



Chartered
Institute of
Taxation

Excellence in Taxation

Draft legislation: The Value Added Tax (Amendment) Regulations 2018 and accompanying documents

Response by the Chartered Institute of Taxation

1 Introduction

- 1.1 The Chartered Institute of Taxation (CIOT) is pleased to set out its comments on the draft Value Added Tax (Amendment) Regulations 2018, as well as the draft Explanatory Memorandum to those Regulations, the draft VAT Notice on Making Tax Digital for VAT, and the draft Addendum to that draft VAT Notice, which were all published for consultation on 18 December 2017.
- 1.2 As an educational charity, our primary purpose is to promote education in taxation. One of the key aims of the CIOT is to work for a better, more efficient, tax system for all affected by it – taxpayers, their advisers and the authorities. Our comments and recommendations on tax issues are made solely in order to achieve this aim; we are a non-party-political organisation.
- 1.3 Our stated objectives for the tax system include:
 - A legislative process which translates policy intentions into statute accurately and effectively, without unintended consequences.
 - Greater simplicity and clarity, so people can understand how much tax they should be paying and why.
 - Greater certainty, so businesses and individuals can plan ahead with confidence.
 - A fair balance between the powers of tax collectors and the rights of taxpayers (both represented and unrepresented).
 - Responsive and competent tax administration, with a minimum of bureaucracy.

2 Executive summary

- 2.1 We remain concerned at the timing of these changes. Firstly, because the start date for mandation in April 2019 closely coincides with the UK's exit date from the EU, and businesses (and HMRC) may simply be overwhelmed with the nature and scale of changes required in a confined period of time. Secondly, notwithstanding the

Government / HMRC's promises of over a year of testing, the vast majority of businesses will not have had enough time – certainly not a year - to choose and trial software, as it is currently a long way from being widely available. We also note the pressure on HMRC resourcing to deliver a significant number of projects in such a short period of time, which we are concerned will lead to unwelcome implementation problems.¹

- 2.2 We remain concerned that the revenue benefits of mandatory MTD appear exaggerated, and the costs to business understated, and that the 'business case' for mandating MTD for VAT (or indeed mandating MTD for business generally) still hasn't been made out. Indeed, the Office for Budget Responsibility continue to rate the estimated revenue benefits as having a high level of uncertainty. We would encourage HMRC to critically appraise the MTD project focussed on the use of compulsion, based on all feedback received from external stakeholders, to prevent simply ploughing ahead with a project that many fear will be costly and disruptive to businesses, and not deliver the intended revenue benefits.
- 2.3 In any event, we would encourage HMRC to consider the two key elements of MTD for VAT (digital record keeping, and submitting the return digitally) separately. The original proposals for MTD centred on reduction of mistakes through digital record keeping (element one). However, digitally linking underlying records, and digitising the VAT return process (element two) are a significant complicating factor in MTD for VAT. We see no reason why these requirements cannot be separated; perhaps mandating digital record keeping for businesses first, with the requirement for digital links and VAT return submission potentially following later.
- 2.4 There is insufficient clarity and explanation around some of the IT-related elements, such as what a 'software program' is, and what constitutes a 'digital link'. The Regulations and Notice should be capable of being understood by non-IT-technical readers, without the need for IT advice.
- 2.5 The 'soft landing' for digital links should be clearly explained and consistent in the examples provided. More importantly, it should be prescribed by law (in a part of the Notice which has the force of law), rather than making all digital links mandatory from the outset, but allowing non-compliant businesses relief from penalties or other sanctions as a non-statutory 'concession'. The interaction with the 'soft landing' for late filing penalties within the first twelve months of MTD² also requires clarification.
- 2.6 The draft Explanatory Memorandum and draft Notice continue to include messages around MTD which are unsubstantiated; for example '*Making Tax Digital (MTD) will bring the tax system into line with what businesses expect from other service providers: a modern digital experience*' and '*using software for all your calculations will reduce the risk of errors in your returns*'.
- 2.7 The examples set out in the draft Notice and the draft Addendum are generally helpful. However, they would be more helpful if there was some consistency between them, both in terms of their numbering and content, so that businesses can easily cross-reference between them and obtain the greatest assistance. Even though it might not be HMRC's intention, readers will look at these closely to see within which example their business 'fits'.

¹ The introduction of the Trust Registration Service, and access through the Agent Services Account, is perhaps one such example.

