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Exploring voluntary sign-up to Making Tax Digital for VAT

Qualitative research with businesses

Ipsos MORI

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Behaviour, Insight and Research Team

OFFICIAL

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Exploring the communication needs of customers for the implementation of changes to Late Payment and Late Submission Penalties

Exploring voluntary sign-up to Making Tax Digital for VAT

Contents

1. Executive Summary.....	4
2. Introduction.....	7
2.1 Background	7
2.2 Research Aims	7
2.3 Method.....	8
3. Findings	10
3.1 Record keeping and VAT behaviours before MTD for VAT	10
3.2 Awareness and understanding of MTD for VAT	12
3.3 Reasons for signing up	13
3.4 Experience of moving to MTD for VAT	18
3.5 Impact of MTD for VAT on businesses.....	20
3.6 What would they say to other businesses?	24
4. Conclusions	26

1. Executive Summary

In July 2020, the government published¹ its 10 year strategy for building a trusted, modern tax administration system, incorporating plans for the gradual extension of Making Tax Digital (MTD). MTD is the first phase of a modern, digital tax service. It allows businesses more time to maximise business opportunities and helps to foster good financial planning. This integrated approach to business administration and tax means that many of the existing paper-based or manual processes are eliminated, and time spent on administration is reduced.

MTD is in the initial phase of roll-out for VAT. VAT registered businesses with a taxable turnover above the VAT registration threshold have been required to operate MTD since April 2019 and over 1.4 million businesses have started using MTD, submitting over 7 million VAT returns.

An estimated 27% of smaller VAT registered businesses, who are not yet required to operate MTD, have chosen to do so voluntarily. HM Revenue and Customs (HMRC) commissioned this study to explore why these businesses have made this choice.

From April 2022, all VAT-registered businesses (regardless of their turnover) will be required to operate MTD rules.

Thirty eight in-depth interviews were conducted with businesses that signed up to MTD for VAT voluntarily to understand their reasons for signing up. The research focused on those who made the decision to sign-up themselves, deliberately excluding businesses who were signed up by their agents. Fieldwork was conducted in August and September 2020.

The businesses used a variety of record keeping systems prior to signing up MTD, including paper, spreadsheets, non-MTD-compatible software and MTD-compatible software. Regardless of the systems they had in place, businesses generally found preparing and submitting their VAT returns straightforward.

Participants struggled to recall how they had first found out about MTD for VAT, but HMRC, accountants and industry bodies were key sources of information for ongoing support. Most did not recall having initial questions about MTD for VAT, but where they did, they focussed on what software they would need to use and how (if at all) MTD would present a change to their record-keeping practices.

The primary reasons businesses had for signing up to MTD voluntarily were because they expected to exceed the VAT threshold in the near future or because they presumed they would

¹ Please see: <https://www.gov.uk/government/publications/tax-administration-strategy/building-a-trusted-modern-tax-administration-system>

have to move to MTD eventually, so thought it was better to do it sooner rather than later. In both instances, businesses wanted to have the right system in place ahead of time, to avoid having to do it reactively during a busy time in the future.

‘It was only a matter of time before I went over the threshold, so it made sense to get registered, it's not good to be rushing around to get set-up.’

Turnover £75k+, typically pay VAT, spreadsheet to bridging software

Most businesses were aware that they were not required to use MTD for VAT unless their turnover had exceeded £85,000. Some were not aware of this, and thought they were required to sign up because HMRC had sent them letters or emails. Either they had (incorrectly) assumed that the voluntary element was being VAT registered, rather than using MTD for VAT, or they had received incorrect advice from their agent or from information shared online.

‘The way it was worded online was that I had to do it. All things being equal, I would have preferred not to.’

Turnover below £50k, typically pay VAT, spreadsheet to bridging software

Participants who were already using MTD-compatible software thought it made sense to sign-up, as they thought it would be easy and more efficient. A few participants hoped that signing up to MTD would lead to more accurate record keeping and to reduce errors. Some also hoped that this would, in turn, lead to fewer traditional compliance checks, reducing the burden for both HMRC and businesses.

‘I hope it will mean that HMRC builds better relationships with businesses around VAT as their relationship on other taxes like PAYE and Corporation Tax is much better than it was because of the availability of online information.’

