RM 211

RETAILERS
&
VAT

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MFEM

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A Introduction

Value Added Tax - what is it?

VAT is a tax on spending. It is ultimately paid and borne only by the final consumers of goods and services and is designed to tax their spending evenly and fairly. It is not a tax on the sellers of goods and services; they will simply collect VAT on behalf of the Government.

VAT will neither favour nor discriminate against individual suppliers. The tax will be charged on virtually all goods and services whether supplied by government, business, or non-profit organisations. It is not a tax on profits and therefore profit-making intentions do not come into consideration.

Almost all retailers will be liable to register for VAT and will have certain new liabilities and responsibilities.

This leaflet is designed to explain the impact of VAT on retailers, and to provide specific information to assist them in understanding VAT.

For more information on registration and accounting for VAT contact Revenue Management Division (RMD) on the VAT Hot-line.

How VAT Works

In effect, VAT works in two steps:

- A registered person, eg a retailer, pays 12.5% tax on all the goods and services purchased for the shop. But a credit can be claimed for this tax, **therefore no VAT is borne by the retailer.**
- The retailer includes 12.5% VAT on the price of all the goods and services sold, and pays this amount minus the VAT on purchases to the Revenue Management Division (RMD) **- therefore the VAT is all charged to the customer.**

So every dollar the retailer pays in VAT is recovered. For example, a retailer buys a shirt from a wholesaler for $40.00 and pays that price plus $5 VAT to the wholesaler. The retailer then sells the shirt to a customer for $50.00 plus $6.25 VAT. The retailer collects this $6.25 from the customer, deducts the $5.00 already paid to the wholesaler and sends the balance, ie $1.25, to the RMD. However, the retailer does not have to wait until he sells the shirt to claim the VAT on the purchase.

In practice, because a credit can be claimed for input tax all VAT is passed on through the production and distribution chain, and only the final consumer of the goods and services actually bears the tax. Like all other private consumers, the retailer will of course bear the cost of VAT on all purchases made for private use.

B Equipment and records

Cash registers

Shops will not need to buy new cash registers, or any other equipment, because of VAT.

Accounting records

As business records are already kept for income tax and business management purposes, it should be possible to complete the VAT return form from normal, book-keeping systems.

Invoices

The introduction of VAT will not mean that retailers will have to change their current method of recording sales. Sales to the general public will **not** require a special sales docket.

However, a **Tax Invoice** must be provided on request for the sale of most goods and services to another registered person. In such a case the following rules apply:

- No **Tax Invoice** is required for sales of less than $50.
- If the amount of the sale more than $50.00, (VAT inclusive) the Tax Invoice must show:
  - the words Tax Invoice in a prominent place
  - an individual serialised invoice number
  - the name and RMD number and address of the supplier
  - the name of the recipient
  - the date
  - the quantity or volume of the goods or services
  - a description of the goods and services supplied
  - either the VAT inclusive price and a statement that it includes a charge for the tax; or the total amount of the tax, the price excluding tax and the price including tax.

Note that retailers must also keep Tax Invoices to support their claims for input credits on goods and services over $50 that they buy themselves. However, the **Tax Invoices** do not need to be sent to the RMD with each return.

C Types of sales

Gift vouchers

When you pay VAT on the issue of a gift voucher will depend on the VAT accounting basis you have.

- **Invoice Basis**

Where a gift voucher has its money value shown on it, **VAT is payable only when the voucher is exchanged for goods or services.**

There is no VAT involved when the gift voucher is bought or sold by the retailer. The retailer selling the voucher will not include the cash from the sale of the voucher in total sales when working out the VAT for that period.

In many cases, the shop will have bought the vouchers at face value from a central agency. No VAT arises on that purchase. VAT will be payable, however, on any commission or service fee charged by a central agency for operation of a voucher system.

The voucher will be exchanged for goods which will have a price, including VAT equal to the value of the voucher. Shops will include the value of vouchers cashed in total sales for the purposes of working out their VAT payment to the RMD. Inclusion of vouchers cashed in with other sales is standard accounting practice so no extra work will need to be done for VAT.

- **Payments Basis**

VAT is accounted for when payment is made. ie, a shop issues a gift voucher to a customer on 30 July 1997 and receives payment for the voucher on the same day. The shop would account for VAT on the date it received the payment, 30 July 1997.

Agents

An agent must account for VAT only on **the commission** earned for agency work. For example, if a retailer sells lottery tickets on behalf of a lottery organiser, the retailer will be required to account to the RMD for VAT only on the commission earned, not on the value of the lottery tickets. However, assuming the lottery organiser is a registered person, VAT will be included in the price of the ticket. The lottery organiser will account for the VAT on the tickets to the RMD.