² See, for example, <https://www.gov.uk/government/consultations/making-tax-digital-tax-administration>

2.8 Our detailed comments on each of the documents is set out in the following sections.

3 Draft Regulations

3.1 General comments

3.1.1 The language used in the Regulations needs to be as plain and straightforward as possible. This is particularly important here as the Regulations deal not only with legal and tax technical matters, but also IT obligations.

3.1.2 It should be possible in relevant places to reproduce the wording of the Regulation in the Notice. For example, the definition of ‘functional compatible software’ should be clear enough in the Regulations to be transposed into the Notice (at paragraph 3.2). At the moment, slightly different language is used, which begs the question whether the Notice is intended to mean something different to the Regulations.

3.2 Regulation 1 – timing

3.2.1 We remain concerned by the introduction of these measures with effect from 1 April 2019, for several reasons.

3.2.2 Firstly, it closely coincides with the expected timing of the UK leaving the EU. Businesses currently do not know the extent of the changes which this will bring – both from a VAT technical, and an administrative point of view. Similarly, businesses do not really know (either through lack of communication, or lack of software availability etc) what changes they will need to make to their systems to comply with MTD. It is likely that businesses (and HMRC) will be faced with a large number of changes within a very short timeframe.

3.2.3 Secondly, the first ‘wave’ of businesses mandated into MTD are those on stagger 1 ie with a VAT return period April to June (and so on). Nearly 40% of businesses use stagger 1 and we are concerned that the largest cohort of businesses are being mandated first. This is likely to put a strain on businesses, their agents, software providers, and HMRC.

3.2.4 Thirdly, the lack of MTD-compatible software, both currently and in the near future, has the potential to cause disruption to businesses who may need to introduce, change or update software part-way through their financial year. For example, a business with a financial year end of 30 June 2019 would wish to be using MTD-compatible software at the start of its financial year ie 1 July 2018. This currently does not look feasible.

3.2.5 It also seems inconsistent with the Government’s July 2017 statement that ‘*We will start to pilot Making Tax Digital for VAT by the end of this year, starting with small-scale, private testing, followed by a wider, live pilot starting in Spring 2018. This will allow for well over a year of testing before any businesses are mandated to use the system*’.³

3.2.6 With all this in mind, we believe it would be more appropriate to extend the application of MTD for VAT in the same way that MTD for Income Tax has been deferred. A decision can then be taken on mandation when it is apparent that

³ <https://www.gov.uk/government/publications/making-tax-digital/overview-of-making-tax-digital>

software has become widely available, and the benefits of MTD substantiated. It will also allow time for businesses to test software, and to select the appropriate package.

3.2.7 In any event, the requirements of MTD for VAT should commence from the start of the first *accounting* year (rather than the prescribed accounting period) commencing on or after the mandation date. Otherwise, businesses will face additional disruption and costs if they have to change accounting systems mid-way through their accounting year. We do not understand the costings to have taken this into consideration.

3.3 Regulation 3 - Amendment of the Value Added Tax Regulations 1995

3.3.1 It is not at all clear, in the definition of '*functional compatible software*', that a spreadsheet is considered to be a 'software program'. This needs to be clearly spelled out either in the Regulations or the Notice.

3.3.2 Further, '*providing information to HMRC*' is potentially very wide and vague. We consider that this should be limited to '*submitting a VAT return to HMRC*' (or similar wording). Indeed, provision of voluntary updates and supplementary data is indeed that – voluntary – and the Regulations should simply reflect a taxpayer's legal obligations.

3.4 Regulation 6 – Insertion of new Regulation 31AA Preservation of records

3.4.1 Sub-section (3) states that '*The functional compatible software must take a form approved by the Commissioners in a specific or general direction.*' Whilst we understand that HMRC will publish (on GOV.UK) a list of MTD compatible software (which we assume will be considered 'approved'), we assume that HMRC does not intend to require specific approval of combinations of software, or software and spreadsheets etc, or in-house software.

3.4.2 To require approval would be incredibly onerous for both businesses and HMRC, although consideration needs to be given as to how to deal with any disputes around, or assurances as to whether, a business's software systems meet the requirements of being '*functional compatible software*'. The same point applies in new 32A(6).

3.5 Regulation 7 – Insertion of new 32A Recording and keeping of information in electronic form

3.5.1 Neither the draft Regulations, nor the draft Notice, explain what '*electronic form*' means. This needs to be clarified, with examples, so that businesses can ensure that they can be compliant.

3.5.2 It is unclear what data needs to be captured in relation to supplies with more than one VAT rate and / or the requirements appear to be more onerous than at present.

