CHAPTER 32

SECOND-HAND GOODS SCHEME

32.1 Introduction

Second-Hand Goods Schemes exist for traders who typically buy goods to sell from unregistered people, in other words, the public. They are therefore not charged input tax on their purchases. If such traders charged output tax on the whole sale price, then the VAT that they would account for to HMRC would be disproportionately large. Normal traders pay VAT on purchases, charge VAT on sales but, because of offset of input tax against output tax, they only **account for VAT on the gross profits they have made.** The margin is VAT inclusive so the VAT fraction would be 7/47 for 2010, increasing to 1/6 for 2011. VATA 1994, s. 50A SI 1995/1268 Arts. 12&13

Illustration 1

A second-hand car dealer buys a car from Fred in 2010, who is a member of the public, for £800. He then sells the car two weeks later to Pete, for £1,500.

If VAT was charged in the normal way the trader would calculate 17½% of the sale price giving £262.50 of output VAT.

Normally VAT charged
£1,500 x 17.5% = £262.50

But, of course, a second-hand car dealer has no input VAT because he purchased the car from a member of the public. Instead, under the Second-Hand Goods Scheme the trader only charges VAT on the profit – on the margin.

Second-Hand Goods Scheme
VAT charged £(1,500 – 800) x 7/47 = £104.25

In other words, the difference between sale price, £1,500, and cost, £800 is the profit element. This £700 of profit is treated as VAT inclusive, so apply our 7 over 47 calculation to give £104.25 of output VAT, to account for on the car sale.

32.2 Operation of Second-Hand Goods Scheme

The Second-Hand Goods Scheme involves calculating a profit made on each item that is bought or sold. This profit is called the margin, and the margin is the difference between the price paid and the sale proceeds. Under the Scheme, the **profit margin is VAT inclusive** so, when multiplied by 7/47, gives the output VAT due on the individual sale. If the sale is made at a loss, in other words there is no profit margin, then there is no VAT due. SI 1995/1268 Art. 2 & 12

If the trader has incurred any costs, for example repairing or improving the item before it is sold, these costs are not taken into account when calculating the profit margin. However, once all the output tax is calculated, any VAT incurred, for example on these costs, is treated as input tax and can be deducted from the output tax in the normal way.

A normal VAT invoice does not accompany sales under the Scheme so a **VAT invoice is not issued**. This means that any purchasers cannot reclaim any of the VAT charged. If a purchaser wants a VAT invoice, and wants to recover any VAT charged, then the item must be accounted for outside the Scheme in the normal way.

Taking items out of the Scheme is allowed. If a VAT registered trader buys something for his business from a second-hand dealer, then that item must be taken out of the Scheme by the dealer, and VAT must be charged in the normal way.

Example 1

Joannie sells antique furniture. She bought a Victorian dresser from a member of the public for £300 in June. She spent £150 plus VAT on restoration by Yuki Ltd but managed to sell the dresser for £800 in July.

Joannie is preparing her VAT return to 31 July 2010. State the output tax/input tax (to nearest £) to be entered on to the return in respect of the above dresser.

32.3 Exclusions from the Scheme

There are certain items that a second-hand dealer must exclude when using the Second-Hand Goods Scheme. These exclusions include items on which the person who sold the goods to the second-hand dealer charged VAT. Remember that the Second-Hand Goods Scheme **only applies to goods that are purchased without payment of VAT**; so from members of the public, etc.

Also excluded from the Scheme are **items on which the customer can recover VAT.** In other words a VAT registered customer who asks for a VAT invoice. In a situation like this, the item must be taken out of the Scheme and VAT accounted for in the normal way on the whole sale price.

32.4 Records

There is a myriad of record-keeping requirements that goes with the Second-Hand Goods Scheme. Firstly, **purchase records** are required. These will have to identify each acquisition of stock and the price paid for that item. Also required are **stock records**. These will identify movements in and out of stock, recording prices paid and received. As part of the record-keeping requirements, **sales records** are also needed which will identify all sales with purchases and the stock records. They should all tie in together with each other.

SI 1995/1268

VAT Notice 718

32.5 TOGC Acquisitions

If a **second-hand dealer's business is transferred as a going concern**, then the **purchaser is also entitled to use the Second-Hand Goods Scheme for sales.** However, when operating the Second-Hand Goods Scheme, the purchase price used by the new owner of the business must be the **price paid by the previous owner of the business** for those goods. Any value assigned to these goods as part of the transfer of the going concern is basically irrelevant – it is just ignored. Effectively, treat the business as if it never changed hands. The same purchase prices will attach themselves to those second-hand goods.

32.6 Global Accounting

The problem with the Second-Hand Goods Scheme is that details of each individual item purchased, and then later sold, has to be recorded. This requirement can lead to a lot of paperwork and an awful lot of administration which, obviously, many traders are not too keen to comply with.

Thus, there is an adaptation to the Second-Hand Goods Scheme called Global Accounting. This is intended to be used where a business sells lots and lots of items, but probably at a low value, and the magnitude of sales is such that it would be rather impractical to track each individual item. Global Accounting is the next step to the basic scheme because it allows output tax to be calculated on a much larger margin; an overall margin for a period of time, in other words for an accounting period.

The **margin is calculated as the difference between sale proceeds of all the items sold in the period, less purchase cost of all the goods purchased in the period.** Instead of just looking at each individual item, sale price less cost/sale price less cost, do the same calculation but for the whole range of items - **total sale proceeds minus total cost**, in a certain period of time.

