RELEVANT TO ACCA QUALIFICATION PAPER F6 (UK)

Value added tax, part 2

This two-part article is relevant to candidates sitting Paper F6 (UK) in either the June or December 2013 sittings, and is based on tax legislation as it applies to the tax year 2012–13 (Finance Act 2012). Read part 1 here.

Paper F6 (UK) will always contain a minimum of 10 marks on value added tax (VAT). These marks will normally be included within Question 1 (focusing on income tax) or Question 2 (focusing on corporation tax), although there might be a separate question on VAT.

VAT returns

VAT returns are normally completed on a quarterly basis. Each return shows the total output VAT and total input VAT for the quarter to which it relates.

VAT returns have to be filed online within one month and seven days of the end of the relevant quarter. Any VAT payable is due at the same time, and must be paid electronically.

Example 1

For the VAT quarter ended 31 March 2013 Jet has output VAT of £12,400 and input VAT of £7,100.

- Jet's VAT return for the quarter ended 31 March 2013 will have to be submitted online by 7 May 2013, being one month and seven days after the end of the quarter.
- VAT of £5,300 (£12,400 – £7,100) is payable electronically, and this will be due on 7 May 2013 when the VAT return is submitted.

Because VAT is a self-assessed tax, HM Revenue & Customs can make control visits to VAT registered companies. The purpose of a control visit is to provide an opportunity for HM Revenue & Customs to check the accuracy of VAT returns.

VAT invoices

A VAT registered business will usually have to issue VAT invoices in respect of standard rated supplies. VAT invoices must contain certain information.

Example 2

Keen Ltd registered for VAT on 1 March 2013.

The company only sells goods, and at present issues sales invoices that show (1) the invoice date and invoice number, (2) the type of supply, (3) the quantity and a description of the goods supplied, (4) Keen Ltd's name and address, and (5) the name and address of the customer. Keen Ltd does not offer any discount for prompt payment.

The company wants to know the circumstances in which it is and is not required to issue a VAT invoice, the period during which such an invoice should be issued, and the additional information that it will have to show on its sales invoices in order that these are valid for VAT purposes.

Issue of VAT invoices

- Keen Ltd must issue a VAT invoice when it makes a standard rated supply to a VAT registered customer.
- A VAT invoice is not required if the supply is exempt, zero-rated, or if the supply is to a non-VAT registered customer.
- A VAT invoice should be issued within 30 days of the date that the supply of goods is treated as being made.

Additional information

The following information is required:

- Keen Ltd's VAT registration number.
- The tax point.
- The rate of VAT for each supply.
- The VAT-exclusive amount for each supply.
- The total VAT-exclusive amount.
- The amount of VAT payable.

The default surcharge

A default occurs if a VAT return is not submitted on time or if VAT is paid late. If the default involves the late payment of VAT then a surcharge may be incurred.

Example 3

Li has submitted her VAT returns as follows:

Quarter ended	VAT paid £	Submitted
30 September 2011	6,200	Two months late
31 December 2011	28,600	One month late
31 March 2012	4,300	On time
30 June 2012	7,600	On time
30 September 2012	1,900	On time
31 December 2012	3,200	On time
31 March 2013	6,900	Two month late

Li always pays any VAT that is due at the same time that the related VAT return is submitted.

- The late submission of the VAT return for the quarter ended 30 September 2011 will have resulted in HM Revenue and Customs issuing a surcharge liability notice specifying a surcharge period running to 30 September 2012.
- The late payment of VAT for the quarter ended 31 December 2011 will result in a surcharge of £572 (28,600 x 2%).
- In addition, the surcharge period will have been extended to 31 December 2012.
- Li then submitted four VAT returns on time.

- The late submission of the VAT return for the quarter ended 31 March 2013 will therefore only result in a surcharge liability notice (specifying a surcharge period running to 31 March 2014).

Errors in a VAT return
A VAT registered business that makes an error in a VAT return that results in the underpayment of VAT can be subject to both a penalty for an incorrect return and penalty interest.

