

TAX PROCESSES FOR BUSINESSES

STUDY TEXT

Qualifications and Credit Framework

Q2022

Finance Act 2024

**For assessments from 27 January 2025 until end
January 2026**

This Study Text supports study for the following AAT qualifications:

AAT Level 3 Diploma in Accounting

AAT Level 3 Certificate in Bookkeeping

AAT Diploma in Accounting at SCQF Level 7

CONTENTS

	<i>Page number</i>
Introduction	P.5
Unit guide	P.9
The assessment	P.21
Apprenticeship learners only	P.22
Study skills	P.23
Reference material	P.26

STUDY TEXT

<i>Chapter</i>	<i>Study Text</i>
1 Introduction to VAT	1
2 VAT registration	27
3 VAT documentation	49
4 Input and output tax	81
5 VAT accounting schemes	95
6 VAT returns and overseas aspects	119
7 Errors, penalties and communicating VAT information	157
8 Employer responsibilities for payroll	185
9 Operating payroll	201
Mock assessment questions	233
Mock assessment answers	249
Index	I.1

ICONS

The study chapters include the following icons throughout.

They are designed to assist you in your studies by identifying key definitions and the points at which you can test yourself on the knowledge gained, or to direct you towards other areas of your studies (past or future) where you will encounter similar issues or skills.



Definition

These sections explain important areas of knowledge which must be understood and reproduced in an assessment.



Example

The illustrative examples can be used to help develop an understanding of topics before attempting the activity exercises.



Test your understanding

These are exercises which give the opportunity to assess your understanding of all the assessment areas.



Reference material

These boxes will direct you to the AAT reference material that you can access during your real assessment. A copy of this reference material is included as an Appendix to this document.



Foundation activities

These are questions to help ground your knowledge and consolidate your understanding on areas you're finding tricky.



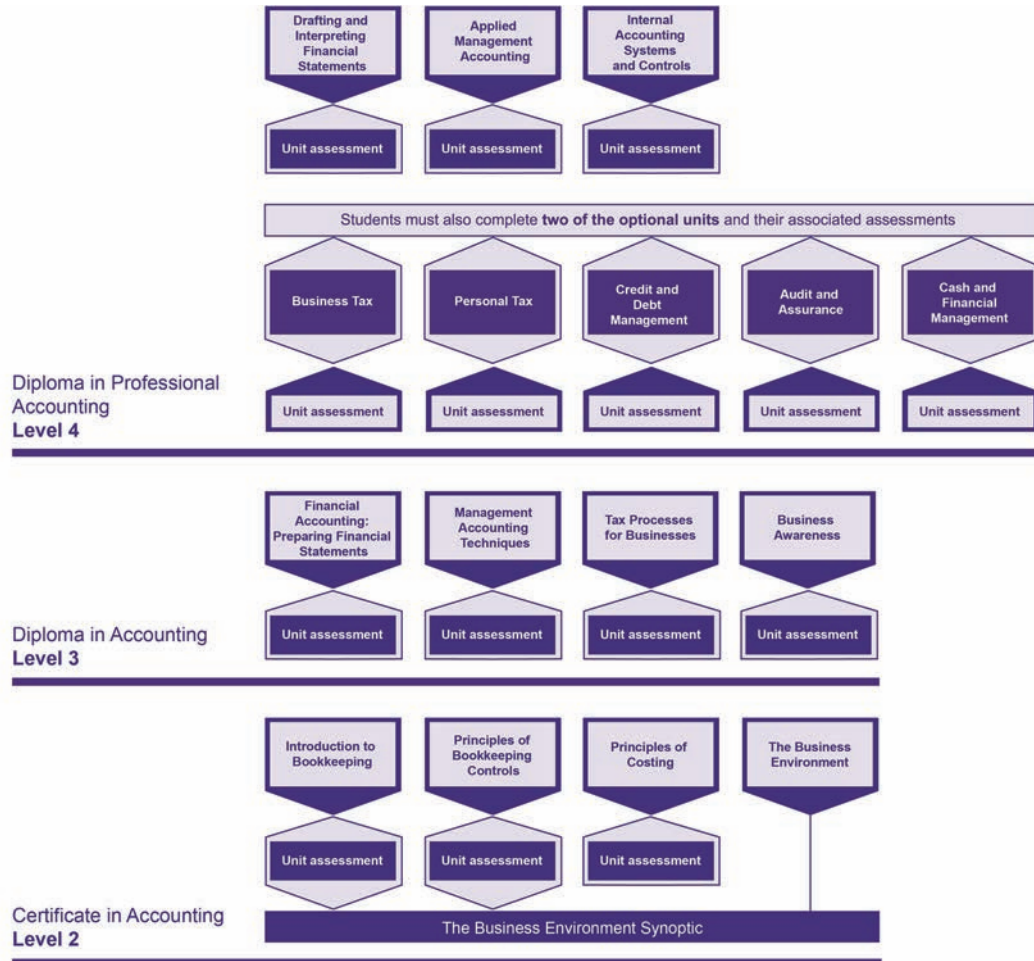
Extension activities

These questions are for if you're feeling confident or wish to develop your higher level skills.

