

## Just when you thought it was safe...

It would be a mistake for businesses to believe that Making Tax Digital for VAT is over and dealt with. There is a monster lurking in the depths of the legislation referred to as the “digital link”.

Those businesses which are caught by this delayed part of the legislation may find they “need a bigger boat” to avoid being in hot water with HMRC.



### So what exactly is this about?

A ‘soft landing period’ was granted to businesses adopting Making Tax Digital (MTD) for VAT when it first came into operation in April 2019.

This gave 12 months to get systems 100% digitally linked, to comply with MTD’s requirements.

In 2020, this soft landing period was extended to April 2021 because of coronavirus disruption.

This soft landing period ends however on 1<sup>st</sup> April after which time, the digital links part of the legislation comes into full force and becomes a legal requirement.

### SUMMARY OF KEY POINTS

Digital Links becomes law from 1<sup>st</sup> April 2021.

VAT notice 700/22 contains some useful examples: [VAT Notice 700/22: Making Tax Digital for VAT - GOV.UK \(www.gov.uk\)](https://www.gov.uk/government/consultations/vat-notice-700-22-making-tax-digital-for-vat)

“Cut or Copy and Paste” does not meet the requirements.

### What is an MTD digital link?

To be compliant with Making Tax Digital for VAT, HMRC requires businesses whose turnover exceeds the VAT registration threshold (£85K per annum) to use “functional compatible software” in order to submit their VAT returns. This has been the case since MTD become mandatory for such businesses in April 2019.

But what if you use more than one piece of software to record your accounting transactions? For example, perhaps you use one piece of software to record sales income and another to collate purchase invoices, then submit your VAT return. You may also use spreadsheets for part of your accounting – for example a daily takings sheet or summary.

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Some businesses may have in the past, used largely manual methods to transfer the information from one piece of software to another. Digital links means transferring the data from one system to another in a digital manner without manual typing of figures or copying and pasting. A digital link also applies to recapturing or modifying the data when moving it between two digital places.

For example, a digital link exists when a business retains all transactions in a spreadsheet and uses a formula to calculate a total.

There are strict rules on what defines a digital link for MTD. According to HMRC, they have two characteristics:

- Data is transferred electronically between software programs, products or applications. This could include linked cells in a spreadsheet, such as a formula.
- The transfer is automated. It does not need manual intervention such as copying over the data by hand or manually moving data between two or more pieces of software. But you can, of course, click a button to initiate the process.

HMRC accepts the following less obvious examples as digital links, although there are others:

- Emailing a spreadsheet so it can be imported into software.
- Using a memory stick or pen drive, even if you physically hand this to somebody else who then imports the data into their software.
- CSV or XML import and export, including the downloading and uploading of files.
- API: This is the technology used when software or computers talk to each other to transfer data. It's how accounting software talks to HMRC's computers in order to submit your VAT return, for example.

HMRC state that it wants digital links, not because it wants to make things more difficult, but rather to reduce the potential for errors. Fewer errors mean a reduced possibility of penalties for businesses and it means HMRC are more likely to collect all the taxes it is due. HMRC also points out that automation can help businesses become more efficient and streamlined.

VAT Notice 700/22 contains guidance for businesses as well as some useful examples and flow charts – find it here: [VAT Notice 700/22: Making Tax Digital for VAT - GOV.UK \(www.gov.uk\)](https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/612222/VAT-Notice-700-22-Making-Tax-Digital-for-VAT.pdf)

### What is not a digital link?

HMRC states one thing which is definitely not a digital link: 'cut and paste' or 'copy and paste' to select and move information, either within a software program or between software programs.

There are different rules for making input/output adjustments such as required for partial exemption, for example. The total of the adjustment must be kept as a digital record but the calculation you use to create it does not need to be digitally linked (although it should be retained for your VAT record keeping). Instead, adjustments can be manually journaled into your VAT accounting.

In other words, this is the one instance where it is acceptable to manually type figures or cut/copy and paste.

### Digital link myths

Perhaps understandably, there has been some confusion about the digital linking requirements. Here are some pointers:

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### *Spreadsheets*

Put simply, the end of the soft landing period does not mean the end of spreadsheets in your VAT accounting. Spreadsheets alone can be used to submit VAT providing they are MTD API-enabled so they can record and submit digital transactions.

