

## Changes to the standard rate of VAT – December 2008

**In his Pre-Budget Report on 24 November 2008, Chancellor Alistair Darling announced a temporary reduction in the standard rate of Value Added Tax (VAT) from 17.5% to 15%.**

The lower rate came into effect on 1 December 2008 and will remain in place until 31 December 2009. The move – intended to boost consumer spending – will inevitably have implications for businesses and individuals as consumers.

Zero-rated supplies, such as basic foodstuffs, children's clothing and books; exempt supplies, such as education and health; and supplies subject to VAT at 5%, such as domestic fuel and power, are not affected by the change.

This guide provides a general overview of the effects of the change for most usual situations, but do contact us if you would like particular help and advice.

### Implications for sales to VAT-registered business

#### ***When 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 1 December 2008 businesses should charge VAT at the new rate of 15%. This means that businesses currently calculating their VAT using the VAT inclusive fraction of 7/47 should use the new fraction of 3/23 from 1 December.

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 (eg. a business which issues a VAT invoice on 1 December 2008 for goods or services provided before 18 November 2008); or
- received payment before 1 December 2008.



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### ***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 1 December 2008, but the goods will be provided (or services delivered) after 1 December 2008 then 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 15% rate and issue a VAT credit note to the customer for the reduction in VAT and, if appropriate, make them a refund.

If the customer has paid, but the business hasn't yet issued a VAT invoice, the business may account to HMRC for VAT at 15% and would normally be expected to refund the difference to the customer.

### ***What about single supply services 'spanning' the rate change?***

Where a business issues an invoice after 1 December 2008 for a **single supply service** which is carried out over a period of time spanning 1 December (eg. a solicitor preparing a Will) the whole supply can be charged to VAT at 15%. If any VAT has already been accounted for at 17.5% because a customer has made a payment on account, the business can still apply the 15% rate and issue a refund/credit note as required.

Where a business makes **continuous supplies of services**, such as leasing of equipment (eg 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 1 December 2008 should be subject to 15% VAT. This means that the annual invoice must be replaced by a new invoice, detailing the revised payments due after 1 December 2008 at the new 15% 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 1 December 2008, they must be issued within 45 days after 1 December 2008.



## **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 1 December 2008.

The main exception to this rule will be where a customer pays for something they have taken away (or the supplier has delivered) before 1 December 2008. In this case, the sale took place before 1 December 2008 and VAT must be accounted for at the rate of 17.5%.

If a retailer has taken a deposit before 1 December 2008 for goods which will be delivered after the 1 December 2008 (e.g. as Christmas presents), the business may choose to account for VAT at either the old or the new rate, but must remember to issue a credit note to the customer where an invoice at the old rate is already in existence.

**Electronic tills**, especially those set up to provide VAT information, will need to be adjusted.

## **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 1 December 2008 most input tax claims will be for the amount shown on the invoice. However, if a supply is made on or after 1 December 2008 and the supplier has incorrectly charged VAT at 17.5%, businesses are only entitled to claim 15% from HMRC and the remaining 2.5% is due from the supplier.

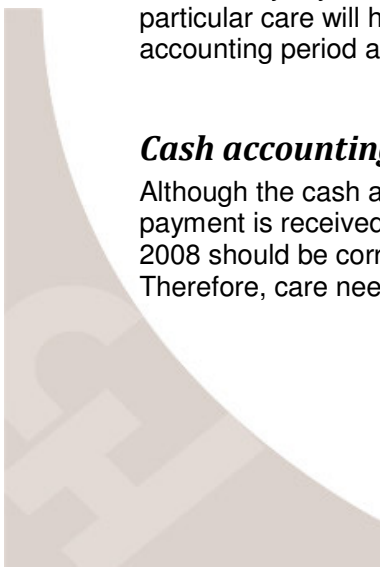
Less detailed VAT invoices will not have a separate amount of VAT identified but since the rate used should be specified a similar procedure should be followed.

### ***VAT returns***

For the majority of businesses the period of their VAT return will span 1 December 2008 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 1 December 2008 should be correctly identified as supplies made at either the 17.5% or 15% rate. Therefore, care needs to be taken.



## ***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 reduced by 2.5%! The revised table of percentages which are to apply to supplies made from 1 December 2008 can be found in Annex E of HMRC's guide VAT – *Change in the Standard Rate*. You can view this here: [www.hmrc.gov.uk/pbr2008/vat-guide-det.pdf](http://www.hmrc.gov.uk/pbr2008/vat-guide-det.pdf).

## ***Fuel scale charges***

There is no change to the fuel scale charges which have applied since 1 May 2008 but the VAT element has been recalculated. The new amounts applicable from 1 December 2008 can be found in Annex D of HMRC's guide VAT – *Change in the Standard Rate*. You can view this here: [www.hmrc.gov.uk/pbr2008/vat-guide-det.pdf](http://www.hmrc.gov.uk/pbr2008/vat-guide-det.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.

## **Further help and advice**

The good news is that HMRC have stated that they will adopt a 'light touch' in relation to errors or mistakes in the first VAT return after the change, which arise as a result of the change. 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 reduction or would like any further information on any of the matters raised here, please contact us.**

