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Research to qualitatively assess the ongoing impact of Making Tax Digital for VAT

Prepared by Kantar Public for HMRC

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The views in this report are the authors own and do not necessarily reflect those of HM Revenue and Customs.

Contents

Glossary of terms	3
Executive summary	4
1. Introduction	7
2. Context for businesses' experiences of Making Tax Digital for VAT	10
3. How and why ongoing experiences of Making Tax Digital for VAT varied	12
4. Experiences of ongoing costs and benefits for fully compatible software users	19
5. Experiences of ongoing costs and benefits for bridging software users	26
6. Conclusions	33

Glossary of terms

Bridging software: Bridging software is an additional software program that extracts relevant data from legacy software (see below) or a spreadsheet in a format that enables the VAT return data to be submitted to HMRC in a Making Tax Digital compliant format. It does not, itself, deal with any of the other requirements of Making Tax Digital for VAT such as digital record-keeping.

Digital links: A digital link is an electronic or digital transfer, or an exchange of data, between software programs, products or applications.

Fully compatible software: VAT record keeping software that fulfils all the requirements of Making Tax Digital within a single application.

Legacy software: VAT record keeping software that was used prior to the introduction of Making Tax Digital but which does not fulfil all the requirements of Making Tax Digital.

Making Tax Digital: Making Tax Digital (MTD) is the first phase of HMRC's move towards a modern, digital tax service. Making Tax Digital aims to help businesses reduce common errors in their tax affairs. Since April 2019 VAT-registered businesses with taxable turnover above the VAT threshold (currently £85,000) have been required to keep records in digital form and file their VAT returns directly from their records using software. Businesses below the threshold are not required to comply until April 2022 but can participate voluntarily.

Simple financial requirements: For the purposes of this report, 'simple financial requirements' refers to businesses within our sample which had a limited number of transactions and/or straightforward VAT obligations. 'Complex financial requirements' refers to businesses within our sample which had a high number of transactions, and/or variable VAT rates and/or involvement with other schemes, such as Construction Industry Scheme.

Small business: For the purposes of this report, small businesses were defined as being businesses with a turnover of below £10 million and fewer than 30 employees.

Executive summary

Making Tax Digital (MTD) is a key part of HMRC's transformation of the tax system to enhance customer experience, make it easier for taxpayers to get their tax right first time and helps reduce scope for error. Since 2019, Making Tax Digital has required VAT-registered businesses with taxable turnover above the VAT £85,000 threshold to keep digital records and use compatible software to submit their VAT tax returns directly to HMRC.

[Qualitative research into the costs and benefits of Making Tax Digital](#), conducted in the first year of Making Tax Digital for VAT, found that businesses were still adapting to the change. Benefits were experienced by businesses, but many felt they needed more time before they would realise them fully.

HMRC commissioned Kantar Public to undertake this further piece of qualitative research to understand the ongoing customer impact of record-keeping behaviour change in response to Making Tax Digital for VAT in the second year of mandation.

This research focused on small businesses (defined here as having fewer than 30 employees and annual turnover of less than £10 million) in the Making Tax Digital for VAT-mandated population, that had signed up for Making Tax Digital for VAT. It involved 60 in-depth interviews with individuals responsible for fulfilling their business's VAT obligations.¹ Interviews took place from March to July 2021. Qualitative research such as this study is primarily exploratory and is used to gain an understanding of underlying reasons, opinions and motivations. Findings cannot be generalised to the wider population.

Businesses' ongoing experiences of the costs and benefits of Making Tax Digital for VAT varied considerably, reflecting variations in businesses' financial requirements and receptiveness to change

Businesses with simple financial requirements reported that they were unlikely to realise benefits as a result of using fully compatible software. These businesses thought that the benefits offered by features of fully compatible software would be either irrelevant for them, minor (and therefore not registered as a benefit) or were outweighed by the costs.

Among businesses that reported having more complex financial requirements which could benefit from fully compatible software, a key driver of variance was businesses' receptiveness to the introduction of Making Tax Digital for VAT. Those businesses willing to embrace the change to Making Tax Digital for VAT or those worried about the change but who felt able to adapt, had reported benefits, while those that opposed the change reported experiencing more costs.

¹ It is important to bear in mind that this research was purposively sampled to capture a wide range of experiences and views on Making Tax Digital for VAT. The research did not seek to and cannot therefore provide an indication of the prevalence of these experiences.

The factors behind a business's receptiveness to the change included their digital and financial confidence, their VAT complexity, the advice they received from agents and peers, where in the business lifecycle they were and how focused they were on future growth (among other things).

Businesses using fully compatible software typically experienced ongoing benefits which outweighed the costs

The benefits of Making Tax Digital for VAT identified by participants using fully compatible software included reduced scope for error, saved time, increased VAT confidence and greater financial confidence, insight and control. These benefits in turn resulted in reduced emotional stress and anxiety.

But there remained a spectrum of views about the impact of Making Tax Digital for VAT:

- those who felt the benefits outweighed the costs tended to be more focused on growth, at an earlier stage in the business life cycle and more able to adapt to change
- participants who felt neutral about the costs and benefits of Making Tax Digital for VAT tended to have already been using accounting software and experienced a minor change
- participants who felt the costs outweighed the benefits were similar to bridging software users in terms of having simple financial requirements
- there were fully compatible software users who reported that they may realise benefits as more time passes and as business activities adapt following COVID-19

Businesses using bridging software (rather than fully compatible software) experienced minimal benefits as a result of Making Tax Digital for VAT

These businesses tended to have either simple financial requirements or they had developed tailored approaches to manage their complex financial requirements. In either case, they were frustrated with what they perceived as an unnecessary requirement. They felt that fully compatible software would either be overly complex and expensive for their simple requirements or not as good as their bespoke systems. Bridging software provided an alternative which was more suitable for their financial requirements. Frustration remained, however, that Making Tax Digital for VAT was mandatory for them, as it was felt more beneficial for larger businesses.

There was high awareness of the requirement to have digital links among bridging software users. However, there was some confusion about the start of a digital trail and the need for it to remain unbroken through to submission. Some participants queried how data could be entered without manual intervention for example when drawing data from an e-mail or invoice. Some participants using legacy software were using a non-compliant method of copying and pasting

between accounting systems and bridging software and saw no other way of transferring data. However, as they were using bridging software, they believed themselves to be compliant.

The costs most commonly reported by bridging software users related to the increased time they now associated with submitting a VAT return. There were participants who also worried about the cost of the software increasing or being discontinued. Some businesses identified small benefits from bridging software. This was mainly that the bridging software digitally pulls information from the spreadsheet into HMRC, eliminating manual intervention and therefore potential for mistakes.

Despite ongoing frustration over the requirements of Making Tax Digital for VAT, there was acknowledgement that bridging software allowed for continued use of spreadsheets and bespoke legacy systems. As a means of enabling compliance whilst retaining existing processes, bridging software was seen as an acceptable compromise between small businesses and HMRC. Participants accepted that Making Tax Digital for VAT is a requirement that businesses must comply with. Bridging software was therefore welcomed as an alternative to having to spend significant amounts on upgrading software or switching to software.

