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VAT due when you forfeit deposits

Some businesses generally require their customers to pay a deposit first before goods or services are provided. More often than not, businesses use the deposit as a way of securing a sale or to obtain some form of protection against fraudulent clients. When a deposit is received, there is no VAT consequences and neither must the VAT registrant account for VAT. But what happens when a deposit is forfeited by a VAT registrant? Keep on reading and let us help you understand the technicalities surrounding deposits and VAT. In this article, words importing the masculine shall be deemed to include the feminine.

Enter deposit

As alluded to above, some businesses require their customers to make an upfront payment of a deposit before the actual sale is settled. This practice is mostly common amongst hotels, Inns, vehicle dealers, or other operators providing a credit facility. Accordingly, a deposit helps vendors to secure a sale or minimise the chances of defaults. In this regard, it is key to note that some business enterprises may refund deposits in the event that a customer fails to pay the balance whilst some operate under a no refund policy. Technically, the latter ends up recognising the deposits as revenue and we now turn to the treatment of the forfeited deposits. Let us now turn to the law for a precise insight.

Enter VAT

Generally, VAT is triggered at the earlier of either issuance of an invoice or receipt of any payment. Some would ask why we assert that deposits do not trigger VAT when the Act clearly states that 'receipt of any payment' triggers VAT? Well, the answer to this question is clearly and purely a technical matter. It is imperative that we first clarify that a payment can only be made as compensation for a supply of goods or services. Consequently, a seller is required to account for VAT on the value of that supply. Now, to put the pieces together, we can all agree that only 'any payment' received as a consequence of a supply triggers VAT. Technically, this implies that in order for a deposit to trigger VAT it should fit in the ambit of a payment for a supply. This is technically referred to as a consideration. Let us dig a little dipper and find out what the VAT Act says about deposits.

In verbatim, the Act states that a consideration i.e., a payment for supply of goods or services, does not include, 'a deposit, whether refundable or not, given in connection with a supply of goods or services, unless and until the supplier applies the deposit as consideration for the supply or such deposit is forfeited.' Based on the quoted VAT law, it is apparent that a deposit is only considered as a payment for a supply when it is utilised towards the purchase price or when it is forfeited. Accordingly, its undebatable that deposits only trigger VAT at the time of forfeiture. In other words, VAT is triggered at the time the seller obtains legal ownership over the deposits.

Conclusion

In this regard, it is key to note that a deposit triggers VAT on forfeiture or when applied towards the purchase price, i.e., not on receipt. Put differently, a forfeited deposit is technically construed to be a consideration for a supply by the VAT registrant who received the deposit.

Well folks, we hope that was insightful. As us the two Yours Truly say goodbye, remember to pay to Caesar what belongs to him. If you want to consult, join our free Tax WhatsApp group or to know about our 9 Tax e-books, send us a text on the cell number below. You can read more tax articles on our website, www.aupracontax.co.bw under the 'Tax articles' tab.