

VAT focus

MTD for VAT: a deep dive

The following is an abridged version of a table produced by the CIOT tax technical team and is reproduced with their kind permission. The full table is available on the CIOT's website (www.tax.org.uk), and it will be updated as MTD for VAT develops.

Current position / approach	Expected position under MTD	Likely problem areas / challenges
Maintaining your business records		
Business can use manual records, spreadsheets, accounting software, or a combination of all three.	Businesses will no longer be able to use manual records, subject to limited exemptions. Businesses must use 'functional compatible software' (digital records) to meet the new requirements. Digital records means a software programme(s) which can connect to HMRC's systems via an API. The software must be able to: <ul style="list-style-type: none"> ● keep the required records in a digital form; ● preserve those records in digital form for up to six years; ● create a VAT return from the digital records; ● provide HMRC with this information digitally; ● provide HMRC with additional data on a voluntary basis; ● receive information from HMRC about the business's compliance record. 	As with the original MTD proposals, transitioning businesses from manual to digital records will be challenging. Business will need advice selecting appropriate software, though HMRC are expected to publish a list of functional compatible software providers (though only the software that has the ability to link to HMRC's systems through APIs). Spreadsheet users will need bridging software or API-enabled spreadsheets to digitally submit the VAT return data to HMRC. Businesses should start planning the move to digital records sooner rather than later, getting advice from their agent where appropriate.
Exemptions from MTD for VAT	The following are exempted: <ol style="list-style-type: none"> The person/business which meets one of HMRC's MTD exemptions: <ul style="list-style-type: none"> ● religious beliefs incompatible with the use of electronic communications; ● not reasonably practical due to age, disability, remoteness of location or other reason; or ● subject to an insolvency procedure. The business is voluntarily registered for VAT and trading under the VAT turnover threshold. 	Exemptions under a. must be applied for, with the application being made to HMRC. The standard of evidence to support the exemption application for 'not reasonably practical' is anticipated to be the same as the current exemption for online filing of VAT returns. It is likely that more businesses will fall within this exemption for MTD for VAT as compared to online filing of returns. A business that is exempt from MTD for VAT under b. may elect not to be exempt and file its returns digitally. It may also withdraw its election at a later time, providing it still fulfils the criteria for exemption. If a VAT registered business's taxable turnover falls below the VAT registration threshold, it must still comply with the requirements of MTD for VAT.
Information / records to be reported / maintained		
VAT-registered businesses must currently keep records of sales and purchases, a separate summary of VAT called a 'VAT account', and issue VAT invoices if necessary.	Regulations SI 2018/261 set out the required content of digital records (and a future VAT Notice, expected by the summer, will provide further explanation). These requirements are more onerous than at present, e.g.: <ul style="list-style-type: none"> ● for supplies made, it appears necessary to record the different rates of VAT applicable, and the amounts chargeable at those rates; ● for supplies received, it is necessary to record the amount of input tax that will be claimed; and ● it is necessary to capture the proportions of the VAT-exclusive values of outputs, split across the various different VAT liabilities. 	Whilst the VAT Notice might provide some relaxations from these requirements, many businesses will not currently capture this level of detail, and so additional work / new processes will be necessary. Indeed, some of the information might not be available at the point of capture, e.g. the amount of input tax to be reclaimed on an expense.
VAT return submission		