In conclusion, fully compatible software users reported increased benefits over time, although these were reduced for those with simple financial requirements (similar to some bridging software users). However, as businesses had built confidence and familiarity with software, benefits had emerged. There is scope for more fully compatible software users to realise more benefits; COVID-19 in particular has curtailed this potential for some over the last year for practical and emotional reasons.

Bridging software users were consistent with the year one research in how they view costs and benefits of Making Tax Digital for VAT. Bridging software users reported that they did not anticipate experiencing more benefits over time. They were also unlikely to transition to fully compatible software, given their acceptance of bridging software.

1. Introduction

1.1. Background to the research

Making Tax Digital is a key part of HMRC's transformation of the tax system to enhance the customer experience, to make it easier for taxpayers to get their tax right first time, and to help reduce the scope for error.

Since April 2019, Making Tax Digital has required VAT-registered businesses with taxable turnover above the VAT £85,000 threshold to keep digital records and use compatible software to submit their VAT tax returns directly to HMRC from those records. Businesses can use digitally linked spreadsheets combined with bridging software to submit their returns. As of 1 April 2021, it was a requirement for all businesses to put digital links in place between all parts of their functional compatible software.

[Previous research conducted in the first year of Making Tax Digital for VAT mandation](#) found that businesses were still adapting to the change. The previous research found that businesses varied widely in terms of how receptive they were to change, the extent of change required to comply with Making Tax Digital for VAT and their motivation to change. This had implications for how businesses experienced the costs and benefits, as well as how they perceived that experience. The research also found that overall, costs were more keenly felt at the point of transition, but less so as time progressed. Benefits were felt less tangibly than costs and tended to emerge with regular use of Making Tax Digital for VAT compatible software.

HMRC commissioned Kantar Public to undertake research which aimed to develop a better understanding of how the costs and benefits of Making Tax Digital for VAT are being experienced amongst mandated businesses in the second year of mandation. As with the year one research, this project also focused on small businesses (defined in this report as having fewer than 30 employees and an annual turnover of less than £10 million). This insight is needed to help HMRC understand how Making Tax Digital can meet its policy objectives of making it easier to get tax right first time, reducing scope for error, and helping businesses integrate tax in the day-to-day running of their business.

The core objectives of this research were to understand the impact of record-keeping behaviour change in response to Making Tax Digital for VAT in the second year of mandation on:

- ongoing costs and benefits experienced by businesses
- scope for error and failure to take reasonable care
- whether/how these costs and benefits vary by record-keeping approach taken

1.2. Methodology

A qualitative in-depth study was conducted with small businesses with a turnover of less than £10 million and fewer than 30 employees that had made the change to Making Tax Digital for VAT following mandation. In-depth interviews took place with individuals who were responsible

for fulfilling their business's VAT obligations. Participants who used an agent for other aspects of tax compliance (e.g. Corporation Tax) were included within the sample. There were maximum quotas on businesses who completely outsourced their VAT submissions to an agent.

Between 25th March and 7th July 2021, interviews were conducted with the relevant individuals within small businesses.² Interviews lasted for 60 minutes. Participants were recruited from a sample randomly drawn from Making Tax Digital for VAT customers provided by HMRC. All businesses within the sample received a letter explaining the purpose of the research and giving them the option to opt out over a two-week period.

To refine the research questions drafted in the Invitation to Tender, Kantar Public and HMRC held a benefits generation workshop to develop a list of anticipated costs and benefits for use in the research.

As part of fieldwork, participants were asked to complete a short pre-task reflecting on their VAT experience under Making Tax Digital for VAT and how this compared to previous submissions. This encouraged participants to reflect and identify details of the various costs and benefits experienced over time.

1.3. Sample

The sample consisted of 60 telephone in-depth interviews in total.

- 24 x small businesses who are now using fully compatible software and who have gone through a 'major change'
- 13 x small businesses who are now using fully compatible software and who have gone through a 'minor change'
- 7 x small businesses who are now using bridging software with digital links and who have gone through a 'major change'
- 6 x small businesses who are now using bridging software with digital links and who have gone through a 'minor change'
- 10 x small businesses who are now using bridging software without digital links³ and who have gone through a 'minor change'

Across the sample there was:

² All participants were screened to ensure they were the person responsible for fulfilling the business's VAT obligations.

³ 'Without digital links' refers to the use of 'copy and paste' to move data between records. The population size of this audience was unknown at the point of the research design. It was decided that efforts would be made to reach 20 small businesses using bridging software without digital links. On 1st April 2021, digital links became a mandatory requirement of Making Tax Digital. This presented a methodological challenge for this research as the sample had been designed to compare the experiences of those with and without digital links. However, the timing of the mandation and the evidently small size of the target population made it challenging to recruit those not using digital links. The method was therefore adapted so that a greater proportion of bridging software users with digital links were included. The experiences of users of both digital links and non-digital links are explored in Chapter 4.

- a mix of business sizes, including nano, micro, and small
- a mix of digital confidence
- a spread of sole trader, partnership and limited companies
- a spread of industries, including those which have mobile workers as well as premises/office based
- spread of length of time VAT registered
- spread of locations across the UK

The research project was qualitative in nature. Qualitative research is primarily exploratory, used to gain an understanding of underlying reasons, opinions and motivations. Due to the nature of qualitative research, findings cannot be used to generalise across the population.

2. Context for businesses' experiences of Making Tax Digital for VAT

This chapter explains some of the common and differentiating features of the small businesses interviewed. As will be outlined in later chapters, there were varied experiences of Making Tax Digital for VAT. This chapter explores some of the context which influenced these different experiences.

Key findings:

A range of small businesses across varied sectors were included within our sample. Despite their commonality in size, they differed widely in their approaches and views towards change, innovation and finances. These differences are explored in depth in Chapter 3.

VAT was generally considered to be a straightforward and relatively small part of running a business. However, this perception of ease was based on familiarity and complexity of the VAT requirement.

COVID-19 has had a significant and wide-reaching impact upon small businesses. Some had been able to adapt and continue working throughout. Others however, particularly those which rely upon in-person contact had struggled and were still in a period of recovery at the time of research.

To understand businesses' experiences of Making Tax Digital for VAT, it is necessary to first understand how Making Tax Digital for VAT fits within business operations. It is also important to consider that the sample was designed to deliberately include businesses with varied experiences to ensure we gathered insight on the full range of costs and benefits.

Within the sample a wide range of businesses, across a mix of sectors, sizes and business types were included. Sectors represented included consultants in a variety of fields, maintenance companies, web design, architecture and farmers. Size of business ranged from nano businesses with no employees to micro businesses and small businesses. Business type included sole traders, partnerships, and limited companies.

The complexity of participants' VAT requirements varied. In common with [the previous research](#), VAT was generally seen as a straightforward process to comply with. Participants were broadly accepting of VAT and its purpose and while some participants made comments about being 'unpaid tax collectors', these were not strongly expressed as active negativity towards VAT. Businesses largely reported that, once they were familiar with VAT processes, VAT returns were relatively easy. Those who found VAT more complex tended to have different VAT rates or to be operating overseas.

