



ICAS comments
Making Tax Digital for VAT: legislation overview
(Published on 13 September 2017)

10 November 2017

About ICAS

1. The Institute of Chartered Accountants of Scotland ('ICAS') is the world's oldest professional body of accountants; we represent over 21,000 members working across the UK and internationally. Our members work in all fields, predominantly across the private and not for profit sectors.
2. ICAS has a public interest remit, a duty to act not solely for its members but for the wider good. From a public interest perspective, our role is to share insights from ICAS members into the many complex issues and decisions involved in tax and financial system design, and to point out operational practicalities.

General Comments

3. ICAS welcomes the opportunity to comment on the MTD for VAT: legislation overview.
4. The overview does not contain sufficient certainty or detail for businesses to start making changes to their systems which will, or might, be necessary for them to implement MTD for VAT. The final regulations, which should provide certainty on the requirements, will not be available until around April 2018, with one year of testing envisaged before mandatory implementation. However, this will be too late for many large companies, other large businesses and local authorities which need up to 2 years to go through the processes required (budget approval, procurement, testing etc) to change their systems. The proposed effective date of 1 April 2019 does not look feasible.
5. Currently only 12% of businesses file VAT returns direct from software; we would expect this percentage to be much higher if it was straightforward to develop software which could deal with the complexities of VAT and company accounting systems - and file returns without any manual intervention. The difficulties of moving to a position where 100% of businesses are filing direct from software do not seem to be recognised and the lead time required for implementation is therefore being underestimated. Far more detail on exactly what will be required is needed urgently, particularly to clarify exactly how spreadsheets can be used and what will be permitted in terms of the interaction between underlying accounting systems, spreadsheets and the VAT return.
6. The interaction between MTD for VAT and MTD for business income tax (which could be introduced in 2020) needs to be clarified. Page 6 of the overview notes that the January 2017 MTD consultation response envisaged that the deadline for submissions of information for VAT and income tax would be aligned. However, it goes on to say that for the time being there will be no changes to VAT return or payment dates. Some businesses will want to use the same MTD software for income tax and VAT and will want to align payment dates. Issues relating to interaction between the two therefore need to be addressed now, so that software developers can take them into account in building their VAT MTD products. If (as suggested in the overview) interaction is not considered until a decision is made on mandatory MTD for income tax some businesses may find in 2020 that they are forced to use different software packages for income tax and VAT, potentially increasing costs.
7. Brexit is likely to mean that there will be significant changes to VAT and customs duties at the same time as the proposed effective date for MTD for VAT of 1 April 2019. We do not think it makes sense to impose all these major changes on businesses (or HMRC) at the same time, given the costs which will be incurred and the resources which will need to be devoted to implementing them. The mandatory implementation of MTD for VAT should be delayed.
8. It would make sense for MTD for VAT to be available on a voluntary basis, alongside MTD for income tax until at least 2020 – preferably longer. This would permit a more realistic timetable for the development of software and for large businesses to make changes to their systems.
9. The Office of Tax Simplification has recently published its report on its review of the VAT system to identify opportunities for simplification and reform; ideally as much

simplification as possible should be undertaken before MTD for VAT is imposed on businesses.

Exemptions

10. We agree that it would be sensible to extend the existing exemptions (for electronic VAT returns) to MTD, as suggested in the overview.
11. We understand that no exemption is being suggested for charities with taxable turnover which exceeds the VAT threshold because of the need for a level playing field. However, there will be no requirement for free software to be available and there is likely to be a particular cost issue for charities because they are unlikely to be able to use cheaper products designed for businesses. Large charities are also likely to have similar problems (with timing and use of spreadsheets) to other large and complex entities; these are discussed in detail below.

