ATT welcome, September 2019

Welcomes

01 September 2019

Sandy feet a distant memory

We can look ahead to a busy autumn now that the sun has set on the summer, and the holidays, be they cultural or sandy, are a distant memory to us.

On my mind this month is the sticky topic of the domestic reverse charge VAT for construction services, which comes into force on 1 October 2019. HMRC have just finalised the legislation and published their further guidance on this new regime, which will require the recipient rather than the supplier to account for the VAT due on certain construction services.

I am concerned that the charge is being introduced without a transitional period and how it will impact significantly on the accounting practices and cash flow of businesses in the construction sector. While it may seem a small matter for a tax adviser, HMRC estimate that it will place an additional burden on 100,000 to 150,000 businesses. It will require changes to trader's sales administration and accounting systems, and staff will need to be trained accordingly.

The aim of the domestic reverse charge is to combat missing trader fraud in the construction sector. Under the new regime, a VAT registered business, which supplies certain construction services to another VAT registered business for onward sale, will be required to issue a VAT invoice stating that the service is subject to the domestic reverse charge. However, it is the recipient of the supply that must account for the VAT due on the supply through its VAT return, instead of paying the VAT amount to the supplier. The recipient may recover that VAT amount as input tax, subject to the normal rules for claiming credit.

Unlike other types of reverse charge, the value of such reverse charge services will not count towards the VAT registration threshold, which is good news for smaller businesses. Construction businesses must ensure their accounting systems are

capable of processing reverse charge supplies and make ongoing checks to ensure that supplies and purchases are correctly treated. As the VAT amount must still be shown on invoices subject to the domestic reverse charge, the risk that suppliers will account for the VAT to HMRC in error and customers will recover it from HMRC is clear.

Subcontractors that rely on VAT collected from their customers as working capital until they have to remit it to HMRC are likely to suffer from the loss of cash flow. These businesses and even their customers will need to consider if payment terms need to be revisited to avoid problems in the supply chain.

Businesses that presently account for VAT under the Cash Accounting Scheme will have to migrate to Invoice-based Accounting – the domestic reverse charge cannot apply under the Cash Accounting Scheme.

Subcontractors will also need to confirm that they are working for a VAT registered business and whether they are working for an end user, or for someone connected to an end user, including landlords and tenants.

Contractors will have to disclose to their subcontractors where they are in fact not the end user. This is a matter that may be commercially sensitive for contractors.

My advice is for construction businesses to review supplies made to and received from other VAT registered contractors to establish where these will be subject to a reverse charge from October 2019. They should also obtain notification from customers that they are an end user and confirmation of their VAT registration and CIS status, and review their contracts now to ensure that this information is captured for all customers.

I would also suggest they consider any adaptations required to ensure that their accounting systems can deal with this change, consider the impact on cash flow from October 2019 and if there are any other ways to mitigate this, and ensure that their staff are clear about the complexities of the new rules.

Sub-contractors should review their cash flow projections carefully. There may be a good argument to change to filing monthly VAT returns to recover input VAT that otherwise would have been netted off against output VAT.

Finally, not only does 1 October 2019 see the introduction of the domestic reverse charge, but those VAT registered businesses that could delay complying with the Making Tax Digital Regulations must now comply with MTDfV. If the business did defer, does it have a letter from HMRC confirming that delay?

Let’s hope that the API-enabled software is such that it can handle the domestic reverse charge too.

Enjoy what is left of the warm weather.

Richard Todd
ATT Vice President