Turnover below £50k, typically receive VAT refunds, full software from start

Finally, the decision to sign-up for MTD (voluntarily) was straightforward for new businesses who had registered for VAT from the outset. They felt that using MTD and full software from the start to monitor their day-to-day finances and compile their VAT returns made sense, and not to use full software would be illogical when all their other business systems were digital.

‘MTD is a ‘no brainer’ ... it’s obviously where things are going, so it just makes sense [to sign up to MTD] from the beginning.’

Turnover below £50k, typically receives VAT, new business

The process of signing up to MTD for VAT was easiest for those already using software. Those with MTD-compatible software had to press a button or tick a box, others had to upgrade their software (which they found simple to do). And some changed their providers as MTD presented an opportunity to review the software they were using.

Signing up was more challenging for businesses using software for the first time. Some found the range of providers and packages overwhelming and found it difficult to know which option would best suit their business.

The impact that MTD for VAT had depended on the extent to which businesses understood and engaged with the policy; this, in turn, depended on whether they saw MTD as a change to how they managed their finances, or whether they saw it as simply a new way of submitting information to HMRC. How much they engaged with the policy affected their software choice, their grasp of the software's functionality and their post-MTD record-keeping practices.

Those who fully understood and engaged with the principles of MTD (and the idea of real-time record-keeping) noted the benefits of monitoring their financial position in real-time, speeding up record keeping due to automation, and additional reassurance that they were getting their VAT returns correct first time.

Most participants did not experience any impact from moving to MTD, either because they were new businesses that signed up from the outset of establishing their business, or because they had not changed their record-keeping practices (they were either already using software, or chose to use bridging software that was similar to their pre-MTD spreadsheets).

Participants who had not fully understood and engaged with the policy reported negative impacts as a result of signing up to MTD. These included: resenting the cost of purchasing software (when the VAT portal had been free), as well as the additional time spent changing their record keeping systems. Some businesses that maintained their pre-MTD spreadsheets alongside their bridging or full software also said that they had made more mistakes with their record keeping since moving to MTD. These businesses reported that they had continued to use their own spreadsheets and copied the figures across into their new software in order to submit their return to HMRC, as they felt more comfortable maintaining a system that they had used for a number of years.²

With the exception of those with low MTD engagement, businesses generally thought that MTD worked well or that it had no material impact on their day-to-day financial management practices. Where they suggested improvements, these included more advice from HMRC on which software to choose (including outlining the pros and cons of bridging versus full software), grants to purchase software or an HMRC-recommended basic package for small businesses and the ability to pay HMRC via direct debits.

Participants said they would recommend MTD for VAT using full software to businesses who were already using software, or those who would find moving to software straightforward. They thought it made complete sense for new businesses to start out using full software, in order to avoid getting used to one system and then having to replace it. However, those with low MTD buy-in who had negative experiences of MTD for VAT were unlikely to recommend it to other businesses. Instead, they suggested delaying signing up until they were required to.

² Under MTD rules, accounting records are required to be digitally linked – meaning no human intervention takes place in compiling VAT returns. Copying and pasting figures from spreadsheets into MTD VAT submission software (also known as bridging software) is not compliant with MTD rules.

2. Introduction

2.1 Background

In July 2020, the government published³ its 10 year strategy for building a trusted, modern tax administration system, incorporating plans for the gradual extension of Making Tax Digital (MTD). MTD is the first phase of a modern, digital tax service. It allows businesses more time to maximise business opportunities and helps to foster good financial planning. This integrated approach to business administration and tax means that many of the existing paper-based or manual processes are eliminated, and time spent on administration is reduced.

MTD is in the initial phase of roll-out for VAT. VAT registered businesses with a taxable turnover above the VAT registration threshold have been mandated to operate MTD since April 2019 and over 1.4 million businesses have started using MTD, submitting over 7 million returns.

An estimated 27% of smaller VAT registered businesses, who are not yet required to operate MTD, have chosen to do so voluntarily. HM Revenue and Customs (HMRC) commissioned this study to explore why these businesses have made this choice.

2.2 Research Aims

This research focuses on businesses whose turnover was below the VAT threshold when they decided to sign-up for MTD. They are therefore described as signing up 'voluntarily'. Research has also been conducted on the experiences of businesses above the VAT threshold, who were required to sign-up for MTD for VAT⁴. These are two distinct populations although, as this study shows, their experiences of operating MTD are broadly aligned.