Third Party Software and Keeping Digital Records

12. The primary legislation in Finance Bill 2017 introduces powers allowing HMRC to make regulations requiring the submission of information relating to VAT and requiring a business to keep and preserve certain records digitally. The overview explains that the regulations will provide that a business must use functional compatible software, which can connect to HMRC systems via APIs to meet these new requirements. The functions of the compatible software must include: keeping and preserving records in a digital form and creating a VAT return from the digital records and providing HMRC with this information digitally.
13. Nowhere is it made clear in the overview document exactly how this is envisaged to work in practice. We understand from government and HMRC statements that spreadsheets will qualify as digital records. In view of the importance of spreadsheets for many businesses filing VAT returns, precisely how they can be used needs to be made explicit as soon as possible. This must include details of how spreadsheets will be required to interact both with the MTD functional compatible software for reporting to HMRC and with a company's underlying digital accounting systems.
14. At a recent meeting HMRC suggested that where all the business records are kept in spreadsheets third party software developers will be able to develop software to 'pull' data from the spreadsheet records into software which will be able to connect to HMRC's API, without too much difficulty. We question how straightforward this will be, in reality, given that if it could be achieved easily we would expect it to have happened already. It is in any case only likely to be relevant to smaller businesses with turnover close to the £85,000 threshold. It fails to address more complex scenarios where spreadsheets are not being used to keep underlying records but for other purposes. Discussions with developers are apparently at an early stage and no products are currently available.
15. Large companies and other large businesses will already be keeping digital records. They are unlikely to have any problems complying with that aspect of the requirements. However, many will have multiple digital accounting systems – for example, for different parts of the business or different product lines. In order to complete a VAT return, data from different systems is collated into spreadsheets; this involves manual intervention/transposition. It is unclear whether this approach will be acceptable in the MTD for VAT regime – or whether the final regulations will **require** digital transfer of data from underlying accounting systems to spreadsheets, as well as from the spreadsheets to the VAT return. This needs to be clarified urgently.
16. We understand that HMRC would prefer an 'end to end' digital process, as suggested by the wording used in the overview (noted in paragraph 12 above) to reduce the risk of error but there are no software products currently available which permit this for businesses of any size or complexity. Many large companies have automated the process as far as possible but still require manual interventions - with checking processes to avoid errors. They need to know whether they will be able to continue to transpose data into spreadsheets from underlying accounting systems. If this will remain acceptable they will be able to concentrate on the work required to create/acquire software to take

data from the spreadsheets to generate the VAT return and connect to HMRC's APIs. Whilst we do not believe this will be completely straightforward it is more likely to be achievable in a short timeframe than the 'end to end' digital process implied by the overview.

17. Many businesses (of all sizes) use spreadsheets to carry out complex VAT calculations, for example, partial exemption calculations. Currently, the adjustments required as a result of the calculations can be manually input into the VAT online return filed via the HMRC portal.
18. Annex 1 indicates that only the total of any adjustment will be required to be kept digitally, not details of the underlying calculations. From comments made at a recent meeting it appears that HMRC believe that businesses could 'journal' in adjustments arising from complex calculations carried out using spreadsheets. However, for many companies it will not be possible to 'journal' the totals back to the underlying accounting systems, due to checking processes and controls (some of which are required by HMRC). It might be possible to take them to a spreadsheet. This raises the same issues already highlighted in paragraphs 15 and 16 about whether 'end to end' digital will be a requirement. Again, clarity on exactly what will be required is urgently needed.

Preservation of Digital Records

19. Page 5 of the overview states that regulations will provide that businesses (including those deregistering) must preserve digital records in functional compatible software for 'up to' 6 years. VAT Notice 700/21 currently states:

"Generally, you must keep all your business records for VAT purposes for at least 6 years. Records that you use for other tax purposes may need to be kept for longer periods. If the 6-year rule causes you serious storage problems or undue expense, or you need advice on records for other types of tax, then you should consult our advice service. We may be able to allow you to keep some records for a shorter period."

The shorter guidance on [GOV.UK](https://www.gov.uk) currently reads: "You must keep VAT records for at least 6 years (or 10 years if you use the [VATMOSS service](#)."

