ACCA

Applied Skills

Taxation (TX – UK) FA 2024

Course Book

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Helping you to pass

BPP Learning Media – ACCA Content Partner

As an ACCA Content Partner, BPP Learning Media gives you the opportunity to use the revision materials created by BPPs expert team of Subject Matter Experts who have years of experience authoring Professional Qualification Content. The Subject Matter Experts ensure the content covers the depth and breadth of the syllabus and provides excellent support for your revision.

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The PER alert

Before you can qualify as an ACCA member, you not only have to pass all your exams but also fulfil a three-year practical experience requirement (PER). To help you to recognise areas of the syllabus that you might be able to apply in the workplace to achieve different performance objectives, we have introduced the 'PER alert' feature (see the next section). You will find this feature throughout the Course Book to remind you that what you are learning to pass your ACCA exams is equally useful to the fulfilment of the PER requirement. Your achievement of the PER should be recorded in your online My Experience record.

Chapter features

Studying can be a daunting prospect, particularly when you have lots of other commitments. This Course Book is full of useful features, explained in the key below, designed to help you to get the most out of your studies and maximise your chances of exam success.

Key to icons

KEY TERM

Key term

Central concepts are highlighted and clearly defined in the Key terms feature. Key terms are also listed in bold in the Index, for quick and easy reference.

Formula to learn

This boxed feature will highlight important formula which you need to learn for your exam.

Formula provided

This will show formula which are important but will be provided in the exam.

PER alert

This feature identifies when something you are reading will also be useful for your PER requirement (see 'The PER alert' section above for more details).

Exam focus point

This feature provides tips about how a specific topic may be examined.

Real world example

These will give real examples to help demonstrate the concepts you are reading about.

Illustration

Illustrations walk through how to apply key knowledge and techniques step by step.

Activity

Activities give you essential practice of techniques covered in the chapter.

Essential reading

Links to the Essential reading are given throughout the chapter. The Essential reading is included in the free eBook (see inside cover for details on how to access this).

At the end of each chapter, you will find a Knowledge diagnostic, which is a summary of the main learning points from the chapter to allow you to check you have understood the key concepts. You will also find a Further study guidance, which contains suggestions for ways in which you can continue your learning and enhance your understanding. This can include: recommendations for question practice from the Further question practice and solutions (available in the digital edition of the Course Book), to test your understanding of the topics in the chapter; and suggestions for further reading which can be done, such as technical articles, and ideas for your own research.

Introduction to the Essential reading

The electronic version of the Course Book contains additional content, selected to enhance your studies. Consisting of revision materials and further explanations of complex areas including illustrations and activities, as well as practice questions and solutions and background reading, it is designed to aid your understanding of key topics which are covered in the main printed chapters of the Course Book.

A summary of the content of the Essential reading is given below.

Chapter		Summary of Essential reading content
1	Introduction to the UK tax system	• Function and purpose of tax • Economic factors – ie to discourage/encourage certain types of activity • Social factors – different taxes, different effects • Environmental factors – eg climate change levy • Tax avoidance and tax evasion
2	Computing taxable income and the income tax liability	• Steps in computing the tax liability and tax payable • Working at the margin examples • Qualifying interest – loan purposes that qualify for relief • Examples of income tax planning for spouses/civil partners
3	Employment income	There is no essential reading for this chapter.
4	Taxable and exempt benefits. The PAYE system	• Detailed example on car and fuel benefit • Further detail on beneficial loans • Further detail on expenses and exempt benefits
5	Pensions	There is no essential reading in this chapter.
6	Property income	There is no essential reading in this chapter.
7	Computing trading income	• Further reading on the badges of trade • Case law information on the distinction between capital and revenue expenditure • The application of the 'wholly and exclusively' rule – the remoteness and duality tests • Table of sundry allowable and disallowable items • Detail of the operation of fixed rate expenses in the cash basis
8	Capital allowances	• Rule concerning date of expenditure for capital allowance purposes • Detailed definition of plant and machinery, buildings, and structures • Treatment of land and computer software • Relevant case law on function vs setting
9	Assessable trading income	There is no essential reading in this chapter.
10	Trading losses	• Loss relief against capital gains • Further example of basis period rules applicable to losses in early years of trading • Disclaiming capital allowances as a tax planning tool

Chapter		Summary of Essential reading content
11	Partnerships and limited liability partnerships	There is no essential reading in this chapter.
12	National insurance contributions	• Detailed definition of 'earnings' for NIC • Operation of earnings periods for directors including an example comparing a director to an employee
13	Computing chargeable gains	• Further detail/example on computing a gain or loss
14	Chattels and private residence relief	• Business use of a residence
15	Business reliefs	• More detail on the business asset disposal relief lifetime limit • Rollover relief – non-business use
16	Shares and securities	There is no essential reading for this chapter.
17	Self assessment and payment of tax by individuals	• Penalties for failure to notify chargeability • Penalties for late filing exceeding 12 months • Circumstances where payments on account are not required or may be reduced • HMRC powers – determinations, discovery assessments and investigating dishonest conduct by tax agents • Detail regarding appeals and Tax Tribunal hearings
18	Inheritance tax: scope and transfers of value	• Deductibility of debts and funeral expenses
19	Computing taxable total profits and the corporation tax liability	• Loan relationships – accounting methods, tax treatment of incidental costs of loan finance, and capital costs • Illustration showing the calculation of property business profit for a company • Comprehensive illustration of the computation of TTP • Comparison of running a business as a sole trader vs a company
20	Chargeable gains for companies	• Detail, including an example, of the impact of bonus and rights issues on the FA 1985 share pool for a company • Treatment of reorganisations and takeovers for a corporate shareholder
21	Loss relief for single companies	There is no essential reading for this chapter.
22	Groups	• The order of offset of losses for a claimant company • Illustration showing the different definitions of a group relief and chargeable gains group
23	Self assessment and payment of tax by companies	• Detail of iXBRL • Detail of how a company can make and amend claims
24	An introduction to VAT	• Example with standard and zero-rated and exempt supplies • Meaning of supplies of goods/services/taxable persons • Categorising a supply • Examples of zero-rated and exempt supplies
25	Further aspects of VAT	• VAT records

Introduction to Taxation (TX – UK)

Videos can be viewed online by accessing your ebook version on VitalSource.

Overall aim of the syllabus

You are introduced to the rationale behind – and the functions of – **the tax system**. The syllabus then considers the **separate taxes** that an accountant would need to have a detailed knowledge of, such as **income tax from self-employment, employment and investments**, the **corporation tax** liability of individual companies and groups of companies, the **national insurance contribution** liabilities of both employed and self-employed persons, the **value added tax** liability of businesses, the **chargeable gains** arising on disposals of investments by both individuals and companies, and the **inheritance tax** liabilities arising on chargeable lifetime transfers and on death.

You will be expected to have a **detailed knowledge** of these taxes, but **no previous knowledge is assumed**. You should **study the basics** carefully and **learn the pro forma computations**. It then becomes straightforward to complete these by slotting in figures from your detailed workings.

As well as being able to calculate tax liabilities, you may be required to **explain the basis of the calculations**, **apply tax planning techniques** for individuals and companies and **identify the compliance issues** for each major tax through a variety of business and personal scenarios and situations.

Members of the Taxation (TX – UK) examining team have written several technical articles including two on Inheritance Tax, two on chargeable gains, one on groups, two on VAT, one on benefits, one on cars, one on adjustment of profit questions, one on objective test questions, one on higher skills, one on using the examiner's reports, one for retake students and one on Finance Act 2023. All these articles are available on the ACCA website. Make sure you read them to gain further insight into what the Taxation (TX – UK) examining team is looking for.

The syllabus

The broad syllabus headings are:

A	The UK tax system and its administration
B	Income tax and NIC liabilities
C	Chargeable gains for individuals
D	Inheritance tax
E	Corporation tax liabilities
F	Value added tax (VAT)
G	Employability and technology skills

Main capabilities

On successful completion of this exam, you should be able to:

A	Integrate knowledge and understanding from across the syllabus to enable you to complete detailed computations of tax liabilities.
B	Explain the underlying principles of taxation by providing a simple summary of the rules and how they apply to the particular situation.
C	Apply tax planning techniques by identifying available options and testing them to see which has the greater effect on tax liabilities.

https://www.accaglobal.com/uk/en/student/exam-support-resources/fundamentals-exams-study-resources/f6/syllabus-study-guide/f6-syllabus-study-guide-united-kingdom-uk.html

https://learningmedia.bpp.com/pages/resources-for-students

Links to other exams

Advanced Taxation –
United Kingdom (ATX – UK)

↑

Taxation –
United Kingdom (TX – UK)

This diagram shows where direct (solid line arrows) and indirect (dashed line arrows) links exist between this exam and others that may precede or follow it.

TX – UK provides a **foundation for Advanced Taxation (ATX – UK)** which will be chosen by those who work in a tax environment.

Achieving ACCA's Study Guide Objectives

This BPP Course Book covers all the Taxation (TX – UK) syllabus learning objectives. The tables below show in which chapter(s) each area of the syllabus is covered.

A	**The UK tax system and its administration**	
A1	The overall function and purpose of taxation in a modern economy	Chapter 1
A2	Principal sources of revenue law and practice	Chapter 1
A3	The systems for self-assessment and the making of returns	Chapters 17, 23
A4	The time limits for the submission of information, claims and payment of tax, including payments on account	Chapters 17, 23
A5	The procedures relating to compliance checks, appeals and disputes	Chapters 17, 23
A6	Penalties for non-compliance	Chapters 17, 23

B	**Income tax and NIC liabilities**	
B1	The scope of income tax	Chapter 2
B2	Income from employment	Chapters 3, 4
B3	Income from self-employment	Chapters 7, 8, 9, 10, 11
B4	Property and investment income	Chapters 2, 6

B5	The comprehensive computation of taxable income and income tax liability	Chapters 2, 3
B6	National insurance contributions for employed and self-employed persons	Chapter 12
B7	The use of exemptions and reliefs in deferring and minimising income tax liabilities	Chapters 2, 5
C	**Chargeable gains for individuals**	
C1	The scope of the taxation of capital gains	Chapter 13
C2	The basic principles of computing gains and losses	Chapter 13
C3	Gains and losses on the disposal of movable and immovable property	Chapter 14
C4	Gains and losses on the disposal of shares and securities	Chapter 16
C5	The computation of capital gains tax	Chapters 13, 15
C6	The use of exemptions and reliefs in deferring and minimising tax liabilities arising on the disposal of capital assets	Chapters 13, 15
D	**Inheritance tax**	
D1	The basic principles of computing transfers of value	Chapter 18
D2	The liabilities arising on chargeable lifetime transfers and on the death of an individual	Chapter 18
D3	The use of exemptions in deferring and minimising inheritance tax liabilities	Chapter 18
D4	Payment of inheritance tax	Chapter 18
E	**Corporation tax liabilities**	
E1	The scope of corporation tax	Chapter 19
E2	Taxable total profits	Chapters 19, 21
E3	Chargeable gains for companies	Chapters 20, 21
E4	The comprehensive computation of corporation tax liability	Chapter 19
E5	The effect of a group corporate structure for corporation tax purposes	Chapter 22
E6	The use of exemptions and reliefs in deferring and minimising corporation tax liabilities	Chapters 19, 20, 21, 22
F	**Value added tax (VAT)**	
F1	The VAT registration requirements	Chapter 24
F2	The computation of VAT liabilities	Chapters 24, 25
F3	The effect of special schemes	Chapter 25

G	Employability and technology skills	
G1	Use computer technology to efficiently access and manipulate relevant information	Skills checkpoint 2 and 4
G2	Work on relevant response options, using available functions and technology, as would be required in the workplace	Skills checkpoint 2 and 4
G3	Navigate windows and computer screens to create and amend responses to exam requirements, using the appropriate tools	Skills checkpoint 2 and 4
G4	Present data and information effectively using the appropriate tools	Skills checkpoint 2 and 4

Syllabus section G is present in the syllabus for all ACCA professional exams; it reflects the skills needed in a computer-based exam and has no specific detailed syllabus content. This area is covered in the exam success skills section later in this introduction.

