



BUDGET 2010

VAT MEMO 2010-2011

Newsletter Issue 1

June 2010

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The VAT standard rate increase to 20% on 4 January 2011 is the obvious **headline** of this Budget. But having dealt with rate changes in December 2008 and January 2010, taxpayers will not be shocked or surprised by this one. The VAT fraction will become 1/6 when the new rate takes over.

► **Output tax**

One proposed change that will have a real effect is the **replacement of default surcharge** with separate penalties for late filing and late payment; this is to happen from a date yet to be announced and because of the systems changes it will necessitate for HMRC it is unlikely to impinge without significant warning.

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OUTPUT TAX

Time of supply

See VM ¶750

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The standard rate of VAT will increase to 20% from 17.5% with effect from 4 January 2011. **Special measures** will be introduced to **prevent** the 17.5% rate applying to supplies made on or after 4 January 2011.

The special rules will apply to standard-rated goods and services only. They will provide for a supplementary charge of 2.5%, due on 4 January 2011, where the customer **cannot recover all the VAT on the supply** and at least one of the following applies:

- » the supplier and customer are connected;
- » the value of the supply (and any related supplies) exceeds £100,000, although this is not a relevant criterion where prepayments or issuing advance VAT invoices is normal commercial practice;
- » the supplier (or someone connected to the supplier) funds a prepayment for the goods or services; or
- » an advance VAT invoice is issued where payment is not due in full within six months (this does not apply to hire purchase invoices issued in accordance with normal commercial practice).

Similar rules will seek to prevent the use of **rights or options** to avoid the supplementary charge. They will cover cases where, before 4 January 2011, the customer is granted the right to receive goods and services after 3 January 2011, either free or at a discount, the customer cannot recover all the VAT on the right or option, and at least one of the following applies:

- » the grantor and the customer are connected;
- » the consideration for the right or option (and any related supplies) exceeds £100,000, although this is not a relevant criterion where the right or option is normal commercial practice; or
- » the supplier (or someone connected to the supplier) funds the payment for the right or option.

The charge becomes due on the date that the option is first exercised on or after 4 January 2011.

The supplementary charge does not apply to prepaid or invoiced rentals of land, buildings or other assets, if the period concerned is a year or less and the prepayment or the issuing of an advance invoice is **normal commercial practice**.

Whether suppliers are able to **adjust the amount payable** under their contracts with customers to take account of any supplementary charges will depend on the contracts themselves.

Rate of VAT

See VM ¶1090

The **standard rate** of VAT will **increase** to 20% from 17.5% with effect from 4 January 2011. No change will be made to the list of zero-rated items and the reduced rate will remain at 5%.

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ENFORCEMENT

Late filing and payment

See VM ¶4047

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From a date **to be announced**, it is proposed that the following regimes be introduced to **discourage** late filing of VAT returns and late payment of VAT due.

Late filing

Where returns are supposed to be submitted quarterly:

- » a £100 penalty as soon as a return is late (whether or not the tax has been paid) — this starts a one-year penalty period, extended for each subsequent late submission;
- » for each further failure within the penalty period the fixed penalty increases by £100, to a maximum of £400;
- » an additional 5% of the tax on the relevant return if it has not been filed after 6 and 12 months; and
- » if, by failing to make the return, the taxpayer is deliberately withholding information to prevent HMRC from correctly assessing the VAT liability, a penalty of up to 100% of the tax.

Where returns are supposed to be submitted monthly:

- » as above, except that the fixed penalties are £100 for the first six failures in any penalty period, then £200 for any subsequent failures.

Late payment

Where payment is supposed to be made quarterly:

- » no penalty for the first late payment, although a one-year penalty period starts;
- » the second failure within the year will lead to a 2% penalty and extend the penalty period to the first anniversary of the second failure;
- » the third failure within the extended penalty period will lead to a 3% penalty and a further penalty period extension; and
- » further failures will attract a maximum penalty of 4%, although additional penalties of 5% of the unpaid tax will be charged at 6 and 12 months from the date of the failure.

Where payment is supposed to be made monthly:

- » as above, except that, after the first failure, the penalties are 1% for the next three failures in the penalty period, 2% for the next three failures, 3% for the next three failures and 4% thereafter.

Change of return period

Special rules will deal with any **change from monthly to quarterly returns**, or vice versa, and with any exceptional payment obligations which may arise.