The aim of this research was to understand participants' motivations for voluntarily signing up to MTD for VAT, to allow HMRC to design a strategy to encourage further voluntary sign-ups and support businesses through the sign-up process ahead of mandate in April 2022. The core objectives of this research were to:

- develop an understanding of the reasons why businesses voluntarily sign up to MTD for VAT.

³ Please see: <https://www.gov.uk/government/publications/tax-administration-strategy/building-a-trusted-modern-tax-administration-system>

⁴ Please see: https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/871582/HMRC_research_report_576_-_MTD_and_small_business_record_keeping.pdf

- understand these customers' perceptions and experiences of signing up to and using MTD.
- identify the perceived benefits of MTD to further refine communications messaging.
- determine what improvements and guidance HMRC can build into the system to mitigate against customer pain points.

2.3 Method

A total of 38 in-depth interviews⁵ were carried out with businesses that signed-up to MTD for VAT while they had a turnover below the VAT threshold. A sample of businesses was provided by HMRC for this research.

All interviews were carried out by members of the Ipsos MORI research team between August 24th and September 17th 2020. Interviews were conducted by telephone and were around 45 minutes in length. Participants were asked to complete a short task before the interview to encourage them to think about the issues to be covered.

2.3.1 Sample

The focus of the research was on businesses who made the decision to sign up to MTD for VAT directly, rather than being signed up by their agents. Though out of scope for this research, it is important to consider this as another reason why businesses under the VAT threshold may sign-up for MTD for VAT voluntarily. Quotas were set for a range of criteria to ensure we included a good mix of eligible businesses. The final composition of the sample is outlined overleaf.

⁵ The initial design for the research was 40 interviews, however it was not possible to achieve this from the sample available due to the number signed up by agents and ineligible businesses included in the sample.

Sample composition

Criteria	Sub-categories	No. interviews
Turnover	£49k or less	20
	£50k - £74,999	11
	£75k +	7
Agent Use	Use an agent	9
	Do not use an agent	29
Bookkeeping confidence	Confident	31
	Not confident	7
Sign-up date	By end September 2019	20
	October 2019 onwards	18
Experience of sign-up	Experienced difficulties	12
	Did not experience difficulties	26
Typically pay or receive VAT payments	Pay	29
	Receive	9

We also had several secondary quotas to ensure a mix of:

- legal entity (limited company, partnership, sole proprietor).
- pre-MTD for VAT record keeping system.
- post-MTD for VAT record keeping system.
- location and industry type.

The initial design also included a quota on confidence with HMRC digital systems but only one business reported that they were not confident at recruitment stage. However, this was not necessarily supported by what businesses described during the interviews.

3. Findings

This report presents qualitative findings about the motivations and experiences of businesses that voluntarily signed up to MTD for VAT while they had a turnover below the VAT threshold. The report starts by describing the record-keeping practices of businesses who signed up to MTD for VAT voluntarily (Section 3.1) and their awareness and understanding of MTD for VAT (Section 3.2), before discussing the various reasons that they had for signing up. The primary focus for this research was to understand why these businesses signed up to MTD for VAT without being required to do so, and the first two sections (3.1 and 3.2) provide important context which helps to answer the main research question.

3.1 Record keeping and VAT behaviours before MTD for VAT

This section explores participants' record-keeping and VAT return practices before they signed up to MTD for VAT voluntarily.

Record keeping before MTD for VAT

Participants used one of four bookkeeping systems to manage finances and record VAT:

- **Spreadsheets:** These were popular because they were perceived to be easy to set-up and manage which meant that businesses felt comfortable using them. They were also seen as relatively easy to understand which made participants feel confident that their figures were accurate. Finally, spreadsheets were either a free or low-cost option.

'I like spreadsheets, I'm comfortable with them, I can set things up the way I like and understand what's going on.'

Turnover below £50k, typically pay VAT, spreadsheet to bridging software

- **Software not compatible with MTD:** This included both standalone and online packages with a wide range of functionality dependent on when it was purchased. Participants used these packages either because they had a high volume of transactions to record, for example a shop, or because they thought it would strengthen record-keeping practices.

'I wanted to know everything was right and to be able to quickly look at our accounts to make sure we were doing all right.'