The exam

Approach to examining the syllabus

- There is no choice in this exam, all questions have to be answered. You must therefore study the **entire syllabus**, there are no short-cuts.
- The first section of the exam consists of 15 **objective test questions**, worth two marks each. These will inevitably cover a **wide range of the syllabus**.
- The second section of the exam consists of three scenarios each being tested with five **objective test questions**, worth two marks each. You must make sure you **understand the scenario** before attempting the related questions.
- The third section of the exam consists of **three constructed response questions**, one 10-mark question and two 15-mark questions.
- Practising longer questions set in the third section of the exam under **timed conditions** is essential. BPP's **Exam Practice Kit** contains 10-mark and 15-mark questions on all areas of the syllabus. Answer all parts of the question. Even if you cannot do all of the calculation elements, you will still be able to gain marks in the discussion parts.
- **Answer selectively** – the examining team will expect you to consider carefully what is relevant and significant enough to include in your answer. Do not include unnecessary information.
- Keep an eye out for **articles** as the **examining team** will use **Student Accountant** to communicate with students. Tax rates, allowances and information on certain reliefs will be given in the exam. You should familiarise yourself with the information provided so that you know how to find it quickly in the exam.

Computer-based exams

All ACCA papers are computer-based examinations (CBEs). The CBE exams for Applied Knowledge modules can be taken at any time; these are referred to as 'exams on demand'. The Applied Skills and Strategic Professional exams can be sat in September, December, March and June of each year; these are referred to as 'exams on sitting'. Taxation is an 'exam on sitting'. Computer-based examinations must be taken at an ACCA CBE Licensed Centre.

The exam is formatted as follows:

Format of the exam		Marks
Section A	**Objective test (OT)** 15 questions × 2 marks	30
Section B	**Objective test (OT) case** 3 questions × 10 marks Each question will contain five subparts each worth 2 marks	30
Section C	**Constructed response (long questions)** 1 question × 10 marks 2 questions × 15 marks	40
		100

The Taxation (TX – UK) syllabus is assessed by a 3-hour exam. The pass mark is **50%**. All questions in the exam are **compulsory**. Section A and B questions will be selected from the entire syllabus. The responses to each question or subpart in the case of OT cases are marked automatically as either correct or incorrect by computer.

The 10-mark Section C questions can come from any part of the syllabus. The 15-mark Section C questions will mainly focus on the following syllabus areas but a minority of marks can be drawn from any other area of the syllabus:

- Income tax (syllabus area B)
- Corporation tax (syllabus area E)

The responses to these questions are human marked.

Videos can be viewed online by accessing your ebook version on VitalSource.

Remote invigilated exams

In certain geographical areas, it may be possible for you to take your exam remotely. This option, which is subject to strict conditions, can offer increased flexibility and convenience under certain circumstances. Further guidance, including the detailed requirements and conditions for taking the exam by this method, is contained on ACCA's website at:

https://www.accaglobal.com/an/en/student/exam-entry-and-administration/about-our-exams/remote-exams/remote-session-exams.html

Essential skills areas to be successful in Taxation (TX – UK)

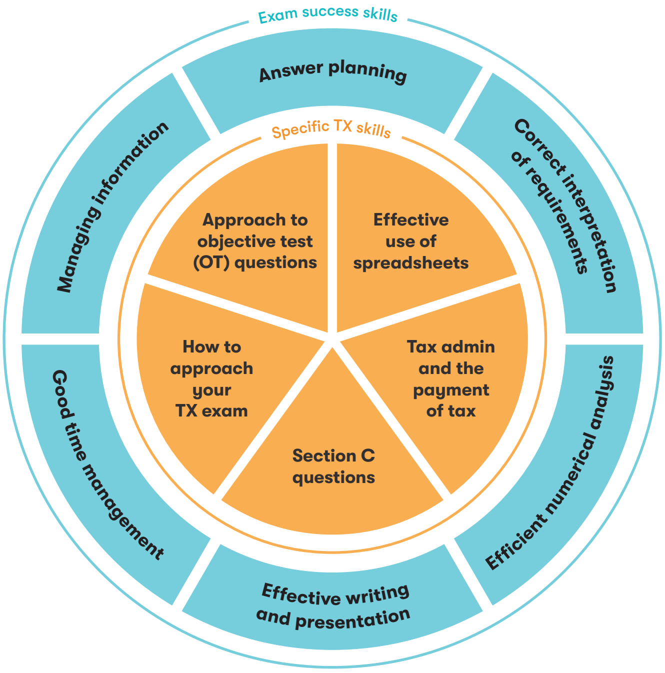
We think there are three areas you should develop in order to achieve exam success in TX – UK:

(a) Knowledge application

(b) Specific TX – UK skills

(c) Exam success skills

These are shown in the diagram below.



Specific TX – UK skills

These are the skills specific to TX – UK that we think you need to develop in order to pass the exam.

In this Course Book, there are five **Skills checkpoints** which define each skill and show how it is applied in answering a question. A brief summary of each skill is given below.

Skill 1: Approach to objective test (OT) questions

Section A of the exam will include 15 OT questions worth two marks each. Section B of the exam will include three OT cases, worth 10 marks each. Each OT case contains a group of five OT questions based around a single scenario. 60% of your TX – UK exam is therefore made up of OT questions. It is essential that you have a good approach to answering these questions. OT questions are auto-marked; your workings will therefore not be considered; you have to answer the whole question correctly to earn their two marks.

A step-by-step technique for tackling OT questions is outlined on the following page.

General guidance for approaching OT questions

STEP 1: Answer the questions you know first.

If you're having difficulty answering a question, move on and come back to tackle it once you've answered all the questions you know.

It is often quicker to answer discursive style OT questions first, leaving more time for calculations.

General guidance for approaching OT questions

STEP 2: Answer all questions.

There is no penalty for an incorrect answer in ACCA exams; there is nothing to be gained by leaving an OT question unanswered. If you are stuck on a question, as a last resort, it is worth selecting the option you consider most likely to be correct and moving on. Make a note of the question using the flag functionality, so if you have time after you have answered the rest of the questions, you can revisit it.

Guidance for answering specific OT questions

STEP 3: Read the requirement first!

The requirement will be stated in bold text in the exam. Identify what you are being asked to do, any technical knowledge required and **what type of OT question** you are dealing with. Look for key words in the requirement such as "which **TWO** of the following," "which of the following is **NOT**"

Guidance for answering specific OT questions

STEP 4: Apply your technical knowledge to the data presented in the question.

Take your time working through questions, and make sure to read through each answer option with care. OT questions are designed so that each answer option is plausible. Work through each response option and eliminate those you know are incorrect.

Skills checkpoint 1 covers this technique in detail through application to an exam-standard question.

Skill 2: Effective use of spreadsheets

It is very likely that you will be required to use the spreadsheet response option in the constructed workspace for Section C questions. It is imperative that you know how to use the spreadsheet functions to prepare accurate and easy to follow calculations.

The key steps are outlined as follows:

Step 1 Start by setting up the spreadsheet.

Step 2 Ensure the numbers are in a separate cell from the label.

Step 3 Always use formulae to perform calculations.

Step 4 Make efficient use of the SUM function.

Step 5 Only use separate workings for longer calculations and cross reference any workings using '=' rather than retyping the numbers.

Step 6 Does your answer look reasonable?

Skill 3: The UK tax system and its administration

You must study the whole syllabus in order to pass the TX – UK exam, but having the administration knowledge at your fingertips will give you extra time in the exam to answer the more difficult questions.

This Skills checkpoint gives you a list of quick fire questions to help you learn the basic information.

Skills checkpoint 3 covers this technique in detail through application to an exam-standard question.

Skill 4: Section C questions

Section C questions contain one 10-mark question and two 15-mark questions. One 15-mark question will focus on income tax and the other one will focus on corporation tax. This means that you know roughly what to expect and you can use proformas where relevant to help with the long calculations. Discursive elements will be relatively short. 10-mark questions often cover more than one tax and are designed to act as a bridge question between TX – UK and the higher-level exam, ATX.

A step-by-step technique for attempting these questions is outlined as follows:

Step 1 Read the requirements first and read them carefully.

Step 2 Learn and use the proformas where relevant.

Step 3 Input easy numbers from the question directly into your proforma.

Step 4 Always use formulae to perform basic calculations.

Step 5 Show longer workings separately.

Skills checkpoint 4 covers this technique in detail through application to an exam-standard question.

Skill 5: How to approach your TX – UK exam

You can answer your TX – UK exam in whatever order you prefer. It is important that you adopt a strategy that works best for you. We would suggest that you decide on your preferred approach and practise it by doing a timed mock exam before your real exam.

A suggested approach to tackling your TX – UK exam is outlined as follows:

Complete Section A first – allocated time 54 minutes

Tackle any easier OT questions first. Often, discursive style questions can be answered quickly, saving more time for calculations. Do not leave any questions unanswered. Even if you are unsure, make a reasoned guess.

Complete Section B next – allocated time 54 minutes

You will have 18 mins of exam time to allocate to each of the three OT case questions in Section B. Use the same approach to OT questions as discussed for Section A.

There will normally be discursive and numerical questions within each case. Again, it is better to tackle the discursive type questions first and make a reasoned guess for any questions you are unsure on.

Finally, complete Section C – allocated time 72 minutes

Start with the question you feel most confident with.

Skills checkpoint 5 covers this technique in detail through application to an exam-standard question.

Exam success skills

Passing the TX – UK exam requires more than applying syllabus knowledge and demonstrating the specific TX – UK skills; it also requires the development of excellent exam technique through question practice.

We consider the following six skills to be vital for exam success. The Skills checkpoints show how each of these skills can be applied specifically to the TX – UK exam.

Exam success skill 1

Managing information

Questions in the exam will present you with a lot of information. The skill is how you handle this information to make the best use of your time. The key is determining how you will approach the exam and then actively reading the questions.

Advice on developing managing information

Approach

The exam is three hours long. There is no designated 'reading' time at the start of the exam, however, one approach that can work well is to start the exam by spending 10–15 minutes carefully reading through all of the questions to familiarise yourself with the exam.

Once you feel familiar with the exam, consider the order in which you will attempt the questions; always attempt them in your order of preference. For example, you may want to leave to last the question you consider to be the most difficult.

If you do take this approach, remember to adjust the time available for each question appropriately – see Exam success skill 6: Good time management.

If you find that this approach doesn't work for you, don't worry – you can develop your own technique.