Whilst 99% of VAT returns are filed online, only around 13% of VAT returns are currently filed direct from software. For the remaining 87%, the VAT return figures are typically entered manually into the HMRC government gateway page and submitted to HMRC that way, i.e. requiring manual intervention.	VAT returns must be filed directly from the digital records, such as from the record keeping software, an API-enabled spreadsheet, or bridging software. Subject to the soft landing period (below), the transfer of data between digital records (including spreadsheets) must be digital, with no manual transposition of figures. These digital links must be in place where the data that is being transferred represents that which is mandated to be captured in digital records. For example, the transfer of input and output VAT amounts between digital records must be done digitally as those values are required to be captured in the digital records. Information which is not required to be captured digitally, such as adjustments to those figures because of partial exemption or fuel scale charges etc., do not need to be undertaken digitally.	Many businesses use spreadsheets or manual calculations to compile the VAT return figures. This process will need to be reviewed, and digitised where necessary, to comply with the requirements. This might involve creating or purchasing new software or developing functionality to enable this automatic linkage to take place.
Soft landing period	For VAT return periods commencing between 1 April 2019 and 31 March 2020, HMRC will not enforce the requirement to have digital links between software programs (the 'soft landing period'). After this time, all transfers of data between digital records must be transferred digitally.	During the soft landing period, we anticipate that the use of 'cut and paste', or manual transposition, should be acceptable. HMRC will publish further examples and more information on the scope of the soft landing in the VAT Notice.
Adjustments are often required prior to submission of the VAT return, such as for fuel scale charges, partial exemption, and so on. These can currently be done in a variety of ways, prior to submitting the VAT return.	There are two main ways in which VAT adjustments can be made under MTD: <ol style="list-style-type: none"> 1. The business undertakes the calculation outside of software, and journals the effect of the calculation back into the software. The VAT return can then be submitted directly from the software. 2. The business exports data from the software into a spreadsheet (a digital link is needed because the data represents that which must be kept digitally). The adjustments and VAT return calculation are undertaken in the spreadsheet. The business then uses bridging software or an API-enabled spreadsheet (i.e. a digital link) to extract the VAT return figures and submit them to HMRC. 	This is one of the more complex areas of MTD for VAT. Examples will be set out in the VAT Notice to illustrate where a digital link is required, and where an adjustment can be made outside of functional compatible software.
VAT return content		
There are nine boxes on the current VAT return. There is no easy way to provide additional information to HMRC alongside the VAT return.	There is currently no proposal for the nine boxes on the VAT return to change. However, businesses will be able to voluntarily submit a specific data set of supplementary information. Further details of this are to be confirmed in the VAT Notice, but are anticipated to include a split of the outputs value between the various rates of VAT, and any adjustments made to input or output tax figures.	If the business is selected for a compliance check, HMRC will review this information to see whether it provides sufficient assurance that the return is correct. Other than the information to be specified in the VAT Notice, we do not expect it to be possible to provide other information, such as copy invoices or written explanations. Whether provision of this information can be done on an ad hoc basis is something we have asked HMRC to confirm. Also, the legal status of this supplementary information is currently unclear (e.g. for compliance / disclosure purposes etc). Errors in supplementary data must be corrected, but will not be subject to a penalty.
Amendments and error corrections		
Amendments and error corrections below certain thresholds can be amended on the next VAT return. Otherwise, a disclosure must be made on a form VAT 652.	These rules will continue as now, although HMRC is considering options for non-mandatory electronic channels for submission of a form VAT 652. Errors in voluntary updates or supplementary VAT information can simply be corrected through the digital records (irrespective of the value) as these are not VAT adjustments under the regulations.	Businesses will need to ensure that any adjustments which must be separately disclosed are excluded from the VAT return prepared by the digital records.