Example 4

During March 2013 Zoo Ltd discovered that it had incorrectly claimed input VAT on the purchase of three motor cars when completing its VAT return for the quarter ended 31 December 2012.

- If the error is less than the higher of £10,000 or 1% of Zoo Ltd's turnover for the quarter ended 31 March 2013, then the error can be voluntarily disclosed by simply entering it on the VAT return for the quarter ended 31 March 2013.
- If the error exceeds the limit, then it can be voluntarily disclosed but disclosure must be made separately to HM Revenue and Customs.
- There will only be penalty interest where separate disclosure is required, but a penalty for an incorrect return might be imposed in either case.

The amount of penalty is based on the amount of VAT understated, but the actual penalty payable is linked to a taxpayer's behaviour.

Example 5

Continuing with Example 4:

- HM Revenue & Customs will not charge a penalty if Zoo Ltd has taken reasonable care, provided the company informs them of the error.
- However, claiming input VAT on the purchase of motor cars is more likely to be treated as careless, since Zoo Ltd would be expected to know that such input VAT is not recoverable.
- The maximum amount of penalty will therefore be 30% of the amount of input VAT incorrectly claimed, but this penalty could be reduced to nil if unprompted disclosure is made to HM Revenue & Customs.

Imports and exports
When a UK VAT registered business imports goods into the UK from outside the European Union, then VAT has to be paid at the time of importation. This VAT can then be reclaimed as input VAT on the VAT return for the period during which the goods were imported.

Example 6

Yung Ltd is registered for VAT in the UK. The company has the choice of purchasing goods costing £1,000 (exclusive of VAT) from either a UK supplier or from a supplier situated outside the European Union.

- If Yung Ltd purchases the goods from a UK supplier then it will pay the supplier £1,200 (1,000 plus VAT of 200 (1,000 x 20%)), and then reclaim input VAT of £200.
- If the goods are instead purchased from a supplier situated outside the European Union, then Yung Ltd will pay £1,000 to the supplier, £200 to HM Revenue and Customs, and then reclaim input VAT of £200.
- In each case Yung Ltd has paid £1,200 and reclaimed £200.

Regular importers can defer the payment of VAT on importation by setting up an account with HM Revenue & Customs. It is necessary to provide a bank guarantee, but VAT is then accounted for on a monthly basis.

When a UK VAT registered business exports goods outside of the European Union then the supply is zero-rated.

Trading within the European Union
When a UK VAT registered business acquires goods from within the European Union, then VAT has to be accounted for according to the date of acquisition. The date of acquisition is the earlier of the date that a VAT invoice is issued or the 15th day of the month following the month in which the goods come into the UK.

This VAT charge is declared on the VAT return as output VAT, but can be reclaimed as input VAT on the same VAT return (this is known as the reverse charge procedure). Therefore for most businesses there is no VAT cost as the output VAT and the corresponding input VAT contra out. The only time that there is a VAT cost is if a business makes exempt supplies, since an exempt business cannot reclaim any input VAT.

Example 7
Continuing with Example 6:

Yung Ltd also has the option of purchasing goods from a supplier situated in the European Union.

- Yung Ltd will pay £1,000 to the supplier. Then on its VAT return the company will show output VAT of £200 and input VAT of £200.
- The end result is the same as with an import from outside the European Union, but with a European Union acquisition there is no need to actually pay the VAT subsequent to its recovery as input VAT.

When a UK VAT registered business supplies goods to another VAT registered business within the European Union then the supply is zero-rated.

International services
Services supplied to a VAT registered business are generally treated as being supplied in the country where the customer is situated. Therefore, where a UK VAT registered business receives international services the place of supply will be the UK.

Example 8

Wing Ltd is registered for VAT in the UK. The company receives supplies of standard rated services from VAT registered businesses situated elsewhere within the European Union. As business to business services these are treated as being supplied in the UK.

- VAT will be accounted for on the earlier of the date that the service is completed or the date it is paid for.
- The VAT charged at the UK VAT rate should be declared on wing Ltd's VAT return as output VAT, but will then be reclaimed as input VAT on the same VAT return.