Active reading

You must take an active approach to reading each question. Focus on the requirement first, underlining key verbs such as 'prepare', 'comment', 'explain', 'discuss', to ensure you answer the question properly. Then read the rest of the question, underlining and annotating important and relevant information, and making notes of any relevant technical information you think you will need.

Exam success skill 2

Correct interpretation of the requirements

The active verb used often dictates the approach that written answers should take (eg 'explain', 'discuss', 'evaluate'). It is important you identify and use the verb to define your approach. The **correct interpretation of the requirements** skill means correctly producing only what is being asked for by a requirement. Anything not required will not earn marks.

Advice on developing correct interpretation of the requirements

This skill can be developed by analysing question requirements and applying this process:

Step 1 Read the requirement

Firstly, read the requirement a couple of times slowly and carefully and highlight the active verbs. Use the active verbs to define what you plan to do. Make sure you identify any sub-requirements and any topics which you are specifically told you do not need to cover in your answer. Also note the number of marks available for each requirement or sub-requirement, as this will indicate the time available and hence the level of depth required in your answer.

Step 2 Read the rest of the question

By reading the requirement first, you will have an idea of what you are looking out for as you read through the scenario. This is a great time saver and means you do not end up having to read the whole question in full twice. You should do this in an active way – see Exam success skill 1: Managing Information.

Step 3 Read the requirement again

Read the requirement again to remind yourself of the exact wording before starting your written answer. This will capture any misinterpretation of the requirements or any missed requirements entirely. This should become a habit in your approach and, with repeated practice, you will find the focus, relevance and depth of your answer plan will improve.

Exam success skill 3

Answer planning: Priorities, structure and logic

This skill requires the planning of the key aspects of an answer which accurately and completely responds to the requirement.

Advice on developing answer planning: Priorities, structure and logic

Everyone will have a preferred style for an answer plan. For example, it may be a mind map, bullet-pointed lists or simply annotating the question. Choose the approach that you feel most comfortable with, or, if you are not sure, try out different approaches for different questions until you have found your preferred style.

For 10-mark Section C questions, it can be useful to draw up a separate answer plan in the format of your choosing (eg a mind map or bullet-pointed lists). You will want to remind yourself of key facts from the scenario to avoid having to reread the question – you should at the very least make a few notes including vital information such as the following key factors:

- Nature of the taxpayer – is it an individual or a company?
- For individuals – their age, any family relationships, their residence and domicile status, whether they are a basic, higher or additional rate taxpayer, and whether the have used their CGT annual exempt amount/IHT exemptions
- For companies – their ownership structure and group relationships
- Relevant dates – the year end(s) of businesses, dates of actual or proposed transactions, the date that a business started, dates of gifts (or death!) for IHT

Exam success skill 4

Efficient numerical analysis

This skill aims to maximise the marks awarded by making clear to the marker the process of arriving at your answer. This is achieved by laying out an answer such that, even if you make a few errors, you can still get some credit for your calculations. It is vital that you do not lose marks purely because the marker cannot follow what you have done.

Advice on developing efficient numerical analysis

This skill can be developed by applying the following process:

Step 1 Use a standard proforma working where relevant

If answers can be laid out in a standard proforma, always plan to do so. This will help the marker to understand your working and allocate the marks easily. It will also help you to work through the figures in a methodical and time-efficient way.

Step 2 Show your workings

Keep your workings as clear and simple as possible and ensure they are cross-referenced to the main part of your answer.

Step 3 Keep moving!

It is important to remember that, in an exam situation, it is difficult to get every number 100% correct. The key is therefore ensuring you do not spend too long on any single calculation. If you are struggling with a solution then make a sensible assumption, state it and move on.

Exam success skill 5

Effective writing and presentation

Written answers should be presented so that the marker can clearly see the points you are making, presented in the format specified in the question. The skill is to provide efficient written answers with sufficient breadth of points that answer the question, in the right depth, in the time available.

Advice on developing effective writing and presentation

Step 1 Use headings

Using the headings and sub-headings from your answer plan will give your answer structure, order and logic. This will ensure your answer links back to the requirement and is clearly signposted, making it easier for the marker to understand the different points you are making. Underlining your headings will also help the marker.

Step 2 Write your answer in short, but full, sentences

Use short, punchy sentences with the aim that every sentence should say something different and generate marks. Write in full sentences, ensuring your style is professional.

Step 3 Do your calculations first and explanation second

Questions often ask for an explanation with supporting calculations. The best approach is to prepare the calculation first but then add the explanation before the calculation. Performing the calculation first should enable you to explain what you have done.

Exam success skill 6

Good time management

This skill means planning your time across all the requirements so that all tasks have been attempted at the end of the three hours available and actively checking on time during your exam. This is so that you can flex your approach and prioritise requirements which, in your judgment, will generate the maximum marks in the available time remaining.

Advice on developing good time management

The exam is three hours long, which translates to 1.8 minutes per mark. At the beginning of a question, work out the amount of time you should be spending on each requirement. If you take the approach of spending 10–15 minutes reading and planning at the start of the exam, adjust the time allocated to each question accordingly.

Keep an eye on the clock

Aim to attempt all requirements but be ready to be ruthless and move on if your answer is not going as planned. The challenge for many is sticking to planned timings. Be aware, this is difficult to achieve in the early stages of your studies and be ready to let this skill develop over time.

Question practice

Question practice is a core part of learning new topic areas. When you practise questions, you should focus on improving the Exam success skills – personal to your needs – by obtaining feedback or through a process of self-assessment.

Sitting this exam as a computer-based exam and practicing as many exam-style questions as possible in the ACCA Exam Practice Platform will be the key to passing this exam. You should attempt questions under timed conditions and ensure you produce full answers to the discussion parts as well as doing the calculations. Also ensure that you attempt all mock exams under exam conditions.

ACCA have launched a free on-demand resource designed to mirror the live exam experience helping you to become more familiar with the exam format. You can access the platform via the Study Support Resources section of the ACCA website navigating to the CBE question practice section and logging in with your myACCA credentials.

1 An introduction to VAT

Learning objectives

On completion of this chapter, you should be able to:

	Syllabus reference no.
Recognise the circumstances in which a person must register or deregister for VAT (compulsory) and when a person may register or deregister for VAT (voluntary).	F1(a)
Recognise the circumstances in which pre-registration input VAT can be recovered.	F1(b)
Explain the conditions that must be met for two or more companies to be treated as a group for VAT purposes, and the consequences of being so treated.	F1(c)
Calculate the amount of VAT payable/recoverable.	F2(a)
Understand how VAT is accounted for and administered.	F2(b)
Recognise the tax point when goods or services are supplied.	F2(c)
Explain and apply the principles regarding the valuation of supplies.	F2(e)
Recognise the principal zero rated and exempt supplies.	F2(f)
Recognise the circumstances in which input VAT is non-deductible.	F2(g)
Recognise the relief that is available for impairment losses on trade debts.	F2(h)
Understand the treatment of the sale of a business as a going concern.	F2(i)

Exam context

Section A questions on basic value added tax (VAT) topics could include identification of the date for registration and dealing with impairment losses. Section B questions could also include computing the amount of VAT payable or recoverable. In Section C, registration requirements may be examined in more detail. Make sure that you know the difference between the historical test and the future test, and the dates by which HMRC must be notified and registration takes effect. Do not overlook pre-registration input VAT. You may also be required to calculate the VAT due for a return period. Watch out for non-deductible input tax and check the dates if there are impairment losses.

Chapter overview

- **An introduction to VAT**
  - The scope of value added tax (VAT)
    - The nature of VAT
    - What is VAT charged on?
    - VAT rates charged
    - Valuation of supplies
  - VAT registration
    - Who must register?
    - Deregistration
    - Voluntary registration
    - Implications of registration
    - Group registration
    - Pre-registration expenses: recovery of input tax
  - Transfer of going concern
  - Administration of VAT
    - VAT periods
    - The VAT return
    - Electronic filing
    - Substantial traders for VAT
    - Refunds of VAT
  - Tax point
  - Relief for impairment losses (bad debts)
  - Recovery of input tax
    - Capital items
    - Non-deductible input tax
    - Motoring expenses

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1 The scope of value added tax (VAT)

1.1 The nature of VAT

Value added tax (VAT) is a tax on turnover, not on profits. The basic principle is that the VAT should be borne by the final consumer. Registered traders may deduct the tax which they suffer on supplies to them (input tax) from the tax which they charge to their customers (output tax) at the time this is paid to HM Revenue and Customs (HMRC). So, at each stage of the manufacturing or service process, the net VAT paid is on the value added at that stage.

Illustration 1: The VAT charge

During 2024, a forester sells wood to a furniture maker for £100 plus VAT. The furniture maker uses this wood to make a table and sells the table to a shop for £150 plus VAT of 20%. The shop then sells the table to the final consumer for £300 plus VAT.

Required

Show how VAT will be accounted for on these transactions.

Solution

VAT will be accounted for to HMRC as follows:

	Cost	*Input tax 20%*	*Net sale price*	*Output tax 20%*	*Payable to HMRC*
	£	£	£	£	£
Forester	0	0	100	20	20
Furniture maker	100	20	150	30	10
Shop	150	30	300	60	30
					60

Because the traders involved account to HMRC for VAT charged less VAT suffered, their profits for income tax or corporation tax purposes are based on sales and purchases net of VAT.

1.2 What is VAT charged on?

VAT is charged on taxable supplies of goods and services made in the UK by a taxable person in the course or furtherance of any business carried on by them. It is also chargeable on the import of goods into the UK (whether they are imported for business purposes or not, and whether the importer is a taxable person or not) and, on certain services received from abroad, if a taxable person receives them for business purposes.

KEY TERM

Taxable supply: A **taxable supply** is a supply of goods or services made in the UK, other than an exempt supply. This means that standard-rated supplies and zero-rated supplies are taxable supplies.

PER alert

In order to fulfil Performance Objective 15 (PO15) Tax computations and assessments of the PER, you must demonstrate that you can prepare or contribute to computations or assessments of indirect tax liabilities. You can apply the knowledge you obtain from this chapter to help to demonstrate this competence.

1.3 VAT rates charged

A **taxable supply** is either **standard-rated** or **zero-rated**. The standard rate is 20%.

Certain supplies, which fall within the classification of standard rate supplies, are charged at a reduced rate of 5%. An example is the supply of domestic fuel.

Zero-rated supplies are taxable at 0%. A taxable supplier whose outputs are zero rated but whose inputs are standard rated will obtain repayments of the VAT paid on purchases.

An exempt supply **is not chargeable to VAT.** A person making exempt supplies is unable to recover VAT on inputs. Therefore, the exempt supplier has to shoulder the burden of VAT. Of course, they may increase their prices to pass on the charge, but they cannot issue a VAT invoice which would enable a taxable customer to obtain a credit for VAT, since no VAT is chargeable on their supplies.

Supply	Examples
Standard-rated	• Most goods/services
Zero-rated	• Non-luxury food • Books • Children's clothes and footwear
Exempt	• Burial/cremation services • Health services • Non-profit-making education • First- and second-class postage stamps

Essential reading

See Chapter 24 Section 1 of the Essential reading for an example showing the effect on businesses of having standard-rated, zero-rated and exempt outputs and details on what is meant by 'supplies.'

The Essential reading is available as an Appendix of the digital edition of the Course Book.

