What SMEs Trading With EU Need to Know About

VAT AFTER BREXIT

VAT contributed an estimated £133.8 billion to the UK economy in 2019-20

Most consumers don't give it a second thought. Businesses, however, need to get to grips with their VAT requirements or risk incurring the wrath of HMRC.

This bite-sized guide will give you everything you need to know to get started.

What is VAT?

VAT stands for 'value-added tax'. This tax is added to most goods and services, though you may not even realise it as it's automatically included in the price.

Whether you're buying a t-shirt, creating a Netflix account, or ordering a coffee, you'll have to pay VAT (subject to the supplier being a VAT-registered business, of course). It's an indirect tax that's paid by consumers, collected by businesses, and then reported to HMRC.

And if you're a vendor, you'll have to charge VAT on everything you sell once you meet the £85,000 annual turnover threshold or new rules—as well as keeping detailed records that you regularly send to HMRC. These records will clearly show how much VAT you received from customers and, therefore, how much you owe HMRC.

What is the VAT rate in the UK?

Standard Rate:
20%

The majority of the products sold in the UK have a 20% VAT rate. If your product is worth £5, you must therefore charge £6. The £1 on top is the VAT that you collect on behalf of HMRC before then paying them back later on.

Reduced Rate:
5%

Certain goods and services (generally those considered to have a positive societal impact) qualify for the reduced rate. Check out this link to learn more about when this rate applies.

Zero Rate:
0%

Zero-rated items are goods on which the Government charges VAT but the rate is currently set to zero. The goods covered by this classification include items such as children's clothes and footwear, water, basic foods, books, and newspapers.

Which businesses need to charge VAT?

The VAT rules here in the UK are simple:

Businesses with a turnover **under £85,000 per year**: If you trade in the UK and your suppliers are in the UK then you **do not need to register** for/charge VAT on their products/services.

Businesses with a turnover **over £85,000 per year: Must register** for, and charge, VAT on their products/services.

Note: These rules apply to both registered companies and sole traders alike.

How can I register my business?

Head to the dedicated HMRC link to apply for VAT online.

Note: You will need to have some crucial information to hand, including:

Your Government Gateway and password

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Your Unique Tax Reference (UTR), a 10-digit number that you received when registering for Corporation Tax

Your company's bank account details, company number, and registered address

Upon registration, you will receive a VAT certificate that will contain the following:

A unique VAT registration number

Information regarding when you need to file your first VAT return and submit your first VAT payment

Your VAT date of registration

By the way, we can help you with company registration. Talk to us to get the job done while you focus on growing your business.

Are any industries/goods/ services VAT exempt?

Crucially, you'll have to get your head around the difference between **zero-rated items** and **exempt items.** Understanding this distinction could save you money.

It works like this: zero-rated items are items that are usually subject to VAT, but where the rate is currently set at zero. Businesses that only make zero-rated supplies can register for VAT to recover overheads and costs.

Whereas, exempt items are those where no VAT is paid or charged. The sale of those goods still have to be recorded on a VAT tax return—however, this means that businesses who produce exempt items cannot recover any VAT as none was paid in the first place.

There are also 'out-of-scope items that exist outside of the scope of VAT, such as voluntary donations to charity or items bought and sold outside of the UK.

Zero-rated items include
(but aren't limited to)

- Printing (books, brochures, newspapers, maps, etc)
- Children's/baby clothing and footwear
- Utilities
- Maternity pads
- Equipment for disabled people
- Civil aeroplanes
- Protective equipment (bicycle helmets, protective boots and helmets for industrial use)

Exempt items, on the other hand, include *(but aren't limited to)*

- Education and training
- Insurance, finance and credit
- Burial or cremation of the dead
- Fundraising events by charities
- Sport and leisure
- Health services by registered medical professionals
- Antiques
- Building and construction

For more information, head to GOV.UK's full list.

Which VAT scheme should I use?

There are a few different methods by which you can pay VAT to HMRC.

Let's dive into a brief overview of each scheme.

Standard Accounting Scheme

What it is:
You're required to submit a quarterly VAT return and pay HMRC any VAT that you owe.

What you need to do:
Keep a detailed record of all VAT that you charge on each sale—and that you pay with each purchase. Refunds are also paid quarterly. This scheme is most commonly used.

Flat Rate Scheme

Summary:
This only applies to businesses with an annual turnover of less than £150,000. It is most commonly used by small businesses and sole traders as it is incredibly simple to understand.

You pay a fixed percentage of your turnover to HMRC each quarter. You don't have to record VAT that you charge customers or pay yourself. Note: with the Flat Rate Scheme, VAT can only be reclaimed on purchases that cost over £2,000.

Annual Accounting Scheme

Summary:
The scheme is only suitable for businesses whose turnover is below £1.35 million per year. You only have to submit one VAT return each year, though you still pay VAT on a quarterly basis based on best estimates.

It works like this: You pay 9 monthly payments amounting to 10% of the previous year's VAT payments, or if you've only been registered for less than 1 year, 10% of the previous year's estimated VAT payments. You can also apply to pay 3 quarterly payments amounting to 25% of the previous year's VAT payments.

However, the scheme isn't for everyone—short term losses should be considered. While submitting a VAT return only once a year saves time and admin, it also means that you can only reclaim VAT once a year. Therefore, the scheme doesn't help businesses who have to regularly claim back VAT.

