



F S P G
CHARTERED ACCOUNTANTS



KEY GUIDE

Making tax digital



Taking tax compliance into the 21st century

Making Tax Digital (MTD) is the HM Revenue & Customs (HMRC) project to get businesses to keep digital tax records for direct reporting to HMRC. HMRC has described it as the biggest change to the UK tax system since the introduction of self-assessment. However, 2017 saw the government backing down on the scope and pace of the reforms, and under the revised plan businesses will not be mandated to use MTD until April 2019 and then initially only to meet their VAT obligations.

Once MTD is fully implemented, users will no longer have to submit an annual self-assessment tax return, but will report information to HMRC quarterly along with an annual declaration. MTD will, says HMRC, make it easier for individuals and businesses to keep on top of their tax obligations.

Going digital

At first sight, the prospect of reporting quarterly to HMRC instead of annually doesn't seem particularly appealing. But the aim is that reporting will be mostly 'painless', because it will be an integral part of businesses' accounting software. For MTD to work, most businesses will have to maintain digital accounting records using software that can send information directly to their personal tax account with HMRC.

Eventually the administration of tax will be fully digitised. You probably already have a personal tax account (also known as a digital tax account), which for employees is automatically populated with details of income and PAYE tax deducted taken from the Real Time Information (RTI) system. Currently, the information in anyone's personal tax account is limited, but HMRC says that by 2020 taxpayers will be able to see a comprehensive picture of their income and tax in their personal tax account at any time during the tax year.



Planning point

Businesses with turnover above the current VAT threshold will have to keep digital records and report to HMRC quarterly on VAT from April 2019.

When will MTD start?

The general election in June 2017 delayed the legislation needed to put MTD in place. In the months before the election, concerns had been raised about the pace of the original timetable, under which some businesses would have had to use MTD from April 2018. Because of the feedback, MTD will now be implemented much more slowly than previously intended.

The revised plan is:

- Only businesses (including companies) with turnover above the VAT threshold (currently £85,000) will have to keep digital records and report their figures quarterly to HMRC.
- This will only be for VAT purposes and will start in April 2019.
- A business whose turnover is below the VAT threshold, but voluntarily registered for VAT, will not be required to use MTD. However, if a business is initially required to use MTD for VAT purposes, it will have to continue to do so if its turnover subsequently drops below the threshold.

- Businesses and landlords will not have to keep digital records and report quarterly for other taxes until it is clear the system works well, and not before April 2020 at the earliest. This is also the earliest date by which MTD will be introduced for corporation tax purposes.
- Businesses and landlords can choose to opt in to MTD earlier than required.

HMRC has started small-scale testing of MTD for VAT, and will follow this with a wider, live pilot starting in spring 2018. This will allow for over a year of testing before any businesses are required to use the system.

With an extended timetable, you now have time to plan, assess and test your systems, invest in relevant software if you need to and ensure your business is ready. The introduction of MTD for VAT could, however, possibly coincide with the UK leaving the EU. The position is currently uncertain, but this could alter the VAT treatment of EU transactions – making any planning much more difficult.

How will MTD affect your VAT returns

VAT returns must be submitted online, with few exceptions. However, businesses can use any type of record-keeping system they like if it provides accurate figures. Some businesses still keep paper records, some use computer spreadsheets, while others use accounting software which may or may not be online or cloud-based. With some online or cloud-based accounting software, you can already connect to HMRC to make your VAT return.

HMRC's software is currently used to file around 90% of VAT returns. Under MTD, however, almost everyone will have to use some form of third-party online or cloud-based software that will link directly with HMRC's MTD systems.



Planning point

You will not have to keep all your records and invoices electronically but will need to compile at least quarterly digital records to submit for your VAT returns.

Example – MTD software

Joan is registered for VAT and will be required to use MTD from April 2019. She currently uses spreadsheets to maintain her VAT records, with VAT returns submitted using HMRC's software. Joan's VAT invoices are stored manually.

Since HMRC will no longer provide its own software, Joan must find a commercial MTD solution, and accounting software producers are already working on enhancing their existing packages to make them compatible with MTD.

HMRC has said that businesses will be able to continue to use spreadsheets for record keeping, provided the spreadsheets meet the necessary requirements of MTD. This is likely to involve Joan combining her spreadsheets with whatever software she chooses.

MTD will not mean having to store invoices electronically, so Joan will be able to continue to store her VAT invoices manually.

Joan's MTD software will need to preserve her digital records for six years.

Submitting returns

Most businesses submit their VAT returns quarterly, but some prepare annual returns and others make monthly VAT repayment claims. These options will still be available under MTD. The move to MTD will also not affect the use of retail schemes or the flat rate scheme.

Taxpayers will be able to authorise their agent or accountant to access their digital tax account, so that the agent can prepare and submit quarterly figures on behalf of their client.

Anyone who is 'digitally excluded' will not have to use MTD. You may be 'digitally excluded' because you have inadequate or no internet access at your location, you cannot use computers because of a disability or your age, or you object to using computers on religious grounds. These are the same exceptions that currently apply to VAT online filing.

Projected benefits of MTD

MTD is a long-term project which is intended to change the way businesses interact with HMRC. HMRC has outlined four broad advantages of MTD, although the full benefits will only come later when MTD encompasses taxes beyond VAT:

- **Better use of information** – individuals will no longer have to provide any information that HMRC can obtain from elsewhere, for example from employers (under RTI), banks and other government departments. Taxpayers will be able to access this information at any time and check whether it is correct and complete.
- **Tax in real time** – HMRC will collect and process information affecting an individual's tax liability almost immediately it is available, which will reduce errors and prevent tax due or repayments owed from building up.
- **A single financial account** – taxpayers will see a comprehensive picture of their liabilities and entitlements in one place.
- **Interacting with HMRC digitally** – taxpayers and their agents will be able to contact HMRC online more easily via webchats and secure messaging at a time to suit them and through their own accounting software.