1.4 Valuation of supplies

KEY TERM

Value of supply: Is the VAT-exclusive price on which VAT is charged.

Consideration of supply: Is the amount paid in money or money's worth.

Using the standard rate of 20%:

Value + VAT = consideration

£100 + £20 = £120 VAT-inclusive price

Formula to learn

The VAT proportion of the consideration is known as the 'VAT fraction.' It is:

$$\frac{\text{Rate of tax}}{100 + \text{rate of tax}} = \frac{20}{100 + 20} = \frac{1}{6}$$

For example, the VAT element of the VAT-inclusive price of £120 is £120 × 1/6 = £20.

Provided the consideration for a bargain made at arm's length is paid in money, the value for VAT purposes is the VAT exclusive price charged by the trader. If it is paid in something other than money, as in a barter of some goods or services for others, it must be valued and VAT will be due on the value.

If the price of goods is effectively reduced with money off coupons, the value of the supply is the amount actually received by the taxpayer.

VAT is calculated on the invoice price less all trade discounts. If a prompt payment discount is offered, VAT must be calculated on the actual amount received. The trader must either provide details of the discount on the invoice or must invoice for the full amount and then issue a credit note if the discount is taken up.

2 VAT registration

2.1 Who must register?

(a) Registration is compulsory if:
   (i) At the end of any month, taxable supplies over the previous 12 months have exceeded £90,000 (historical test); or
   (ii) In the next 30 days, taxable supplies are expected to exceed £90,000 (future test).

(b) This requirement may be waived if the trader can satisfy HM Revenue & Customs (HMRC) that taxable supplies in the following 12-month period will be less than £88,000.

(c) Taxable supplies is the VAT-exclusive value of all zero rated and standard rated supplies.

(d) The trader has 30 days to notify HMRC.

(e) Registration is effective from:
   (i) The first day of the second month after the £90,000 was exceeded, or from an earlier date if they and the trader agree (historical test); and
   (ii) Start of 30-day period if future 30-day test applies.

(f) When determining the value of a person's taxable supplies for the purposes of registration, supplies of goods and services that are capital assets of the business are to be disregarded, except for non zero rated taxable supplies of interests in land.

Note that if a trader does not register when they should, output VAT will still be due from the date that they should have registered for VAT.

Exam focus point

The registration limit and deregistration limit are given in the tax tables. Be sure you know the difference between the historic and future tests.

Illustration 2: VAT registration and dates

At the end of every month, a trader must calculate their cumulative turnover of taxable supplies for the previous 12 months to date.

Fred started to trade cutlery on 1 January 2024. Sales (excluding VAT) were £8,500 a month for the first nine months and £9,000 a month thereafter.

Required

From what date should Fred be registered for VAT?

Solution

Sales to 31 October 2024	£85,500
Sales to 30 November 2024	£94,500 (exceeds £90,000)

Fred must notify his liability by 30 December 2024 (**not 31 December**) and will be registered and charge VAT from 1 January 2025.

Activity 1: Notifying HMRC

Jack commenced trading on 1 January 2024. His quarterly turnover (spread evenly over the quarter) is as follows:

Quarter ended	Turnover
	£
31 March 2024	7,500
30 June 2024	13,500
30 September 2024	18,000
31 December 2024	24,000
31 March 2025	36,000
30 June 2025	39,000

Required

By what date is Jack required to notify HMRC that he is liable to register for VAT?

Solution

Activity 2: Notification and registration dates

Jill commenced trading on 1 January 2024 with monthly sales as follows:

Goods	Turnover per month
	£
Goods ABC (standard rated)	8,000
Goods DEF (zero rated)	7,000
Service GHJ (exempt)	10,000

On 14 April 2024, Jill signed a contract to provide £30,000 of Goods ABC and £47,000 of Goods DEF on 2 May 2024 in addition to the monthly supplies detailed above.

By what date is Jill required to notify HMRC that she is liable to register for VAT, and from which date must she be registered?

- ○ Notify by 30 June 2024 and register from 1 July 2024
- ○ Notify by 30 May 2024 and register from 1 June 2024
- ○ Notify by 14 April 2024 and register from 14 April 2024
- ○ Notify by 13 May 2024 and register from 14 April 2024

Solution

2.2 Deregistration

If the business ceases to make taxable supplies, it must deregister. If in the next year, VAT-exclusive taxable supplies will be below £88,000, the business may deregister.

There is a deemed supply of business assets such as plant, equipment or trading inventory when a business ceases to be VAT registered. However, if the transfer is of a going concern, it is outside the scope of VAT.

2.3 Voluntary registration

A person making taxable supplies which do not exceed the registration threshold may nonetheless register for VAT voluntarily.

Advantages:

- Able to reclaim input VAT
- Imposes discipline on the business to keep accurate records
- Lends credibility to a business

Disadvantages

- Adds to administrative costs
- Reduces the competitive edge and deters business if the customers are not VAT registered

For example, consider a trader who has one input during the year which cost £1,000 plus £200 VAT; they work on the input which becomes their sole output for the year and they decide to make a profit of £1,000.

- If they are not registered, they will charge £2,200 and will not be able to reclaim the £200 VAT on the original purchase.
- If they are registered, they will charge £2,000 plus VAT of £400. Their customer will have input tax of £400 which they will be able to recover if they, too, are registered.

2.4 Implications of registration

(a) Traders making standard or zero rated supplies must charge VAT on all taxable supplies using tax invoices.

(b) These traders can recover related input tax suffered.

(c) However, input tax is not recoverable on:

  (i) Cars (unless involved in motor trade)

  (ii) UK customer entertaining

  (iii) Non-business purchases

(d) Exempt traders (eg an insurance company):

  (i) Register (as they make no taxable supplies)

  (ii) Recover input VAT suffered

Activity 3: Reclaiming VAT

Chester Ltd, which is registered for VAT, incurred the following expenditure (including VAT) during the quarter ended 31 December 2024.

	£
New car for salesperson (private use)	14,500
Three new vans	28,200
Second-hand container lorry	29,370
Entertaining	
– UK customers	4,935
– Employees	5,250

Required

How much VAT can be reclaimed in respect of the above and on what amount will Chester be entitled to claim capital allowances?

Solution

2.5 Group registration

Companies may apply for group VAT registration. The effects and advantages of group registration are as follows:

- Allows group companies to nominate one company in the group to prepare one VAT return for the companies in the group (the 'representative member').
- Intra-group transactions are disregarded for VAT purposes.
- It is administratively much easier.
- All members of group registration are jointly and severally liable for VAT liability.

2.5.1 Who can form a group?

The holding entity must **control subsidiaries** (ie by voting power) and the entities within the group registration must have **a fixed establishment in the UK**. The **holding** entity can be a **company, sole trader or partnership** but the **rest of the group members must be corporate**. The holding entity must control the UK company(/ies) that they wish to form a group with.

Entities must elect to form a VAT group, it is not automatic, and not all eligible entities need to be included.

2.6 Pre-registration expenses: Recovery of input tax

VAT incurred on goods and services before registration can be treated as input tax and recovered from HMRC subject to certain conditions.

If the claim is for input tax suffered on **goods** purchased prior to registration, the following conditions must be satisfied.

(a) The goods were acquired for the purpose of the business which either was carried on, or was to be carried on by them, at the time of supply.

(b) The goods have **not been supplied onwards or consumed before the date of registration** (although they may have been used to make other goods which are still held).

(c) The VAT must have been incurred in the **four years prior to the effective date of registration**.

If the claim is for input tax suffered on the supply of **services** prior to registration, the following conditions must be satisfied.

(a) The services were supplied for the purposes of a business which either was carried on or was to be carried on by them at the time of supply.

(b) The services were supplied within the **six months prior to the date of registration**.

Input tax attributable to **supplies made before registration** is not deductible even if the input tax concerned is treated as having been incurred after registration.

Activity 4: Input VAT

Bilbo Ltd commenced trading on 1 August 2024 and applied to register for VAT with effect from 1 October 2024.

Prior to registration, it had incurred VAT on the following VAT exclusive amounts:

	£
Accountancy fees – invoice dated 10 March 2024	5,000
Van purchased new on 23 June 2024	8,000
Inventory of spare parts as on 30 September 2024	12,000

What input VAT can Bilbo Ltd claim in respect of each of these items assuming the van and inventory are still held on 1 October 2024?

Accountancy fees £ ______

Van £ ______

Inventory £ ______

Solution

3 Transfer of going concern

When the assets of a VAT registered business are sold, each asset will be subject to VAT at the appropriate rate.

When, however, the **whole business is sold as a going concern** then the supply of assets is outside the scope of VAT and **no VAT is chargeable**.

There are conditions for the transfer of a going concern to apply:

- The purchaser of the business must also be VAT registered.
- The same kind of business will be carried on.
- There is no significant break in trading.

4 Administration of VAT

The administration of VAT is dealt with by HM Revenue and Customs (HMRC).

Local offices are responsible for the local administration of VAT and for providing advice to registered persons whose principal place of business is in their area. They are controlled by regional collectors.

From time to time, a registered person will be visited by HMRC staff from a local office to ensure that the law is understood and is being applied properly. If a trader disagrees with any decision as to the application of VAT given by HMRC, they can ask their local office to reconsider the decision.

If HMRC believe that a trader has failed to make returns, or if they believe those returns to be incorrect or incomplete, they may issue **assessments of the VAT** due to the best of their judgement. The time limit for making assessments is normally four years after the end of a VAT period, but this is extended to 20 years in the case of fraud, dishonest conduct, certain registration irregularities and the unauthorised issue of VAT invoices.

A trader may appeal to the Tax Tribunal in the same way as an appeal may be made for income tax and corporation tax (see earlier in this Course Book). VAT returns and payments shown thereon must have been made before an appeal can be heard.

4.1 VAT periods

The VAT period (also known as the tax period) is the period covered by a VAT return. It is usually three calendar months. The return shows the total input and output tax for the tax period.

HMRC allocate VAT periods according to the class of trade carried on (ending in June, September, December and March; July, October, January and April; or August, November, February and May), to spread the flow of VAT returns evenly over the year. When applying for registration, a trader can ask for VAT periods which fit in with their own accounting year. It is also possible to have VAT periods to cover accounting systems not based on calendar months.

A registered person whose input tax will regularly exceed their output tax can elect for a one-month VAT period, but will have to balance the inconvenience of making 12 returns a year against the advantage of obtaining more rapid repayments of VAT.

Certain small businesses may submit an annual VAT return (see later in this chapter).

4.2 The VAT return

The regular VAT return to HMRC is made on form VAT 100.

Input and output tax figures must be supported by the original or copy tax invoices, and records must be maintained for six years.

4.3 Electronic filing

Nearly all VAT registered businesses must file their VAT returns online and make payments electronically.

The time limit for submission and payment is one month plus seven days after the end of the VAT period. For example, a business which has a VAT quarter ending 31 March 2025 must file its VAT return and pay the VAT due by 7 May 2025.

4.3.1 Making tax digital (MTD)

For VAT periods starting on or after 1 April 2019, most businesses which are VAT-registered and have a taxable turnover above the registration threshold must follow the Making Tax Digital (MTD) rules. Other VAT-registered businesses (eg those who are voluntarily registered) can choose to follow the MTD rules.