Quality and accuracy are of the utmost importance to us so if you spot an error in any of our products, please send an email to: mykaplanreporting@kaplan.com with full details.

Our Quality Co-ordinator will work with our technical team to verify the error and take action to ensure it is corrected in future editions.

TAX PROCESSES FOR BUSINESSES



Introduction to VAT

Introduction

This chapter introduces some of the basic ideas of value added tax (VAT), including who it is charged to and how it is collected. One key concept to cover is that of tax points. The rules for determining the tax point are important. The tax point is the date that determines in which VAT period the VAT on transactions should be included.

This unit requires you to have knowledge of VAT rules, to be able to identify errors in VAT returns, to understand VAT penalties, and understand the powers that HMRC has.

ASSESSMENT CRITERIA

Understand UK tax law principles relating to VAT (1.1)
VAT registration and deregistration requirements (1.2)
Extracting relevant data from accounting records (2.1)
VAT calculations (2.3)
Legislation, regulation, guidance and codes of practice (5.2)

CONTENTS

- 1 Introduction
- 2 Types of supply
- 3 Tax point
- 4 HM Revenue and Customs

1 Introduction

1.1 Sources of tax law and practice

The basic rules of the UK tax system are built on several key pillars.

Firstly, tax strategies, such as the rate of VAT, are determined by the government, which is elected by the UK public through a democratic process. These strategies outline how taxes should be applied and collected.

Secondly, tax legislation forms the legal framework that governs taxation. Compliance with these laws is mandatory. Each year, the annual Finance Act updates tax legislation, ensuring it stays current and relevant.

Additionally, case law plays a crucial role in the UK tax system. This refers to the decisions made in tax-related court cases. Often, these cases involve debates over the interpretation of tax laws. The rulings from these cases are binding and provide valuable guidance on how tax laws should be understood and applied.

This helps create consistency and clarity in the application of tax laws.

1.2 What is VAT?

VAT is:

- an indirect tax on consumer spending
- charged on most goods and services supplied within the UK
- suffered by the final consumer, and
- collected by businesses on behalf of HM Revenue and Customs (HMRC).

Overview of how VAT works

VAT is collected by businesses at each stage in the production and distribution process of supplying goods and services as follows:

- businesses account to HMRC for the tax (known as output VAT) on sales
- if the customer is VAT registered and uses the goods or services for business purposes, then the customer can recover the tax which was paid over on the purchase of the item or service (known as input VAT)
- accordingly, businesses actually account to HMRC for the tax on the 'value added' to the product at that stage of the process.

TAX PROCESSES FOR BUSINESSES

Businesses are merely acting as collectors of VAT on behalf of HMRC and they do not suffer any tax.

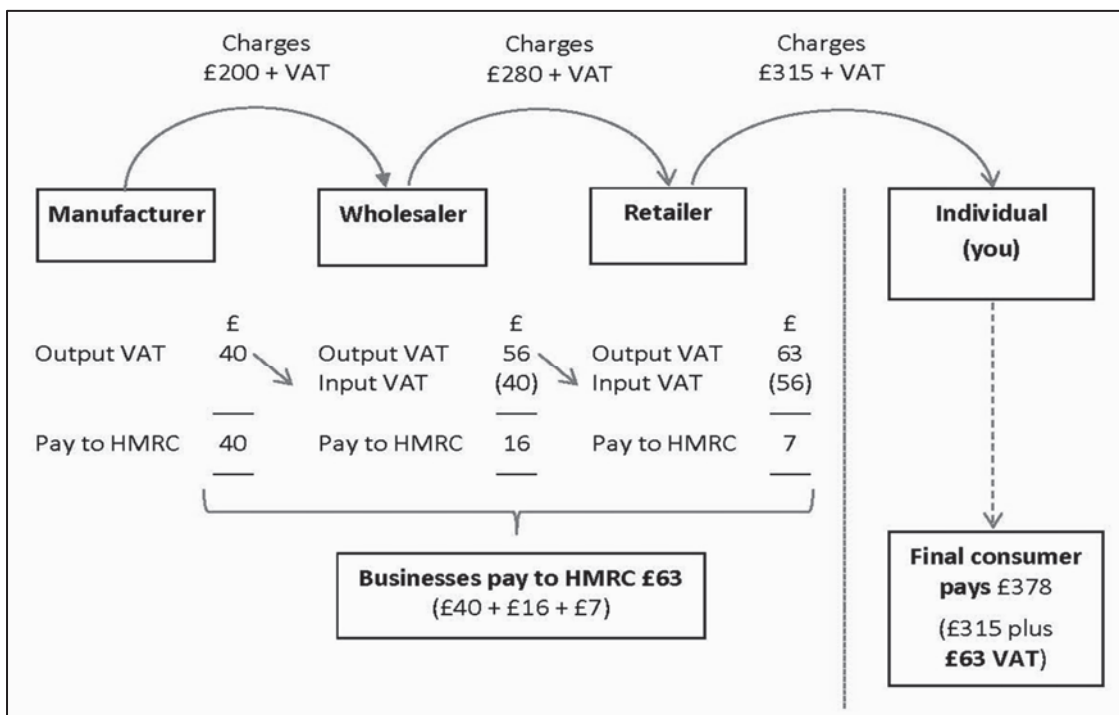
It is only the final consumer, who cannot recover the input VAT, who suffers the tax.