Further gains will arise from the use of digital accounting packages. These gains, already available from existing software, include:

- Access to your business records at any time wherever you have an internet connection.
- Regular management accounts to help you manage your finances and make business decisions.
- Immediate access to your customer and supplier account balances, and stock levels.
- Ability to create and send invoices.



Planning point

The long-term purpose of MTD is to allow taxpayers to access their information from a single account, submit in real time and interact digitally with HMRC.



Planning point

The extended timetable for MTD provides an opportunity to review your accounting software fully and decide what your needs and requirements really are.

- Recording sales and receipts.
- Connecting with your business bank accounts.
- Direct access for your agent or accountant.
- Updates to ensure your accounts and business records always comply with any changes in the law.
- Easier preparation of your tax returns even before MTD is extended to income tax.

Accounting software

Access to accounting software generally incurs a monthly charge. The price depends on the level of sophistication required. However, using an accounting package may reduce accountancy fees if it improves the quality of your business records so that we have less to prepare.

Although HMRC will not provide software, commercial companies are expected to make free software available to businesses with the most straightforward affairs, such as:

- Those that are unincorporated.
- Businesses that have income under the VAT threshold.
- Businesses that have no employees.

HMRC is working with software developers to define the minimum functionality of a free software package that would meet MTD requirements. This would most likely allow businesses to:

- Keep digital records.
- Generate and send quarterly updates to HMRC.
- Complete end of year activity to ensure compliance with MTD requirements.
- Include arithmetical error correction.
- Include a basic level of built-in prompts and nudges, with basic help functions.
- Enable information to be sent from HMRC to businesses about their tax liability.

Free software is unlikely to be available for businesses with turnover above the VAT threshold – these are the only businesses that will have to use MTD from April 2019.

Although businesses will only have to use MTD for VAT to start with, it is important to look to the future. Your accounting system will need to work for all taxes and it is better to get it right from the outset.

Preparing for MTD

If your business is registered for VAT and your turnover is above the VAT threshold, you will have to use MTD from April 2019.

Example – Review of software

ABC Ltd's bookkeeper uses an accounting software package to maintain the company's accounting records. The company will be required to use MTD from April 2019.

It is likely that ABC Ltd's software provider will simply add MTD compatibility to its accounting software package, so that ABC Ltd's bookkeeper will simply need to make sure that the relevant updates are installed.

However, this is an opportunity for the company to review whether the software it is currently using best serves the current and future needs of the business.



Planning point

Review your systems, software and processes regardless of when MTD may impact your business so you can plan and budget for any changes that might be necessary, or advisable.

If your business turnover is above the VAT threshold and you are not currently using accounting software, this is a good time to consider enhancing your recording keeping by adding the capabilities that digital accounting can provide.

Secure your systems

If you move to online accounting, it is essential that your data will be secure (indeed the same applies to any use of a device connected to the internet). IT systems are vulnerable to many kinds of attack, for example malware, viruses, worms, hacking, phishing, access by unauthorised persons, theft of data and theft of hardware. Software and hardware can malfunction or suffer other accidental damage. However you should not let the risks put you off. There are several basic precautions you should take:

- Regular and frequent backups of data.
- If data is stored in the cloud, access to it must be protected and the data must be backed up.
- Use strong, memorable passwords and change them regularly, preferably without keeping them written down. Other secure access forms are available from password storage software to fingerprint recognition.
- Only give your employees and agents access to those systems and data that they need to carry out their jobs.
- Keep anti-virus and other protective software up-to-date (some operating systems do this automatically).
- Ensure that you and anyone else who uses your computers in your business exercise great care in dealing with emails, especially those containing links or attachments.
- Keep your premises secure.

You may well already do many of these things to protect your business, especially if you bank, pay bills and interact with suppliers and customers online.

Complying with your general tax obligations

Whether or not you will have to use MTD, it is essential that you keep complete and accurate records of your business and other income so you can make accurate tax and VAT returns.

MTD on its own will not guarantee accuracy. You still must make sure that all relevant income and outgoings are recorded. However, HMRC says that MTD will help businesses to get their tax bills right first time. MTD is not HMRC's only strategy for ensuring everyone pays the correct amount of tax due:

- HMRC makes compliance checks on tax returns, which may be triggered by the figures in the return or simply be random.
- An increasing amount of information comes from third parties, which HMRC uses to check information in tax returns.
- HMRC task forces target specific business sectors and locations where there is a high risk of tax evasion.

Where HMRC finds that a person has not taken enough care to make accurate tax returns, penalties will usually be charged. Pleading ignorance of the rules, or even an honest mistake, will generally not avoid penalties. Material inaccuracies are likely to be spotted, so it is therefore worth making the effort to get your tax right.

How we can help

All businesses, whether or not they will have to use MTD from April 2019, need to keep good accounting records to enhance business efficiency and to make accurate tax returns. We can review your accounting systems and advise on accounting software that will best serve your business needs.

If you will have to use MTD from April 2019, we can help you prepare by ensuring your software is compatible and, where necessary, helping you set up new systems and become proficient at using them. We can make the necessary reports for you by having direct access to your accounting data and software. We can help you on IT security and keep you up-to-date on any changes in tax and accounting compliance that affect your business.

This publication is for general information and is not intended to be advice to any specific person. You are recommended to seek competent professional advice before taking or refraining from taking any action on the basis of the contents of this publication. This publication represents our understanding of law and HM Revenue & Customs practice as at 10 January 2018.



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