Many VAT records must be kept digitally under MTD. These include business name and address, registration number, and details of the supplies the business makes and receives (eg time of supply, value of supply and VAT rate charged or input tax reclaimed). The records can be kept by using a software package, which is also used to submit the return directly to HMRC, or other software such as spreadsheets to keep the records which are then submitted using bridging software to connect to HMRC.

Businesses which do not follow MTD rules continue to submit their returns electronically through the HMRC website.

The time for submission of returns and payment of VAT are not changed by the introduction of MTD.

4.4 Substantial traders for VAT

Once a trader's **total VAT liability for the 12 months or less to the end of a VAT period exceeds £2.3 million, the trader must start making payments on account of each quarter's VAT liability during each quarter**.

Two payments on account of each quarter's VAT liability must usually be made. The first is due one month before the end of the quarter and the second is due at the end of the month which is the final month of the quarter. The amount of each payment on account made during the quarter is 1/24 of the trader's annual VAT liability in the period in which the threshold is exceeded. For the purposes of calculating the payments on account (but not for the purposes of the £2.3 million threshold for entry into the scheme), a trader's VAT due on imports from overseas is ignored.

If the VAT liability for the quarter exceeds the total of the payments on account, a balancing payment is due one month after the end of the quarter to bring the total payments for that quarter to the amount of the VAT liability. If the VAT liability for the quarter is less than the total of the payments on account, HMRC will make a repayment to the trader.

Payments must be made and the quarterly VAT return submitted by the last day of the relevant month (ie there is no additional seven days). Payments must be made electronically.

A penalty system (see the next chapter) applies to late payments.

Illustration 3: Substantial traders

Large Ltd is liable to make payments on account of VAT calculated at £250,000 each for the quarter ended 31 December 2024.

Required

What payments/repayment are due if Large Ltd's VAT liability for the quarter is calculated as:

1 £680,000?

2 £480,000?

Solution

1

Date	Payment
30 November 2024	Payment on account of £250,000
31 December 2024	Payment on account of £250,000
31 January 2025	Balancing payment of £680,000 – £250,000 – £250,000 = £180,000 with submission of VAT return for quarter

2

Date	Payment/repayment
30 November 2024	Payment on account of £250,000
31 December 2024	Payment on account of £250,000
31 January 2025	Repayment by HMRC of £480,000 – £250,000 – £250,000 = £20,000 on submission of VAT return for quarter

Once a trader is in the scheme, the payments on account are reviewed annually at a set time. However, the trader **can apply to reduce payments on account at any time if the total VAT liability for the latest four returns is less than 80% of the total on which the payments on account are currently based**, ie the VAT liability decreases by 20% or more. Conversely, **HMRC**

may increase the payments on account in between annual reviews if the trader's total 12-month VAT liability increases by 20% or more, ie the VAT for the last four periods is at least 120% of the amount on which the payments on account are currently based. A trader can apply to **leave the scheme if their 12-month VAT liability is below £1,800,000**. A trader whose VAT liability at the annual review was below £2.3 million will be automatically removed from the scheme six months later.

A trader may elect to pay their actual VAT liability monthly instead of making payments on account. For example, the actual liability for January would be due at the end of February. The trader can continue to submit quarterly returns as long as HMRC is satisfied the trader is paying sufficient monthly amounts.

4.5 Refunds of VAT

There is a four-year time limit on the right to reclaim overpaid VAT. This time limit does not apply to input tax which a business could not have reclaimed earlier because the supplier only recently invoiced the VAT, even though it related to a purchase made some time ago. Nor does it apply to overpaid VAT penalties.

If a taxpayer has overpaid VAT and has overclaimed input tax by reason of the same mistake, HMRC can set off any tax, penalty or interest due to them against any repayment due to the taxpayer and repay only the net amount. In such cases, the normal four-year time limit for recovering VAT, penalties, interest, etc by assessment does not apply.

HMRC can refuse to make any repayment which would unjustly enrich the claimant. They can also refuse a repayment of VAT where all or part of the tax has, for practical purposes, been borne by a person other than the taxpayer (eg by a customer of the taxpayer) except to the extent that the taxpayer can show loss or damage to any of their businesses as a result of mistaken assumptions about VAT.

5 Tax point

Each tax invoice is assigned to a return period according to its tax point.

The basic tax point is when goods are made available, or when services are completed.

If the invoice is issued or payment is received before the basic tax point, the earlier date becomes the tax point.

If the earlier date rule does not apply and the invoice is issued within 14 days after the basic tax point, the invoice date can become the tax point.

Illustration 4: Tax point

Julia sells a sculpture to the value of £1,000 net of VAT. She receives a payment on account of £250 plus VAT on 25 April 2024. The sculpture is delivered on 28 May 2024. Julia's VAT return period is to 30 April 2024. She issues an invoice on 4 June 2024.

Required

Outline the tax point(s) and amount(s) due.

Solution

A separate tax point arises in respect of the £250 deposit and the £750 balance payable.

Julia should account for VAT as follows.

Deposit

25 April 2024: Tax at 20% × £250 = £50

This is accounted for in her VAT return to 30 April 2024. The charge arises on 25 April 2024 because payment is received before the basic tax point (which is 28 May 2024 – date of delivery).

Balance

4 June 2024: Tax at 20% × £750 = £150

This is accounted for on the VAT return to 31 July 2024. The charge arises on 4 June because the invoice was issued within 14 days of the basic tax point of 28 May 2024 (delivery date).

Activity 5: Tax points

On 31 May, Bang Ltd ordered a new printing machine and on 16 June paid a deposit of £6,000. The machine was despatched to Bang Ltd on 30 June. On 18 July, an invoice was issued to Bang Ltd for the balance due of £54,000. This was paid on 23 July.

Required

1 What is the tax point for the £6,000 deposit?

2 What is the tax point for the balance of £54,000?

Solution

6 Relief for impairment losses (bad debts)

A trader may claim a **refund of VAT on amounts unpaid by debtors if:**

(a) They have accounted for VAT;

(b) The debt is **over six months old**; and

(c) The debt has been **written off** in the creditor's accounts.

If the debtor later pays all (or part) of the amount owed, the corresponding amount of VAT repaid must be paid back to HMRC.

Impairment loss relief claims must be made within **four years of the time the impairment loss became eligible for relief** (in other words, within four years and six months from when the payment was due).

Illustration 5: Impairment loss relief

Elixir Ltd has VAT accounting periods ending on 31 March, 30 June, 30 September and 31 December. The company sold standard rated goods to Ben on 1 July 2024. The VAT inclusive amount on the invoice was £2,000 and payment was due by 15 July 2024. Ben paid Elixir Ltd

£500 as part payment on 1 October 2024 but then became untraceable and Elixir Ltd has written off the remaining debt.

Required

State how much impairment loss relief can be claimed by Elixir Ltd and the earliest VAT return on which the claim can be made.

Solution

The amount of the loss is £2,000 – £500 = £1,500.

The VAT on the loss is £1,500 × 1/6 = £250, so this amount can be claimed as impairment loss relief.

Payment was due on 15 July 2024 and so the six-month period ended on 15 January 2025. The earliest VAT return on which an impairment loss relief claim is that for the quarter ending 31 March 2025.

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7 Recovery of input tax

Not all input VAT is deductible. For input tax to be deductible the payer must be a taxable person in the course of their business.

7.1 Capital items

There is no distinction between capital and revenue expenditure for VAT. (Note that capital and revenue expenditure are sometimes called asset expenditure and expenses.) A manufacturer paying VAT on the purchase of plant to make taxable supplies will be able to obtain a credit for all the VAT immediately.

7.2 Non-deductible input tax

The following input tax is **not deductible**:

(a) **VAT on purchased cars** not used wholly for business purposes. VAT on cars is never reclaimable unless the car is acquired new for resale or is acquired for use in or leasing to a taxi business, a self-drive car hire business or a driving school (see below for treatment of car expenses).

(b) **50% of the VAT on leased cars which are 'qualifying cars.'** The 50% restriction covers any private use of the car. A qualifying car is one on which input tax has not already been irrecoverable.

(c) **VAT on business entertaining** where the cost of the entertaining is not a tax deductible trading expense unless it is entertainment of overseas customers in which case the input tax is deductible.

(d) VAT on expenses incurred on domestic accommodation for directors or proprietors of a business.

(e) **VAT on non-business items passed through the business accounts.** If goods are bought partly for business use, the purchaser may:

  (i) Deduct all the input tax, and account for output tax in respect of the private use; or

  (ii) Deduct only the business proportion of the input tax.

(f) VAT which does not relate to the making of supplies by the buyer in the course of a business.

7.3 Car expenses

7.3.1 Accessories and maintenance costs

Input VAT can be reclaimed if accessories for business use are fitted after the original purchase of a car and a separate invoice is raised.

If a car is used for any business purposes (even if it is also used for private purposes) any VAT charged on repair and maintenance costs can be treated as input tax.

7.3.2 Fuel

If a business pays for fuel which is only used for business purposes, it can claim all the input tax paid on that fuel. However, many businesses will pay for fuel which is used for private motoring by employees.

If a business does provide fuel for private and business use to an employee, but the employee reimburses the business the full cost of the private fuel, there is an actual taxable supply by the business valued at the amount received from that employee. The business can claim its input tax on all fuel, but then must account for output tax on the amount paid by the employee. HMRC will accept that the full cost of all private fuel has been reimbursed where a log is kept recording private miles and the employee pays a fuel-only mileage rate that covers the average fuel cost (on its website, HMRC publishes a set of such rates for different sizes of engine).

If a business provides fuel to its employees for private use without charge or at a charge below the full cost, there is a deemed taxable supply.

The business then has the following options for how to account for VAT on fuel:

(a) **Not to claim any input tax in respect of fuel** purchased by the business. **No output tax is charged**. In effect, the fuel is not brought into the VAT system at all.

(b) **Claim input VAT only on the fuel purchased for business journeys**. This requires the business to keep detailed mileage records of business and private use. **No output tax is charged in respect of private use.** In effect, the private fuel is not brought into the VAT system.

(c) **Claim input tax on all fuel purchased and charge output tax based either on the full cost of the private fuel supplied** (again, this requires detailed mileage records to be kept) **or the VAT fuel scale charge** which reflects the deemed output in respect of private use. The fuel scale charge is based on the CO_2 emissions of the car and the length of the period**.**

Illustration 6: Fuel scale charge

Iain is an employee of ABC Ltd. He has the use of a car with CO_2 emissions of 176 g/km for one month and a car with CO_2 emissions of 208 g/km for two months during the quarter ended 31 August 2024. ABC Ltd pays all the petrol costs in respect of both cars without requiring Iain to make any reimbursement in respect of private fuel. Total petrol costs for the quarter amount to £390 (including VAT). ABC Ltd wishes to use the fuel scale charge as detailed records of private mileage have not been kept.

VAT scale rates (VAT inclusive) for three-month periods:

CO_2 emissions	£
175	437
205	544

Required

What is the VAT effect of the above on ABC Ltd?

Solution

Value added tax for the quarter:

	£
Car 1	
£437 × 1/3 =	146
Car 2	
£544 × 2/3 =	363
	509

	£
Output tax:	
– 1/6 × £509	85
Input tax	
– 1/6 × £390	65

Activity 6: Fuel

John is an employee of BBT Ltd. He has the use of a car which is used for both business and private mileage for the current VAT quarter.

BBT Ltd pays all the petrol costs in respect of the car totalling £1,200 of which 20% is for private mileage.

