exempt goods or services in your taxable turnover for VAT purposes. And if you buy exempt items, there is no VAT to reclaim.

Exempt items are different from zero-rated supplies. In both cases VAT is not added to the selling price, but zero-rated goods or services are taxable for VAT at 0%.

When to register for UK VAT

You should register for VAT when your taxable turnover is more than £85,000 over the last 12 months. You have 30 days after the end of the month when you went over the threshold to register.

If you expect your taxable turnover to be more than £85,000 in the next 30 days, you have to register by the end of that 30 day period.

If you trade overseas, including the EU, there may also be specific VAT registration requirements in the UK and in those countries you trade with.

Once you have registered for VAT you usually submit a VAT Return to HM Revenue and Customs (HMRC) every 3 months.

What is taxable turnover?

Taxable turnover is the total value of sales a business makes that is subject to tax after VAT exempt amounts are removed.

Zero rated sales are included.

Claiming back VAT from before registration

You may be able to reclaim VAT paid on goods or services bought before you registered for VAT if the purchases were made within certain time limits.

If I only sell exempt supplies can I register for VAT?

If you only sell or otherwise supply goods or services that are exempt from VAT then your business is an exempt business and:

- You cannot register for VAT.
- You cannot recover any VAT you incur on your purchases or expenses.

This is in contrast to where you sell or otherwise supply zero-rated goods or services. Here you can reclaim the VAT on any purchases that relate to those sales.

Do I need to be a limited company to register for VAT?

VAT registered doesn't just apply to limited companies. Other types of business must register for VAT, such as sole traders and partnerships.

If I have more than one business can I register these separately or not register at all?

If the same person owns two or more separate businesses, they may need to be considered together for VAT registration purposes.

A key question would be “Are the businesses closely bound by financial, economic and organisational links?".

The pros and cons of registering for VAT

If you are under the VAT threshold you do have the option to voluntarily register for VAT.

The advantages of doing so are as follows:

- You can reclaim the VAT paid for business purposes.
- It looks professional.
- It can hide the fact that your turnover may be lower than the threshold.

The disadvantages of doing so are as follows:

- You will have to increase your prices – this will matter if your customers are individuals. If your customers are VAT registered businesses, they will not incur this price increase, as they will be able to claim the VAT back.
- You will have to do more regular accounting.
- You may need to submit quarterly VAT returns within deadlines.

How to register for VAT

Most businesses can register online - including partnerships and a group of companies registering under one VAT number.

You will need to create a Government Gateway account to do this.

You will need to know details like:

- Your effective date of registration - the date you want to be registered from. This can depend on why you are registering – see page 5: 'when to register for UK VAT', for basic registration dates.
- If you are registering voluntarily – an estimate of your taxable supplies/ zero rated supplies/exempt supplies in the next 12 months.

How to account for VAT and prepare your VAT return

From Tuesday 1 November 2022, VAT-registered businesses must sign up to Making Tax Digital (MTD) and use MTD-compatible software to keep their VAT records and file their **quarterly or monthly** VAT returns.

HMRC has a list of compatible software on its website.

Costs against which VAT cannot be claimed

As a VAT registered business, you will charge VAT to your customers and reclaim back the VAT you are charged from suppliers.

Providing you have a VAT invoice or receipt for your costs, you will be able to work out the VAT you have been charged and reclaim this on your VAT return.

You cannot reclaim the VAT on entertainment expenses.

There are special rules for working out how to reclaim VAT for:

- Cars, for example buying, repairing, fuel costs
- Staff travel expenses, for example accommodation and transport expenses
- Businesses that are partly exempt from VAT

VAT return deadlines and VAT payment

The deadline for submitting your return online and paying HMRC are usually the same: one calendar month and seven days after the end of an accounting period.

You need to allow time for the payment to reach HMRC's account.

VAT schemes

Before you start to account for VAT, you must decide which scheme you are going to use.

- **Standard or accrual accounting for VAT**

If you have not chosen another scheme, this is the scheme you will use.

You will charge VAT to customers on your invoices and the VAT is due to HMRC according to the date of the invoice.

The VAT you pay for your costs can be reclaimed from HMRC according to the date of the invoice or receipt.

Usually, you would prepare your return on a quarterly basis. So for a quarter ended 31 March, you would include all the invoices dated 1 January to 31 March that you have received or sent.

You need to hold all the documentation with your records to support your VAT return.

- **Cash accounting for VAT**

To join the scheme, your VAT taxable turnover must be £1.35 million or less.

You must leave the scheme if your VATable turnover is more than £1.6million.

With cash accounting, you account for VAT on the date you're paid as opposed to the date you send the invoice. This can be especially helpful if you have slow payers, since you won't have to pay VAT before you've been paid.

However, this option isn't well suited to businesses that buy a lot of items on credit. You can't reclaim the VAT until payment has been made.

As with the standard VAT accounting method, you still have to complete your returns every quarter.

You can't use this scheme if you are not up to date with your VAT returns or payments, or you use the VAT Flat Rate Scheme.

- **Flat rate scheme**

To join the scheme your VAT turnover must be £150,000 or less (excluding VAT), and you must apply to HMRC.

Under this scheme, you simply pay a percentage of your total turnover as VAT.

The actual amount you pay depends on the type of business you run – different industries have different flat VAT rates.

You'll still have to charge VAT on your invoices, but you don't have to account for the VAT details of every purchase or sale.

- **VAT annual accounting scheme**

You can join the scheme if your estimated VAT taxable turnover is £1.35 million or less.

This is just like the standard VAT accounting method, except that you don't fill in quarterly returns. Instead you have an annual VAT reporting and payment deadline.

With the Annual Accounting Scheme you:

- Make advance VAT payments towards your VAT bill - based on your last return (or estimated if you're new to VAT)
- Submit one VAT return a year.

When you submit your VAT return you either:

- Make a final payment - the difference between your advance payments and actual VAT bill, or
- Apply for a refund - if you've overpaid your VAT bill

This scheme is useful if you want to monitor your cashflow as the payments are more evenly spread throughout the year. You also only have one deadline to submit your return, which is two months after the end of the VAT accounting period.

If you regularly claim repayments this will not be the scheme for you.

- Other scheme available for specific industries

VAT retail schemes.

VAT margin schemes.

Agricultural flat rate scheme.

Partial exemption for VAT

A business is partly exempt if it makes, or intends to make, both taxable and exempt supplies and incurs tax on costs which relate to both. If your business is partly exempt, you may not be able to recover all your input tax. You will have to use a partial exemption method to work out how much input tax you can recover.

Opting to tax - VAT on commercial property

You can 'opt to tax' any building that you have an interest in. You do not have to own it.

You cannot charge VAT on the rental or sale of a building or land unless you opt to tax.

You cannot claim back VAT on any expenses that relate to the land or property unless you opt to tax.

If you have other taxable turnover and expenses and you are VAT registered, you may need to prepare your VAT return using the partial exemption method.

If you own the building consider the implications on the sale of the building. You would have to charge VAT on any future sale of the property. This could be an issue if you are selling to a non-VAT registered person or business. In order to claim back the VAT on the purchase of a building, you would need to opt to tax the property, before claiming back the VAT on your VAT return.

An opt to tax will last for 20 years unless revoked.

You would need to charge VAT on all future rentals and sales.
The option to tax allows a business to choose to charge VAT on the sale or rental of a commercial property. It does not affect residential buildings. If your VAT-registered business uses a property entirely for its own trade, you do not need to opt to tax.

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