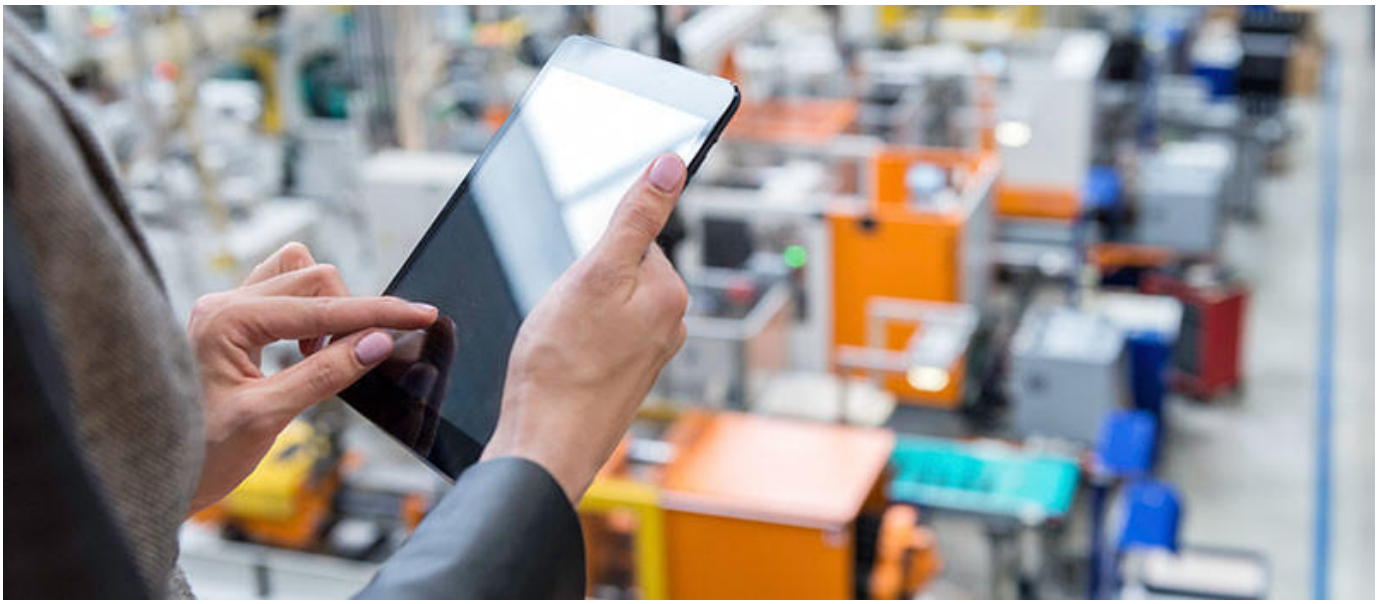
VAT: Annual accounting and VAT exempt income

Indirect Tax



22 January 2025

As part of their membership of HMRC's Joint VAT Consultative Committee, the CIOT and ATT can raise technical and procedural issues with the VAT system for further consideration.

The forum's purpose is 'to exchange views between HMRC and representative organisations relating to the procedures and operations of VAT, and to consider and discuss VAT issues arising from member organisations with the aim of strengthening HMRC's understanding of the needs of the business customer/taxpayer'. A recent member case that has been submitted to HMRC highlights how different procedural requirements cause conflict within the VAT system.

Annual accounting

The VAT annual accounting rules allow eligible businesses to submit a single annual VAT return each year rather than make quarterly returns. Businesses can apply for

VAT annual accounting if their taxable turnover is estimated to be £1.35 million or less. HMRC publish guidance on the annual accounting scheme in VAT notice 732 (tinyurl.com/3mhuyru4) and on GOV.UK (tinyurl.com/yr2hjuay).

Taxable turnover threshold

A key point to note is that the annual accounting threshold is based only on *taxable* turnover; that is, income derived from sales subject to the standard, reduced or zero rate of VAT. Supplies that are VAT exempt are excluded from the turnover threshold, as stated in paragraph 2.2 of VAT Notice 732 – annual accounting (tinyurl.com/3mhuyru4).

Administrative issue

A procedural issue can arise for affected businesses that have taxable income within the annual accounting threshold, but also exempt income that causes their combined income to exceed £1.35 million. HMRC's system automatically removes those businesses from annual accounting based on the turnover declared in the VAT return, as the Box 6 outputs figure requires both taxable and exempt income to be declared as one figure. There is no separate box on the annual accounting VAT return to separately disclose taxable and exempt turnover, or to make it clear that the taxable turnover is within the annual accounting threshold.

When a business is automatically removed from annual accounting in error, they must contact HMRC to resolve the issue, and in the meantime may receive centrally issued assessments for missing quarterly VAT returns. All of this takes time and resource to rectify, and if they use a VAT agent to assist, they incur costs too.

The CIOT is interested in understanding the impact of this procedural issue and would like to hear from members who have experienced it themselves or on behalf of affected clients. Please contact technical@ciot.org.uk or atttechncial@att.org.uk.

Other VAT issues

Please note that referrals to the Joint VAT Consultative Committee about issues with VAT procedures or operations must come directly from the CIOT or ATT rather than from members themselves. They should represent a general issue that impacts the wider community, as opposed to escalating a case for an individual business, though

we can, and do, highlight individual cases where they are an example of a wider issue. For example, we are still highlighting individual cases experiencing excessive delays beyond HMRC’s published service level agreement timings, which are generally 40 working days for most VAT service lines.

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