3.5.3 For example, subsection 3(a) requires for each supply made within the period—

- (i) the time of supply,
- (ii) the value of the supply, and
- (iii) the rate of VAT charged;

3.5.4 What is a business required to record if it makes, for example, a standard rated and a reduced rated supply on the same invoice? If there is an expectation that

businesses will need to record separately supplies at different rates of VAT, this will give rise to additional obligations which might be more onerous for many businesses, especially if this requires software changes, either because it represents more than they currently record, or because their current software / spreadsheet is not set up to capture multiple VAT rates.

3.5.5 Subsection 3(b) requires for each supply received within the period—

- (i) the time of supply,
- (ii) the value of the supply, and
- (iii) the total amount of input tax for which credit is allowable under section 26 of the Act;

3.5.6 Many businesses will simply record the invoice date, assuming that is sufficient and / or adequately reflects the time of supply. We foresee problems if HMRC strictly apply this rule where the invoice date is not also the time of supply, and it might be more appropriate for the Regulations to allow the invoice date *or* the time of supply to be recorded, and for the Notice to explain the difference between the two, and the implications for the recovery of VAT.

3.5.7 At the time of capturing the transaction in the accounting records, a business might not know the amount of input tax for which credit is allowable, particularly if the business is partially exempt. For example:

- Some businesses might record the VAT amount in full, and make a restriction later,
- Some businesses might record the transaction gross, and undertake a separate exercise to identify and calculate the amount of VAT reclaimable,
- Some businesses might reclaim a provisional percentage, but then adjust that percentage at the end of the year.

3.5.8 Therefore, the wording of subsection 3(b)(iii) will need changing to reflect these variations in record-keeping, all of which seem to be perfectly valid.

3.5.9 Subsection 3(f) requires businesses to identify for each accounting period '*the proportions of the total of the VAT exclusive value of all outputs for the period which are attributable in each case to standard rated, reduced rated, zero-rated, exempt or outside the scope outputs*'.

3.5.10 It needs to be clear what is meant by '*outside the scope outputs*'. There is currently no requirement to capture and report income which is entirely outside the scope of VAT (for example, for Box 6 of the VAT return). This provision adds additional complexity for charities and other businesses; for example, a garage which undertakes MOTs will need to record separately the MOT (outside the scope of VAT) from any servicing or repair work undertaken (standard rated) when recording the transaction in software or on a spreadsheet. Alternatively, if '*outside the scope*' is intended to mean goods and services that would have been taxable if supplied in the UK, this should be made clear.

3.5.11 We would strongly recommend that the requirements of MTD exactly mirror the existing record keeping requirements, at least in the early days of MTD. Otherwise, not only will businesses need to change their practices so as to become accustomed to digital record keeping and reporting, they will also have to make additional changes to capture this further information. On the basis that none of this information

is currently required for the correct preparation of the VAT return, it should not be a requirement to capture such data. Was this additional requirement factored into the transitional and ongoing costs for businesses?

3.5.12 We interpret sub-paragraph (8) to require businesses to have recorded the transactions in their software by the earlier of the due date of the VAT return, or the date it is actually submitted. This seems acceptable, although;

- It would be helpful to make clear, perhaps in the Notice, that an agent or bookkeeper can maintain the business's records, and that this can take place on a quarterly basis, and
- Will businesses potentially face two penalties if they fail to keep their records on time, thus leading to a failure to submit their VAT return on time? It would appear that businesses could face both a record keeping penalty, and a default surcharge (until that regime is removed). Is this the intention? If so, this should be made clear to businesses.

3.5.13 The timescale imposed by sub-paragraph (9) could in certain circumstances be incredibly short. For example, a business on stagger 1 which moves premises on 30 March would need to update this information by the end of the following day. This seems unnecessary considering the fact that this 'permanent' data does not form part of the VAT return submission. Perhaps the end of the following prescribed accounting period would be more realistic?

3.5.14 A similar point arises in relation to sub-paragraph (10). Whilst we agree that errors should be corrected without undue delay, an error by a business on stagger 1, identified on 30 June, would need to be corrected that day. Perhaps the requirement should be that the error is corrected before the due date of the VAT return, or the date it is actually submitted? In any event, these requirements should be consistent with those set out in Notice 700/45, which suggests that businesses keep a separate record of errors, before deciding at the end of the prescribed accounting period what method of adjustment is necessary.

3.6 Regulation 7 – Insertion of new 32B Exemption from the electronic recording requirements

3.6.1 In sub-paragraph (4) the term 'taxable period' is used. This is a new term and is undefined. Should reference be to 'prescribed accounting period', or alternatively the new term needs explanation.

