Braced for Brexit?

Richard Asquith suggests that accountants should ensure that their clients are fully prepared for the UK's exit from the European Union.

TEN SECOND SUMMARY

1 Brexit includes leaving the EU VAT regime and probably the Customs Union.
2 140,000 businesses face new tax and customs declarations obligations.
3 Clear threats include tax penalties and the disruption to trade, but schemes available to smooth the disruption.

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Businesses are not braced for Brexit. In Avalara's annual Brexit readiness survey, of the more than 100 businesses questioned, only 7% of businesses with international commerce had undertaken "substantial preparations" – 47% were partially ready, while 46% had not even started planning.

Given that the UK's departure from the EU represents the biggest economic change to impact this country in more than a generation, this is alarming. With potentially less than five months until a violent rupture from the UK's main trading partners' indirect tax and tariffs systems, it is time for businesses to understand how it may disrupt their international trade.

What changes on Brexit?

The UK is scheduled to leave the EU on 29 March 2019, two years after the government's triggering of the Lisbon Treaty's Article 50 exit procedure. Subject to a potential transition period to December 2019, this means the UK leaves the EU VAT regime and the Customs Union early next year. At this point, the UK becomes a "third country" in the eyes of the EU. This will lead to the loss of many tax simplifications, new obligations to pay import VAT and customs duties and – for smaller businesses – obligations to register for VAT in other EU countries.

The UK will be free to control more of its own VAT rules, including the provision of subsidies to particular causes and industry sectors. It will also be able to start setting and collecting its own duties – or indeed cut them to provide a boost to UK consumers and importers. All the powers to implement such polices are now enshrined in the Taxation (Cross-Border Trade) Act 2018, passed in September.

It will be small businesses, with limited finance resources and expertise, that will feel the brunt of this colossal return of taxing powers to Westminster. The details can be seen by an examination of the impact on various sectors and business models.

Importers of goods face import VAT

Importers of goods into the UK from the EU will face two major changes: import VAT and customs declarations.

Any goods clearing into the UK from the EU after Brexit will be subject to 20% UK import VAT. This is due when goods clear customs into the county and may be recovered by the business in their next VAT return by offsetting against any sales (output) VAT or claiming a credit refund. This will represent a considerable new cash flow bill for importers, requiring a potential extra bank credit line. However, the good news is that government has indicated that it will introduce a "postponed accounting" VAT deferment scheme to alleviate this. In this case, importers would not have to pay the import VAT and will simply record the import in their next VAT return.

Brexit will affect British exporters to the EU in the same way. Sellers into the EU27 will have to pay import VAT at the appropriate national rate. However, 19 EU states offer an import VAT deferment scheme like the one now proposed by the UK.

Post-Brexit, UK companies will no longer be required to complete Intrastat reports, which detail goods sent across EU borders.

Loss of EU VAT registration exemptions

A major loser on Brexit will be small UK e-commerce sellers to consumers in the other EU states. Currently, they do not have to VAT register in their customers' countries as long as they stay below the "distance selling thresholds", which permit the sellers to charge UK VAT and pay this to HMRC. These thresholds are usually €35,000 a year for each country – the exceptions are Germany and the Netherlands, which have a €100,000 annual limit.

For an estimated 27,000 sellers, from their first sale they will have to VAT register in their customer's home country immediately to charge the correct VAT. It is possible to avoid this by forcing the customer to collect the goods from a local post office or delivery agent, but this will include an unpleasant import VAT bill for the customer who may be reluctant to make repeat purchases.

Given the EU estimates that each EU VAT registration costs €6,000 a year in agent and opportunity costs, this may discourage small UK traders from promoting their online offering in the EU, so cutting off a slice of their incomes. Further, 20 EU countries will require such traders to appoint a local fiscal representative for VAT. Since these share the seller's VAT liability, they are expensive and may demand a bank guarantee.

New paperwork and irrecoverable tariffs

For small businesses, the UK exiting the Customs Union may be a bigger headache. Inside the union, businesses may sell or source goods across borders without any immediate form filling or tariff payments.

Post-Brexit, this will change because all goods imported into the UK from the EU will have to be declared to the UK customs authorities. This will require the completion of a customs import declaration (SAD) form. This requires details such as: the importer of record; customs treatment; details of the goods and customs code; Incoterms; tariffs due and method of payment.

HMRC estimates that, after Brexit, about 140,000 businesses will have to start preparing such declarations for the first time. It is expecting a rise of declarations from less than one million a year today to more than 2.5 million. Aside from the extra bureaucracy, importers will have to start determining tariff charges related to their goods, which run into thousands of combinations.

UK sellers to any EU27 country will also have to start declaring the movement of goods into those states for customs purposes. This will require EU SAD declarations, which are harmonised in the EU.

E-service providers face new registration

Currently, providers of digital services – including streaming and downloading media or software – to consumers, must charge the VAT rate of their EU consumers' home states. However, since 2015 they may declare and pay any VAT due through a single mini one-stop shop (MOSS) quarterly VAT return. After Brexit, the UK leaves this simplification and UK businesses will have to seek a single VAT registration in any EU27 state to continue to make the declarations and returns.

Companies that have been reclaiming foreign VAT on their hotel, taxi or exhibition costs in the rest of the EU27 will no longer be able to use the post-2010 electronic declarations system. This is managed by HMRC with the rest of the EU member countries. Instead, UK companies must go back to the old paper-invoice application process, which tends to take longer and results in cash delays.

Good news for business services

One sector that will suffer no VAT cross-border changes is B2B general and digital services. Sales or purchases of services between UK and EU27 VAT registered businesses will remain VAT-exempt.

Under the "reverse charge" mechanism, both parties simply record the transaction in their VAT returns with no cash payment. UK companies will also no longer have to complete HMRC's monthly EC sales listings. These declarations list sales to other VAT registered businesses in other EU countries.

Time to act

So what should businesses be doing now to prepare? Here are some basic, first steps.

- Map out cross-border sales or purchases and identify whether VAT registrations, charges or duty payments will become due.
- Identify whether supply chains be interrupted by new border controls and consider building-up extra stocks to avoid immediate shortages at Brexit.
- Ascertain whether the purchase of extra stock is covered in price or existing contracts. Can accounting software or logistics systems easily cope with any changes?
- Contact logistics agents for advice on new customs declarations and obligations.
- Businesses selling goods between the UK and EU should investigate obtaining "Authorised Economic Operator" status, which helps speed-up the clearance of goods through the UK or EU customs controls.
- Obtain from HMRC a free, binding customs tariff statement to help importers understand their potential duties bill.
- Importers can also look at various customs suspension schemes, including bonded warehousing and inward processing relief.

In short, small businesses should start planning and investigating various mitigating alternatives to avoid a "bracing" Brexit.