

# VAT Brief

## Managing VAT in a Downturn

### In this edition...

of VAT Brief, given the current state of the economy and the credit crunch, businesses across all industries are coming under significant pressure to meet their ever demanding cash-flow commitments. At a time when “cash is king”, this Brief outlines some of the key cash-flow saving mechanisms in keeping their VAT liability to a minimum. In addition, some businesses may be entitled to retrospective VAT claims providing a welcome cash injection.

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### Basis of Accounting – Cash Receipts v. Invoice

Where a business accounts for VAT on the invoice basis, it is obliged to pay the VAT on its invoices issued irrespective of whether or not it has been paid by its customers. This can present significant cash-flow consequences for businesses as payment of the invoice may not be received for some time. However, where a business qualifies and accounts for VAT on the cash receipts basis (i.e. turnover < €1 million or at least 90% of its customers are unregistered persons), it is only obliged to remit the VAT due once it has actually been paid by the customer.

Given the increased delays in payment experienced by many suppliers, businesses currently on the invoice basis should consider if, due to a change in their circumstances, now qualify for the cash receipts basis. This in turn would reduce a business's commitment to meet its VAT payments until such VAT has been received.

During these challenging times, many businesses are seeing a decrease in sales. Consequently VAT liabilities are also decreasing. Any business paying VAT by way of direct debit payments should ensure such payments have been revised to reflect the change in circumstances.

## Continuous Services

Where a business, accounting for VAT on the invoice basis, supplies services on a continuous basis, they should consider using pro-forma invoices in order to defer the VAT liability until payment on account has been received.

Similarly, where a business is obliged to issue a VAT invoice, this must issue by the 15th day of the following month in which the supply took place. Businesses should ensure they are availing of the invoicing time limits to maximise their cash-flow position.

## Bad Debt Relief

Where a business has accounted for VAT but has yet to receive payment from its customer and the debt is ultimately written off, that business is entitled to claim bad debt relief on the VAT previously paid (not in the case of immovable goods). While certain conditions must be met before the relief is granted, there is no time limit in which a business must wait in order to claim the relief.

If a business has written off a debt and previously accounted for VAT on same, it should ensure it has claimed an appropriate input credit in respect of such VAT. Retrospective bad debt relief is possible subject to the 4-year time limit.

## Deposits & Cancellation Charges

Following a ruling by the European Court of Justice (ECJ), Revenue has revised the VAT treatment in respect of forfeited deposits and cancellation charges.

Essentially, when a business receives a deposit (being an advance payment in respect of a supply of a taxable good/service) from a customer, the business is obliged to account for VAT on receipt of same. However, where the supply does not subsequently take place as a result of the customer's cancellation and the deposit is not refunded, the business may reclaim the VAT previously accounted for on the deposit.

The same VAT treatment also extends to a cancellation charge levied by a business where the supply does not proceed. All businesses should ensure

they are claiming their appropriate entitlement in respect of cancellation charges. Retrospective VAT reclaims are possible subject to the 4-year time limit.

## Section 13B Status

Where at least 75% of a business's annual turnover relates to the supplies of goods (or certain types of contract work) outside the State that business is entitled to a VAT13B. Qualifying for VAT13B status ensures that the business's suppliers do not charge VAT. This provides significant cash-flow advantages as the business does not suffer the time delay of reclaiming the VAT in the normal manner.

All businesses supplying goods outside the State should consider whether or not they qualify for such status. Businesses already availing of VAT13B status should ensure their certificates are still valid and, if due to expire, reapply to Revenue in a timely manner.

Businesses supplying continuous VATable services to non-Irish customers should consider the possibility of using the VAT60B procedure. Consequently the supplier would not be obliged to charge VAT. Such status would benefit both parties especially where the supplier is accounting for VAT on the invoice basis.

## Principal Contractors & Reverse Charge

Since 1 September 2008, subcontractors can no longer charge VAT to principal contractors in respect of construction services to which RCT applies. Instead the principal will be obliged to self-account for VAT on the value of the services received.

Such a change is likely to provide cash-flow benefits for both the principal and the subcontractors.

## Multiple and Composite Supplies

Many businesses supply goods and/or services as a package for a single consideration. Such packages can be by way of a composite supply (i.e. a single supply which comprises of a principal and an ancillary element) which typically will be subject to VAT at the rate appropriate to the principal element or alternatively a multiple supply (i.e.

two or more individual supplies which are economically dissociable) which are subject to VAT at the rate appropriate to each individual supply.

Traders should examine any "package" supplies to ensure that the correct VAT treatment is being applied as opportunities can arise in some circumstances.

## VAT on Property – Letting of Residential Property by Property Developers

Where a property developer who completes a residential property post 1 July 2008 and was entitled to claim VAT on development (e.g. trading stock) subsequently let out the property, the developer will not suffer an immediate claw-back of the VAT. Instead the developer will be required to repay the VAT by way of annual instalments pending sale. In this regard, Revenue view the property as being 'completed' when the letting commences.

In the current economic climate this cash-flow benefit is likely to prove very attractive.

## Change in VAT Rate

The recent budget increased the standard rate of VAT from 21% to 21.5% with effect from 1 December 2008.

This rate increase, becoming effective in the middle of a bi-monthly period, is likely to have an impact from a business systems and invoicing perspective. In addition, businesses which have advertised their prices in catalogues etc should consider the impact the rate increase will have on their margins and whether or not the VAT can be passed on to the customer.

## Conclusion

The above merely outlines some of the areas in which a business can manage and control its VAT obligations through these challenging times. It is not an exhaustive list. Consequently should you wish to discuss any aspect of the brief in more detail please call your usual PwC contact or one of the contacts provided on the previous page.