3.6.2 It also needs to be made clear that the exemption would apply if a business can maintain digital records but cannot make VAT return submissions electronically (and vice versa).

3.7 Regulation 7 – Insertion of new 32C Election not to be exempt

3.7.1 We are sceptical as to the number of businesses who would elect not to be exempt from the requirements, but it is unclear what would happen if a business who was not mandated to use 'functional compatible software' did so and complied with the MTD requirements, without making such an election.

4 Draft Explanatory Memorandum

4.1 General comments

4.1.1 In our view, the draft Explanatory Memorandum makes statements which do not appear to be supported by evidence and are not representative of business views, such as *'It is anticipated that this will make it easier for businesses to get their tax right the first time'* and *'Making Tax Digital will improve the quality of record keeping, reducing the likelihood of mistakes ... and help businesses to manage their cash flow more effectively'*.

4.1.2 The results of our member survey (in which 1,082 members participated) suggest otherwise.⁴ For example:

- Over 95% of members consider that compulsory digital record keeping and quarterly reporting will place an additional burden on their clients.
- Around 40% of members consider that compulsory digital record keeping and quarterly reporting will increase errors by their clients, with a similar number (ie a further 40%) considering it will have limited impact. Only 1% of members felt it would lead to a significant reduction in errors, with around 9% thinking it will lead to a small reduction in errors.

4.1.3 We do not consider it appropriate for the Explanatory Memorandum to include supposition and unsupported statements.

4.2 Specific comments

4.2.1 The wording in paragraph 7.6 *'Businesses will not need to adjust their VAT reporting dates or be required to provide any more VAT information than they do already'* is misleading. It implies that there are no additional requirements being placed on businesses, when in fact (as set out elsewhere in this submission) there are. This should be made clear or, as recommended here, those additional requirements removed.

4.2.2 In paragraph 11.3, how can HMRC guarantee that for *'all sectors affected by the changes'* it *'will ensure there is software and support in place that meets their needs'*? This is a bold statement in relation to something which is largely outside HMRC's control.

4.2.3 In section 12, HMRC should commit to publishing the results of these monitoring and review activities so that all stakeholders are aware of the full impacts and benefits of MTD.

5 Draft VAT Notice

5.1 General comments

5.1.1 As with the draft Explanatory Memorandum, the draft VAT Notice makes statements which do not appear to be supported by evidence and do not appear to be representative of business views, such as *'Making Tax Digital (MTD) will bring the tax system into line with what businesses expect from other service providers: a*

⁴ See <https://www.tax.org.uk/policy-technical/submissions/making-tax-digital-ciota-and-att-member-survey>

modern digital experience, *'However, a digital link will reduce the chance of errors'*, *'However using software for all your calculations will reduce the risk of errors in your returns'*. Again, we do not consider it appropriate for the Notice to include supposition and unsupported statements.

5.1.2 Indeed, the Notice needs to be readable and understandable for all business users. It should use simple language and avoid jargon, and ensure that IT / technological terms such 'digital record', 'digital link' etc are fully explained. At the moment it assumes that many of these terms will already be understood, which we do not believe will be the case.

5.1.3 Whilst the draft Notice (and other documents) were issued for consultation, at this stage these drafts are unlikely to be read by the type of business that will turn to them when MTD becomes real. HMRC should proactively go out to real businesses to test whether they understand what is said in the Notice, and the implications for their business.

5.1.4 The draft Notice does not currently cover a range of important issues which, in our view, should be included, such as the consequences of non-compliance with the rules (ie what penalties might be applied, and what are the rights of appeal), how to appoint an agent etc – even if that simply constitutes links to other guidance. Readers should be presented with the 'full picture'.

5.2 Paragraph 2.1 – Turnover test

5.2.1 The wording *'You must follow the rules in this notice if your business' VAT taxable turnover is more than the VAT registration threshold (currently £85,000) for VAT Periods starting on or after 1 April 2019'* could be taken to mean that you start counting towards the £85,000 threshold on or after 1 April 2019 ie you ignore turnover before that date. As the intention appears to be to capture businesses who are (inter alia) already compulsorily VAT registered, then this look back needs to be made clear. Also, the term 'VAT Periods' should also be made clearer – does it mean VAT return periods (ie prescribed accounting periods)?

5.2.2 Further, the use of the words 'next accounting period' could be interpreted to mean the next financial accounting period (eg a year) rather than a prescribed accounting period (ie the next VAT return period). Again, this should be made clear, though see our comments elsewhere about the start date for MTD.