'Compared to other taxes I find it very easy.' (Micro)

'It's black and white, something either has VAT or it doesn't.' (Nano)

The research was conducted at a time when many businesses were still adjusting to the impact of the COVID-19 pandemic. There is, therefore, value in understanding the contextual impact of COVID-19. Across the sample, businesses reported that COVID-19 had had an initial impact on operations but that they were mostly able to adapt and continue operating albeit at reduced levels for some. The early stages of COVID-19 were described as 'challenging', as operations halted or were severely disrupted. However, participants felt that they were mostly able to respond to the impact of the pandemic in an agile way and found that given time they could adapt to the 'new normal'. Those in industries requiring in-person contact were the hardest hit and were still recovering from the initial impact.

'We've had to adapt and implement some new processes,
but we are able to keep working.' (Small)

'We are still operating at 30-40% of pre-COVID-19 levels in terms
of takings – the public are nervous.' (Micro)

'There was no particular impact, heating services were still needed so we
didn't stop working at any point.' (Micro)

3. How and why ongoing experiences of Making Tax Digital for VAT varied

Businesses' ongoing experiences of Making Tax Digital for VAT varied considerably. This chapter focuses on why some businesses felt they had benefitted overall from the change while others said they continued to experience more costs than benefits as a result of Making Tax Digital for VAT. How the perceived costs and benefits varied is explored in detail for both fully compatible software users (Chapter 4) and bridging software users (Chapter 5). Anonymised 'pen portraits' of participants are included later in this chapter to help illustrate the range of factors that underpinned varied experiences of Making Tax Digital for VAT.

When considering these findings, it is important to bear in mind that businesses participating in this research were purposively sampled to capture a wide range of experiences and views on Making Tax Digital for VAT. The research did not seek to and cannot provide an indication of the prevalence of these experiences.

Key findings:

Attitude to change was found to be a key factor which influenced perceptions of the costs and benefits of Making Tax Digital for VAT.

Three cohorts were identified in relation to how change was perceived – those who had embraced the change, those who were afraid of change but able to adapt, and those who opposed the change – which in turn affected the extent to which they experienced costs and benefits.

Using the COM-B model (about which there is further information below) it is possible to understand the drivers of receptiveness and attitudes to change. Individuals' levels of capability and motivation were particularly either sources of engagement or resistance to change.

Both internal and external factors impacted businesses' receptiveness to change including: their perceived capability to adapt, how focused they were on future growth opportunities, and how they were advised and supported by others.

Businesses reported mixed experiences of Making Tax Digital for VAT across a scale of experiencing either higher costs or benefits overall. This is consistent with [the year one findings](#). However, there was now a clear distinction between the experiences of those that were more open to change compared to those that were opposed to change.

A key driver of difference amongst participants was their receptiveness to the introduction of Making Tax Digital for VAT. Participants fell into three broad categories, associated with their attitude to change and how this impacted their experiences of Making Tax Digital for VAT:

- those who were willing to embrace the change to Making Tax Digital for VAT had realised benefits
- those who were afraid of the change to Making Tax Digital for VAT, but able to adapt, had realised benefits
- those who opposed the change to Making Tax Digital for VAT had experienced more costs than benefits

Whilst these were the key categories identified, within each category there was a range of attitudes and experiences.

3.1. Using COM-B to identify influencing factors

In analysing responses, we used the behavioural model, COM-B, to identify the drivers behind a businesses' receptiveness to the change to Making Tax Digital for VAT.⁴ Within this research, the COM-B framework suggests three components that influence behaviour:

- Capability refers to whether we have the knowledge, skills and abilities required to engage in a particular behaviour (e.g. digital confidence)
- Opportunity refers to the external factors which make the execution of a particular behaviour possible (e.g. nudge from accountant)
- Motivation refers to the internal processes which influence our decision making and behaviours (e.g. wanting to spend less time doing VAT, and more time on other parts of the business)

Capability

Key factors that influenced businesses' perceived capability to adapt to Making Tax Digital for VAT included their confidence, attitude and circumstances. The variation in individual confidence, attitude and business circumstances was seen clearly in the following four areas.

The first area was digital confidence. The more digitally confident and experienced the key individuals within the business, the stronger their ability to adapt. The more digitally confident were also used to changes in their digital process. They had previous exposure to digital changes such as upgrading software and trying new apps. These individuals were therefore inherently more confident in their ability to learn and adapt to a new digital process. They also tended to be more confident in learning how to use a new digital feature and were more trusting in the usability of programmes and apps, than other less digitally confident participants.

⁴ Susan Michie, Maartje M van Stralen, Robert West. (2011). *The behaviour change wheel: A new method for characterising and designing behaviour change interventions*. Implementation Sci, vol. 6 (1). doi:10.1186/1748-5908-6-42.

The second area was financial confidence. Individuals who had confidence in how they managed their financial requirements tended to be confident that they would have the capability to adapt to a new approach.

The third area related to how individuals felt about change in general. Those who disliked or were afraid of change tended to doubt their own capabilities and be more resistant. Those who had gone through change previously and benefitted, were inclined to be more positive and open minded about future changes.

The final area was VAT complexity. Within our sample, the more straightforward a business's VAT affairs, the higher the individual's perception of capability and ability to adapt to new processes. There were businesses with straightforward VAT requirements, such as those on the VAT Flat Rate Scheme, and the individuals involved in their finance saw VAT as a simple calculation. They therefore had high confidence in their own abilities to apply VAT correctly. There were also businesses with more complex VAT requirements, for example that were operating overseas or applied different VAT rates depending on the product. Within these businesses, individuals recognised that there was a greater margin for error as the calculation was more complex. They therefore tended to have lower perceptions of their capability and ability to adapt to new requirements and processes.

Opportunity

Making Tax Digital for VAT provided customers with an opportunity to change their behaviour. However, external factors either supported or obstructed how they engaged with this opportunity.

'[Without Making Tax Digital for VAT] I would have still done [my VAT return] the same way, without a doubt. I didn't know any better and I didn't know enough to risk changing something that I knew worked...it's the best thing we've ever done!' (Micro)

Software providers and agents played an important role in encouraging take up of the opportunity. Within our sample, they were often responsible for nudging users into using fully compatible software as well as offering training, video guidance and ad-hoc support.

Friends, peers and colleagues who had embraced fully compatible software and found it to be beneficial were an additional source of encouragement for those within our sample. This helped reduce some of the 'mystery' surrounding the change and create social norms around its usage.

However, there were also factors which made it easier for businesses to resist using fully compatible software. Within this research, the role of agents was important. There were agents who supported take-up and engagement and who supported their customers to adapt. There were also agents who advised their customers against engaging at all. These agents tended to already be heavily involved in their client's finances and were easily able to take responsibility for navigating the change. Then there were other agents who recommended using bridging software. These agents recognised the challenges which their clients might face in transitioning to fully compatible software and therefore recommended bridging as an easier option to take.

'My bridging software was recommended by my accountant who said, "that's the cheapest, but it does what you need it to do".' (Nano)

COVID-19 presented a distraction which created a barrier to fully maximise the opportunity. It was hard for some businesses, particularly those that were worst affected, to take advantage of additional software features or to stop using spreadsheets as well as software concurrently.

A lack of peer support and not being exposed to social norms reduced opportunity to change. Without exposure to others' experiences, it was harder for businesses to dispel concerns, misconceptions and anxieties around the change.

Finally, there were those within the sample who were already using fully compatible software. For these participants, the change was very minor and so the opportunity was already limited.

