

VALUE ADDED TAX (VAT)

WHAT IS VAT?

VAT is a tax charged on most goods and services provided in the UK. It is only charged by those companies that are registered for VAT and is calculated at 20%.

HOW DOES VAT REGISTRATION WORK?

An application to register for VAT should be submitted online to HMRC. Within 2 to 3 days, your company will be issued with a VAT number and can begin to charge VAT from the effective date.

WHEN SHOULD YOU REGISTER FOR VAT?

COMPULSORY REGISTRATION

Were your company turnover to exceed £85,000 in a 12 month period then you must register for VAT with HMRC. You must do this within 30 days of breaching the threshold to avoid penalties.

VOLUNTARY REGISTRATION

If your turnover is below the compulsory threshold you can register for VAT on a voluntary basis and take advantages of the benefits of registration.

WHAT ARE THE BENEFITS OF BEING REGISTERED FOR VAT?

- Being registered for VAT can make your company appear larger than it really is and can add more credibility to your business.
- Some customers or suppliers may only deal with VAT registered companies. So this may increase your ability to attract clients or a better supply chain.
- If registered on the standard scheme, you can recover the VAT you have been charged on business purchases.
- If registered on the flat rate scheme, the saving will increase your company profits.

VAT SCHEMES

Every quarter a VAT return must be submitted electronically to HMRC. The return confirms the VAT for the period and the amount due to be paid or refunded.

STANDARD SCHEME

Under the standard scheme, the amount of VAT due is calculated as the VAT you have charged on your sales invoices less any VAT you have suffered on business purchases.

Example:

You raise sales invoices in the quarter for £10,000. The invoices would show £10,000 sales + VAT (20%) £2,000 = total £12,000. The client would then pay you the full amount, £12,000

You incur "VATable" expenses in the quarter of £1,000 (net). The total amount paid would be £1,000 expenses + VAT (20%) £200 = total £1,200

Therefore at the end of the quarter you would owe the following amount to HMRC.

VAT on sales	£2,000
Less VAT on purchases	(£200)
Amount due to HMRC	£1,800

It is important to note that not all expenses are subject to VAT and therefore not all inputs are recoverable, for example trains, flights, entertainment, expenses incurred abroad.

FLAT RATE SCHEME

Under the flat rate scheme, the amount of VAT due is calculated on a flat percentage of your gross sales invoices (including VAT). This percentage is less than the 20% VAT charged and therefore can result in savings for your company. When compared to the standard scheme, this scheme can also offers reduced administration as it is simpler to calculate and requires less detailed bookkeeping.

In the first year of registration, it is possible to obtain a 1% reduction on the flat rate percentage that applies to your business.

HMRC introduced a new flat rate of 16.5% for "limited costs traders" from 1st April 2017. This rate will apply to businesses in any sector. In effect, this change will result in 19.8% of the 20.0% VAT charged, being payable to HMRC.

A limited cost trader will be defined as one whose VAT inclusive expenditure on goods is either:

- less than 2% of their VAT inclusive turnover in a prescribed accounting period
- greater than 2% of their VAT inclusive turnover but less than £1000 per annum if the prescribed accounting period is one year (if it is not one year, the figure is the relevant proportion of £1000)

Goods, for the purposes of this measure, must be used exclusively for the purpose of the business but exclude the following items:

- capital expenditure
- food or drink for consumption by the flat rate business or its employees
- vehicles, vehicle parts and fuel (except where the business is one that carries out transport services - for example a taxi business - and uses its own or a leased vehicle to carry out those services)

These exclusions are part of the test to prevent traders buying either low value everyday items or one off purchases in order to inflate their costs beyond 2%.

To give you a quick example, let's say you raised an invoice for £2,000 + VAT (20%) £400

(Gross sales = £2,400)

Under the new rules, with your Flat Rate Percentage fixed at 16.5% on Gross Sales, you would pay VAT of £396 to HMRC. You have charged £400 to your Customer. This means an overall saving of just £4 (£396 - £400).

You can find out further information on the changes [here](#).