5.2.3 In any event, there should be a reference to the requirement to register for VAT if the business' VAT taxable turnover is more than the VAT registration threshold, and a link to the VAT Notice 700/1: should I be registered for VAT?

5.3 Paragraph 2.2 - Other exemptions

5.3.1 We would recommend HMRC include the contact details of the VAT Helpline, rather than expect readers to look elsewhere.

5.3.2 The VAT Helpline will need increased resources to deal with the number of enquiries it will undoubtedly receive in the spring of 2019, especially considering stagger 1 businesses are being mandated first, and the fact that it coincides with Brexit.

5.3.3 It would also be helpful to set out what 'alternative arrangements' might be acceptable to HMRC, so businesses who contact HMRC already have in mind the types of arrangements that might be accepted. There will also be a large number of

individuals and businesses who might require ‘digital assistance’, and HMRC should be adequately resourced to help those businesses be compliant.

5.4 Paragraph 2.3 - Can I choose not to be exempt?

5.4.1 It is not clear what happens if a business which is not mandated into MTD simply starts submitting its VAT returns using functional compatible software; for example because the software it is using then becomes MTD compatible, without making an election. Is that acceptable, or are there consequences of doing so? This should be explained.

5.5 Paragraph 3.1 - Digital record-keeping

5.5.1 The wording ‘*Any records that are not listed in this notice do not need to be kept in a set way*’ is misleading. Businesses who operate special VAT or accounting schemes, or operate processes such as self-billing, may be required to maintain records in a ‘set way’, and so this sentence may need caveating or clarifying. For clarity, it might be helpful to refer readers specifically to paragraph 3.3 which sets out what digital records need to be maintained.

5.5.2 Many businesses might be choosing software for the first time, or will need to upgrade their software, and will need help. HMRC say they will publish on GOV.UK details of MTD compatible software, and a link to that page should be provided. Businesses should also be encouraged to seek advice from their agent and / or software provider.

5.6 Paragraph 3.2 - What is functional compatible software?

5.6.1 The requirement for a digital link is set out in a paragraph which has the force of law ie ‘*If a set of compatible software programs is used there must be a digital link between the pieces of software.*’

5.6.2 We strongly recommend that the ‘soft landing’ in relation to these digital links is also set out in a paragraph which has the force of law.

5.6.3 By way of illustration, it could say ‘*If a set of compatible software programs is used there need not be a digital link between the pieces of software for the first twelve months of being subject to the MTD for VAT requirements. However, after that time, there must be a digital link between the pieces of software.*’

5.6.4 Having such an approach is particularly important so that businesses can be compliant with the law during the ‘soft landing’ period; rather than what is currently proposed ie not being compliant with the law, but with HMRC not taking any penalty or remedial action. The vast majority of businesses want to comply with their legal obligations, even if there is no risk of penalties.

5.6.5 The Examples 1 to 3 are helpful, but it would be much clearer and easier to follow if the examples followed the same numbering and format as the examples in the draft Addendum. That way, readers would be able to cross-refer between the written guidance and the diagrams, which would make it much easier to understand the requirements.

5.7 Paragraph 3.3 - What records need to be kept digitally?

- 5.7.1 Please see above our comments in relation to the new Regulation 32A which similarly apply here.
- 5.7.2 We understand that some businesses have separate elements to, or have more than one, VAT account; for example, separate accounts for input VAT and output VAT, whose balances would be transferred to a VAT settlement account at the end of each VAT accounting period. It would be helpful if the Notice envisaged and approved this type of configuration.
- 5.7.3 Note there is a typo in the 'Designatory data' which should say principal (rather than principle) place of business. The same error also arises in paragraph 6.2.
- 5.8 Paragraph 3.4 – Adjustments
- 5.8.1 It would be helpful to give examples or a list of adjustments that businesses can make outside of software – perhaps based on the list in the legislation overview published on 13 September 2017.
- 5.9 Paragraph 4.1 - Submitting your VAT return
- 5.9.1 This paragraph is wholly inadequate and potentially misleading. First it assumes all businesses will be using software other than spreadsheets. Secondly, it does not envisage that businesses can and will need to take additional steps (recognised elsewhere in the draft Notice, and the draft Addendum) to adjust the VAT return figures produced by the software.
- 5.9.2 This paragraph needs redrafting entirely and linking back to the explanations and examples in section 3 of the draft Notice, and those in the draft Addendum.
- 5.10 Paragraph 4.2 - Can my agent submit my VAT return?
- 5.10.1 Again, this paragraph is inadequate and potentially misleading as it provides just one way in which an agent may be involved in the preparation or submission of a client's VAT return – giving the impression that this is the only route which is acceptable to HMRC.
- 5.10.2 Again, it would be preferable if the examples were better linked to those elsewhere in the draft Notice and in the draft Addendum. Indeed, Example 2 contradicts the explanation in paragraph 4.1.
- 5.10.3 We also recommend that (on the subject of agents) it is made clear either in this section, or in section 3, that it is perfectly acceptable for agents to maintain their client's records, as well as assist with the submission of the VAT return to HMRC.
- 5.11 Paragraph 5.1 – Voluntary updates
- 5.11.1 There seems to be no purpose / benefit to business in submitting a voluntary update. It will not discharge the VAT return obligation and does not create a legal liability.
- 5.11.2 If MTD is mandated for Income Tax and / or Corporation Tax, the benefits of aligning VAT return periods, and / or submitting voluntary updates could be explained at that time. Until then, we see no merit in building a system of voluntary updates into MTD for VAT and we feel this is just likely to create confusion.
- 5.12 Paragraph 5.2 - Correcting a VAT update

