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# ALLENSACCOUNTS

## **VAT DOMESTIC REVERSE CHARGE FOR THE CONSTRUCTION INDUSTRY**

As covered previously a domestic reverse charge (DRC) for VAT purposes will be introduced in the Construction Industry **with effect from 1 March 2021**.

This change has been postponed twice having previously been due to take effect from 1 October 2019 and then 1 October 2020 but we understand that it will not be delayed a third time.

The reverse charge is a mechanism for accounting for VAT whereby **the customer charges themselves VAT** on a supply, rather than the supplier. This is designed to prevent missing trader fraud on the basis that a supplier cannot pocket VAT and disappear without paying it to HMRC if they cannot charge it to the customer in the first place.

### **When Will it Apply?**

The reverse charge applies when all the following are met:

- The supply is of 'specified services' – in other words the work falls within scope of the Construction Industry Scheme (CIS) – if in doubt please consult the HMRC guidance at <https://www.gov.uk/what-is-the-construction-industry-scheme>
- The work is subject to either 5% or 20% VAT (zero-rated sales are

- excluded from the new regime, for example work on new dwellings)
- The customer is registered for VAT – it is recommended that a supplier check a customer’s VAT registration number using **HMRC’s new VAT number checker** <https://www.gov.uk/check-uk-vat-number>
  - The customer is registered for the CIS – should be checked using the usual online service
  - The customer intends to make an onward supply of construction services to their own customer i.e. they are not the ‘end user’ or ‘intermediary supplier’ – you should obtain written confirmation from your customer

The reverse charge does not apply to businesses who are supplying staff or workers rather than construction services.

The reverse charge also applies to materials supplied as well as labour.

The legislation is designed so that if there is a reverse charge element in a supply then the whole supply will be subject to the domestic reverse charge. However, if the value of the ‘reverse charge’ work is 5% or less of the invoice total, then the normal VAT rules will apply to the invoice.

### **Applying the Reverse Charge**

1. The supplier making the reverse charge supply should:

- Not charge any VAT to their customer on the sales invoice;
- Validate that their customer is VAT and CIS registered, and obtain confirmation that they are not an end user;
- Not include any output VAT in box 1 on the return, because that becomes the responsibility of their customer;
- Include the VAT exclusive value of the sale in box 6; and
- Ensure the sale invoice raised:
  - includes wording that makes it clear that the reverse charge applies and that their customer is required to account for the VAT – something along the lines of “Reverse charge: Customer to pay the VAT to HMRC” ; and
  - state how much VAT is due under the reverse charge, or the rate of VAT that applies.

The supplier can still reclaim any input VAT suffered in respect of making reverse charge supplies.

2. The customer receiving the reverse charge supply should:

- Include the output VAT payable on the supply under the reverse charge in box 1;
- Not include the VAT exclusive value of the supply in box 6 (as already done by the supplier);
- Include the same amount as input VAT in box 4 (subject to the normal rules); and
- Include the VAT exclusive value of the purchase in box 7 in the normal way.

This should mean a VAT neutral position for the vast majority of customers as the VAT on the reverse charge supply will go in both box 1 and box 4 i.e. they cancel each other out.

### **Monthly Returns**

If a supplier undertakes a significant amount of work that will be subject to the reverse charge it will probably lead to regular repayments of VAT from HMRC on materials, tools and overheads. As a result it may be worth moving on to monthly returns to accelerate these repayments. An application to move to monthly returns can be made through your online VAT account. This would however mean 12 returns need to be completed and filed each year rather than 4.

### **Errors**

HMRC has confirmed that it will adopt a light touch as far as penalties are concerned for errors made in the first six months of the new legislation (i.e. until 31 August 2021) '*as long as you are trying to comply with the new legislation and have acted in good faith*'.

### **HMRC Flowcharts**

HMRC have produced two useful flow charts, one for the supplier and one for the customer.

[https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment\\_data/file/878587/Annex\\_1\\_-](https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/878587/Annex_1_-)

[\\_VAT\\_domestic\\_reverse\\_charge\\_for\\_building\\_and\\_construction\\_services.pdf](#)

[https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment\\_data/file/878594/20.01.15\\_annexe\\_2\\_customer\\_flowchart.pdf](https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/878594/20.01.15_annexe_2_customer_flowchart.pdf)

Detailed guidance can be obtained at <https://www.gov.uk/guidance/vat-reverse-charge-technical-guide>

The Team at Allens

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