Motivation

With regards to motivation, we found that, where a business is within the business lifecycle and its focus on future growth can impact on individual motivation for innovation and change. This aligned with findings from [the previous research](#).

The earlier stages of the business lifecycle involve the initial creation of the business, followed by a phase of 'learning the ropes', establishing new processes and systems before settling into the day-to-day running of a business. Within the sample, participants who were at these earlier stages of the business lifecycle were more proactively thinking about and planning for the future of their business. They tended to want to capitalise on opportunities which would help to create efficiencies. They also recognised the value of change and of automation and were open-minded about incorporating these into their business.

A later stage of the business lifecycle can involve a focus on maintaining the status quo. This period could last for any length of time before the business eventually moves into a final stage of winding down. If the individual running the business starts to focus on winding down, for example, if they are approaching retirement, their interest in innovating and change can wane. Participants within the sample who were at later stages of the business lifecycle tended to have systems and processes which were set up to ensure maximum efficiency for key individuals within the business. They also tended to be very wedded to these processes, having built up familiarity over the years. They did not perceive a strong need for change, it was felt that what was working now was good enough.

3.2. Pen Portraits

The following pen portraits are based on research participants. Any identifying features have been altered to preserve anonymity. They demonstrate how different elements within the COM-B model (capability, opportunity and motivation – flagged within the pen portraits) can impact on the perception of Making Tax Digital for VAT. This in turn also impacts on how the costs and benefits of Making Tax Digital for VAT are experienced.

Pen portrait: Bridging software adds complication (low capability – low opportunity – low motivation)

'John' is 63 and has owned his pub for 25 years. He has a bookkeeper and an accountant but manages the VAT returns himself. The business has been hit hard by COVID-19, and he is hoping to keep it going for another few years before retiring. He describes himself as not digitally confident (low technical capability).

Pre-Making Tax Digital for VAT, John's bookkeeper would give him a completed paper VAT return form, which John would check over, sign, and post to HMRC. When Making Tax Digital for VAT became mandatory, he purchased the bridging software that his accountant recommended as this would presumably link to the spreadsheets his bookkeeper uses (low opportunity).

Under Making Tax Digital for VAT, John's bookkeeper emails him the VAT return 'form' with the figures entered in the relevant boxes. The bridging software then links to cells on the form his bookkeeper has sent him, and then submits the VAT return. He often needs to refer to the bridging software instructions and is not confident that he always does it correctly. He finds the process more complicated than pre-Making Tax Digital for VAT, and that it takes more time. He spends about an hour on the VAT return now, whereas pre-Making Tax Digital for VAT it would take him about ten minutes.

John doesn't see any need to use fully compatible software or digital tools for his type of business. Now that he has got used to the new process under Making Tax Digital for VAT, he would not want to change again (low motivation).

John's pen portrait has been included because he is an example of someone who is nearing the end of the business life cycle and has no interest in change. John represents someone who opposed the change to Making Tax Digital for VAT and has experienced more costs.

'It's pressing the links in a sequence, and you get boxes that keep popping up and asking you questions and if you don't answer correctly you end up getting nowhere and you go round in a circle.'

'It isn't straightforward. It's not a ten-minute job, it's an hour job – and that's assuming you're doing it correctly, so it's become more difficult.' (Micro)

Pen portrait: Neutral impact on simple business structure (high capability – high opportunity – low motivation)

Phil, 56, is a software engineer and the sole director of his limited company. He has been running the company for 10 years and aims to keep the business stable in the future.

Before Making Tax Digital for VAT he used spreadsheets for record-keeping, which he would update twice a month. When Making Tax Digital for VAT became mandatory, he purchased bridging software which digitally extracts the relevant data from his spreadsheet. He decided not to use fully compatible software because it would be an extra cost and did not think his

business would need or benefit from the additional functionality that fully compatible software could provide (high opportunity, low motivation).

Phil considers his business accounts to be very simple. He enters all incomings and outgoings once a fortnight and reconciles these entries every month. His spreadsheets have formulas built in them and he carries out manual checks of entries, which give him full confidence in the accuracy of his records (high capability). To submit a VAT return, he runs the bridging software which asks him if he wants to submit the return, and Phil just has to click 'yes'.

Phil considers that the time he spends running the bridging software to submit the VAT return is about the same as logging on to Gov.uk to submit a VAT return pre-Making Tax Digital for VAT.

Phil represents someone who has not been impacted by the change to Making Tax Digital for VAT and has therefore not experienced any new costs or benefits.

'I had everything set up before, all the calculations were done in the spreadsheets. So that bit hasn't changed, it's purely the submission part that has changed.'

'The time it took to log into government gateway and enter those 3 figures is about the same as the time it takes now to log in and run the software and submit. So it's about the same.'

Pen portrait: VAT is easier and more accurate (medium capability – high opportunity – high motivation)

Robert, 57, and his wife, Mary, have been running a chicken broiler farm and agricultural machinery business for over ten years. They are responsible for the finances of the business and only use an accountant to prepare the end of year accounts.

Before Making Tax Digital for VAT became mandatory, they used spreadsheets for record-keeping, with four different spreadsheets for the different sides of the business, and for sales, purchases and VAT. They would manually update the spreadsheets on a weekly basis from paper invoices and receipts (high motivation).

When Making Tax Digital for VAT became mandatory, they purchased fully compatible software that was recommended by a financial advisor (high opportunity). They have found the software has made VAT returns very simple and easy to manage but are still anxious about trusting it completely. They therefore still check the data, so they do not find the process is any quicker (medium capability). Before Making Tax Digital for VAT they would update and check records at the end of each quarter, but now, with the software, they do this on a daily basis so that it has become embedded into their daily work. This has made Robert feel more aware of the business financials at any point in time.

Robert believes the software has improved the accuracy of their VAT returns, as he considers it was easier to make mistakes in spreadsheets and without digital links. Feeling more

confident in the accuracy of their record-keeping has made Robert view VAT more positively, as this causes less anxiety.

Robert represents someone who was afraid of the change to Making Tax Digital for VAT but has been able to adapt and has realised benefits as a result.

‘Now that everything is in one place it’s easier to keep on top of things.’

‘I don't know whether I spend any more or less time, it just seems to be less of a bore at the end of the quarter. It just seems to go more easily.’

‘I used to dread the accountant's report where he would identify loads of mistakes that needed fixing. Now we rarely make mistakes.’

Pen portrait: Big improvements to efficiency and confidence (high capability – high opportunity – high motivation)

Simon, 35, runs a car garage and is the company director. His role includes day to day accounting, such as payroll, invoicing and bookkeeping. He feels confident managing the business’ finances (high capability) and uses an accountant for end of year accounts.

Before Making Tax Digital for VAT, record-keeping was paper based, which made processes time-consuming but familiar. Making Tax Digital for VAT led him to purchase fully compatible software and thereby provided the opportunity to improve the efficiency of his record-keeping methods (high opportunity, high motivation).

Simon likes that the software gives him real-time information, including on VAT, on the dashboard, so that he is always aware of the company’s VAT status. This makes him feel more in control of the company’s VAT, which in turn gives him greater peace of mind. He also likes that many accounting processes are now automated by the software, making them easier and quicker. This includes preparing and submitting the VAT return, which can now be done at the click of a button, as well as bank reconciliation and invoicing. Overall, he estimates that using fully compatible software has saved him four days every month that he used to spend on bookkeeping activities. Instead, he can now spend that time on work that is chargeable to customers and other business affairs.