This will presumably continue to apply for businesses which file VAT returns but are not within the scope of MTD for VAT, either because they are below the VAT threshold or because they fall within an exemption.

20. Is it the intention that the requirement to retain records for businesses within MTD for VAT will remain the same as currently – the only difference being that the records must be retained in 'functional compatible software'? This is suggested by the comments on page 3 but it is slightly less clear from the comments on page 5.
21. Keeping records for 6 years in software (and maintaining access to them) may involve significant costs; this could be particularly onerous where a business deregisters when it ceases trading (but has to continue paying for software for 6 years), or where a business wishes to move from one software provider to another (where it might have to pay for both the old and new software for the next 6 years). There may also be problems where a software provider goes out of business. Will HMRC be producing guidance to help businesses? Will HMRC maintain a version of the various software platforms, so that businesses will only have to retain a back-up which could be submitted to HMRC if required? This would remove the need for taxpayers to continue to pay for software they are no longer using.

Content of Digital Records/Annex 1

22. We believe that most businesses which currently comply with VAT record-keeping requirements should be able to keep digital records of the information listed in Annex 1. Many large companies will probably already be keeping most of this information in digital accounting systems. As noted above there will be problems for many large businesses if an 'end to end' digital approach is a requirement – but these are related to generating returns rather than the underlying record keeping systems.

23. Some smaller entities have already moved to cloud based accounting software and this is likely to accelerate with the introduction of MTD. This should permit them to keep digital records of the information set out in Annex 1. However, like large companies, those with complex VAT calculations will have issues dealing with an 'end to end' digital approach because of the need to calculate adjustments.
24. The overview does not deal with margin schemes – such as TOMS or the second-hand margin scheme. It would be helpful to have clarification on the requirements for these schemes, as there may be some issues with keeping all information digitally.

Supplementary data

25. HMRC believes that businesses and HMRC could both benefit from the submission of supplementary voluntary data. However, as this section of the overview notes the '9 Box' return does have advantages for businesses in terms of reduced administrative burdens. The only suggested benefit to businesses from submitting extra data appears to be that it might reduce the risk of an enquiry from HMRC, by allowing HMRC to 'target' compliance activity more accurately. Even this suggested benefit is presumably not a certainty, given that the section concludes by saying that HMRC will be able to 'test' with businesses the extent to which they and HMRC benefit from the supplementary data. It is also the case that the additional data might prompt an enquiry in some cases; this is unlikely to be viewed as beneficial by the business (even if it arguably prevents greater problems later).
26. It appears from the limited information provided in the overview that the approach will be an 'all or nothing' one ie a business either supplies summary totals of all the information required to be kept in digital records (as listed in Annex 1) – or it cannot 'benefit' from submitting additional information. It is also unclear whether a business which has submitted additional information will be required to do so for all subsequent returns – or if (and when) it will be possible to revert to the normal '9 box' returns. Given the doubtful benefits and the increased administrative burden the proposal seems to provide little incentive for businesses to decide to supply supplementary data.
27. We believe that the proposals for submitting supplementary data need to allow more flexibility in the additional data to be submitted. They should also explicitly permit a business to stop providing additional data and revert to the '9 box' return, either at any time, or after a set period. This would allow the additional data to be tailored to different types of businesses, with different risk areas and would also allow a business to opt out of providing the extra data if it found it too onerous. HMRC should consult with businesses to identify what additional data would genuinely be useful in 'de-risking'.
28. Reducing the risk of an enquiry is not a positive benefit which businesses can measure; an enquiry might not have taken place anyway and it is possible that in some cases the additional data could prompt an enquiry. Consideration should therefore be given to whether more tangible, visible benefits could be offered to businesses in return for submitting additional data.
29. One tangible benefit which could be offered to businesses, in return for submitting the supplementary data, would be that they would normally be deemed to have taken reasonable care (for penalty purposes) should an error subsequently emerge. Another possibility would be to allow extra time for making payments (similar to that offered to those paying by direct debit) – or to offer quicker repayments.