If a shop sells carvings on behalf of individual carvers but ownership of the work remains with the carvers, then the shop accounts for VAT only on the commission earned on sales. In other words, the shop is acting as an agent for the carvers. If the carver is a registered person, VAT will of course be charged on the sale, but it is the carver who must account for the VAT to the RMD.
Only the commission received by and agent need be taken into account in calculating turnover for the purposes of the $30,000 threshold.

Credit card sales

Credit card transactions are structured in a variety of ways. Generally, VAT will be charged at the time the credit card sale is made. The credit card company may settle transactions with the retailer on the same day as the sale is made - in this case, such sales are effectively the same as cash sales. The total value of the credit card sales vouchers will be included in the VAT output tax calculation for the appropriate period.

The fees charged by the credit card company for use of the credit card service will generally be exempt from VAT as a financial service.

Discounts

- **Prompt payment discounts**

Where goods are sold on credit and a discount is given for prompt payment, the VAT will be charged on the gross amount of the invoice. For example:

	$
10 metres floor tiles	1,000
VAT @ 12.5%	125
Total	**1,125**

A discount of 2% may be taken if paid within 7 days

In this example, if the discount is taken, the retailer will have to account for the $125 VAT in the VAT on sales calculation. The retailer will then claim a credit for the $2.50 VAT on the discount. If the two transactions occur in different return periods, $125 would be accounted for in the first return and a credit of $2.50 claimed in the next.

If the sale is to a registered person, the invoice should be a **Tax Invoice**. A credit note will not however be required to be issued even though the VAT on the **Tax Invoice** is now incorrect. This is because the discount was shown on the original invoice.

- **Trade or bulk purchase discounts**

Trade and bulk purchase discounts are really special prices offered to certain customers. The special price will always be the amount paid by the customer for the goods and VAT will be payable on that price. For example:

	$
100 kilos of nails	400.00
Less discount 5%	20.00
	380.00
VAT @ 12.5%	47.50
Total amount payable	**427.50**

Lay-by sales

Lay-by sales are delayed sales. When VAT is accounted for will depend on the accounting basis you are on.

- **Invoice Basis**

The VAT must be paid to the RMD in the return period when the goods purchased under a lay-by agreement are delivered or uplifted. If the lay-by sale is cancelled and the retailer retains some of the money paid, VAT is payable on the retained amount at the date of cancellation.

Cash received in installments on lay-by sales will be excluded when working out VAT until the goods are uplifted or the contract is cancelled. This is the normal accounting procedure for lay-by sales and accordingly will not require any special treatment for VAT purposes.

- **Payments Basis**

VAT will be accounted for on the individual payments made on the lay by item, at the time these payments are made. Part payment invoices will be required to make a claim for business related purchases paid for through a lay by system.

Hire purchase

- **Invoice basis**

The VAT liability arises when the hire purchase agreement is entered into. VAT is calculated only on the cash price of the goods noted in the hire purchase agreement. Credit charges are a financial service and are exempt from VAT. The VAT is payable to the RMD in the return period in which the contract is entered into.

- **Payments basis**

Under a payments basis VAT is payable or claimable when each hire purchase payment is made.

The assignment of the hire purchase agreement which is a financial service and is exempt from VAT.

Repossession

In hire purchase arrangements, goods are usually repossessed and re-sold if the buyer does not keep up the payments. The original buyer (not the repossessor) is considered to supply the goods to the new purchaser if there is a forced sale.

The repossessor will then be able to claim back 1/9 of the debt waived (if any).

- **Customer is a registered person**

If the goods that are sold are used in a taxable activity, VAT must be accounted for when they are sold after repossession. The repossessor is responsible for sending in a special VAT return to RMD.

- **Customer who is not registered**

  Where the customer is not a registered person, the repossession constitutes the sale of second-hand goods for which the re-possessor will be entitled to deduct input tax of 1/9th of the debt waived. (if any) No VAT is payable to the RMD, therefore a special return is not required in these cases.

Exempt goods and services

There are only two exempt categories and no input tax credit can be claimed for them:

- financial services
- donated goods and services sold by a non-profit body

The category most likely to affect retailers is financial services and this will affect only those retailers who make a charge for credit.

VAT on purchases of goods and services relating to the provision of customer credit cannot be claimed as an input tax credit, so some means of identifying those purchases will need to be established.

Example: a retailer buys a computer:

- If it is to be used to calculate customer credit, **no VAT on purchases can be claimed.**
- If it is to be used for stock control, **a full credit for the VAT can be claimed.**
- If it is used principally for stock control, and it is also used to calculate customer credit

then an apportionment has to be made to the VAT to be claimed to take account of that exempt use.