Current position / approach	Expected position under MTD	Likely problem areas / challenges
VAT groups / organisations with multiple accounting systems		
Individual entities/divisions etc. can maintain their own records in whatever form they choose, and those figures are consolidated each period for the preparation and submission of the VAT return by the representative member.	As outlined above, there needs to be a digital link from the various digital records held by VAT group members / divisions etc., through to the submission of the VAT return to HMRC.	VAT groups/complex organisations will need to create or purchase new software or functionality to enable this digital linkage to take place in order to enable the VAT return to be submitted from the digital records.
Overseas businesses trading in the UK		
As with UK businesses, overseas businesses have flexibility in how they maintain their records, and can submit returns through the HMRC portal.	Overseas businesses that have UK taxable turnover in excess of the UK VAT registration threshold will be subject to the requirements of MTD for VAT. Overseas businesses registered for UK VAT but whose UK taxable turnover is below the UK VAT registration threshold are not mandated, but can opt in to MTD for VAT if they so wish.	It may be more difficult for overseas businesses to comply with MTD for VAT as their UK activities are likely to be just a part of a larger whole. Further, the record keeping may be undertaken in the business's 'home' country and the submission undertaken from there. However, we understand that overseas agents will be able to access MTD for VAT.
Annual accounting		
Under the annual accounting scheme businesses submit just one VAT return a year, and make advance VAT payments based on the last return submitted.	Annual accounting will be retained with the current conditions. However, the MTD requirements will otherwise apply, i.e. digital records must be maintained, and the annual VAT return must be filed through API-enabled software.	See comments elsewhere.
Retail schemes		
Retail schemes have their own special rules, both around record keeping requirements and calculations of VAT due.	Retail schemes users will be permitted to electronically record sales transaction data based on daily gross takings, rather than recording details of each sale. However, the MTD requirements will otherwise apply. More information is set out in the draft income tax notice and will be clarified in the VAT Notice.	See comments elsewhere.
Flat rate scheme (FRS)		
Businesses eligible to use the FRS account for output tax as a specified percentage of turnover and don't claim input tax on most purchases.	Digital record keeping requirements will mirror current record keeping requirements, i.e. FRS users must keep digital records of sales, but only need to record purchases of capital goods costing £2,000 or more including VAT. 'Relevant goods' used to determine if the limited cost business rate applies do not need to be kept digitally. However, the MTD requirements will otherwise apply.	See comments elsewhere.
Other special schemes		
There are a number of other special schemes within VAT, such as margin schemes etc., each of which have their own record-keeping nuances.	We expect MTD the requirements of MTD to apply to business who use these special schemes, but the requirements adapted to facilitate the particular nuances of those schemes. For example, the stock book will not need to be a digital record for businesses using the second hand margin scheme.	See comments elsewhere.
Businesses that are voluntarily registered for VAT because their turnover is below the VAT threshold		
They have the same record keeping and reporting obligations as businesses that are compulsorily registered for VAT.	These businesses will not be required to comply with the MTD record keeping and reporting obligations. The existing method of online filing of VAT returns will be retained for these businesses for as long as necessary. However, they can choose to enter MTD for VAT on a voluntary basis. If they do elect to use MTD, they have the option to withdraw at a later time (unless the position changes as MTD is rolled out to other taxes).	We do not know when (or if) these businesses will have to comply with MTD for VAT, although if businesses are mandated into income tax in April 2020 (or later), it is possible that the VAT requirement will be extended to voluntary VAT registrations at that stage. In the meantime, HMRC will have to run two systems, and at some point they will wish to 'turn off' the VAT portal.
Brexit		
Sales/purchases from the EU are fairly straightforward and understood. Whilst there are some administrative obligations, the VAT and customs position is greatly simplified.	The position is currently unclear. Sales and purchases of goods to and from the EU could become exports and imports and subject to VAT and duty if there is a 'hard' Brexit. The VAT liability of some transactions might change (eg financial services). Reporting obligations will change.	Again there are many, including making sure businesses understand the tax-technical and administrative changes caused by leaving the EU. Software will need to be developed and implemented to deal with the changes, which could be challenging because it might not be until much nearer March 2019 or into the proposed transitional period ending on 31 December 2020, when it is known what the actual requirements are.
Agents		
At present, agents can maintain the accounting records, submit the VAT return data to HMRC etc.	An agent's abilities should be mirrored with their clients under MTD. MTD for VAT functionality will be part of the new agent services account. For existing agents, client authorisations are expected to be mapped over to the agent's ASA where an existing online filing authorisation is in place.	Agent functionality will be offered to volunteers in the MTD for VAT pilot later this year. At the moment, information around agent functionality is relatively sparse.
Non-VAT / other reporting		
Only VAT is within the scope at present. Other indirect taxes seem to be able to continue as at present, as does the current method of reporting statistical VAT information (Intrastat, EC sales lists etc).	No change, although it may be that some elements become increasingly digitised (e.g. Intrastat).	Businesses may have to cope with two types of accounting records/reporting, if VAT becomes digital, but other taxes/aspects are not.
Pilots / software testing		
The pilot of MTD for VAT started in April 2018. The pilot builds on the small-scale technical testing HMRC started at the end of 2017, and HMRC has started to invite a small number of businesses with the simplest VAT affairs first. The pilot is expected to be opened up more widely in the summer, and HMRC will publish a list of MTD-compatible software products on GOV.UK. However, we understand that more complex businesses are unlikely to be able to join the pilot until around October 2018, and public bodies until November or December 2018. Businesses should ask their software provider when their product will be updated for MTD.		
Costs		
Businesses that don't currently use software will need to buy software (and possibly hardware) to be MTD compatible. Other businesses will need to upgrade or develop bespoke systems. Businesses may also require further help from their agent, or additional internal resource, at least initially to transition to digital records, and create the digital flow of data to HMRC. In a technical note published on 1 December 2017, HMRC estimated the average transitional cost for businesses to become MTD compliant was just £109. They also estimated (net) additional ongoing additional costs on average of just £31p.a. These estimates seem surprisingly low as compared with the requirements outlined above.		