Office of Tax Simplification: VAT review

Indirect Tax

01 January 2018

The CIOT welcomes the Office of Tax Simplification's (OTS) first report on how the VAT system can be simplified, published on 7 November.

Eagerly awaited, this report follows a call for evidence, to which the CIOT submitted a variety of information and engaged regularly with the OTS team on its key areas of complexity. You can find the report on GOV.UK.

What are the key recommendations?

The report makes 23 recommendations in total, with 8 core areas for the government to focus on as a priority. These are:

- The government should examine the current approach to the level and design of the **VAT registration threshold**, with a view to setting out a future direction of travel for the threshold, including consideration of the potential benefits of a smoothing mechanism.
- HMRC should maintain a programme for further improving the **clarity of its guidance** and its responsiveness to requests for rulings in areas of uncertainty.
- HMRC should consider ways of **reducing the uncertainty and administrative costs** for business relating to **potential penalties** when inaccuracies are voluntarily disclosed.
- HM Treasury and HMRC should undertake a **comprehensive review of the reduced rate, zero-rate and exemption schedules**, working with the support of the OTS.
- The government should consider **increasing the partial exemption de minimis limits** in line with inflation, and explore alternative ways of removing the need for businesses incurring insignificant amounts of input tax to carry out

partial exemption calculations.

- HMRC should consider further ways to **simplify partial exemption calculations** and to improve the process of making and agreeing **special method applications**.
- The government should consider whether **capital goods scheme categories** other than for land and property are needed, and review the land and property threshold.
- HMRC should review the current requirements for **record keeping and the audit trail for options to tax**, and the extent to which this might be handled on-line.

What is the CIOT's response?

We strongly support making VAT rules less complex and easier to apply; in the expectation that it should lead to less uncertainty among business and fewer disputes with HMRC. Simplifying partial exemption and capital goods scheme rules could positively impact on many small and large businesses as well as charities and public bodies.

In the Autumn Budget 2017, the Chancellor responded to the OTS report by stating an intention to consult on the design and level of the VAT registration threshold. In the meantime, the current threshold of £85,000 will remain unchanged until 31 March 2020.

Future examinations of the VAT threshold will have to balance the issues of barriers to growth with administrative simplification and cost for both business and HMRC. Many small businesses have spent their lifetimes not dealing with VAT and having correspondingly less regular contact with HMRC. Much will depend on how any change to the threshold is implemented, and whether and how Making Tax Digital is rolled out in relation to income tax and corporation tax. This may present an opportunity to refresh or extend the VAT Flat Rate Scheme, or consider a smoothing mechanism to mitigate the impact of exceeding the threshold.

We especially agree with the OTS that the government should further improve its guidance as many areas are lacking in detail and are updated too slowly. This is something our members contact us regularly about and on which we continue to liaise with HMRC. We will support work in this area.

Challenging the government to improve its responsiveness to requests for rulings in areas of uncertainty is something we also endorse. HMRC often decline to give rulings on the basis that the issue is adequately covered in guidance, but if the business or its adviser does not believe the matter is clear this leads to an unwelcome impasse.

The OTS has said it is keen to work with the Treasury and HMRC to undertake a comprehensive review of the reduced rate, zero-rate and exemption schedules. We welcome attempts to deal with anomalies that complicate the VAT system but any approach must also assess the impact on those with the lowest incomes in the UK, who may be disproportionately impacted by any price rises caused by the withdrawal of zero rating in food, travel or children’s clothing.

We will review this report in further detail and welcome any comments.