The supply of international services by a UK VAT registered business will generally be outside the scope of UK VAT as the place of supply will be outside the UK.

The cash accounting, annual accounting and flat rate schemes

The cash accounting, annual accounting and flat rate schemes are all available to small businesses. Be careful that the schemes are not confused, as they are completely different from each other.

The cash accounting scheme enables a business to account for VAT on a cash basis. The scheme will normally be beneficial where a period of credit is given to customers. It also results in automatic relief for impairment losses. The disadvantage is that input VAT will only be recovered when purchases and expenses are paid for.

Example 9

Ming is registered for VAT. She has annual standard rated sales of £800,000. This figure is inclusive of VAT. Ming pays her expenses on a cash basis, but allows customers three months credit when paying for sales. Several of her customers have recently defaulted on the payment of their debts.

- Ming can use the cash accounting scheme if her expected taxable turnover for the next 12 months does not exceed £1,350,000 exclusive of VAT.
- In addition, she must be up to date with her VAT returns and VAT payments.
- Output VAT will be accounted for three months later than at present since the scheme will result in the tax point becoming the date that payment is received from customers.
- The recovery of input VAT on expenses will not be affected as these are paid in cash.
- The scheme will provide automatic relief for an impairment loss should a customer default on the payment of a debt.

In contrast, the advantage of the annual accounting scheme is mainly administrative, since a business only has to submit one VAT return each year.

Example 10

Newt Ltd is registered for VAT. The company has annual standard rated sales of £950,000. This figure is inclusive of VAT. Because of bookkeeping problems Newt Ltd has been late in submitting its recent VAT returns.

- Newt Ltd can apply to use the annual accounting scheme if its expected taxable turnover for the next 12 months does not exceed £1,350,000 exclusive of VAT.
- In addition the company must be up to date with its VAT payments.
- Under the scheme only one VAT return is submitted each year. This is due within two months of the end of the annual VAT period.
- The resulting reduced administration should mean that default surcharges are avoided in respect of the late submission of VAT returns.
- Nine monthly payments are made on account of VAT commencing in month four of the annual VAT return period. Any balancing payment is made with the VAT return.
- Each payment on account will be 10% of the VAT payable for the previous year. This will improve both budgeting and possibly cash flow where a business is expanding.

The flat rate scheme can simplify the way in which small businesses calculate their VAT liability. Under the flat rate scheme, a business calculates its VAT liability by simply applying a flat rate percentage to total income. This removes the need to calculate and record output VAT and input VAT.

The flat rate percentage is applied to the gross total income figure (including exempt supplies) with no input VAT being recovered. The percentage varies according to the type of trade that the business is involved in, and will be given to you in the exam.

Example 11

Omah registered for VAT on 1 January 2013. He has annual standard rated sales of £80,000, and these are all made to the general public. Omah has annual standard rated expenses of £12,000. Both figures are exclusive of VAT. The relevant flat rate scheme percentage for Omah's trade is 13%.

- Omah can use the flat rate scheme if his expected taxable turnover for the next 12 months does not exceed £150,000 exclusive of VAT.
- In addition, the expected total income (including VAT and exempt supplies) for the next 12 months must not exceed £230,000.
- The main advantage of the scheme is the simplified VAT administration. Omah's customers are not VAT registered, so there will be no need to issue VAT invoices.
- Using the normal basis of calculating the VAT liability, Omah will have to pay annual VAT of £13,600 (80,000 – 12,000 = 68,000 x 20%).
- If he uses the flat rate scheme then Omah will pay VAT of £12,480 (80,000 + 16,000 (output VAT of 80,000 x 20%) = 96,000 x 13%), which is an annual saving of £1,120 (13,600 – 12,480)

Conclusion

There is quite a lot to remember when studying VAT, although the subject itself is not particularly complicated. You will normally find that several different topics are covered within each VAT question, and so it is important that you cover the whole subject area.

Written by a member of the Paper F6 examining team