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SIMPLIFIED ACCOUNTING SCHEMES

Flat rate scheme percentages

See VM ¶4666, ¶9979

When the standard rate of VAT goes up to 20% on 4 January 2011 the following percentages will apply under the flat rate scheme:

Category of business	Appropriate percentage
Accountancy or book-keeping	14.5
Advertising	11
Agricultural services	11
Any other activity not listed elsewhere	12
Architect, civil and structural engineer or surveyor	14.5
Boarding or care of animals	12
Business services that are not listed elsewhere	12
Catering services including restaurants and takeaways	12.5
Computer and IT consultancy or data processing	14.5
Computer repair services	10.5
Dealing in waste or scrap	10.5
Entertainment or journalism	12.5
Estate agency or property management services	12
Farming or agriculture that is not listed elsewhere	6.5
Film, radio, television or video production	13
Financial services	13.5
Forestry or fishing	10.5
General building or construction services*	9.5
Hairdressing or other beauty treatment services	13
Hiring or renting goods	9.5
Hotel or accommodation	10.5
Investigation or security	12
Labour-only building or construction services*	14.5
Laundry or dry-cleaning services	12
Lawyer or legal services	14.5
Library, archive, museum or other cultural activity	9.5
Management consultancy	14
Manufacturing fabricated metal products	10.5
Manufacturing food	9
Manufacturing that is not listed elsewhere	9.5
Manufacturing yarn, textiles or clothing	9
Membership organisation	8

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Category of business	Appropriate percentage
Mining or quarrying	10
Packaging	9
Photography	11
Post offices	5
Printing	8.5
Publishing	11
Pubs	6.5
Real estate activity not listed elsewhere	14
Repairing personal or household goods	10
Repairing vehicles	8.5
Retailing food, confectionary, tobacco, newspapers or children's clothing	4
Retailing pharmaceuticals, medical goods, cosmetics or toiletries	8
Retailing that is not listed elsewhere	7.5
Retailing vehicles or fuel	6.5
Secretarial services	13
Social work	11
Sport or recreation	8.5
Transport or storage, including couriers, freight, removals and taxis	10
Travel agency	10.5
Veterinary medicine	11
Wholesaling agricultural products	8
Wholesaling food	7.5
Wholesaling that is not listed elsewhere	8.5

* "Labour-only building or construction services" means building or construction services where the value of materials supplied is less than 10% of relevant turnover from such services; any other building or construction services are "General building or construction services".

Flat rate scheme thresholds

See VM ¶4714

The increase in the standard rate of VAT to 20% on 4 January 2011 will affect the flat rate scheme thresholds. Businesses with a total taxable annual turnover of up to £150,000 will be eligible to join the scheme as now. However, the threshold beyond which businesses will have to **leave the scheme** is a VAT-inclusive figure and so will go up, from £225,000 to £230,000. If a business exceeds that threshold as a result of a one-off transaction, it will be allowed to **remain in the scheme** if its tax-inclusive turnover in the following year is not expected to exceed £191,500 (£187,500 until 4 January 2011).

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AS PREVIOUSLY ANNOUNCED

Postal services exemption

See VM ¶474

From 31 January 2011 the exemption for postal services will be restricted to supplies of public postal services (and incidental goods) by the universal service provider (currently Royal Mail). Postal services supplied on terms which are **individually negotiated**, and services not made under a licence duty, will become standard-rated from that date.

Zero-rating of aircraft

See VM ¶1298

For zero-rating purposes, a qualifying aircraft will no longer be determined by its weight or commercial design. From 1 January 2011 zero-rating will depend on the recipient of the supply being an airline **operating for reward chiefly on international routes**. When previously announced the implementation date was 1 September 2010.

Lennartz mechanism

See VM ¶1525, ¶1841

The Lennartz mechanism is to be made unavailable in respect of purchases of **land, property, boats and aircraft**. The Lennartz mechanism applies where an asset is purchased for both business and private purposes. Under this mechanism full input tax recovery is permitted on purchase and output tax is accounted for in respect of private use over the asset's economic life. From 1 January 2011 full input tax recovery will not be available on purchase; instead input tax will be restricted to the business use proportion. The Capital Goods Scheme will be amended to take account of this change.

HMRC has also recently announced an **amended policy** under which Lennartz is not available unless non-business use is private use (as opposed to, for example, use by a charity for non-commercial purposes). Legislation will be introduced to ensure that those affected by this change of policy do not gain an advantage by, for example, ceasing to account for output tax on non-business use.

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