



Bookkeeping and Accountancy Ltd

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Navigating VAT Returns and Compliance

Step-by-step advice on filing accurately and avoiding penalties

Introduction: Understanding VAT

Value Added Tax (VAT) is a tax on consumer spending collected by businesses on behalf of HMRC. While the mechanics can seem complex, understanding the basics helps you stay compliant and avoid costly mistakes. VAT-registered businesses charge VAT on their sales (output tax), reclaim VAT on their purchases (input tax), and pay the difference to HMRC. This guide covers everything you need to know about VAT registration, returns, and compliance.

Top Tip: Even if you are below the threshold, voluntary VAT registration can make you appear more professional and allow you to reclaim VAT on purchases.

When to Register for VAT

VAT registration is compulsory in certain circumstances, but you can also register voluntarily:

Compulsory Registration

You must register for VAT when:

- Your taxable turnover exceeds £90,000 in any rolling 12-month period
- You expect to exceed £90,000 in the next 30 days alone
- You take over a VAT-registered business as a going concern
- You receive relevant goods from the EU exceeding the registration threshold

Voluntary Registration

You may choose to register even when below the threshold:

- Reclaim VAT on start-up costs and equipment purchases
- Appear more established to business customers
- Avoid the shock of sudden mandatory registration
- Claim VAT on purchases going back 4 years (goods) or 6 months (services)

Registration Process

Register online through your Government Gateway account. You will need your business details, bank account information, and details of any previous registrations. HMRC typically processes applications within 30 days, though it can take longer.

Choosing the Right VAT Scheme

Different VAT schemes suit different businesses. Choosing the right one can simplify your administration and even save money:

Standard VAT Accounting

The default method where you pay the difference between output and input VAT. Suitable for most businesses with straightforward transactions and significant input VAT to reclaim.

Flat Rate Scheme

Pay a fixed percentage of your gross turnover (including VAT) instead of calculating actual VAT. Rates vary by business sector from 4% to 14.5%.

- Simpler record-keeping required
- Can be profitable if you have few purchases
- Must have taxable turnover under £150,000
- New businesses get 1% discount in first year
- Cannot reclaim VAT on most purchases

Cash Accounting

Account for VAT based on when you receive and make payments, rather than invoice dates:

- Helps with cash flow - do not pay VAT until customer pays you
- Must have taxable turnover under £1.35 million
- Useful if you have slow-paying customers
- Automatically provides bad debt relief

Annual Accounting

Make interim payments throughout the year with one annual return:

- Reduces admin burden - only one return per year
- Easier to budget with regular interim payments
- Must have taxable turnover under £1.35 million
- Interim payments based on estimated annual liability

Top Tip: Review your scheme annually - what suited you as a startup may not be optimal as you grow.

Completing VAT Returns

VAT returns are due quarterly, with 9 boxes to complete:

- Box 1: VAT due on sales and other outputs
- Box 2: VAT due on acquisitions from EU member states
- Box 3: Total VAT due (Box 1 + Box 2)
- Box 4: VAT reclaimed on purchases and other inputs
- Box 5: Net VAT to pay or reclaim (Box 3 - Box 4)
- Box 6: Total value of sales excluding VAT
- Box 7: Total value of purchases excluding VAT
- Box 8: Total value of EU supplies excluding VAT
- Box 9: Total value of EU acquisitions excluding VAT

Top Tip: Submit and pay your VAT return promptly - the deadline is one month and 7 days after the end of your VAT quarter.

Reclaiming VAT on Purchases

You can reclaim VAT on goods and services used for your business, but there are important rules:

What You Can Reclaim

VAT is reclaimable on legitimate business expenses where you have a valid VAT invoice showing the supplier VAT number, your business name and address, the VAT amount, and the date of supply.

Blocked Input VAT

You cannot reclaim VAT on certain items:

- Business entertainment (except for overseas customers)

- Cars not used wholly for business
- Goods and services for private use
- Purchases not used for taxable business activities

Partial Exemption

If you make both taxable and exempt supplies, you can only reclaim VAT on purchases that relate to taxable activities. Purchases used for both must be apportioned using an approved method.

Making Tax Digital for VAT

All VAT-registered businesses must now comply with Making Tax Digital requirements:

- Keep digital records of all VAT transactions
- Use MTD-compatible software to maintain records
- Submit VAT returns directly through your software
- Ensure digital links between all parts of your records
- No manual transcription or copying between systems
- Penalties apply for non-compliance

Top Tip: Most cloud accounting software (Xero, QuickBooks, FreeAgent, Sage) is fully MTD compliant.

Common VAT Mistakes and Penalties

HMRC issues penalties for various VAT errors and non-compliance:

- Late registration - penalty based on VAT that should have been charged
- Late returns - default surcharge increasing with repeated lateness
- Late payment - interest charged from due date
- Careless or deliberate errors - penalties up to 100% of VAT underpaid
- Failure to keep records - penalties for non-compliance
- Common errors include claiming VAT on exempt items, transposing figures, missing deadlines, and not checking supplier VAT numbers

Top Tip: If you discover an error, tell HMRC promptly - penalties are reduced for unprompted disclosure.

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