The relevant quarterly scale charge is £508.

Both figures are inclusive of VAT.

1 **What is the VAT effect of the above on BBT Ltd if it uses the quarterly scale charge?**

- ○ Output VAT of £85, input VAT of £40
- ○ Output VAT of £85, input VAT of £200
- ○ Output VAT of £17, input VAT of £200
- ○ Output VAT of £17, input VAT of £40

2 **What is the VAT effect of the above on BBT Ltd if it charges John for the private fuel?**

- ○ Output VAT of £40, input VAT of £48
- ○ Output VAT of £48, input VAT of £48
- ○ Output VAT of £48, input VAT of £200
- ○ Output VAT of £40, input VAT of £200

Solution

Chapter summary

An introduction to VAT

The scope of value added tax (VAT)

The nature of VAT
- Tax on turnover, borne by final consumer
- Registered traders deduct input tax from output tax and pay net VAT to HMRC

What is VAT charged on?
- Taxable supplies of goods/services made in the UK by a taxable person
- Import of goods into the UK

VAT rates charged
- Standard 20%
- Zero 0%
- Exempt

Valuation of supplies
- Value of supply = VAT exclusive price
- Consideration for a supply = amount paid ie value + VAT
- VAT fraction = 1/6

VAT registration

Who must register?
- If taxable turnover exceeds £90,000 in past 12 months (historic) or will be in next 30 days (future)

Deregistration
- If cease to make taxable supplies
- Voluntary if taxable supplies next year will be below £88,000

Voluntary registration
- Able to reclaim input VAT
- But adds to admin costs

Implications of registration
- Must charge VAT on taxable supplies
- Can recover related input VAT
- Exempt traders cannot register nor recover input VAT

Group registration
- Group nominates 'representative member' who prepares one VAT return for entire group
- Intragroup sales are ignored
- All members of group are jointly and severally liable

Pre-registration expenses: recovery of input tax
- Goods/services acquired/supplied for the purpose of the business
- Goods not supplied onwards or consumed before registration date
- VAT on goods must have been incurred in 4 years before registration date
- Services supplied within 6 months before registration date

Transfer of going concern

- If assets sold each has VAT at the appropriate rate
- If a transfer of a going concern (TOGC) then no VAT chargeable
- Conditions to be met:
  - Purchaser VAT registered
  - Same kind of business carried on
  - No significant break in trade

Administration of VAT

VAT periods

- Quarterly – normal

The VAT return

- Form VAT 100
- Maintain records for six years

Electronic filing

- Most must file returns and make payments online
- Due a month and seven days after end of VAT period

Substantial traders for VAT

- Payments on account if VAT liability exceeds £2.3 million

Refunds of VAT

- 4 year limit on right to reclaim overpaid VAT

Tax point

- Earliest of:
  - Despatch date
  - Invoice date
  - Cash received

Relief for impairment losses (bad debts)

- Refund of VAT on bad debts if:
  - Trader has accounted for VAT
  - Debt is over six months old
  - Debt has been written off in the creditor's accounts

Recovery of input tax

Capital items

- No distinction between capital and revenue expenditure for VAT

Non-deductible input tax

- Cars
- 50% of VAT on leased cars that are qualifying cars
- Business entertaining
- Expenses incurred on domestic accommodation for directors/ proprietors
- Non-business items
- VAT not related to making of supplies by buyer in course of business

Motoring expenses

- Input VAT on accessories and maintenance after original purchase can be reclaimed
- Input VAT can be reclaimed on fuel used only for business purposes
- Several options if business provides fuel for private use

Knowledge diagnostic

1. **Charge to value added tax (VAT)**

   VAT is charged on taxable supplies made by taxable persons in the course of their trade.

   Some supplies are taxable (standard rate, reduced rate, zero rate). Others are exempt. Make sure you understand the difference and can work out VAT from the VAT-exclusive and VAT-inclusive price.

2. **Registration**

   A trader becomes liable to register for VAT if its taxable supplies over a 12-month period exceeds £90,000 or in the next 30 days its taxable supplies will exceed £90,000. A trader may also register voluntarily.

   Group registration allows only one VAT return to be prepared for the group as a whole.

3. **Transfer of going concern**

   VAT is not charged on the transfer of a going concern.

4. **Administration of VAT**

   VAT periods can be a month, a quarter or a year. Payment made electronically usually by seven days from the end of the month following the VAT period. Substantial traders must make payments on account.

5. **Tax point**

   Basic tax point is when goods are made available or when services are completed. Actual tax point can be earlier or later.

6. **Impairment losses (bad debts)**

   A trader can claim refund of output tax on impairment losses which remain unpaid six months from the time that payment is due and have been written off.

7. **Recovery of input tax**

   General principle is that input tax is only recoverable in relation to business use. No input tax is recoverable on cars with private use and business entertaining (other than overseas customers). Input tax can be recovered on fuel, but output tax may be charged on private fuel using the fuel scale charge.

Further study guidance

Question practice

Now try the following from the Further question practice bank (available in the digital edition of the Course Book):

Section A:

Q46, Q47, Q48

Section C:

Q109 Ongoing Ltd

Further reading

The following technical articles are available on ACCA's website:

- Value added tax Part 1
- Cars

The article called 'Value added tax – Part 1' considers VAT registration and deregistration, and output and input VAT. These topics are covered in this chapter.

There is also an article called 'Cars' that explains the implications of acquiring, running or having the use of a car for income tax, corporation tax, value added tax (VAT) and national insurance contribution (NIC).

https://www.accaglobal.com/uk/en/student/exam-support-resources/fundamentals-exams-study-resources/f6/technical-articles.html#Technical-articles---UK-exams

You are strongly advised to read these articles in full as part of your preparation for the TX exam.

Activity answers

Activity 1: Notifying HMRC

Annual turnover does not exceed £90,000 until 31 March 2025 (on a month-by-month basis). Jack does not become liable to register until then. He must notify HMRC within 30 days (ie by 30 April 2025). He will then be registered from 1 May 2025 or an earlier date by mutual agreement.

Spreadsheet

Edit Format

100%

	A	B	C
1	Month	Supplies (£)	Cumulative 12 months' sales (£)
2	January 2024	2,500	
3	February 2024	2,500	
4	March 2024	2,500	
5	April 2024	4,500	
6	May 2024	4,500	
7	June 2024	4,500	
8	July 2024	6,000	
9	August 2024	6,000	
10	September 2024	6,000	
11	October 2024	8,000	
12	November 2024	8,000	
13	December 2024	8,000	63,000[1]
14	January 2025	12,000	72,500[2]
15	February 2025	12,000	82,000[3]
16	March 2025	12,000	91,500
17	April 2025	13,000	100,000
18	May 2025	13,000	108,500
19	June 2025	13,000	117,000

[1] =SUM(B2:B13)

[2] =SUM(B3:B14)

[3] =SUM(B4:B15)

Videos can be viewed online by accessing your ebook version on VitalSource.

Activity 2: Notification and registration dates

The correct answer is: Notify by 13 May 2024 and register from 14 April 2024

The historical test would be breached on 31 May 2024. Taxable supplies in the first five months amount to 5 × (£8,000 + £7,000) = £75,000, plus the special orders placed in May take the total to above £90,000.

The future test is breached on 14 April 2024 because, on that date, Jill knows her taxable supplies in the next 30 days will exceed the registration threshold: £8,000 + £7,000 + £30,000 + £47,000 = £92,000. Notification is required 30 days from the test (count 14 April as day 1) and registration takes effect from 14 April 2024.

Activity 3: Reclaiming VAT

Input tax reclaimed

	£
Vans (£28,200 × 1/6)	4,700
Lorry (£29,370 × 1/6)	4,895
Entertaining employees (£5,250 × 1/6)	875
	10,470

Capital allowance values

	£
Car	14,500
Vans (£28,200 – £4,700) =	23,500
Lorry (£29,370 – £4,895) =	24,475

Activity 4: Input VAT

Accountancy fees £ 0

Van £ 1,600

Inventory £ 2,400

	£
Accountancy fees – not recoverable as > 6 months prior to registration	0
Van – in use post-registration £8,000 × 20%	1,600
Inventory – still held at date of registration £12,000 × 20%	2,400
	4,000

Activity 5: Tax points

1 16 June

The basic tax point is the date the goods are made available on 30 June. However, the actual tax point for the deposit is the earlier payment.

2 30 June

The basic tax point is the date the goods are made available on 30 June. The later issue of the invoice does not displace this date because the invoice was issued more than 14 days after the basic tax point.

Activity 6: Fuel

1 The correct answer is: Output VAT of £85, input VAT of £200

If John is not charged for the private fuel, BBT Ltd can reclaim input VAT of £200 (£1,200 × 20/120) and will have to account for output VAT of £85 (£508 × 20/120) based on the scale charge. The answers output VAT of £17 or input VAT of £40 reduces the VAT based on the private mileage percentage which is not relevant when using the quarterly scale charge.

2 The correct answer is: Output VAT of £40, input VAT of £200

If John is charged £240 (£1,200 × 20%) for the private fuel, BBT Ltd will reclaim input VAT of £200 and will have to account for output VAT of £40 (£240 × 1/6) based on the charge to John. The answer £48 assumes £240 is the VAT exclusive price (ie VAT is 20% × £240).

2 Further aspects of VAT

Learning objectives

On completion of this chapter, you should be able to:

	Syllabus reference no.
List the information that must be given on a VAT invoice.	F2(d)
Understand when the penalties for late submission/filing and late payment, and the interest for late payment will be applied.	F2(j)
Understand the VAT treatment of imports, exports and trade outside the UK.	F2(k)
Understand postponed accounting for VAT on imports.	F2(l)
Understand the operation of, and when it will be advantageous to use, the VAT special schemes:	
• Cash accounting scheme	F3(a)(i)
• Annual accounting scheme	F3(a)(ii)
• Flat rate scheme	F3(a)(iii)

Exam context

The topics in this chapter could be examined in any of Sections A, B or C. Penalties are an important topic as they are used to enforce the VAT system, but the special schemes are designed to make life simpler for small businesses. You may be asked to advise on the VAT treatment of imports and exports outside the UK. The flat rate scheme may also lead to a small extra profit for the business, depending on the flat rate percentage and the level of inputs.

Chapter overview

Further aspects of VAT

- VAT invoices
- Penalties
  - Late returns
  - Late payment penalty
  - Late payment interest
- Overseas VAT
  - Imports and exports of goods
  - Supplies of services
- Special schemes
  - Cash accounting scheme
  - Annual accounting scheme
  - Flat rate

Videos can be viewed online by accessing your ebook version on VitalSource.

1 VAT invoices

A taxable person making a taxable supply to another VAT registered trader must supply a VAT invoice within 30 days of the time of supply, and must keep a copy. There is no requirement to supply a VAT invoice if the supply is exempt or if the supply is to a non-VAT registered customer.

The invoice must show:

(a) The supplier's name, address and registration number
(b) The date of issue, the tax point and an invoice number
(c) The name and address of the customer
(d) A description of the goods or services supplied, giving for each description the quantity, the unit price, the rate of VAT and the VAT exclusive amount
(e) The rate of any cash discount
(f) The total invoice price excluding VAT (with separate totals for zero-rated and exempt supplies)
(g) Each VAT rate applicable and the total amount of VAT

If an invoice is issued, and a change in price then alters the VAT due, a credit note or debit note to adjust the VAT must be issued.

