



July 2010

Increase in the VAT rate to 20% on 4 January 2011

As you will be aware, the VAT rate will increase to 20% with effect from 4 January 2011. There are no changes to the current zero rates (0%), reduced rates (5%) and exemptions from VAT.

The basic principle is that goods and services supplied on or after 4 January 2011 will be liable at the 20% rate, but there are some additional complications when supplies, payment or invoicing occurs just before and after this date.

- Where goods are provided or services are completed before 4 January 2011 but are invoiced after – the supplier would normally charge VAT at 20% but can choose to charge VAT at 17.5% if they wish.
- Where an invoice is issued or payment is received before 4 January 2011 for goods or services provided after that date – the supplier should normally charge VAT at 17.5%, but can choose to charge at 20% if they wish.
- Where goods or services are provided over a period of time which spans the rate change, e.g. supplies of electricity and gas or consultancy services, the supplier can either just use the rate applicable when they raise the invoice, or can choose to apportion the charge between the VAT rates before and after the rate change, using any reasonable apportionment method.

Opportunities for VAT savings

There may be opportunities to benefit from the existing 17.5% rate by bringing forward some purchases, but you need to take into account the “anti-forestalling” legislation introduced by HM Revenue & Customs (HMRC) in the 2010 Budget – these rules are effectively the same as those which applied when the rate reverted to 17.5% from 15% in January 2010.

These rules are designed to prevent purchasers of goods and services from taking what HMRC considers to be unfair advantage of the rate change. When the anti-forestalling rules apply, a supplier who has charged VAT at 17.5% would be required to issue a supplementary invoice for an additional 2.5% VAT on 4 January 2011.

A supplementary VAT charge will apply if the customer cannot reclaim the VAT it incurs, AND one of the following conditions applies:

- The supplier and the customer are “connected” (e.g. associated companies), OR
- The supplier funds the purchase (e.g. by loaning money to the customer), OR
- A VAT invoice is issued and payment is not due for at least 6 months, OR
- A pre-payment (or invoice) of more than £100,000 is made before the rate change (i.e. before 4 January 2011) for goods or services to be provided after the rate change. This condition will not apply if the pre-payment is in accordance with normal commercial practice.

Practical implications for NHS bodies - purchases

If NHS bodies follow their normal practice in buying goods and services then it is unlikely that these rules will affect them. The following are some examples of how the rules will apply in practice.

Example 1

If you have an annual contract for the lease of equipment or other services and an invoice is issued before 4 January 2011, then VAT should be charged at 17.5%. As long as this is normal practice for this contract and payment is due within 6 months there will be no supplementary VAT charge, regardless of the value.

Example 2

If a quarterly property rental invoice is issued in December 2010, the VAT rate used should be 17.5% for the whole charge.

Example 3

If goods of any value are ordered, invoiced, delivered and paid for by 4 January 2011 there will be no supplementary VAT charge. This means that the purchase of goods could be advanced to obtain a VAT saving before the rate increases to 20%.

Example 4

If goods to the value of £110,000 are ordered and invoiced in December 2010 but are not delivered until February 2011, then the supplier will probably need to issue a supplementary invoice for VAT of 2.5% on 4 January 2011.

Example 5

For on-going construction contracts (where VAT recovery is relatively low), it will be beneficial to ask contractors to issue invoices for the value of work carried out up to 3 January 2011 so that it can be charged at the 17.5% rate. An advance payment for future works could also be made (up to £100,000), subject to the rules outlined above.

Alternatively, you can ask a supplier who raises an invoice after 3 January 2011 to split the invoice between the two rates, based on the value of the work undertaken before and after the rate change.

Practical implications for NHS bodies – sales

In the run up to 4 January 2011 we would strongly recommend that you seek to ensure that your invoicing is as up to date as possible. Complications can arise when invoices are issued some time after goods or services are supplied, so when a VAT rate change is in prospect it is particularly important to ensure that invoices are issued at the correct time. This will of course ensure you get paid sooner so is generally best practice anyway.

Conclusion

If you have any queries on this matter please contact your usual Liaison adviser or our free VAT Helpline on 0800 700 652.

Every effort has been made to ensure the accuracy of this information. However, it may not be comprehensive for your particular situation and recipients should not act on it without first seeking professional advice.