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VAT after Brexit

What could happen to VAT after the UK has left the European Union?

On 23 June 2016, the British public voted in one of the most important referendums of modern times.

The public's decision to leave the EU will have an impact on almost every aspect of economic life. Trading relationships will need to be reformulated and new ways of attracting foreign investment may have to be sought. Future governments will have a new-found sovereignty over taxation policy. Outside of EU state aid rules and tax law, governments have the potential to make structural changes to our tax system that have not been witnessed in recent decades.

The UK will have at least 2 years to negotiate its exit from the EU after invoking article 50 of the Lisbon Treaty. During this period the UK will remain inside the EU and businesses will continue to operate inside the same regulatory framework as they did before the referendum.

Anticipating future challenges is one of the cornerstones of running a successful business. With this in mind, this guide will examine the potential impact of Brexit on VAT.

The current system

VAT is chargeable on taxable supplies made in the UK by 'taxable persons'. VAT law covers all types of supply of goods

or services, whether of a revenue or capital nature. Supplies include the sale, hire, or loan of goods.

Credit is given for tax paid to other businesses and the net balance is payable or reclaimable - normally on a quarterly basis.

A taxable person is any person carrying on a business which is, or is required to be, registered for VAT and includes the following:

- individuals
- partnerships
- unincorporated associations, e.g. trusts or charities
- limited companies
- limited liability partnerships.

Registration

All businesses must register for VAT when their taxable turnover is above £83,000. This is known as the VAT registration threshold. After registration, businesses will need to collect and pay VAT, submit quarterly returns and comply with VAT accounting rules.

Businesses that sell e-services to consumers living in other EU member states must also register with the VAT MOSS scheme or with the relevant tax authority in the European country. VAT MOSS eliminates the need to register with separate EU countries but users will face extra reporting requirements.

Rates

The standard rate of VAT in the UK is 20%. This is the rate levied on most goods and services. A reduced 5% VAT rate is levied on certain goods and services such as home energy and heating equipment. In addition to this, the government provides zero-rate VAT for industries such as print publishing and babywear, and VAT exemptions for the insurance and financial services industries.

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Returns

VAT returns must be submitted every 3 months. Individuals must account for total sales and purchases, the amount of VAT payable to HMRC and the amount of reclaimable VAT.

Businesses registered with the VAT MOSS scheme must prepare separate returns that account for VAT collected from consumers living in the EU.

Schemes

The EU permits the UK government to administer several VAT accounting schemes. These can make reporting easier and in some cases reduce the amount of tax payable, but they are subject to eligibility criteria.

Flat rate scheme: Businesses with an annual turnover of less than £150,000 can pay a reduced fixed rate of VAT to HMRC. Businesses charge customers the standard rate of VAT but pay HMRC the reduced rate.

Cash accounting scheme: Businesses with an annual turnover of less than £1.35 million can pay and reclaim VAT as and when invoices are paid, instead of paying VAT regardless of customer payment.

Annual accounting scheme: Businesses with an annual taxable turnover of less than £1.35 million can submit one return per year and make advance VAT payments based on the previous year's return.

How will Brexit affect UK VAT?

VAT is just one of the many things that may change in light of the UK's decision to leave the EU. As the UK government begins to negotiate its exit, how will Brexit affect UK VAT rules?

Rates

Currently, UK VAT rules are derived from European law and legislative bodies must apply VAT according to European directives and the rulings of the European Court of Justice. After the UK leaves the EU, the government will take full control over its VAT policies.

Potential changes include:

The standard VAT rate: EU law prevents member states from lowering the standard rate of VAT below 15%. Future UK governments may choose a rate under 15% after Brexit.

VAT exemptions: Leaving the EU will allow the government to introduce a zero-rate of VAT on specific goods and services, or entire industries.

Different VAT rates: The government will be able to introduce different VAT rates for different services.

Reporting

The reintroduction of economic borders between the UK and EU member states will affect how businesses trading in the EU account for VAT.

Some sectors will face larger transformations than others. For instance, businesses operating in the travel and tourism sector might not have to account for VAT under the Tour Operators Margin Scheme.

The end of VAT MOSS?

The decision to leave the EU has thrown the UK's future participation in the digital single market – and therefore EU VAT legislation on business-to-consumer e-services – into doubt.

EU VAT rules will continue as normal while the UK remains in the EU, and businesses will continue to use VAT MOSS for the foreseeable future.

EU VAT Action, a campaign group calling for reform of the European VAT system, has warned that the UK will have less influence on the digital single market legislation after it formally triggers article 50 and begins its exit negotiations. This could mean that businesses face an unreformed EU VAT system should the UK remain in the single market after the negotiations are concluded.

EU VAT rules will presumably cease to apply if the government chooses to fully leave both the EU and the single market.

However, predicting the outcome of negotiations that are yet to begin is an impossible task. No-one yet knows what our future relationship with the EU will look like.

Devolution

An unintended consequence of the UK voting to leave the EU may be the devolution of VAT powers to Scotland.

Independent think tank Reform Scotland recently submitted a paper to an inquiry set up by Holyrood's European and External Relations Committee in which it argued that control over VAT should be fully devolved in light of the referendum result.

EU law prevents a single member state from having multiple VAT rates.

However, the referendum result means that the UK's relationship with EU law will be unclear until the end of its exit negotiations.

With a possible second Scottish independence referendum – as well the start of the UK exit negotiations – still to come, it remains possible that the UK government may choose to devolve VAT powers to Scotland.

Wondering how the EU referendum will affect your business? Speak to one of our advisers for information about the implications of Brexit.