



John M. Taylor & Co

CHARTERED ACCOUNTANTS
AND BUSINESS ADVISORS

Incorporating Sheppard & Co.

9 Glasgow Road, Paisley Renfrewshire PA1 3QS

Tel: 0141 848 7474 Fax: 0141 848 7419

Email: mail@johnmtaylor.co.uk

www.johnmtaylor.co.uk

Increase of the Standard Rate of Vat to 20%

The standard rate of VAT is currently 17.5% but increases to 20% from 4 January 2011. Commentators suggest that this will raise additional monies for the treasury of around £12billion per annum so it is a key, albeit largely unwelcome, part of the government's drive to reduce the deficit. As a result, businesses will have to ensure they have systems in place to cope with the rise in the standard rate of VAT from 4 January 2011 as HMRC are unlikely to offer much leeway if things go wrong. Initially, the process may seem relatively straightforward but as many saw with the reduction in the VAT rate in 2008, there are many factors to consider when implementing the VAT rise.

Sales to Vat-Registered Clients

From what date should the new rate be applied?

The rate of VAT that businesses charge depends on the date that goods or services are supplied. For VAT purposes this is the date that goods physically change hands (or a service is completed); or payment is received; or an invoice is issued - whichever is the earliest. The rules are modified in certain situations, including when there is a change in the standard rate of VAT.

For any sales of standard-rated goods or services that take place on or after 4 January 2011 businesses should charge VAT at the new rate of 20%. This means that businesses currently calculating their VAT using the VAT inclusive fraction of 7/47 should use the new fraction of 1/6 from 4 January.

However, the old rate of 17.5% should be used if a business has:

- provided goods or services more than 14 days before the issue of a VAT invoice (e.g. a business which issues a VAT invoice on 4 January 2011 for goods or services provided before 21 December 2010); or
- received payment before 4 January 2011.

What about sales spanning the rate change?

If a business has received a payment or issued an invoice using the old 17.5% rate before 4 January 2011, but the goods will be provided (or services delivered) after 4 January 2011, the supplier has two options:

Option 1: Leave the VAT charged at 17.5% and account for that to HMRC.

Option 2: account for VAT at the new 20% rate and issue a revised VAT invoice to the customer reflecting the increase in VAT charged and additional payment due. This is unlikely to be a problem where the customer can recover 100% of the VAT paid.

If the customer has paid, but the business hasn't yet issued a VAT invoice, the business may account to HMRC for VAT at 20% and recover the additional VAT from the customer.

What about single supply services spanning the rate change?

Where a business issues an invoice after 4 January 2011 for a single supply service which is carried out over a period of time spanning 4 January (e.g. a solicitor preparing a will) the

whole supply can be charged to VAT at 20%. If any VAT has already been accounted for at 17.5% the work carried out prior to 4 January can be charged at 17.5% and the balance carried out after 4 January 2011 can be charged at 20%.

Where a business makes continuous supplies of services, such as leasing of equipment (e.g. computers), it can normally choose either to issue regular invoices at intervals during the year, or to issue one invoice covering a period of up to a year ahead, setting out the amounts due (including VAT) and payment dates. Any invoices issued or payments received on or after 4 January 2011 should be subject to 20% VAT. This means that the annual invoice must be replaced by a new invoice, detailing the revised payments due after 4 January 2011 at the new 20% rate. It should specifically refer to and cancel that part of the old invoice which has been superseded.

Where credit notes are issued for sales that span 4 January 2011, they must be issued within 45 days after 4 January 2011.



Implications for retailers

For businesses such as retailers and restaurants, which principally make cash sales to customers not registered for VAT, the new rate will apply to all takings received on or after 4 January 2011.

The main exception to this rule will be where a customer pays for something they have taken away (or the supplier has delivered) before 4 January 2011. In this case, the sale took place before 4 January 2011 and VAT can be accounted for at the rate of 17.5%.

If a retailer has taken a deposit before 4 January 2011 for goods which will be delivered after the 4 January 2011, the business may choose to account for VAT on the deposit at either the old or the new rate, but any balance paid after 3 January 2011 must be charged at 20%.

Electronic tills, especially those set up to provide VAT information, will need to be adjusted. In some circumstances this may require a software update or a visit from the provider so it is important to consider how you will do this in advance of the rate change.

Other issues

Business purchases

In most cases it is up to the supplier to ensure that the VAT is correct on any invoice that they issue, and the customer will then use it to claim back the VAT charged in the normal way. After 4 January 2011 most input tax claims will be for the amount shown on the invoice. However, if a supply is made on or after 4 January 2011 and the supplier has incorrectly charged VAT at 17.5%, businesses are only entitled to claim 17.5% from HMRC.

Less detailed VAT invoices will not have a separate amount of VAT identified but since the rate used should be specified a similar procedure should be followed.

VAT returns

For the majority of businesses the period of their VAT return 4 January 2011 will fall in the middle of a VAT

quarter and particular care will have to be taken to allocate supplies and purchases to the correct accounting period and to use the correct rate.

Cash accounting

Although the cash accounting scheme allows businesses to account for VAT at the point that payment is received, it does not affect the amount of VAT due and receipts after 4 January 2011 should be correctly identified as supplies made at either the 17.5% or 20% rate (i.e. before or after 4 January 2011). Therefore, care needs to be taken.

The turnover threshold at which a business must leave the cash accounting scheme is unchanged at £1.6million for businesses already in the scheme. For businesses not already in the scheme the cash accounting scheme is available to all businesses with an anticipated turnover of less than £1.35million.

Annual accounting

The rules for annual accounting should not require any adjustment as a result of the change to the standard VAT rate but if you do expect your VAT liability to change significantly before the end of the accounting period, please contact us to help you calculate revised instalments for consideration by HMRC.

Flat rate

New flat rate percentages apply for most but not all categories of business. Note that the flat rate percentages have not simply been increased by 2.5%! The revised table of percentages applicable to supplies made from 4 January 2011 can be found in Annex D of HMRC's guide VAT - *Change of the Standard Rate to 20%*. You can view this here:

<http://www.hmrc.gov.uk/vat/forms-rates/rates/rate-rise-guidance.pdf>

In light of the changes in the flat rate percentages, the VAT inclusive annual flat rate turnover

threshold at which a business must leave the flat rate scheme will increase to £230,000 from 4 January 2011.

Fuel scale charges

There is no change to the fuel scale charges which have applied since 1 May 2010 but the VAT element has been recalculated. The new amounts applicable from 4 January 2011 can be found in Annex C of HMRC's guide VAT - *Change of the Standard Rate to 20%*. You can view this here: <http://www.hmrc.gov.uk/vat/forms-rates/rates/rate-rise-guidance.pdf>

Accounting software

Most accounting software packages have a facility to change the rate of VAT or create an additional rate of VAT, but if you would like any advice on adjusting your accounting package please contact us.

General Planning

Finally, if you are likely to be purchasing any goods or services shortly after 4 January 2011 it is worth considering bringing the purchase forward in order to benefit from the reduced VAT rate that will apply before this date. For small purchases the saving may be relatively small but the larger the purchase the greater the saving.

Further help and advice

Unlike in 2008 where HMRC adopted a light touch approach to errors or mistakes there is no indication that a similar approach will be taken this time round. It is therefore imperative that you consider fully the implications of the increase in the standard rate of VAT and be ready to implement them from 4 January 2011. If you do make a mistake this should be corrected in the normal way by making a voluntary disclosure or correcting it on the next VAT return (subject to the normal limit).

If you have any concerns about the VAT increase or would like any further information on any of the matters raised here please contact us.