



Implications of VAT Rate Change to Optics

Background

As you will be aware the Chancellor announced that the standard rate of VAT will be reduced from 17.5% to 15% from Monday December 1 2008.

This reduction of 2.5% is likely to have limited impact in the dispensing of optical appliances as the reduction will only apply to the sale of the goods as the Dispensing Service is exempt from VAT. Based on a 60% exemption rate for the supply of the dispensing service, the VAT rate reduction will fall to approx 0.8% of the total selling price.

For example:

17.5 % VAT rate

Sale of Spectacles	= £150.00
Dispensing Fee 60%	= £90.00
Goods subject to VAT at 17.5%	= £60.00
VAT due £60 x 7/47	= £8.93

15% VAT Rate

Sale of Spectacles	= £150.00
Dispensing Fee 60%	= £90.00
Goods subject to VAT at 15%	= £60.00
VAT due £60 x 3/23	= £7.82

VAT Differential = £8.93 - £7.82 = £1.11

VAT arising as percentage of sale price = 0.74%

The fact that the VAT rate has been reduced does not legally require a business to reduce its prices in line with the VAT reduction.

However, this change does throw up a number of issues for opticians in accounting for VAT correctly and we have identified these below.

Accounting for VAT

As the new rate of VAT of 15% is effective for all sales made from Monday Dec 1 2008 it is a straight forward matter in accounting for the VAT on those sales. The VAT fraction to be applied to the VAT inclusive total is 3/23 as opposed to the current fraction of 7/47.

Where you have taken a deposit from a customer in advance of supplying the optical appliance and the dispensing is completed after Monday, the whole consideration can be subject to VAT at 15%.

If your VAT accounting period ends on Nov 30 2008 you will need to ensure that VAT on the deposit is accounted for at 15% and not 17.5%. This may require you to separately identify deposits received prior to Dec 1 2008 but for goods and services delivered post Dec 1 2008.

Where customers are on a direct debit payment scheme you have the option of leaving the monthly payment as it or offering a customer a small reduction in the price. Clearly this is dependent on the terms of your contract with your customer and you will need to see whether the monthly payment has any mention of VAT and whether it refers to a rate of 17.5% or states 'the amount includes VAT'

Apportionment Calculations

As the cost of goods in any Full Cost Apportionment calculation will be reduced as the amount is calculated on a tax inclusive basis, the result will be a marginal increase in the rate of exemption. However, given that the Chancellor has stated the rate reduction will only last for just over 12 months, you may consider that the time and effort to be expended in doing a new calculation for a marginal benefit outweighs the marginal increase in the exemption rate for the 12 month period.

The only other change of note to the apportionment calculation is that the new VAT fraction of 3/23 is applied to the goods value of any sale.

Fuel Scale Charges

There is no change to the fuel scale charge applicable since May 1 2008 but the VAT due will be based on the new rate of 15%. You will need to review the amount of VAT to be declared from Dec 1 2008.

Refunds

If you provide a customer with a refund after Dec 1 for a sale made before that date you will need to adjust your takings to take account of the VAT charged at 17.5%. For refunds of sales made after Dec 1 2008, an adjustment will be made based on the new rate of 15%

Partial Exemption

The de minimis rules have not changed and you can recover all of your input VAT if the amount attributable to making exempt supplies is less than £625 per month on average and less than half of the total input VAT claimed.

For those businesses who are just above the threshold they will need to recognise that the reduction in the VAT rate will mean they will incur less VAT than previously and they may well fall below the threshold.

For those businesses affected they will need to monitor the amounts of exempt input VAT they incur to see whether they fall below the presented limits and can recover the input VAT in full.

Computer Systems & Software

Systems should be modified prior to December 1, 2008 to account for VAT at the new rate of 15%, but if this cannot be done in time, HMRC will allow you to carry out a manual adjustment to allow you to account for VAT at the reduced rate.

If you are issuing tax invoices after December 1, 2008 and have not been able to amend your software to show the 15% rate you must account to the HMRC for the 17.5% rate charged on the invoice. However, you should raise a credit note adjusting for the amount of VAT incorrectly charged. This credit note will then reduce the amount of VAT payable to the correct rate of 15%.

The Future

Although the Chancellor announced that the reduced rate will only apply until December 31, 2009 he did not confirm that the rate will rise back to 17.5% and there is a likelihood that the rate will be set between 17.5% and 20% in the future.

In making any adjustments to your accounting systems you should bear in mind the need to be able to raise the standard rate again in 12 months time. You may also consider this eventuality in coming to a decision over your pricing strategy at this time.

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