Credit notes must give the reason for the credit (such as 'returned goods'), and the number and date of the original VAT invoice. If a credit note makes no VAT adjustment, it should state this.

A less detailed VAT invoice may be issued by a taxable person where the invoice is for a total including VAT of up to £250. Such an invoice must show:

(a) The supplier's name, address and registration number
(b) The date of the supply
(c) A description of the goods or services supplied
(d) The rate of VAT chargeable
(e) The total amount chargeable including VAT

Zero-rated and exempt supplies must not be included in less detailed invoices.

VAT invoices are not required for payments of up to £25 including VAT which are for telephone calls, or car park fees, or made through cash operated machines. In such cases, input tax can be claimed without a VAT invoice.

Every VAT registered trader must **keep records** for **six years**.

Essential reading

See Chapter 25 Section 1 for information on keeping VAT records.

The Essential reading is available as an Appendix of the digital edition of the Course Book.

2 Penalties

There are penalties for:

- Late filing (submission)
- Late payment
- Errors

There is also:

- Late payment interest

2.1 Penalties for late filing

Exam focus point

The new penalties for VAT replace the default surcharge system and will only be examined in the context of **quarterly returns**.

- A business incurs a penalty point for every quarterly return that it submits late.
- Penalty points expire after two years unless the threshold of four points has been reached.
- Once the threshold has been reached, a penalty of £200 is charged. A further £200 is charged for each subsequent late return until the business has completed a 'period of compliance.'
- The business must then submit VAT returns on time over a 12-month period of compliance (four quarterly returns) for the points to be reset to zero.

Number of penalty points	Penalty
	£
Threshold = 4 points	200
Subsequent late returns	200

2.2 Late payment penalties and interest

- Fixed penalties are charged depending on how late the payment is (VAT due × penalty percentage – rates given in tax rates and allowances in the exam).
- In addition, a 4% daily penalty is incurred if the payment is more than 30 days late (VAT due × 4% × n-30/365).
- Late payment interest is also charged from the due date until the VAT payment is made (VAT due × n/12 or n/365 – read the question).
- The late payment interest rate is given on the tax rates and allowances in the exam.

Penalties and interest:

Days late	Fixed penalty (VAT due × penalty percentage)	Daily penalty (daily charge: VAT due × 4% × n-30/365)	Interest (overdue VAT × n/12 or n/365)
Up to 15 days	None	None	Yes
16–30 days	2%	None	Yes
More than 30 days	4%	4% daily penalty (based on the number of days above 30 days)	Yes

Exam focus point

You must read the question carefully when calculating charges to see whether you need to use the number of months or the number of days for interest payments and daily penalties. Unless otherwise instructed, you are generally required in TX to calculate to the nearest month, but this makes little sense for a daily charge and so you may be asked to calculate the daily penalty or interest charge based on the number of days. Read the question carefully. (Note that the fixed penalty is not time apportioned.)

Activity 1: Late filing and late payments

Kayoss Ltd submitted all VAT returns on time up to March 2023/24. After that, the returns and payments were submitted as follows:

Quarter ended	VAT liability	Return and payment days late
	£	
30 June 2024	45,000	15 days
30 September 2024	50,000	17 days
31 December 2024	35,000	32 days
31 March 2025	40,000	7 days

1 **What is the late payment interest charge for the quarter ended 30 June 2024? (Use the number of days for your calculation and round to the nearest whole number.)**

£ [ ]

2 **Select the correct option to indicate whether there will be a penalty charge and/or an interest charge relating to the quarter ended September 2024.**

Interest: [▼]

Penalty: [▼]

Pull down list

- No
- Yes

3 **What is the total penalty charge for the quarter ended 31 December 2024? (You should calculate the daily penalty charge using days.)**

[▼]

Pull down list

- £1,400
- £1,408
- £1,523
- £1,608

4 **What is the total late payment and late filing penalties and interest for the quarter ended 31 March 2025?**

- ○ £200
- ○ £259
- ○ £50
- ○ £281

2.3 Penalties for errors

The common penalty regime for making errors in tax returns discussed in Chapter 17 also applies to VAT returns.

Errors on a VAT return not exceeding the greater of:

- £10,000
- 1% × net VAT turnover for return period (maximum £50,000)

may be **corrected on next return**.

Other errors should be notified to HMRC in writing (eg by letter or email).

In both cases, a penalty for the error may be imposed. Correction of an error on a later return is not, of itself, an unprompted disclosure of the error and fuller disclosure is required for the penalty to be reduced.

Default interest (see next) on the unpaid VAT as a result of the error is only charged where the limit is exceeded for the error to be corrected on the next VAT return.

2.4 Default interest

Interest (not deductible in computing taxable profits) is charged on VAT which is the subject of an assessment (where returns were not made or were incorrect), or which could have been the subject of an assessment but was paid before the assessment was raised. This interest is sometimes called 'default interest'. It runs from the date the VAT should have been paid to the actual date of payment but cannot run for more than three years before the assessment or voluntary payment.

3 Overseas VAT

Videos can be viewed online by accessing your ebook version on VitalSource.

The terms **import and export** refer to purchases and sales of goods with countries **outside the UK**.

Exam focus point

The UK left the EU in January 2020 and, on 1 January 2021 it left the EU's customs union and VAT system. From that date, the VAT treatment of imports and exports of goods to or from the UK is the same regardless of which country they are to or from. In January 2021, a new system called postponed accounting was introduced. For the purposes of the TX – UK exam, it should be assumed that postponed accounting applies to all **imports of goods**.

3.1 Imports and exports of goods

Export/import outside the UK	VAT treatment
UK VAT registered trader exports (sale of goods) outside the UK	Zero-rated sales
UK trader imports (purchases) from outside the UK	• Account for import VAT on the VAT return covering the date the goods imported • Reclaim on same VAT return

VAT is charged on goods imported into the UK and it used to be collected at the time of importation. Postponed accounting means that VAT no longer has to be paid immediately at the port of entry, but is declared on the VAT return as output VAT. It can be reclaimed as input VAT on the same VAT return. The system prevents goods being held at customs until the VAT is paid and also improves cash flow.

3.2 Supplies of services

(a) The general rule is that supplies of services to any business customer are charged where the customer is established/situated.

(b) If a UK VAT registered trader is supplied with services from another country, the place of supply is deemed to be the UK. The UK trader accounts for output VAT on the supply but the equivalent amount is the input VAT for the supply. So, the transaction is usually neutral.

(c) Supplies of services from a UK VAT registered trader to another business outside the UK are usually outside the scope of UK VAT as the place of supply is not in the UK.

4 Special schemes

PER alert

One of the competencies required to fulfil **Performance Objective 15 (PO15) Tax computations and assessments** of the PER is to explain the basis of tax calculations, and interpret the effect of current legislation and case law. You can apply the knowledge you obtain from this section of the Course Book to help to demonstrate this competence.

Special schemes can make VAT accounting easier and ease cash flow for certain types of trader.

4.1 Cash accounting scheme

(a) A trader whose annual taxable turnover (exclusive of VAT) does not exceed £1.35 million can apply for it.

(b) A trader can join only if all returns and VAT payments are up to date.

(c) VAT can be accounted for on the basis of cash paid and received, thus giving automatic impairment loss (bad debt) relief.

(d) A trader must cease using the cash accounting scheme as soon as turnover exceeds £1.6 million; however, the trader can continue to bring outstanding VAT into account on a cash basis for a further six months after leaving the scheme.

4.2 Annual accounting scheme

(a) Only available to traders who are up to date with VAT payments and regularly pay VAT to HMRC (not to those who normally receive payments).

(b) Available for traders whose taxable turnover (exclusive of VAT) for the 12 months starting on their application to join the scheme is **not expected to exceed £1.35 million**.

(c) All traders with turnover of up to £1.6 million can stay in the scheme.

(d) Only file one return per year but make payments on account (POA) throughout the year via direct debit.

(e) POA = 90% previous year's net VAT liability in nine monthly payments starting at the end of the fourth month of the year.

(f) Balance and return due within **two months after year end**.

Advantages of annual accounting:

- Only **one VAT return each year** so fewer occasions to trigger a default surcharge
- Ability to **manage cash flow** more accurately
- **Avoids need for quarterly calculations for input tax recovery**

Disadvantages of annual accounting:

- Need to **monitor future taxable supplies** to ensure turnover limit not exceeded
- **Timing of payments have less correlation to turnover** (and hence cash received) by business

- **Payments based on previous year's turnover may not reflect current year turnover** which may be a problem if the scale of activities has reduced.

4.3 Flat rate scheme

(a) The optional flat rate scheme simplifies the way in which small traders calculate their VAT liability.

(b) The scheme can be used if VAT-exclusive taxable turnover for the next 12 months is not expected to exceed £150,000.

(c) To calculate the VAT liability, simply apply a flat rate percentage to total (VAT-inclusive) turnover.

(d) The flat rate percentage will usually depend upon the trade sector into which the trader falls. If the trader makes no, or limited, purchases of goods, a rate of 16.5% applies so there is very little advantage to using the scheme.

(e) A 1% reduction off the flat rate percentage can be made by businesses in their first year of VAT registration.

(f) No input VAT is recovered.

(g) The scheme means there is no need to calculate and record output and input VAT; however, VAT at 20% is still treated as being charged where a supply is made to a registered trader, and therefore a VAT invoice must still be issued.

(h) A trader must leave the scheme if total annual VAT-inclusive turnover > £230,000.

Exam focus point

The flat rate percentage will be given to you in your exam.

Illustration 1: Flat rate scheme

Brian is an accountant who has been registered for VAT for many years and undertakes work for individuals and for business clients. In a VAT year, the business client work amounts to £75,000 and Brian issues VAT invoices totalling £90,000 (£75,000 plus VAT at 20%). Turnover from work for individuals totals £18,000, inclusive of VAT. Brian provides some exempt financial services which amount to £2,000 in a VAT year. The flat rate percentage for an accountancy business is 14.5%. Brian also incurs annual standard rated expenses of £4,800 inclusive of VAT relating to the taxable supplies.

Required

Advise Brian whether he should register for the flat rate scheme.

Solution

Under the flat rate scheme VAT due to HMRC will be £90,000 + £18,000 + £2,000 = £110,000 (VAT inclusive amount) × 14.5% = £15,950.

Under the normal VAT rules, the net VAT due to HMRC would be:

	£
£75,000 × 20%	15,000
£18,000 × 1/6	3,000
Output VAT	18,000
Less input VAT £4,800 × 1/6	(800)
VAT due to HMRC	17,200

Brian should therefore register for the flat rate scheme as he will save VAT of £17,200 – £15,950 = £1,250. The reduced VAT administration cost of using the flat rate scheme should also be taken into account.

Activity 2: Flat rate or not flat rate

Cool Kids Ltd has annual turnover of £91,900. 85% of the sales are standard rated and 15% are zero rated. Standard rated expenses are £14,100.

All figures are exclusive of VAT.

The relevant flat rate percentage for Cool Kids Ltd trade is 11%.

