
VAT: CHANGE OF STANDARD RATE: ANTI-FORESTALLING LEGISLATION

Who is likely to be affected?

1. VAT registered businesses unable to recover the VAT they incur and their suppliers, who enter into schemes or arrangements to avoid the effect of the increase in the standard rate of VAT to 20 per cent.

General description of the measure

2. Legislation will be introduced in Finance Bill 2010 to counter arrangements that purport to apply the 17.5 per cent VAT rate to goods or services to be delivered or performed on or after 4 January 2011.
3. The measure provides that in certain circumstances a supplementary charge to VAT of 2.5 per cent will be due on supplies of goods or services on which VAT of 17.5 per cent has been declared.
4. The legislation has been targeted on artificial arrangements and is unlikely to affect suppliers conducting their business as they normally do when no VAT rate increase is anticipated.

Operative date

5. The scope of the legislation will be announced by the Exchequer Secretary to the Treasury in a Written Ministerial Statement on 22 June 2010. The legislation will have effect for transactions on and after that date.

Current law and proposed revisions

6. Forestalling occurs when arrangements are put in place for a VAT invoice to be issued by a supplier or payment received by a supplier before the rate increase, where goods are not due to be delivered or services to be performed, until on or after the date that the rate increases to 20 per cent. The grant of a right or similar option may also be used for forestalling.

7. The legislation applies to standard-rated goods and services. It prevents forestalling by introducing a supplementary charge to VAT on the supply of goods or services where the customer cannot recover all the VAT on the supply, and one or more of the following conditions are met:

- the supplier and customer are connected parties;
- the value of the supply (and any related supplies made under the same scheme) exceeds £100,000. But this does not apply if the prepayment or issuing an advance VAT invoice is normal commercial practice;
- the supplier or someone connected to the supplier funds a prepayment for the goods or services; or
- an advance VAT invoice is issued where payment is not due in full within six months (except hire purchase invoices issued in accordance with normal commercial practice).

The supplementary charge to VAT is due on 4 January 2011 and must be accounted for on the supplier's VAT return covering that date.

8. Similar provisions prevent the use of the grant of standard-rated rights or similar options as an avoidance mechanism. They cover cases where before the rate increase the customer is granted the right to receive goods and services after the rate increase, either free or at a discount, and the customer cannot recover all the VAT on the right or option.

9. The supplementary charge to VAT on rights and options applies if one or more of the following conditions are met:

- the grantor and the customer are connected parties;
- the consideration for the right or option (and any related supplies made under the same scheme) exceeds £100,000. But this does not apply if the right or option is normal commercial practice; or
- the supplier or someone connected to the supplier funds the payment for the right or option.

The charge becomes due on the date that the option is first exercised on or after 4 January 2011.

10. The charge does not apply to prepaid or invoiced rentals of land, buildings or other assets, if the period concerned is a year or less, and the prepayment or the issuing of an advance invoice is normal commercial practice.

11. Suppliers may adjust the amount payable under contracts with customers for any supplementary charges, unless the contracts say otherwise.

12. The anti-forestalling legislation is contained in a Schedule to Finance Bill 2010 and does not amend the VAT Act 1994.

Further advice

13. Guidance for businesses has been published today on the HM Revenue & Customs website. Further details of the change to the standard rate of VAT are contained in BN43.

14. If you have any questions about this change, please contact the VAT Helpline on 0845 010 9000. Information about Budget measures is Available on the HM Revenue & Customs website at www.hmrc.gov.uk