



Domestic Reverse Charge

The Domestic Reverse Charge (“DRC”) should be coming into force on 1 October 2020 for the construction industry, however there are rumours that it may be delayed due to COVID-19.

A reverse charge is an anti-fraud measure and is designed to ensure that a supplier does not charge VAT and then fails to account for it to HMRC. The introduction of the reverse charge in the construction industry is a result of perceived widespread fraud in this sector.

It will only apply where construction services are “wholesaled” or onward supplied to another person in the chain. Therefore, final users will not need to operate the reverse charge. The reverse charge also only applies to services taxed at 5% or 20%. Hence, most services in the course of construction of new houses, Relevant Residential Purpose (“RRP”) and Relevant Charitable Purpose (“RCP”) buildings will not be caught by the reverse charge.

The definition of construction services for the DRC is similar to that for CIS. Broadly, if you are supplying services that are caught under the CIS scheme, you will need to look at whether the reverse charge applies.

You can prepare for the 1 October 2020 implementation date by:

- Checking whether the DRC affects either your sales, purchases or both;
- Consider whether you are an end user, if so you will need to issue certifications;
- Making sure your accounting systems and software are updated to deal with the DRC;
- Considering whether the change will have an impact on your cash flow; and
- Making sure all your staff who are responsible for VAT accounting are familiar with the DRC and how it will operate.

How does the reverse charge work?

The reverse charge is a means of accounting for VAT by the recipient rather than the supplier. Instead of a supplier charging VAT on services and the recipient claiming that VAT as input tax, the recipient accounts for both output and input tax.

For example:

A contracts with B to provide bricklaying services for an office block valued at £1,000.

Before 1 October 2020 the transaction would be:

- B would charge £1,000 (value of services) plus VAT £200 (20%) to A.
- B would include £200 in box 1 of its return as output tax and £1,000 in Box 6 as its net sale.
- A will pay B £1,200.
- A would claim the £200 VAT charged as input tax in Box 4 of its return and £1,000 in box 7 as a net purchase.

After 1 October 2020 the transaction will be:

- B will invoice £1,000 for its services and state on the invoice that the reverse charge applies.
- B will include £1,000 in box 6 as its net sale.
- A will pay £1,000 to B.
- A will claim the £200 VAT due as input tax in Box 4 of its return and £1,000 in box 7 as a net purchase. A will also claim the £200 VAT element due in Box 1 of its return as output tax and £1,000 in Box 6 as a net sale.

Overall, the same amount of VAT is being accounted for, it is just the way that it is accounted for that is changing.

If you would like further information about the DRC please contact one of team who will be happy to help.

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