1 **What is the VAT liability if Cool Kids Ltd does not use the flat rate scheme?**

- ○ £10,669
- ○ £15,560
- ○ £12,803
- ○ £15,623

2 **What is the VAT liability if Cool Kids Ltd does use the flat rate scheme?**

- ○ £10,109
- ○ £12,131
- ○ £11,828
- ○ £9,008

Solution

Chapter summary

Further aspects of VAT

VAT invoices

- Supplier's name, address and registration number
- Tax point and invoice number
- Name and address of customer
- Description of transaction
- Rate of cash discount
- Rate of VAT
- VAT – exclusive amount
- Amount of VAT

Penalties

Late returns

- Penalty point per late return
- £200 penalty for 4 points
- £200 penalty for subsequent late returns

Late payment penalty

- See tax tables
- VAT due × penalty %
- Daily penalty if > 30 days late

Late payment interest

- Due date until VAT paid
- Rate × overdue VAT × n/12 or n/365
- Late payment interest rate on tax tables

Overseas VAT

Imports and exports of goods

- Sales zero rated
- Purchases – account for VAT on VAT return, reclaim on same VAT return

Supplies of services

- Generally treated as being supplied in country where customer is situated
- Supplies of services to a UK business from overseas are charged to UK VAT
- Supplies of services by a UK VAT registered trader to business customers outside the UK are generally outside the scope of UK VAT

Special schemes

Cash accounting scheme

- Annual turnover not exceeding £1.35 million
- Tax point = receipt/payment of cash
- Automatic impairment loss relief
- Cease when turnover > £1.6 million

Annual accounting scheme

- Annual turnover in next 12m not exceeding £1,350,000
- One return due two months after year end
- Pay 90% of previous year's liability over nine months starting in month four
- Balance due within two months after year end

Flat rate

- Taxable supplies < £150,000
- Optional
- VAT liability = % (industry specific) × VAT inclusive sales
- Still charge VAT to customer
- Admin simplified

Knowledge diagnostic

1. **VAT invoice**

   There are various items of information that must be shown on a VAT invoice which is used to charge VAT.

2. **Penalties**

   There are penalties for late filing of a VAT return and late payment of VAT. For late filing, there are £200 penalties once a business has reached its penalty points threshold. For late payment, there are penalties based on how late the payment is which are 2% and 4% of the amount outstanding at certain points and possible daily penalties.

3. **Overseas VAT**

   Imports from outside the UK are subject to VAT and exports outside the UK are zero rated.

   Postponed accounting for goods imported allows import VAT to be declared on the VAT return as output VAT. Input VAT is reclaimed on the same return.

4. **Special schemes**

   Special schemes exist to aid traders.

   Cash accounting gives automatic relief for impairment losses.

   Annual accounting simplifies the submission of VAT returns.

   Flat rate scheme makes the calculation of the VAT liability easier.

Further study guidance

Question practice

Now try the following from the Further question practice bank (available in the digital edition of the Course Book):

Section A:

Q49, Q50, Q51

Section C:

Q110 Kiln Ltd and Log Ltd

Further reading

The following technical article is available on ACCA's website:

- Value added tax Part 2

The article covers VAT returns, VAT invoices, penalties, overseas aspects of VAT and special VAT schemes.

https://www.accaglobal.com/uk/en/student/exam-support-resources/fundamentals-exams-study-resources/f6/technical-articles.html#Technical-articles---UK-exams

You are strongly advised to read this article in full as part of your preparation for the TX exam.

Activity answers

Activity 1: Late filing and late payments

1 £ $\boxed{143}$

£45,000 × 7.75% × 15/365 = £143

Note that a penalty point will be incurred for **late filing** but **no late payment penalty** will be charged because the liability was paid in under 16 days.

2 Interest: $\boxed{\text{Yes}}$

Penalty: $\boxed{\text{Yes}}$

There will be a penalty charge of 2% relating to **late payment** because the payment is made within 16 and 30 days of the due date. There is no penalty relating to **late filing** because the threshold of 4 points has not been reached. September 2024 incurs a penalty point and so the company now has two penalty points.

Late payment interest is always charged.

3 $\boxed{\text{£1,408}}$

A fixed 4% **late payment** penalty is charged because the VAT was paid over 30 days late.

(£35,000 × 4% = £1,400)

There is an additional **daily late payment penalty** for 2 days (32 days – 30 days).

(£35,000 × 4% × 2/365 = £8)

£1,400 + £8 = £1,408

There is no penalty relating to **late filing** because the threshold of 4 points has not been reached. December 2024 incurs a penalty point and so the company now has three penalty points.

Distractors:

£1,400: penalty without daily penalty

£1,523: £35,000 × 4% × 32/365

£1,608: includes two penalty payments

4 The correct answer is: £259

There will be no penalty charge relating to **late payment** because the payment is made within 15 days of the due date. However, March 2025 incurs a penalty point for **late filing** and so the company now has four penalty points and this triggers a £200 penalty.

Late payment interest is always charged (£40,000 × 7.75% × 7/365 = £59).

Total charge = £200 + £59 = £259

Distractors:

£50: late payment interest

£200: late filing penalty

£281: includes daily penalty £250 + (£40,000 × 4% × 7/365)

Activity 2: Flat rate or not flat rate

1 The correct answer is: £12,803

	£
Output VAT	
£91,900 × 85% × 20%	15,623
Input VAT	
£14,100 × 20%	(2,820)
VAT payable	12,803

The answer £10,669 treats the amounts as VAT-inclusive ((£91,900 @ 85%/6) – (£14,100/6)). The answer £15,560 calculates output tax on total sales ((£91,900 @ 20%) – £2,820)). The answer £15,623 does not deduct input tax.

2 The correct answer is: £11,828

Using the flat rate scheme

((£91,900 × 85% × 1.20) + (£91,900 × 15%)) × 11% = £11,828

The answer £10,109 is the VAT-exclusive amount times the flat rate (£91,900 @ 11%). The answer £12,131 calculates the VAT-inclusive amount on all sales, ie (£91,900 × 1.20) × 11%. The answer £9,008 deducts the input VAT which is only recoverable under the normal VAT rules (£11,828 – £2,820).

1

An introduction to VAT

Essential reading

1 The scope of VAT

1.1 Example: Standard-rated, zero-rated and exempt supplies

Here are figures for three traders, the first with standard-rated outputs, the second with zero-rated outputs and the third with exempt outputs. All their inputs are standard-rated. The standard rate is 20%.

	Standard-rated	*Zero-rated*	*Exempt*
	£	£	£
Inputs	20,000	20,000	20,000
VAT	4,000	4,000	4,000
	24,000	24,000	24,000
Outputs	30,000	30,000	30,000
VAT	6,000	0	0
	36,000	30,000	30,000
Pay/(reclaim)	2,000	(4,000)	0
Net profit	10,000	10,000	6,000

VAT legislation lists zero-rated, reduced rate and exempt supplies. There is no list of standard-rated supplies. Therefore, any supplies that do not appear on the zero-rated, reduced rate or exempt lists will be assumed to be standard rated by default.

1.2 Supplies of goods

Goods are supplied if exclusive ownership of the goods passes to another person.

The following are treated as supplies of goods:

- The supply of any form of power, heat, refrigeration or ventilation, or of water
- The grant, assignment or surrender of a major interest (the freehold or a lease for over 21 years) in land
- Taking goods permanently out of the business for the non-business use of a taxable person or for other private purposes including the supply of goods by an employer to an employee for their private use
- Transfers under an agreement contemplating a transfer of ownership, such as a hire purchase agreement

Gifts of goods are normally treated as sales at cost (so VAT is due). However, business gifts are not supplies of goods if:

(a) The total cost of gifts made to the same person does not exceed £50 in any 12-month period (if the £50 limit is exceeded, output tax will be due in full on the total of gifts made; once the limit has been exceeded, a new £50 limit and new 12-month period begin)

(b) **The gift is a sample** (unlimited number of samples allowed)

1.3 Supplies of services

Apart from a few specific exceptions, **any supply which is not a supply of goods and which is done for a consideration is a supply of services**. Consideration is any form of payment in money or in kind, including anything which is itself a supply.

A supply of services also takes place if:

- Goods are lent to someone for use outside the business;
- Goods are hired to someone; or
- Services bought for business purposes are used for private purposes.

1.4 Taxable persons

The term 'person' includes individuals, partnerships (which are treated as single entities, ignoring the individual partners), companies, clubs, associations and charities. If a person is in business making taxable supplies, the value of these supplies is called the taxable turnover. If a person's taxable turnover exceeds the registration limit, they are a taxable person and should be registered for VAT.

1.5 Types of supply

VAT legislation lists zero-rated, reduced-rated and exempt supplies. There is no list of standard-rated supplies. If a trader makes a supply, you need to categorise that supply for VAT as follows:

Step 1 Consider if it is a zero-rated supply. If not:

Step 2 Consider if it is exempt. If not:

Step 3 Consider if it is reduced-rated supply. If not:

Step 4 The supply is standard rated.

Exam focus point

In the exam, you will not be expected to categorise all the zero-rated and exempt supplies. The main supplies in each group are listed below.

1.6 Zero-rated supplies

The following are some common items on the **zero-rated list**.

(a) Human and animal food

(b) Printed matter used for reading (eg books, newspapers)

(c) Construction work on new homes or the sale of the freehold, or a lease over 21 years (at least 20 years in Scotland), of new homes by builders

(d) Exports of goods

(e) Clothing and footwear for children and certain protective clothing (eg crash helmets)

1.7 Exempt supplies

The following are some common items on the **exempt** list:

- Sales of freeholds of buildings (other than commercial buildings within three years from completion) and leaseholds of land and buildings of any age including a surrender of a lease
- Financial services
- Insurance

1.8 Exceptions to the general rule

There are many exceptions to the general rule. For example, the zero-rated list states that human food is zero-rated. However, the legislation then states that food supplied in the course of catering (eg restaurant meals, hot takeaways) is not zero-rated. Luxury items of food (eg crisps, peanuts, chocolate covered biscuits) are also not zero-rated.

In terms of exemptions, we are told that financial services are exempt. However, the legislation then goes on to state that this does not include credit management, except if the credit management is by the person who also granted the credit. Great care must be taken when categorising goods or services as zero rated, exempt or standard rated. It is not as straightforward as it may first appear.

2

Further aspects of VAT

Essential reading

1 VAT records

Every VAT registered trader must keep records for six years, although HMRC may sometimes grant permission for their earlier destruction. They may be kept on paper, on microfilm or microfiche or on computer. However, there must be adequate facilities for HMRC to inspect records.

All records must be kept up to date and in a way which allows:

- The calculation of VAT due; and
- Officers of HMRC to check the figures on VAT returns.

The following records are needed:

- Copies of VAT invoices, credit notes and debit notes issued
- A summary of supplies made
- VAT invoices, credit notes and debit notes received
- A summary of supplies received
- A VAT account
- Order and delivery notes, correspondence, appointment books, job books, purchases and sales books, cash books, account books, records of takings (such as till rolls), bank paying-in slips, bank statements and annual accounts
- Records of zero-rated and exempt supplies, gifts or loans of goods, taxable self supplies and any goods taken for non-business use

Glossary

Chapter 1: An introduction to VAT

Consideration of supply: Is the amount paid in money or money's worth.

Taxable supply: A **taxable supply** is a supply of goods or services made in the UK, other than an exempt supply. This means that standard-rated supplies and zero-rated supplies are taxable supplies.

Value of supply: Is the VAT-exclusive price on which VAT is charged.

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