Spreadsheets can also be used as part of a larger software suite, assuming there are digital links in place between all the software used.

### *Manual adjustments*

As mentioned earlier, the end of the soft landing does not mean the end of manual adjustments for things like the capital goods scheme, partial exemption and so on. Manual adjustments prior to submission are completely acceptable so long as the adjustments are held digitally and retained for VAT records.

For example:

Based on the underlying transactions, Betty's software records VAT box 1 as £1,000.

Betty then makes a manual adjustment for £100 (for which she has supporting evidence/calculations), and the software automatically calculates that the revised box 1 figure is £1,100.

This is acceptable.

What would not be acceptable is if, based on the underlying transactions, Betty's software records VAT box 1 as £1,000 and she manually overwrites this figure with £1,100.

### *Bridging software*

Many people think that the end of the soft landing period means bridging software can no longer be used. This is not correct. As long as bridging software is used in the appropriate way and digital links are in place then it is fine to keep using it. This will be the case for the foreseeable future.

### **What should I do if I think I have a problem with my digital links?**

First, check if the data that you want to cut/copy and paste is that specified as a **digital record** in the MTD for VAT Notice 700/22. Your VAT records are likely to be extensive but the MTD for VAT rules encompass only certain figures. For example, you do not need to keep a digital record of customer names and addresses. Read sections 4.3.1 to 4.3.3 for more examples.

If you are using the Flat Rate Scheme, you don't need to keep digital records of your purchases (unless they are capital expenditure goods on which the input tax can be claimed). So, you can happily cut/copy and paste data relating to these purchases.

Retail businesses need to keep a digital record of their daily takings. It is permissible to key the daily takings directly into your MTD accounting software to create the digital record – you do not need your till to link to the VAT software, but this should be shown daily and not added together for a longer period.

A rule of thumb is that MTD record-keeping requirements cease at the invoice level. For example, you can handwrite invoices, if you like, provided the transactional data is transferred to your digital VAT accounting solution as soon as possible. You need to transfer the tax point date, the value of the sale, the VAT rate applied, and the VAT element from the invoice.

You should seek advice however, from us or HMRC, if you are uncertain about whether your processes and procedures will meet the MTD for VAT digital links requirements.

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## Can I get a digital link extension for MTD for VAT?

Due to the coronavirus disruption, and despite the extension to April 2021, some businesses may continue to have problems converting their legacy IT systems to get ready for the end of the soft landing period.

HMRC is allowing some businesses to apply to extend the soft-landing period beyond April 2021. See section 4.2.1.3 of VAT Notice 700/22 for specifics, but in summary, to be eligible, your business will need to tick one of the following boxes:

- Your business uses complex or legacy IT systems that mean 100% digital linking genuinely is not possible by April 2021. This will typically be for reasons outside of your direct control.
- You have recently acquired another business and it is impossible to get everything digitally linked by April 2021.

Note that cost alone is not considered a good reason.

To apply for the extension, email [mtdspecificdirections@hmrc.gov.uk](mailto:mtdspecificdirections@hmrc.gov.uk) to request a form, and then set out your case about why your systems cannot be 100% digitally linked in time, including explaining why your current setup does not meet the requirements and why you cannot purchase better software.

You will need to provide details of your current MTD for VAT accounting solution, including a “map of your existing VAT systems, highlighting the exact areas that cannot be digitally linked”.

And finally, you will need to provide a timetable for getting 100% digital linking in place.

### Conclusion

If you have questions about the ability of your processes or procedures to meet the digital links requirements of MTD for VAT, then get in touch with us now. We are here to help. We have specialist staff who are able to analyse your current situation and advise you on any changes you may need to make. They can recommend software and solutions and help you put any changes in place, including training you or your staff.

Penalties for incorrect accounting are very real and could end up costing your business. Any expense you might object to spending upfront should be considered alongside this. Contact us below:

[VAT@thomsoncooper.com](mailto:VAT@thomsoncooper.com) or call 01383 628800 or 0131 226 2233