

VAT

NEW ACCOUNTING PROCEDURES FOR BUILDERS



New procedures are being introduced on 1 March 2021. These changes were originally due to come into effect from October 2019 but were delayed to give businesses more time to prepare. The changes affect any VAT-registered construction business that does the following:

- Buys in construction services from other builders and makes an onward supply of those services to another customer e.g. where a subcontractor invoices the main contractor on a project, and the main contractor invoices the final 'end-user' client.
- Sells construction services to other builders where the builders make an onward supply of the services to their customer.

WHAT IS CHANGING?

Under current rules, a builder charges VAT to their customer, collects the VAT from the customer and accounts for it in Box 1 of their relevant VAT return.

This is changing for supplies between VAT-registered builders. The builder will invoice their builder customer without charging VAT and the customer makes the Box 1 entry instead on their own VAT return.

In effect, there will be no cash flow issue for the builder receiving services because the same amount of VAT declared in Box 1 will also be included as input tax in Box 4: i.e. a nil effect overall. This is known in VAT speak as a "reverse charge" procedure.

REASON FOR CHANGE

HMRC has identified that certain builder supplies have been prone to VAT fraud, where the supplier charges VAT to his customer, receives money for this VAT from the customer but never declares it on a VAT return. The new procedures aim to prevent this from happening because the supplier is never paid VAT in the first place.

WHICH SALES ARE CAUGHT BY THE NEW RULES?

The new reverse charge procedures will apply to the following transactions:

- The legislation refers to "specified services" but these do not apply to services supplied to non-construction businesses, such as a retailer having their premises improved or any other end-user customer or building owner;
- The reverse charge will also apply to any goods supplied by the builder as part of their work;
- Employment businesses are excluded from the new rules;
- The reverse charge is based on the rate of VAT that applies for the work in question but only supplies subject to either 5% or 20% VAT. Zero-rated sales are excluded.

EXAMPLE

Mike is an electrician, VAT registered as a sole trader. He is doing some work on an office block, invoicing the main contractor Steve for his work.

Steve is also VAT registered, and will then invoice the building owner. Steve is not an “end-user” because he is making an onward supply of construction services to his own customer. He is an “intermediary supplier”.

The invoice raised by Mike will be subject to the new procedures i.e. no VAT is charged. Let’s say the value of his work including materials will be for £5,000:

Mike’s VAT return will only include the value of the sale in Box 6 (outputs) of his VAT return:

- Box 6 – outputs - £5,000

Steve will do the reverse charge calculation and make the following entries on his return:

- Box 1 – output tax £1,000 (i.e. £5,000 x 20%)
- Box 4 – input tax - £1,000 (same figure as Box 1)
- Box 7 – inputs - £5,000 (net value of payment made to Steve)

OTHER ISSUES TO CONSIDER

Taking the Steve and Mike example a stage further, they each have their own responsibilities with the new rules.

Mike must ensure that Steve is both registered for the CIS (Construction Industry Scheme) and also has a valid VAT number.

Mike must also specify on his sales invoices the amount and rate of VAT that Steve must declare with the reverse charge i.e. 5% or 20% VAT.

Mike should include wording on the sales invoice along the lines of: “Reverse charge: customer to pay the VAT to HMRC.”

Steve must tell Mike if he is an “end-user” or “intermediary supplier”. If he is an intermediary supplier, then Mike will not charge him VAT because the reverse charge applies.



It is important that Steve does not pay VAT incorrectly to Mike because HMRC could raise an assessment for the VAT that he should have declared, i.e. as if the reverse charge had been done correctly.

Here are a few other points to consider:

- Checks should be applied to ensure building contractor clients invoiced under the new rules are properly registered for VAT and are bona fide. Section 9 of HMRC VAT Notice 735: Domestic reverse charge procedure gives further information.
- HMRC suggests that if there are any doubts about the credentials of a builder customer, then a deposit equal to the amount of VAT not being charged should be collected from the customer eg if they have applied for but not received a VAT number.
- VAT Notice 735 mentioned above gives examples of customer checks that should be considered at para 9.3.1.

Users of the Flat Rate Scheme who will be affected by this will need to consider whether they should revert to using standard VAT accounting.

PENALTIES ISSUED BY HMRC FOR ERRORS

HMRC has confirmed that penalties will not be charged for mistakes with the new procedures for a six month period after the reverse charge comes into effect, the exception being if “you are deliberately taking advantage of the measure by not accounting for it correctly.”

SUMMARY

If you have any questions about the new VAT rules, please contact your usual Moore tax adviser.

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