VAT is therefore an indirect tax:

- because it is paid indirectly to traders when you buy most goods and services, rather than being collected directly by HMRC from the taxpayer as a proportion of their income or gains.

How VAT works is shown in the illustration below.

Assume that the rate of VAT throughout is 20%.



Who charges VAT?

VAT is only charged

- by **taxable persons**
- when they make **taxable supplies**
- in the **course of their business**.

VAT is not generally charged on non-business transactions.

For example, you would not have to charge VAT if you simply sold some of your spare clothes to a friend.

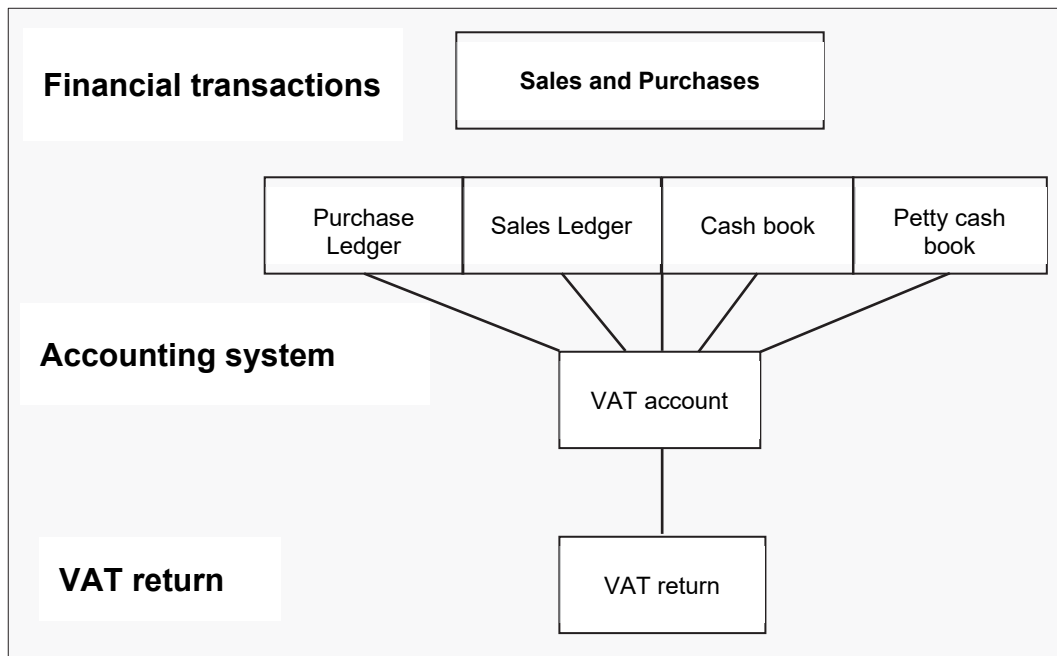
How is VAT recorded in the accounting system?

VAT is charged on most goods and services and the amount of VAT is shown on the sales and purchase invoices.

The VAT on invoices and credit notes is then recorded in the relevant book of prime entry, the totals from the daybooks are transferred into the general (or nominal) ledger.

The relevant ledger account for the VAT entries is the VAT control account, sometimes this is simply referred to as the VAT account.

Making Tax Digital (MTD) software then extracts the information from the VAT account and automatically completes the VAT return (Chapter 6). The business then reviews the draft return to check that the figures are correct. Once satisfied that the return is correct it is then submitted electronically using the MTD software directly to HMRC.



1.3 Taxable persons



Definition

Taxable persons are businesses which are (or should be) registered for VAT.

A person can be an individual or a legal person such as a company.

VAT registration rules are dealt with in Chapter 2.



You are viewing a sample

Interested in the full version?