

Making Tax Digital for VAT

Draft Statutory Instrument: The Value Added Tax (Amendment) Regulations 2018, Explanatory Memorandum, VAT Notice and Addendum

Response from the Low Incomes Tax Reform Group (LITRG)

1 Executive Summary

- 1.1 We believe a large proportion of small businesses who are compulsorily VAT registered due to the level of their turnover but who make very modest profits for income tax purposes will use spreadsheets as the basis for their digital recordkeeping and not accounting software packages. Therefore the Regulations or Notice need to specifically state that spreadsheets are an acceptable form of 'functional compatible software' and so comply with the new digital recordkeeping requirement.
- 1.2 We note that some kind of API enabled spreadsheets and/or bridging software is proposed to enable those using spreadsheets for their recordkeeping to actually file their VAT returns under the Making Tax Digital for VAT (MTDfV) regime. We are concerned that the software community may not see a development need for such software and so may not be particularly keen to produce this type of product. There is likely to be a significant lead time to design and test a completely new product and we would be keen to know how much progress has been made to date in developing these tools.
- 1.3 As HM Revenue & Customs (HMRC) have stated that the software industry will not be required to produce free software which is compatible with MTDfV, many small businesses will incur additional costs, whether this is in purchasing MTDfV compliant software, or computer/IT hardware – these can be significant for those on low incomes. We continue to be of the opinion that HMRC should require adequate free software be made available so that this cost can be avoided if a business so chooses. HMRC's apparent transition cost of

£109 per business would not cover these additional expenses for many businesses, leaving aside the time and opportunity costs involved with set up, learning etc.

- 1.4 In order to avoid a huge influx of businesses ‘joining’ MTDfV with effect from April 2019 at the same time, under stagger 1 (calendar quarter VAT periods), we recommend that a business must become compliant with MTDfV from the beginning of its first accounting period after April 2019. This will then be consistent with the current intention for Making Tax Digital for Business (MTDfB), whereby a business must comply with the MTDfB regime from the beginning of the first accounting period after the start date of MTDfB.
- 1.5 We are pleased that the current exemption criteria (other than based on turnover) for electronic filing of VAT returns has been carried into this regime, and indeed has been brought into the MTDfB regime too. However there is no mention of specific support for those who may fall into the ‘digitally assisted’ category. HMRC must be prepared to make sufficient resources available to provide help to this cohort of VAT filers in due course.
- 1.6 As many small businesses are voluntarily registered for VAT and so not within the new MTDfV rules, HMRC must prioritise a communications campaign to let businesses know who will and who will not be required to comply with MTDfV. As part of this campaign they must confirm to those who are not required to join the new regime that they can continue to file returns in their usual way, including via the HMRC online portal, assuming the intention is still for this to be maintained.
- 1.7 The examples set out pictorially in the draft Addendum will be used by unrepresented taxpayers to establish how they should comply with MTDfV and so when they are finalised HMRC must ensure they are consistent, easy to understand, written in layman’s terms and, most importantly, convey relevant information accurately.

2 About Us

- 2.1 The Low Incomes Tax Reform Group (LITRG) is an initiative of the Chartered Institute of Taxation (CIOT) to give a voice to the unrepresented. Since 1998 LITRG has been working to improve the policy and processes of the tax, tax credits and associated welfare systems for the benefit of those on low incomes. Everything we do is aimed at improving the tax and benefits experience of low income workers, pensioners, migrants, students, disabled people and carers.
- 2.2 LITRG works extensively with HMRC and other government departments, commenting on proposals and putting forward our own ideas for improving the system. Too often the tax and related welfare laws and administrative systems are not designed with the low-income user in mind and this often makes life difficult for those we try to help.
- 2.3 The CIOT is a charity and the leading professional body in the United Kingdom concerned solely with taxation. The CIOT’s primary purpose is to promote education and study of the

administration and practice of taxation. One of the key aims is to achieve a better, more efficient, tax system for all affected by it – taxpayers, advisers and the authorities.

