**Reverse charge letter template: A letter to send to your subcontractors**

The letter should go to all VAT registered Subcontractors who you pay for construction services, whether paid under gross or net status under the Construction Industry Scheme.

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Dear XXXXX,

We are writing to you because you are a valued VAT registered subcontractor who provides us with construction services under the construction industry scheme (CIS).

From 1 March 2021 there will be a significant change to how suppliers in the construction industry supply chain account for VAT. The changes will apply to businesses making or receiving specified services that are reported under the Construction Industry Scheme (CIS). These changes will affect services that you invoice us for after this date that are subject to the standard (20%) or reduced rate (5%) of VAT. Zero rated services such as those on a new build dwelling are not subject to the new reverse charge rules. It is important that you understand the changes and plan for them because they may have a large repercussions for your cashflow this spring.

The published guidance that has been released by HMRC so far is at: www.gov.uk/government/publications/vat-reverse-charge-for-building-and-construction-services

It is also useful to look at and understand the published guidance on the CIS scheme itself which can be found at [www.gov.uk/government/publications/construction-industry-scheme-cis-340](http://www.gov.uk/government/publications/construction-industry-scheme-cis-340).

**How will this affect you as a Subcontractor**

It seems likely that when working as a subcontractor for us the new reverse charge rules will apply to all the applications for payment or invoices that you send to us. This means that after 1st March 2021 when you do £1,000 of standard work for us:

* You will invoice for £1,000 showing your supply as standard rated but NOT adding the £200 VAT to the amount due from us;
* We will pay £1,000 (not £1,200 as now);
* Our VAT return will show £1,000 plus £200 VAT as both an input and an output .We will therefore gain no advantage from the change;
* Because you have not been paid £200 VAT by us , you will not owe HMRC £200 VAT ;
* If you buy substantial materials used in subcontracted work, you may need to speak to your accountants to decide whether you should ask to send in monthly VAT returns in order to recover the VAT you have spent on materials each month rather than wait for a quarterly repayment;
* If you do some work for end consumers like domestic customers, or for customers who are not VAT registered , you will continue to bill them the VAT as you do now. The new rules only affect supplies you make to firms who are not the final user of the building or structure and who are VAT registered. It is therefore sensible from now on to keep a record of your customers VAT numbers and ask them whether they include the payments they make to you on a CIS return (ie the work is within the CIS scheme and they are CIS registered).

The change is mandatory VAT treatment, therefore you must prepare to ensure that you are compliant with the new VAT legislation.

If the contractors you work for do not pay you VAT after 1st March 2021 there will be implications for the flow of cash in your business and you MUST check how you can manage these.

For example:

* Will you have the money to pay your historic VAT bill from the last quarter in the old rules if no VAT is paid to you after 1st March 2021?
* Can you afford to pay wages and PAYE if VAT is not flowing through your bank account?

We will not be allowed to pay you VAT after the date of change so you must have prepared to withstand a period when cash flow may be stretched. Your invoices will need to be in a new format that does not add VAT to the total due. Your invoices should instead include the following narrative:

*Customer to account to HMRC for the reverse charge output tax on the VAT exclusive price of items marked ‘reverse charge’ at the relevant VAT rate as shown above.*

If you invoice us for VAT after 1 March 2021 we will return the invoice to you to be reissued, which will delay the payment. Be prepared.

**Transition to the new rules**

The cut-off date is 1st March 2021. Invoices dated up till 28th February 2021 will request VAT and can be paid with VAT. Invoices dated on 1st March 2021 and after will not show VAT in the amount payable columns.

Staged or interim payments made after an application for payment when a QS has certified work will be governed by the date of the payment itself. So staged or interim payments made up to or on 28th February 2021 will have VAT added. Those paid after that date will not be paid with VAT.

We understand that this is a major change for everyone and will worry you, therefore please…

* Read the government website
* Talk to your accountant or contact Armstrong Watson at help@armstrongwatson.co.uk.
* Plan out how you will pay your bills through the next VAT quarter when cashflow will be at its most difficult
* Redesign your invoices and applications for payment and make sure your accounting software can cope with the change.
* Consider how you will monitor whether your customers are VAT registered and CIS registered
* Think about whether you will need to be a monthly repayment trader.

Remember that the Government will soon have a dedicated reverse charge website where there will be more information. This letter is intended only to warn you of the change and allow you to make your own preparations. We hope you find it helpful.

Yours faithfully,