Simon represents someone who was willing to embrace the change to Making Tax Digital for VAT and has realised benefits.

‘I think it's great, honestly, I think it's brilliant...at any point at the click of a button it tells me exactly what VAT we're on... I'm now constantly in the workshop whereas before I'd have to pull myself out every now and again...[the software] does it all for you.’

4. Experiences of ongoing costs and benefits for fully compatible software users

This chapter explores the costs and benefits experienced by fully compatible software users which [previous quantitative research](#) has shown to constitute the significant majority of Making Tax Digital for VAT businesses. We provide a descriptive account of businesses' experiences of using Making Tax Digital for VAT. We consider variations in how businesses perceived the costs and benefits of Making Tax Digital for VAT, identifying three groups of participants (those who felt the benefits outweighed the costs, those who felt neutral, and those who felt the costs outweighed the benefits). This chapter explores each of these groups in more detail.

Key findings:

Fully compatible software users typically experienced ongoing benefits which outweighed the costs of Making Tax Digital for VAT. Amongst these were participants who reported realising more benefits over time as their familiarity with the software increased.

Fully compatible software users who felt neutral about the costs and benefits of Making Tax Digital for VAT tended to have experienced a minor change and tended to have already been using accounting software. However, despite perceived neutral cost and benefits, they were still positive about Making Tax Digital overall and could see indirect benefits from the minor changes they had made.

Fully compatible software users who felt that the costs outweighed the benefits displayed similarities with bridging software users in terms of either having simple financial requirements or bespoke record keeping approaches.

Some fully compatible software users felt that there was scope for more benefits to emerge with more time and engagement. For them engagement has been curtailed by the COVID-19 pandemic.

There was consistency across participants who felt that the benefits outweighed the costs. These included saved time, increased VAT confidence and greater financial confidence, insight and control.

4.1. The participants who felt neutral about the costs and benefits of Making Tax Digital for VAT

Some fully compatible software users felt the costs and benefits of Making Tax Digital were neutral. They had already been using accounting software prior to the introduction of Making Tax Digital for VAT. This was up-to-date software which was straightforward to upgrade to be Making Tax Digital for VAT compliant. As a result, these participants had gone through a minor change when transitioning and were positive about Making Tax Digital for VAT overall. The

direct impact on their record keeping had been minimal and so they had a neutral perspective on the costs and benefits. However, they recognised the value Making Tax Digital for VAT could offer in helping to reduce errors and increase digitisation more generally. And while it may have only resulted in a minor change, for some businesses this involved upgrading their software meaning they were able to access additional features.

‘I was already using [a] market leader [before Making Tax Digital for VAT] and I’d been using it for so many years, I know it inside out so there’s been no real difference for me’

4.2. The participants who felt the costs of Making Tax Digital for VAT slightly outweighed the benefits

Fully compatible software users who felt that the costs of Making Tax Digital for VAT outweighed the benefits had similar financial requirements, processes, and growth plans to bridging software users. They tended to be at the later stages of the business lifecycle, at which point their business focus was on maintaining the status quo. Winding down and retirement were potentially imminent, so their interest in innovation and change were more limited.

These participants felt that they had gone through a major change (moving either from legacy software or spreadsheets) in adapting to Making Tax Digital for VAT. They reported having struggled with using fully compatible software; often finding it complex and not user friendly. These participants also often tended to have simple financial requirements. For them, fully compatible software felt overly complex and sophisticated for their needs.

These poor user experiences had led to some participants losing trust and confidence in the fully compatible software, creating an emotional cost of anxiety and uncertainty. Those who were the least confident reported still relying on spreadsheets for checking their calculations in addition to using the fully compatible software. They were therefore spending additional time using both methods when preparing their VAT return. For some, this meant that they regretted their choice and may have adapted better to bridging software or an alternative software provider instead.

However, either through lack of awareness or understanding of the options, or because they were following advice from their agents or peers which directed them to fully compatible software, this was the approach they had taken. Based on their reported feeling and given their business setup and positioning within the business life-stage, these participants may continue to perceive that the costs of Making Tax Digital for VAT outweigh the benefits.

However, those fully compatible software users currently lacking in confidence in the software and relying on spreadsheets as ‘back up’ may move to only using fully compatible software. The motivation and opportunity to make this leap had in part been curtailed by COVID-19, which had pulled businesses’ attention onto other areas and limited opportunities to make use of software features. Where COVID-19 had a significant impact on operations, businesses may also have fewer transactions than they usually do. Businesses have also been significantly distracted and

disrupted by COVID-19. It has shifted focus away from change, onto survival and adapting to the 'new normal'.

'I know there are ways to make life easier like receipt capturing but at the moment I just don't need to use it as nobody is doing any travelling. Maybe when we're back collecting lots of receipts, I might look into it' (Small)

'I still have my spreadsheet in there just to make sure the calculation are right, or something has not messed up in my software or anything - just to make sure that both the numbers are corresponding with each other.' (Micro)

As people adjust to life with COVID-19 and business activities pick up again, businesses may well begin to engage with and make use of software features and therefore experience more benefits in the future. Therefore, the balance of costs and benefits may alter, as businesses utilise more features of the software and their confidence in it grows.

4.3. The participants who felt that the benefits of Making Tax Digital for VAT outweighed the costs

Fully compatible software users who felt that the benefits outweighed the costs tended to be more focused on growth and to be at an earlier stage in the business lifecycle. They also tended to be more able to adapt to change and were thinking and focussing on the long-term future of their business. They were willing to innovate and try new approaches which could be beneficial to them. They also tended to have multiple employees and a high number of financial transactions.

In the previous research, businesses with these characteristics expected to realise more benefits from Making Tax Digital for VAT over time. This research indicates that, given that additional time and familiarity, several benefits have emerged which they feel significantly outweigh the costs. These benefits will now be explored in detail.

4.3.1. Reduction in scope for error

The increase in automation which fully compatible software provides was recognised to have reduced scope for human error. As fully compatible software automatically spots inconsistencies, inaccuracies, and oddities within records, it mitigates against 'human error'. Users thought that the accuracy of VAT returns has increased with fully compatible software usage, particularly for those who previously used paper and calculators.

Increases in accuracy were reported by those with more complex VAT requirements. For example, some participants manage different VAT rates and software has been able to support with recognising these. Those using receipt capturing software also appreciated the elimination of manual data entry, where entering a wrong digit is easily done. Receipt capturing software

also helped when keeping on top of multiple receipts and users appreciated that there was less risk of rushing and making mistakes or of losing receipts.

'The way it is now there's probably less chance of mistakes from human error, I would say.' (Micro)

'I think it's easier to be much more accurate and also to be confident that it's accurate.' (Small)

4.3.2. Time saving

Time saving was identified as a key benefit. Participants who perceived this as an advantage had embedded their fully compatible software into day-to-day operations. This enabled them to keep on top of record-keeping in bite-sized chunks rather than as a single big task at the end of the month or quarter. This also meant that record-keeping, invoicing, and expenses were maintained and kept on top of when individuals were out of the office and 'on the go'.