There are two major differences in respect of the Global Accounting Scheme when compared to the regular Second-Hand Goods Scheme. The first difference is that **losses on an item are automatically offset against profits on items.** Thus losses and profits are offset together in the period.

There is also a **timing advantage** with Global Accounting because **all purchases made in the period are included, even if those goods are not actually sold in the same period.** In fact, sometimes the situation arises where a periods purchases are actually larger than the sales so there is a negative difference. This difference is carried forward and treated as a purchase in the next return period.

There are various **exclusions from Global Accounting**. These include cars, and **individual items costing more than £500**. For the latter it is the cost that is important; the sale price of the item is irrelevant. So only if they cost more than £500 are they not included in the Global Accounting Scheme.

Finally, of course, also excluded from the Global Accounting Scheme are the regular exclusions from normal Second-Hand Goods Schemes that we looked at before.

Illustration 2

Julian sells used stamps. In the quarter to 30 June 2010 he buys 6 English stamps for £300 each and one German stamp for £550.

He sells two of the English stamps for £600 each and the German stamp for £750.

He operates Global Accounting

Any purchase in excess of £500 is not in Global Accounting, so the German stamp cannot be accounted for in the Scheme. It can, however, be accounted for in the regular Second-Hand Goods Scheme.

Julian's output tax is:

Global Accounting		£
Purchases	6 x £300	1,800
Sales	2 x £600	1,200
Carry forward		(600)

This is the situation where purchases exceed sales - a negative £600 balance hence, no output tax to account for on the Global Accounting Scheme this quarter, but a £600 purchase to start off the next quarter.

The German stamp can come under the normal Second-Hand Goods Scheme. The margin of £750 sale minus £550 cost, at 7/47, would give us £29.79 of output tax for this quarter's return. Output tax is £30 to put on the quarter's return to 30 of June 2010.

Example 2

In Julian's next quarter to 30 September 2010, he buys 4 more English stamps at £400 each and sells the remaining stamps purchased in the last quarter for £600 each.

You are required to calculate the output tax due for this quarter.

32.7 Auctioneers

Auctioneers of second-hand goods are allowed to **operate a margin scheme** to simplify their VAT accounting. However, they are only allowed to do this if the **transaction takes place between two unregistered parties,** and thus both the seller and the buyer are unregistered for VAT. In that case, neither will be entitled to recover input VAT.

Auctioneers typically charge a commission to the purchaser, which is called the buyer's premium. They also charge commission to the vendor, the seller. Under the normal rules of VAT, the **Auctioneer has to charge VAT separately to the vendor and to the buyer** and VAT is charged on these commissions. However, take care with these commissions because they affect the calculation of the margin under the Second-Hand Goods Scheme. Remember that when working out cost, **deduct selling commission from the hammer price**; the hammer price being whatever it was sold for in the Auction. When working out the sale proceeds, **add the buyer's premium to the hammer price.**

With this adjusted cost and this adjusted sale proceeds calculate the margin on which the Second-Hand Goods Scheme operates in the normal way.

FA2006 changed the law to ensure that commission charged by an auctioneer will be taxed in the same way irrespective of whether the auctioned goods are within temporary importation (TI) arrangements or are in free circulation within the EU.

The UK previously interpreted European VAT law in such a way that one form of commission, the Buyer's Premium, in respect of goods auctioned within TI was taxed by including the commission in the valuation of the goods at final importation into the EU. The effect of this approach was that the commission was taxed at an effective reduced rate of VAT equal to 5%. The ECJ recently decided that the commission should in fact be taxed at the standard rate of VAT.

Ss21(1) & 21(2) VATA 1994 state that the value of goods being imported into the UK shall be taken to include incidental expenses such as commission. S21 will be amended to ensure the auctioneers' commission (including Buyer's Premium) will be excluded from the valuation calculation for Import VAT purposes. The effect of the change means that commissions will no longer be taxed at the effective reduced rate of VAT.

Currently, under the VAT (Treatment Of Transactions) Order 1995 (SI 1995/958), auctioneers' commissions (including Buyer's Premium) relating to sales of goods by auction within TI arrangements are not treated as a supply for VAT purposes. As such, commissions longer be taxed within the value of goods at final importation, the Order is amended so that normal taxation provisions will apply to the auctioneers' commissions.

Answer 1

Margin £(800 – 300) = £500

Output tax £500 x 7/47 = £74.46 = £74

Input tax £150 x 17.5% = £26.25 = £26

Answer 2

The correct answer is £29.79.

Global Accounting - quarter to 30 September 2010

		£
Purchases		
B/fwd		600
In quarter	4 x £400	1,600
		2,200
Sales	4 x £600	2,400
		200
Output tax		
Margin	£200 @ 7/47	£29.79

Look at all the purchases, both in the period and also the £600 balance of purchases brought forward from the last quarter into this quarter. The brought forward £600 starts the calculation plus four stamps purchased at £400 each, making £1,600, gives £2,200 of purchases for the period.

Match this to sales. The question says that he sold the remaining stamps purchased in the last quarter. He purchased six English stamps and a German stamp in the last quarter, and in the last quarter he sold two English stamps and a German stamp. There are therefore only four English stamps left, so he must have sold those at £600 each totalling £2,400 of sale proceeds. Take off the £2,200 of purchases, and there is a margin of £200 for this quarter.

Apply 7 over 47 to the margin to get £29.79 of output tax to put on this quarter's VAT return.