- 5.12.1 Our view is reinforced by the fact that a voluntary update will need correcting if it is wrong.
- 5.12.2 First, it is not explained what a ‘correct’ voluntary update requires. Is a voluntary update just submission of input and output information (like a quarterly update for Income Tax might be), or should adjustments be made such as partial exemption, fuel scale charges etc?
- 5.12.3 Secondly, we cannot understand why a business would need to tell HMRC of a correction to a voluntary update if it is superseded by the subsequent submission of the VAT return. Having to correct voluntary updates seems unnecessary, resulting in additional compliance costs for those businesses which choose to provide voluntary updates, both in ensuring that the voluntary update is accurate, and making corrections if not.
- 5.12.4 Thirdly, it also appears inconsistent with the Income Tax proposals in relation to MTD, where errors in quarterly updates are simply corrected through submission of the following update.
- 5.12.5 As above, at this stage we see no merit in building a system of voluntary updates into MTD for VAT.
- 5.13 Paragraph 6.2 - What information will my software send?
- 5.13.1 Whilst the explanation around supplementary data in 6.1 is informative, paragraph 6.2 requires further clarification, such as:
- What is ‘the period’ referred to in relation to this information? Is it the VAT return period (if sent alongside a VAT return), the voluntary update period (if sent alongside a voluntary update), the period since the last submission of supplementary data, or something different?
 - What is meant by ‘adjustment to’ in relation to output tax and input tax? In particular, for input tax, is this the amount of the input tax disallowed (eg due to partial exemption), or something else?
 - Whether only part of the supplementary data listed in the Notice can be provided, or whether it is an ‘all or nothing’.
- 5.13.2 It would appear that HMRC has decided not to provide ‘white space’ or other facility which might help the business explain fluctuations in VAT return figures, or upload copy invoices etc to support input tax claims. This is a missed opportunity as we consider that would have significantly reduced the level of unnecessary enquiries by HMRC if the supplementary data is being used as set out in paragraph 6.1.
- 5.14 Paragraph 6.3 - Correcting Supplementary data
- 5.14.1 Like voluntary updates above, we question the benefits of submitting supplementary data. We recognise that HMRC might review this data and conclude that a compliance check is not required, but again we are concerned about a) the fact that it is not clear what ‘correct’ supplementary data is, and hence when it is incorrect, and b) the compliance costs associated with providing this data, ensuring it is accurate, and correcting any errors.
- 5.14.2 We are also concerned that HMRC will assume that a business has ‘something to hide’ if it does not provide supplementary data, when in fact it might simply have concerns about the administrative burden in providing the requisite data.

- 5.14.3 On the presumption that HMRC will place some reliance on the supplementary data (hence requiring it to be corrected if it is wrong), additional legislation is likely to be needed, such as to penalise uncorrected errors in supplementary data). Again, this seems to be a potential deterrent for submission of supplementary data.

6 Draft Addendum to VAT Notice

6.1 General points

- 6.1.1 First of all, it is worth stating that these examples are very helpful in illustrating the processes which are acceptable for the preparation and submission of VAT returns under MTD.

- 6.1.2 Whilst there is a tension between either just illustrating the principles to be applied, and giving extensive examples, readers will attempt to identify themselves with one of the examples ie 'that's us'. So, it is important that the examples are as comprehensive as possible (even if the same example covers a number of scenarios), and that they are clear and consistent. Many businesses that use an agent may deal with VAT themselves (instructing their agent for accounts / tax returns only in order to limit costs), so businesses will want to rely on what it stated within the examples.