Exported goods

There are no special VAT concessions for tourists buying goods in the Cook Islands. However, a shop posting goods overseas for a tourist or for a Cook Islands resident wishing to send gifts overseas may enter the goods for export with the Customs section of RMD. The goods will be classed as exports and VAT will be charged at a zero rate rather than the standard 12.5%. VAT paid by the retailer on the purchase of those goods would be subject to a full VAT credit in the normal way.

D Goods

For own use

Stock taken from the shop for private use is subject to VAT. The value for VAT purposes is the **lesser** of the cost of the stock or its open market value.

Sold at less than market value

Goods sold for less than their market value to an associated person' who is not registered for VAT must be valued at the open market value of the goods.

Purchased for private use

A VAT credit cannot be claimed if goods are bought through a business account for private use.

Returned

A VAT credit may be claimed on goods returned by a customer if VAT has already been paid to the RMD for those goods. If a refund is made from the till a record should be kept so that the appropriate credit can be claimed in the VAT return.

Damaged

Nothing has to be done for VAT purposes about goods which have been purchased but which cannot be sold because of damage. The VAT credit will have been claimed for the purchase and there is not requirement to match purchases with sales.

If however damages are claimed from the supplier, the supplier will issue a credit note and the retailer will account for VAT on that figure.

Hired

VAT will apply to items hired out to customers and is payable with each periodic payment.

E Transitional arrangements

Credit for Turnover tax

A full credit will be given to registered persons for the turnover tax content(charged at the rate of 1% or 10%) of trading stock and stationery held at 30 June 1997. A credit will not be given for Turnover tax on:

- Goods which are part of a business's capital assets

or

- Hired goods or goods available for hire;

or

- Second-hand goods

The claim may be made in any one return before 30 September 1997. RMD must be satisfied that Turnover tax has been paid on goods for which a claim is made.

Retailers who cease to be liable for Turnover Tax and VAT from 1 July 1997

Any goods forming part of the retailers business on 30 June 1997 are deemed to be sold on that date for an amount equal to either:

- the market value of the goods on hand; or
- the greater of either, the sale proceeds or the cost of purchases, in the three month period of April to June 1997.

- The person will not have to pay the TOT liability that arises all at once. They will be able to pay it in three equal installments in July August and September 1997.

Pricing

Re-pricing during the transition period will need to take account of the removal of turnover tax on goods subject to turnover tax because of VAT

Price Tags

To avoid confusion all goods on display or advertised to the public must show an all-up price. There are several ways of showing prices to customers but in each case the total price (including VAT) must be shown.

Sales spanning introduction

Special provisions exist for situations where the invoicing, payment for and delivery of goods and services spans the VAT introduction date. In cases where:

- Invoicing and/or payment occurs before 1 July 1997 but delivery of the goods and services takes place after that date, eg a mail order item, the goods and services will be taxable because VAT is charged at the time of delivery.
- Invoicing and/or payment occurs on or after 1 July 1997 but delivery of the goods and services takes place before that date, eg trading stock delivered before 1 July which is invoiced on 20 July, no VAT will be payable because the goods were delivered before VAT came into force

Note: This is a guide to cover the situations of most retailers, but it is not a fully comprehensive list which covers the situation of all registered persons.

Further assistance/information

If you require further assistance in regard to administering VAT as part of your business, contact the Revenue Management Division of MFEM. They will be pleased to help you.

F Guide to VAT return preparation

VAT on sales/income calculation

		$
Total cash received (except from debtors and commissions)		50,000
Credit sales		40,000
Credit card sales		20,000
Hire purchase sales		5,000
Goods on lay-by uplifted		500
Vouchers redeemed		500
Commissions earned		200
Goods for own use/exempt use		1,000
Sub-total		117,200
Less:		
Cash from agency sales	700	
Installments on lay-by goods	600	
Hire purchase installments	1,000	
Prompt payment discounts taken	600	2,900
Total		**114,300**
Divide Total by 9:	**VAT collected on Income**	**$12,700**

VAT on purchases/expenses calculation

		$
All purchases of goods and services		80,000
Except:		
Salaries and wages		
Interest		
Loan repayments		
Other financial services		
Personal drawings		
Purchases from non-registered persons		
Purchases for private or exempt use		30,000
Total		**50,000**
Divide Total by 9:	**VAT paid on purchases**	**$5,555.55**

Alternatively, VAT can be calculated by adding up the VAT on all **Tax Invoices** received during that period.

Final calculation

VAT on sales	$12,700.00
Less VAT on purchases	$ 5,555.55
VAT payable to RMD	**$ 7,144.45**