3 Introduction

- 3.1 The LITRG constituency that are likely to come within MTDfV are those businesses trading above the VAT registration threshold but who make relatively little profit. Typically this might be a self-employed business such as a retail business, corner shop/convenience store, café, or small restaurant, particularly in tourist areas where trade is seasonal.
- 3.2 Many such businesses are not sophisticated, but they keep adequate business records based around till rolls and supplier invoices, recording data in handwritten cash books or, if IT literate, on spreadsheets. Our experience suggests very few have any kind of accounting software and if they do, they will not always be using it quite as it is intended to be used. They almost exclusively all use HMRC's online VAT return completion service to deal with their quarterly VAT returns.
- 3.3 It is with this taxpayer base in mind that we make the observations below. However please note that we fully endorse all the comments made in the submission by the CIOT, which are as applicable to low-income VAT registered businesses as they are to all other VAT registered businesses.

4 Use of spreadsheets

- 4.1 We anticipate that the majority of the businesses described above will continue to use, or be persuaded to make a transition to, spreadsheets for their business recordkeeping; formal accounting software may well be a step too far for many. As HMRC have confirmed on many occasions that the use of spreadsheets will be acceptable for digitalising business records, this should be made very clear, preferably in the Regulations or Notice, but at least in the guidance that this is the case.
- 4.2 The proposal to use API enabled spreadsheets or some kind of bridging software to enable the VAT return to be submitted is an interesting one. We assume the creation of such software has been discussed with software developers and that HMRC are confident products could be designed and delivered. However the time frame is tight for developing, testing and marketing a completely new product like this which may well need to integrate with existing spreadsheet records. It is vital that the software companies are 'bought into' providing this type of software and it is not being assumed by HMRC that they will deliver what HMRC say they need.
- 4.3 We strongly believe that free MTDfV compliant software should be made available to small businesses, for the same reasons as free MTDfB compliant software is to be made available. There is no reason to distinguish VAT compliant software from income tax compliant software – it is the same group of taxpayers who will potentially incur costs for these

products which they cannot afford. It is a misconception that a VAT registered business is necessarily making significant profits and so can afford additional costs such as software and/or hardware.

5 Timing

- 5.1 We share the concerns expressed by the CIOT and many other commentators that introducing MTDfV at the same time as the UK formally leaves the EU could mean that businesses are overwhelmed by many changes taking place at the same time. Further, with the introduction date of April 2019 being little over a year away, the time available for businesses to modify or replace their existing record keeping systems and test them is unlikely to be the 12 month window that was promised. Therefore we endorse the view that serious consideration must be given to deferring the full introduction of MTDfV.
- 5.2 However, on its introduction we would like to see businesses joining the new regime at the beginning of the first **accounting** period which follows the introduction date. This would then mitigate to some extent a potential surge of businesses with stagger 1 VAT periods all being mandated into MTDfV at the same time and would also align with the rules for joining MTDfB in due course. Using the same rules for both regimes would hopefully make it easier for businesses to be clear about their MTDfB start date.

6 Digital assistance

- 6.1 We are pleased that the current exemption criteria (other than based on turnover) for electronic filing of VAT returns has been carried into this regime, and indeed has been brought into the MTDfB regime too. However there will be a significant number of VAT registered businesses who will not be exempt but who will struggle to get to grips with the new rules and/or with the technology and so will need support to comply with their legal obligations. There will also be those with accessibility needs who may need additional support. The support must be available through non-digital channels such as telephone helplines, and not just via digital services such as web chat. The extent to which digital assistance will be required must not be underestimated, and appropriate resources must be properly funded to ensure the programme is a success.

7 Communications

- 7.1 It is imperative that an effective communications plan is put in place quickly as, to date, there is very little information available to unrepresented businesses about MTDfV. It is vital that those businesses who are to be affected by the new regime are aware of this as soon as possible, and those that will not be affected are clear what their ongoing obligations will continue to be.

- 7.2 Although many small businesses engage the services of an agent to prepare their year-end accounts and tax return, many will often deal with their VAT themselves as a way of keeping costs down. Unrepresented taxpayers rely on HMRC guidance and so the guidance for the MTDfV programme must be well written and easily understandable, comprehensive and detailed. The examples in the draft Addendum will be used by unrepresented taxpayers to establish how they should comply with MTDfV and so when they are finalised HMRC must ensure they are consistent, easy to understand, written in layman's terms and, most importantly, convey relevant information accurately.

LITRG
8 February 2018