6.2 Information transfer for VAT: General principles

- 6.2.1 We would recommend that the information set out here might be better incorporated into the Notice. Therefore, the Notice provides the necessary explanations, and the Addendum is limited to setting out the examples.

- 6.2.2 A lot of jargon is used in this section. For example, the opening line states '*Information transfer between interfaces must be digital where the records are part of the MTDfB journey*'. That in itself will confuse a lot of readers ie

- What are interfaces?
- What does digital mean?
- What is the MTDfB journey?

- 6.2.3 The language used must be simple, informative and jargon free, designed to be understood by non-IT specialists if it is to be of greatest impact.

- 6.2.4 As set out elsewhere, we believe the soft landing should be introduced differently, so that businesses are legally compliant in both the first and subsequent years, rather than just being 'let off' penalties.

6.3 Journeys / Legend

- 6.3.1 As stated elsewhere, it would be more helpful to the reader if the examples were numbered (rather than slide numbers) and linked back to the examples in the Notice.

- 6.3.2 In the legend 'Digital Link' it is stated that '*Data should ideally be imported/exported...*' Saying 'ideally' implies that this is aspirational rather than mandatory, and so should be deleted as the rest of the paragraph sets out what the soft landing means.

6.4 The Examples

- 6.4.1 The step to illustrate submission of the VAT return from a spreadsheet is set out differently in example 3 from how it is illustrated in examples 4 and 5. This step needs to be illustrated consistently so as to avoid confusing readers.
- 6.4.2 Similarly, application of the ‘soft landing’ appears inconsistent. In example 3 it does not apply to spreadsheet-spreadsheet. In example 4 it does apply to software-spreadsheet. In example 5, it does apply to both software-spreadsheet and spreadsheet-spreadsheet. The precise nature and scope of the soft landing needs to be clearly set out in both the Notice and the Addendum.
- 6.4.3 In example 7, the wording in the bubble ‘*Any correction of mistakes...*’ should envisage correction by the client and the agent, not just the agent.
- 6.4.4 We also note that the soft landing does not apply to the link from client to agent software. We raise whether this is appropriate as it might risk clients being prevented from using agents, and potentially fall into error, if they cannot make that link digitally from the outset.

7 **Other comments / observations**

7.1 ‘Benefits’ of MTD for VAT

- 7.1.1 We are concerned that the revenue benefits of MTD for VAT appear exaggerated, and the costs to businesses underestimated.
- 7.1.2 Mandating Making Tax Digital is predominantly aimed at reducing the tax gap caused by failure to take reasonable care, and error. We understand from HMRC that around 80% of the value of those mistakes arise in businesses who trade below the VAT registration threshold, and so compulsorily VAT registered businesses are clearly not the central focus of MTD.
- 7.1.3 It was particularly surprising, therefore, to calculate⁵ that MTD in its current form (ie mandated for VAT only) is expected to generate additional revenues of around £400m per annum in steady state, especially when compared to the original MTD proposals which were designed to generate around £900m per annum. So, even though only 20% of mistakes arise in businesses which are in the scope of MTD for VAT, additional revenues will still be around 45% of those originally estimated.
- 7.1.4 Further, considering the requirements of MTD for VAT and the points set out above (some of which highlight new, additional requirements on businesses), the average transition cost published by HMRC of just £109 per business appears significantly underestimated, and the idea that there will be ongoing administrative savings fanciful. These costs will also impact the greatest on the smallest compulsorily VAT registered businesses.
- 7.1.5 We would remind HMRC of the results of our survey around the (original) MTD proposals as set out above. HMRC’s revenue and cost estimates are significantly out of line with those operating ‘at the coal face’.

⁵ Note that the ‘net’ revenue benefit figure for the current MTD proposals has not been clearly published.

7.1.6 MTD seeks to bring about a major cultural and technological change, which will incur additional transition and ongoing costs for business. Over time, many businesses will tolerate these costs because they will deliver benefits to their business (as well as HMRC). It is premature to mandate MTD before willing volunteers have tested the systems and achieved these benefits, which itself would lead to more and more businesses joining voluntarily. Currently, we do not believe the case for mandation is clear, specific or well made.

7.2 Letting agents / events organisers / third parties etc

7.2.1 There are many circumstances in which a third party (an agent) will collect income, incur expenditure, and record these transactions on behalf of a business (the principal). These include letting agents, events organisers, local branches of charities and so on.

