

Reverse Charge VAT



Overview

Reverse Charge VAT is a major change to the way VAT is collected in the building and construction industry and comes into effect on 1 March 2021.

It applies to individuals or businesses registered for VAT in the UK where providing or receiving specified services is reported under the HMRC Construction Industry Scheme (CIS).

Under the new rules, the provision of standard or reduced-rate building services will not be invoiced in the normal way. Under Reverse Charge VAT, the main contractor would account for the VAT on the services of any subcontractor and will have to pay the VAT due to HMRC instead of paying the subcontractor. If the service is zero-rated for VAT, Reverse Charge VAT will not apply.

Preparing for Reverse Charge VAT

To prepare for the introduction of Reverse Charge VAT on 1 March 2021, businesses in the construction industry should:

- Check to see if reverse charge affects their sales, purchases or both
- Make sure their accounting systems and software are updated to deal with the reverse charge
- Consider whether the change will have an impact on their cashflow
- Make sure their staff who are responsible for VAT accounting are familiar with the reverse charge and how it will operate.

What contractors need to do

Contractors will need to review all their contracts with subcontractors, to decide if the reverse charge will apply to the services they receive under those contracts. They will need to notify the providers if it will.

What sub-contractors need to do

Subcontractors will also need to contact their customers to get confirmation from them on whether the reverse charge will apply, including confirming if the customer is an end user or an intermediary supplier.

Type of works affected

The reverse charge will affect building and construction services provided at the standard or reduced rates of VAT that also need to be reported under CIS.

There is an important difference between CIS and the reverse charge where materials are included within a service. The reverse charge applies to the whole service whereas CIS payments to net status subcontractors are apportioned and no deductions are made on the materials content.

Services affected in the building trade include, but are not limited to, construction, alteration, repair, demolition, installation of heat, light, water and power systems, drainage, painting and decorating, erection of scaffolding, civil engineering works and associated site clearance, excavation, foundation works, etc. The definitions are linked to those defined by the CIS legislation.

Type of works excluded

Some works will not be covered by Reverse Charge VAT and invoicing will continue as is. This includes:

- Professional services of architects or surveyors, or of consultants in building, engineering, interior or exterior decoration or in the laying out of landscape
- Drilling for, or extraction of, oil, natural gas or minerals, and tunneling or boring, or construction of underground works, for this purpose
- Manufacturing of building or engineering components or equipment, materials, plant or machinery, or delivering any of these things to site
- Manufacturing components for systems of heating, lighting, air-conditioning, ventilation, power supply, drainage, sanitation, water supply or fire protection, or delivering any of these things to site
- Signwriting and erecting, installing and repairing signboards and advertisements
- The installation of seating, blinds and shutters and the installation of security systems

Changes to Pegasus CIS to support Reverse Charge VAT

Pegasus CIS v4.10 has been fully updated to handle the processing of domestic Reverse Charge VAT but this will require both Pegasus CIS and the back-office accounts system to be set up accordingly.

In addition to this, the Sales Invoice and Contract Certificate Invoice report layouts will need to be updated to be in accordance with the new legislation so that they meet the legal requirements. The standard layouts have all been updated to reflect these new requirements.

Reverse Charge VAT is applied to invoices based on the settings picked up from the VAT Codes table, ie VAT Codes need to be specifically set up to handle Reverse Charge VAT. The actual figures posted to the VAT Return when Reverse Charge VAT is applied are as follows:

Sales:

- The VAT that a customer is due to pay on behalf of a subcontractor is calculated on all Sales Invoices, Contract Internal Valuations, Contract Applications and Contract Certificates so it can be displayed on invoice layouts, but the VAT value is not added to the invoice total.
- These VAT values are essentially only notional figures and ultimately a zero-rated invoice is posted into the Sales Ledger. This will therefore only end up affecting Box 6 (Value of Sales) on the VAT Return.

Purchasing and Subcontractors:

- The VAT that the company (acting as the Customer) is due to pay on behalf of their suppliers/subcontractors is calculated on all Purchase Invoices, Subcontractor Internal Valuations, Subcontractor Applications, Subcontractor Certificates, Subcontractor Invoices and Subcontractor Payments (in the case of Deferred VAT on Subcontractor Certificates), but the VAT value is not added to the invoice total as it is not due to be paid to the Supplier/Subcontractor.
- When these transactions are posted into the back-office accounts system (via the Purchase Ledger for Purchase Invoices or as Nominal Journals for Subcontractor transactions), in addition to the usual postings affecting Box 4 (VAT on Purchases) & Box 7 (Value of Purchases) on the VAT Return, it also posts the VAT value to Box 1 (VAT on Sales).

These changes were implemented in Pegasus CIS v4.10 released in August 2019. Opera 3 must be upgraded to release (2.61.01) or above.

Opera 3 and Reverse Charge VAT

Opera 3 already allows for VAT codes to be defined as Reverse Charge. This is used in the telecommunications industry where VAT must be accounted under the reverse charge mechanism and applies to reverse charge sales and reverse charge purchases.

This mechanism can also be used by Opera 3 customers who operate in the construction industry but do not have Pegasus CIS to handle their sales and purchase transactions.

Further information



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