'I'll probably be saving 4 days a month...frees me up as a member of staff for 4 days.' (Micro)

'Emotionally it feels that I'm working more on what I do best rather than finances.' (Small)

'It used to be a case of sitting down for probably a weekend, most of the weekend doing it all. But now half an hour a day, or an hour every couple of days and it's done.' (Micro)

Features of the software such as automatic invoicing have helped to save time and emotional effort. For example, if an invoice is overdue some software can automatically send reminders. One participant within the sample reported that they typically worked on client projects for years at a time. They previously found it stressful and anxiety-inducing having to chase up for overdue payments. Knowing that software would send reminders for them automatically if a payment was overdue, neutralised anxiety and stress.

Participants felt that the time saving created by using the software resulted in days that they had either invested back in the business or taken as leisure time.

4.3.3. Increased VAT confidence

Participants who had more exposure to the software and had embedded it into their systems and record-keeping processes reported having more confidence. This constant engagement with financial processes helped to increase their confidence and to ease the emotional burden around producing a VAT return. The VAT return process was now more familiar, and the elements which contribute to it were better understood.

This increase in confidence was reinforced by the trust which these participants placed in the accuracy of the software. Now that the software is familiar, they perceive that only a quick sense check is needed, rather than a comprehensive review.

'Now it automatically does it. If I make a typing error inputting the data, the software will tell me that it doesn't add up.' (Micro)

'I used to do the whole quarter's VAT all in one go because I hated it so much...it's now so much more straightforward, routine and it actually keeps me almost focused on the finances of the business as well, because you're doing these minor jobs every day.' (Nano)

4.3.4. Greater insight and financial control

Greater insight and financial control were identified as benefits of using software by participants who felt that the benefits outweighed the costs. One example of this was that the software provided a means of easily seeing the businesses' finances; particularly what VAT is owed. This level of detail was not always as easy to access or understand in a spreadsheet.

Having this real-time financial clarity has helped build a feeling of control of the business finances. This has helped with planning for the future and more effectively being able to anticipate and mitigate challenges. There were participants who reported feeling out of touch with their business' finances prior to using fully compatible software. They now felt they had a clearer sense of how their business was operating and were better able to understand areas to focus upon and how to prioritise and inform future decisions.

In addition to this increased oversight, businesses also appreciated specific features offered by fully compatible software. Participants with high numbers of transactions, suppliers and clients reported being able to easily analyse data on their key audiences. Software features can provide wider insight, for example, how sales and outgoings are performing compared to previous years. This can help inform decisions such as whether to change suppliers or to reach out to cold clients.

'The biggest positive change is I am intuitively more in touch with my finances. That has been the beneficial outcome of Making Tax Digital.' (Nano)

'Now all my receipts and invoices are just automatically linked to [software package] for me and I just need to look down on [software package], have a glance over everything, make sure there's nothing out of place. It's just all there, it's just so simple.' (Micro)

'At any point at the click of a button it tells me exactly what VAT [we owe.]'
(Micro)

Digital tools such as receipt capturing, bank reconciliation, automatic invoicing and payment reminders were recognised as enablers of key benefits. However, their usage depended upon

perceived need. For businesses with more straightforward financial requirements, digital tools could be perceived as unnecessary or overly complicated. This perception could prevent engagement with digital tools and therefore with associated benefits such as increased financial insight.

4.4. Commonalities with the findings from the year one research

At the time of this research, the transition for businesses to Making Tax Digital for VAT seemed mostly complete. Whilst we found businesses whose adaptation has been impacted by COVID-19, most of our participants had made the changes to complete transition. At the time of the year one research, both bridging software and fully compatible software users were still adjusting to the introduction of Making Tax Digital for VAT.

Despite the differences in environment and context between the two projects, commonalities and consistencies have been identified across both projects.

The same benefits were identified across both projects. More businesses may now be experiencing these benefits as they have adapted to Making Tax Digital for VAT and moved past the period of adaptation. As has been explored, due to the impact of COVID-19, there are still those who have yet to fully realise all of the benefits which fully compatible software has to offer. There was optimism that these would be embraced with more time.

There remain fully compatible software users who felt that the costs outweighed the benefits identified in year one. However, they previously tended to attribute the increased costs to the new approach. Now that they have adapted and are familiar with the software, a feeling that the software they have chosen may not be optimal for them or their business has emerged.

‘It cost hundreds of hours transitioning over [to full software]. If I was to do the process again, I would use bridging software.’ (Nano)

As with the year one research, fully compatible software users who had previously used software largely felt neutral about the costs and benefits of Making Tax Digital for VAT.

5. Experiences of ongoing costs and benefits for bridging software users

This chapter explores the experiences of those using bridging software. This includes insight into the awareness and understanding of digital links and how bridging software was viewed in this research compared to [year one research](#).

Key findings:

Participants using bridging software were generally frustrated about the mandation of Making Tax Digital for VAT. This was consistent with the year one research and is suggestive that the behaviours and approaches taken to deal with Making Tax Digital for VAT are now likely to be entrenched.

Bridging software users tended to perceive that the costs of Making Tax Digital for VAT outweighed the benefits. The costs experienced related to the increased time required to submit a VAT return. However, there were participants who worried about the cost of their bridging software increasing or being discontinued.

The main benefit identified was seen as being 'minor'. This benefit related to how the bridging software digitally pulls information from the spreadsheet into HMRC, eliminating a manual intervention.

There was high awareness of the requirement to have digital links. However, instances of inadvertent non-compliance were reported, particularly amongst participants who were using legacy software which is not compatible with bridging software.

Despite ongoing frustration over the requirements of Making Tax Digital for VAT, there was acknowledgement that bridging software allowed for continued use of spreadsheets. As a means of enabling compliance, bridging software was therefore recognised as an acceptable compromise between some small businesses and HMRC.

5.1. Experiences of ongoing costs and benefits for those using bridging software

Businesses using bridging software tended to have less complex financial operations with few transactions, their VAT return in particular required few calculations compared to businesses in our sample who were using full software. Participants also tended to be at the later stages of the business lifecycle. Their focus was upon maintaining the status quo and thinking about winding down to retirement, rather than on growing their business. Bridging software users also tended to have simple financial requirements. However, there were businesses within the sample with more complex financial requirements and bespoke software

Participants with more complex requirements tended to have invested time, energy and money in ensuring their financial processes were as efficient as possible. This meant their processes and software were bespoke to both the business and the individuals responsible for the VAT return. These participants felt that their processes could not be improved. For them, Making Tax Digital for VAT did not offer benefits, as they felt they had a system which already worked in the best way possible. This investment in bespoke processes and software has led these businesses to be more entrenched, having created other processes and systems to support this preferred way of working.

Whilst they were mostly confident using a computer and spreadsheets, they reported feeling uncomfortable with new technology applications. Adapting to fully compatible software was therefore seen as being a big step which was too far away from their comfort zone. Furthermore, there was a perception that the full software options consisted of large expensive packages which would be overly complicated for their needs.

'I need to be very efficient as I'm a one-man band. I can do the VAT return in under an hour and a half, I'm not looking to change anything.' (Nano)

We also found a lack of clarity for some regarding the language of Making Tax Digital for VAT. There were participants who felt their VAT process was already digital because they were using computers, spreadsheets and submitting figures via HMRC's website. This confusion built into early resistance towards Making Tax Digital for VAT. Whilst a point of confusion for participants, this had not led to active resistance as it had done at the point of Making Tax Digital's introduction.