7.2.2 It is assumed (but not clearly stated) that these third parties can, if their systems permit, record these transactions in software and transfer the data digitally to the business.

7.2.3 However, in practice, it is likely that it will take some time for these third parties to accommodate the requirements of MTD (if at all), and in the meantime the business will need to maintain its own records in software. This will inevitably mean a duplication of effort (two set of records) and HMRC should consider whether the requirements of MTD can be relaxed, at least initially, to accommodate these complexities.

7.2.4 In any event, clear guidance is needed in the Notice and Addendum, to explain what HMRC expect to happen in these circumstances.

7.3 Inconsistencies / interaction with Income Tax / Corporation Tax

7.3.1 We know that it hasn't escaped HMRC's attention that certain elements of VAT differ from Income Tax (and potentially Corporation Tax). The cash basis is one such example, and we are pleased that HMRC acknowledge these issues and recognise that some simplification would be required to ensure consistency across the regimes.

7.4 Retention of records

7.4.1 Similarly, we understand that HMRC are considering the record-keeping requirements and how they can be satisfied, such as after a business has ceased (should it be required to pay its software licence for a further six years?) or if a software supplier goes bust. Also, where / how should spreadsheets be maintained? Clear guidance needs to be provided in relation to these matters.

7.5 Communications

7.5.1 Communication to date from HMRC around MTD, certainly MTD for VAT, has been sparse. Many smaller VAT-registered businesses, particularly unrepresented ones, might be blissfully unaware of MTD for VAT.

7.5.2 Whilst we understand that HMRC are holding back on communications until they can get businesses involved with MTD, such an approach could be too late for many. The main change for many businesses will be the requirement for businesses in scope to maintain digital records. HMRC has been encouraging the profession to spread the

word about MTD, the benefits of keeping digital records etc, but HMRC has done little promotion of that itself.

- 7.5.3 HMRC should step up its communications around MTD without further delay. It could start ‘setting the scene’ around digital record keeping now, before providing more detail as the requirements become certain.

7.6 Spreadsheets

- 7.6.1 Many smaller businesses trading just above the VAT registration threshold might currently maintain manual records, or use simple spreadsheets.

- 7.6.2 Whilst some of these businesses might, with help from an agent, be able to transition to basic software, we suspect that a large proportion will simply rely on spreadsheets.

- 7.6.3 However, we are unclear as to the likely availability and cost of API-enabled spreadsheets, which might be the only realistic way for these smaller business to be MTD compliant. It would be helpful if HMRC could provide some assurances on this issue.

7.7 VAT return validation / parameters

- 7.7.1 We are receiving reports that the MTD for VAT API incorporates a validation check that will reject a VAT return if the VAT on sales in box 1 is greater than 20% of the total sales in box 6, or where VAT on purchases in box 4 is greater than 20% of the total purchases in box 7.

- 7.7.2 There are many valid reasons why boxes 1 / 4 might be greater than 20% of boxes 6 / 7. Whilst it might be appropriate to include a prompt to highlight this during the process of submitting the return (like the VAT portal currently does), simply rejecting returns will simply block a huge number of correct returns.

8 **Acknowledgement of submission**

- 8.1 We would be grateful if you could acknowledge safe receipt of this submission, and ensure that the Chartered Institute of Taxation is included in the List of Respondents when any outcome of the consultation is published.

9 **The Chartered Institute of Taxation**

- 9.1 The Chartered Institute of Taxation (CIOT) is the leading professional body in the United Kingdom concerned solely with taxation. The CIOT is an educational charity, promoting education and study of the administration and practice of taxation. One of our key aims is to work for a better, more efficient, tax system for all affected by it – taxpayers, their advisers and the authorities. The CIOT’s work covers all aspects of taxation, including direct and indirect taxes and duties. Through our Low Incomes Tax Reform Group (LITRG), the CIOT has a particular focus on improving the tax system, including tax credits and benefits, for the unrepresented taxpayer.

The CIOT draws on our members' experience in private practice, commerce and industry, government and academia to improve tax administration and propose and explain how tax policy objectives can most effectively be achieved. We also link to, and draw on, similar leading professional tax bodies in other countries. The CIOT's comments and recommendations on tax issues are made in line with our charitable objectives: we are politically neutral in our work.

The CIOT's 18,000 members have the practising title of 'Chartered Tax Adviser' and the designatory letters 'CTA', to represent the leading tax qualification.

The Chartered Institute of Taxation
9 February 2018