Cash Accounting Scheme

Summary:
Suitable for businesses with a turnover under £1.35 million per year, this scheme means that you pay VAT on all sales (provided the customer has paid you) as well as reclaiming VAT on any purchases (provided you've paid the supplier).

The Cash Accounting Scheme requires businesses to record income when it's received, and record expenses when they are paid. This is different to the Standard VAT Accounting Scheme, where VAT is recorded on the date of issuing or receiving a VAT invoice.

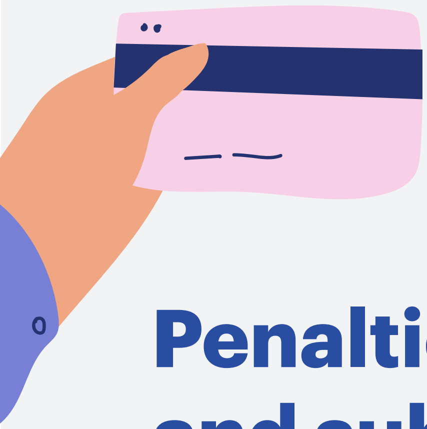
This is beneficial if you have customers who regularly pay late. On the flip side, startups making initial investments in new equipment (and purchasing the aforementioned stock on credit) should avoid using this scheme—you cannot reclaim VAT until you have paid the supplier.

How to pay VAT?

There are a variety of payment methods that you can use. However, remember that not all payments are processed equally as quickly. If you're fast approaching your deadline then make sure to choose one of the same or next day methods.

Same/next day

- **Online banking**
- **Telephone banking**
- **CHAPS**



3 working days

- **Direct debit (this is probably the best option—not only is the money in your account for three more working days, but you'll also never miss a payment)**
- **Bacs**
- **Standing Order (though this only applies to businesses using the Annual Accounting Scheme or Payments on Account)**
- **I-person payment at your bank or building society**

Penalties for late payments and submissions

HMRC is not a massive fan of late payments and submission. As a result, they use a range of methods to incentivise businesses to pay up on time, every time.

Default surcharge

Essentially, if you don't pay on time then you'll have to pay an additional surcharge. Each time that you default, you'll be sent a Surcharge Liability Notice and a Surcharge Liability Notice Extension. These will arrive at the end of the quarterly accounting period.

That said, you are afforded a certain leniency if it's your first default in the past 12 months. Defaulting for a second time, however, incurs a far more expensive penalty. This means that while we never recommend defaulting on your VAT payments, you shouldn't worry too much if you've made a one-off, accidental mistake. Just learn your lesson and don't do it again!

How has Brexit impacted VAT?

Unfortunately, Brexit has profoundly impacted how British companies that deal with EU customers/companies handle their VAT requirements. This mainly affects importers.

If you're exporting goods from the UK to the EU then you don't charge UK VAT now as these are 'zero-rated'. However, you might have to register for VAT in each of the European countries in which you sell goods—for more details, check out our guide, 'How British SMBs Can Navigate Brexit'.

Importing goods under the value of £135 into the UK

UK-based sellers must now charge sales VAT at the point of checkout on their website. Clearly state that VAT was paid at the point of sale—otherwise you'll be forced to pay additional VAT at customs. Your sales invoice is then used by customs to determine the value of your shipment, so it's important that it's 100% correct.

If the customer is a VAT-registered business here in the UK, they should provide the seller/OMP with their VAT number. This means that the UK customer can use the reverse charge mechanism, reporting the VAT themselves, and therefore qualifying for zero-rating.

Importing goods valued at over £135 into the UK

The old rules still apply. In other words, the seller is in charge of paying the import VAT and duties, which they can then reclaim if they have a UK VAT number.

How to prepare for visits by VAT officers?

Whilst it's a very rare occurrence, VAT officers could theoretically pop by to your place of business. They may on occasion even turn up unannounced. These visits can range in duration according to the size and complexity of your business. If you're a small firm then it may only last a couple of hours, while for bigger organisations, this might stretch to a few days.

What's the purpose of their visit?

HMRC essentially wants to confirm that your VAT returns are accurate and trustworthy. This means they'll do a little digging into various sides of your business, determine if you're over/underpaying VAT currently, and advise you on how best to proceed going forward.

How can I avoid VAT visitor-related anxiety?

In a nutshell, by sticking to the rules at all times.

Report everything you owe and pay in full, on time. That's the best approach.

However, having your paperwork in order will also be incredibly useful for visiting VAT officers. Use this as an opportunity to ask the VAT officers questions. Not only will this ensure that you're paying the right amount of VAT, but it will also demonstrate your ongoing willingness to comply with the VAT law.

Where can I find more information?

If you need help with your VAT requirements then don't worry—we've got you sorted. Osome's accounting experts are on hand 24/7. They'll be happy to guide you through any and all VAT issues that you encounter, meaning you can focus on what you love: growing your business.

Get in touch today.

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Osome facilitates business management for small and medium businesses. Its suite of services includes accounting, tax, business registration, corporate secretary services and payroll management. Osome's automations handle the routine, giving human experts have more time to focus on complex advisory. It services over 5000 SMEs in the UK, Singapore and Hong Kong.

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