'It was digital anyway. I didn't ring up somebody. You know, I didn't write it in a quill pen and send it in the post to somebody at HMRC who opened a paper envelope and transcribed the data from my handwriting into their own.' (Nano)

This frustration has been further compounded by a sense that Making Tax Digital for VAT is really aimed at larger businesses or businesses with more complex setups which could benefit from the features that fully compatible software offers. For small businesses with simple financial requirements the prospect of using fully compatible software was not felt to be worthwhile. They doubted they would benefit from the additional features and felt that such a significant upgrade would be 'overkill'. This created some frustration for them at being amalgamated with other businesses who could benefit, with what was perceived to be little consideration for their needs.

This frustration was reported in [the previous research](#). In this study frustration was reported as feelings of resentment about being forced to go through an unasked-for change. This ongoing frustration after Making Tax Digital for VAT has had time to bed-in suggests that some businesses may never view the benefits of Making Tax Digital for VAT as being greater than the costs.

In addition to the generalised frustration expressed within the bridging software sample, there was also a niche cohort whose frustration related directly to HMRC's compliance requirements. These tended to be legacy software users who were open to upgrading their software but felt

trapped by the need to maintain seven years of financial records. Their perception and concern was that transferring across so many backdated records would incur heavy costs (in both time and money) which they were unable to afford. They therefore felt trapped, against their choice and frustrated.

5.2. Awareness and usage of digital links

Within the sample of bridging software users, awareness of the requirement to have digital links was high. [A digital link as defined by HMRC is](#): 'A digital link is an electronic or digital transfer, or an exchange of data, between software programs, products or applications.'

Digital links were understood to be the mechanism which eliminated the need for data to be moved from one source to another via a manual intervention such as through copy and paste.

There was also high awareness that from April 2021 digital links were a mandatory requirement. Businesses had received alerts directly from HMRC as well as from agents about the requirement.

The rationale behind digital links to limit 'manual' intervention was well received. It was understood that limiting human intervention would lead to a reduction in simple errors such as incorrect digits being entered accidentally, thereby increasing the accuracy of VAT returns.

However, questions were raised over when a digital link begins and whether it is possible to have data entered without some form of manual intervention. For example, those who were currently copying data from an e-mailed invoice or manually entering from a paper receipt or invoice queried how this process could be digitised.

'I've used digital links for a while. If you know it's quite easy really' (Micro)

'You're never going to get rid of that manual interface. Not efficiently anyway. When you've got an automatic implant in my brain that means that I can control my invoicing and payments without having to type anything, let me know.' (Nano)

There also appeared to be confusion over the requirement to have a complete digital trail from the point that data has been entered into software. Some participants described using bridging software to submit their return but had copied and pasted in other aspects of record keeping when creating the VAT return. These participants could be inadvertently non-compliant. For example, businesses with outdated or bespoke legacy record keeping software, which was incompatible with bridging software, were manually transferring data via cut and paste but were unaware this was non-compliant.

'The only difference is now I have to cut and paste from my accounting package to a spreadsheet instead of straight into an online form.' (Nano)

Participants using incompatible legacy systems also reported perceived challenges with transferring to a new record keeping system. They felt that a significant financial investment would be required to enable the transfer of records from legacy software to fully compatible software.

5.3. Costs of bridging software

For bridging software users, costs such as additional time and perceived ‘hassle’ were consistent with the findings from the previous research suggesting these costs are unlikely to abate as time goes on.

Participants felt that they now had to go through additional steps such as logging into their bridging software and uploading spreadsheets in order to submit their VAT return. The amount of additional time taken varied within the sample, although those lacking digital confidence typically took longer than others. The digitally unconfident audience included participants who did not have access to a computer and so had to rely on friends and family to be able to create and submit their VAT return. These participants also reported spending longer on creating their return due to slower typing speed and needing to repeatedly check that they had used the bridging software in the correct way.

Participants who were digitally confident recognised that the process takes less time now than when they first started using software due to now having familiarity. This was not seen as being a positive given that overall, the process still takes longer than it did before Making Tax Digital for VAT.

‘The VAT return has gone from taking me about an hour a quarter to taking me 3 or 4 hours a quarter and costing me money. I now have to pay for software to submit it to HMRC.’ (Micro)

‘It’s added time, it’s a real pain and it produces no extra security whatsoever just because HMRC won’t take in any standard format’ (Micro)

‘It was all a bit silly really because I’m in the same boat but just have to use another company to submit what I used to submit.’ (Small)

An ongoing non-financial cost for bridging software users was anxiety about whether they would need to change or update their bridging software in the future. This cost tended to be prevalent amongst those businesses whose initial experiences finding bridging software had been stressful and time consuming. These participants were anxious about needing to repeat the process again, potentially with an even smaller pool of available software providers.

This cost was not found in [the previous research](#). It is likely that this has emerged in this research due to a perception that bridging software providers could end free trials and even the provision of the bridging software itself, leaving fully compatible software as the only alternative. This perception was driven both by direct experiences of free trials of bridging software ending

and speculation that providers would discontinue bridging software.⁵ Furthermore, as more time has passed, and familiarity with the bridging software used has increased, so has concern about trials ending. This anxiety was particularly acute amongst those using free or very cheap software who anticipated an increase in fees as providers end free trials and special offers.

‘I do worry about the cost of the software going up as I’d have to shop around to find one as straightforward as I use now.’ (Micro)

‘I used free bridging software for the first year but now I pay. I changed because they applied a massive charge after the first free year’ (Micro)

5.4. Benefits of bridging software

For participants using bridging software, the perceived benefits included a reduction in scope for error and lower accounting fees, although as the reduced risk and fees were small, these were considered minor. The main benefit was that bridging software acting as a digital link into HMRC removes the need to copy and paste figures at the point of submission. For many of those within the sample, this was previously the only manual part of their VAT submission and therefore was recognised to help eliminate potential errors. However, participants’ perceptions were that they were not making any errors or inaccuracies in their returns prior to Making Tax Digital for VAT. They therefore did not see this benefit as being of relevance to them.

Participants who had progressed from using paper ledgers to spreadsheets with bridging software did however perceive a further benefit. These participants reported saving on accountancy fees due to being able to digitally share their records with their accountant, saving their accountant considerable time.

‘[Direct digital links have] taken out the manual error of going from one spreadsheet to another.’ (Micro)

‘My accountant used to charge me a lot more money for doing my end of year accounts. Previously I used to give him a shoebox of paper and now I give him a spreadsheet.’ (Micro)

For bridging software users, the perceived value of bridging software was that it enabled them to continue using spreadsheets for preparing their VAT return. The lack of features, such as automatic calculations, to improve financial confidence and oversight were not seen as negatives as they were recognised as not being part of the bridging software offer.

The introduction of digital links had also had little impact on perceptions of financial confidence and accuracy. This lack of impact was partly due to digital links being a means of automating the transfer of data, rather than also automating calculations. Therefore, if an error was made in the calculations, digital links would transfer this error throughout, rather than correcting or

⁵ It is important to note that at the time of publication HMRC has no plans to end the provision of bridging software.

spotting it. It was acknowledged that bridging software did not have the features to be able to spot or correct inaccuracies and this was accepted. However, bridging software users were already confident in their processes and systems. From their perspective, there was little to no scope for improvement, even if they were using fully compatible software.

5.5. Comparison to the findings from the year one research

There was commonality in the types of businesses in this sample who were using bridging software and the bridging software users from the previous research. These businesses tended to have simple transactions and operations which were very tailored to their needs. Participants in both projects also tended to lack digital confidence.

Whilst there were commonalities in the types of participant, a distinction has emerged amongst the bridging software audience and their views towards bridging software. This distinction has emerged over time as evidenced by the difference in findings between the two projects.

At the time of the previous research, bridging software users were still adjusting to the introduction of Making Tax Digital for VAT. There was frustration both over the disruption of change and the requirement to change at all. There was resistance to accepting that this was a requirement which was here to stay.

This research indicates that bridging software users still feel a sense of resistance to Making Tax Digital for VAT and frustration over the change they had been obliged to undergo. However, despite this frustration, there was a sense that they were starting to accept that this is how they will have to submit their VAT returns from now on. This move towards acceptance was not evident in the previous research.

In addition to accepting that they would need to continue using bridging software, there was a perception that the alternative (full software options) were expensive packages which would be overly complicated for businesses like theirs. Therefore, bridging software was seen by participants as an acceptable compromise between small businesses and HMRC. It was welcomed as an alternative to having to substantially change their record keeping approach.

‘The alternative [fully compatible software] would have been like a sledgehammer to crack a nut!’ (Micro)

‘Not big enough to warrant a massive accounting software...bridging software was a godsend.’ (Micro)

‘I was worried we were going to have to overhaul our whole invoicing system – I wouldn’t know how to start; I just know how to make gates!’ (Micro)

6. Conclusions

This qualitative research sought to develop a better understanding of what the cost and benefits of Making Tax Digital for VAT have been in the second year of mandation for small businesses. In this chapter we reflect on the research questions, how these findings compare to previous research conducted in the first year of mandation and consider lessons from the research.

To recap, the core objectives of this research were to understand the impact of record-keeping behaviour change in response to MTD for VAT in the second year of mandation on :

- ongoing costs and benefits experienced by businesses
- scope for error and failure to take reasonable care
- whether/how these costs and benefits vary by record-keeping approach taken

It is important to remember that the findings from the research are based on a qualitative sample with responses representing the full range of previous record-keeping behaviour of the participants. The findings can therefore not be generalised for the wider population.

6.1. Reflections against the research objectives

The findings on ongoing costs and benefits of Making Tax Digital for VAT varied considerably between the two approaches to record-keeping (bridging software / fully compatible software). Therefore, here we reflect on findings relative to each of those separately.

Ongoing costs and benefits for those using fully compatible software

For those who transitioned from legacy software or spreadsheets the costs of fully compatible software were identified as being the following:

- the cost of either upgrading existing software or purchasing new software
- the cost of additional time spent building familiarity with the software

Participants with simple financial requirements and those winding down may have adapted better to bridging software instead. For these participants, bridging software may have been a less disruptive transition to make, enabling them to maintain their core processes.

The ongoing benefits of fully compatible software were identified as being the following:

- greater insight and financial control from software features and digital tools such as receipt capturing and automatic invoicing
- increased accuracy of returns and records
- increased financial confidence and oversight
- increased VAT confidence

- saved time

Fully compatible software users were able to access a wider range of benefits than bridging software users. The features which are available and the opportunities to incorporate these features into the day-to-day running of the business meant there was greater scope for improvement. For those already using software, there was the benefit of minimal change to their record keeping practices.

Ongoing costs and benefits for those using bridging software

The ongoing costs of bridging software were identified as being the following:

- cost of bridging software (typically an annual fee)
- additional time and effort for an extra process of submitting a VAT return

A further cost for bridging software users related to the emotional cost of participants worrying about free options ending or the cost of software increasing. However, this cost depended on the participant's choice of software provider and whether they had indicated plans to increase the cost or discontinue the product.

The ongoing benefits of bridging software were identified as being the following:

- one less manual intervention, thereby less risk of common errors (such as typos or decimal points in the wrong place)
- that it is an alternative to fully compatible software. This means businesses can continue using existing working practices and minimise perceived disruption

Bridging software users knew that they were using a basic approach and they were content. However, it provided a means to keep using their spreadsheets and previous record keeping approaches. For them, no feature of fully compatible software would be more attractive than this perceived benefit.

Impact on scope for error and failure to take reasonable care

It is challenging to determine the impact of Making Tax Digital for VAT upon scope for error and failure to take reasonable care. This is due to participants having a perception that they were not making errors or inaccuracies in their returns prior to Making Tax Digital for VAT.

However, participants were able to identify the benefits Making Tax Digital has on errors:

- digital links in bridging software could help to minimise manual errors
- features within fully compatible software could spot inconsistencies, inaccuracies, and oddities within records and mitigate against 'human error'

- those using receipt capture software appreciated the elimination of manual data entry, where entering a wrong digit is easily done

6.2. Reflections on how the findings compare to year one research

The businesses which participated in this research were purposively sampled to capture a wide range of experiences and views on Making Tax Digital for VAT. None of the businesses were interviewed as part of the previous research. Whilst commonalities have been identified, it is not possible to draw direct comparisons between the two research projects.

Amongst fully compatible software users, there has been a positive trajectory to realising benefits; as more time passes, additional benefits may continue to be realised. As businesses have built confidence and familiarity with the software, so more benefits have begun to emerge. This realisation of benefits was anticipated in the year one research as businesses recognised they were still adjusting to a change. Scope therefore remains for others to realise more benefits. COVID-19 has also delayed this potential for some for practical and emotional reasons.

However, there were some fully compatible software users who continue to view Making Tax Digital for VAT as unnecessary. These businesses perceive themselves as being too simple to warrant using fully compatible software which they perceive to be complicated and costly.

Bridging software users have remained consistent with the year one research in how they view the costs and benefits of Making Tax Digital for VAT. For most within our research population, the addition of digital links has had minimal impact. The minor benefit which digital links have provided is not enough to counter the perceived costs of Making Tax Digital for VAT. Overall, as this population has become more entrenched, it seems unlikely that they will realise additional benefits over time. However, bridging software was welcomed as an alternative to having to spend significant amounts on upgrading software or switching to software.

6.3. Learnings from the research

Analysis of the findings presents some lessons regarding ways to help businesses realise more benefits with regards to Making Tax Digital for VAT. These learnings are similar to those identified in [the year one research](#).

Acknowledging the different starting points of capability can help to overcome barriers such as financial and digital confidence, and emotional barriers such as anxieties about change.

Providing clarity over what the requirement is, and how different levels of capability are being accounted for could help reassure businesses, particularly those with very entrenched processes.

Small businesses have their own idiosyncrasies with regards to their systems and processes and this should be recognised. Presenting benefits which are tailored and relevant to how a business operates could help to make benefits feel relevant and worthwhile. This could help engagement and prevent people dismissing things that could be beneficial because they do not feel relevant.

Key gatekeepers, such as agents and software providers, can either leverage or shut down engagement. It is important that agents, in particular, communicate that the benefits of Making Tax Digital for VAT can both be wider than just VAT and be relevant to small businesses as a route for further digitisation and automation.