Turnover below £50k, typically pay VAT, software to bridging software

- **MTD-compatible software:** This was mainly used by those that had started trading after MTD for VAT was launched. These participants knew they would need MTD compatible software eventually so used an MTD package from the start.

'I chose to use software to make my job easier.'

Turnover below £50k, typically pay VAT, full software from start

- **Paper:** This was uncommon but used by participants that did not feel a formal system was necessary due to the small number of invoices and receipts they handled.

‘I tend to have very few, largish invoices so it doesn't really make much difference if I jot them down on paper...or if I put them in a spreadsheet.’

Turnover below £50k, typically pay VAT, paper to bridging software

The key drivers when choosing a bookkeeping system were timing, confidence and need. Participants' pre-MTD systems often reflected common practice at the time they started their business and once they were comfortable and confident in their system, they were reluctant to change it. Participants sometimes used basic accounting systems because they did not believe their finances were complex enough to warrant more automated systems, with greater functionality. Conversely, those with the most up-to-date systems chose them because they wanted their record keeping to be more efficient, or because they felt their business would grow and require a more robust system.

Preparing and submitting VAT returns before MTD

Regardless of the system used, participants generally found preparing and submitting their VAT returns straightforward. There were three steps to this:

1. **Record:** Most participants reported that they updated their systems regularly (daily, weekly or monthly) but some only updated their records in order to prepare a VAT return. Regularity depended on the volume of invoices and receipts the business handled as well as the business owner or director's attitude to record keeping.
2. **Prepare:** Participants would check their records were up to date and then manually or automatically generate the figures needed. This could take a few minutes or many hours, depending on complexity and confidence. Some checked figures with their agent.
3. **Submit:** To submit, they logged onto the VAT portal and entered their figures. This step was seen as quick and easy. No issues were reported with submitting figures or with using the portal. Participants were confident with the process.

For some participants, there was a fourth step to correct their VAT submission after finding they had made an error, by incorrectly marking something as VAT or non-VAT liable or because they had missed a receipt which they wanted to reclaim VAT on. Many of these participants said they amended almost every return they submitted.

These directors or owners described some disorganised record-keeping practices including only updating their records when a VAT return was due and rushing to get it together in time. This meant that even those who used MTD compatible software were submitting returns with errors that needed to be corrected and they saw this as a standard part of the process.

'It was fine, I would update it all when the return was due and then inevitably find a few receipts I wanted to claim the VAT on and make a correction.'

Turnover £50k - £75k, typically pay VAT, full software

3.2 Awareness and understanding of MTD for VAT

This section explores how businesses who signed up for MTD voluntarily became aware of MTD for VAT, their initial questions or concerns and their understanding of sign-up being voluntary for their business.

Awareness of MTD for VAT

Participants generally struggled to recall exactly how or when they became aware of MTD for VAT, but most believed they first heard through communications, either letters or emails, sent by HMRC⁶. Some said they received a great deal of communication about the change and were aware that a pilot took place before the system was launched, but others had only vague recollections of receiving a letter or email. Besides HMRC communications, others found out about MTD for VAT from the following sources:

- **Software:** Those who were already using MTD-compatible software received messages from the software provider and some also recall seeing a countdown to launch.
- **Agents:** Many participants who used an agent had discussed MTD for VAT with them. These conversations were normally started by the agent when discussing end of year accounts and planning.
- **Industry bodies:** Some participants became aware through their sector's trade bodies' social media accounts, email newsletters or online articles.
- **News:** A small number first heard about MTD for VAT on national broadcast news.

Reactions, questions and concerns

Most participants described feeling neutral about MTD for VAT when they first heard about it. These participants did not really question why MTD was being introduced or what impact it might have but simply accepted that a shift towards greater automation was inevitable and that MTD must have some benefits for HMRC.

⁶ Please note: HMRC only sends MTD correspondence to mandated businesses and those near the VAT threshold. Therefore, not all of those interviewed would have received information directly from HMRC.

‘This is just the way the world is going. It's not good or bad, it just is.’

Turnover below £50k, typically pay VAT, full software from start

Those with some experience of other digital systems, such as Real Time Information, tended to be positive about the change as they thought it might improve accuracy and efficiency for both businesses and HMRC. There were no specific negative views on the change although some did report concerns that MTD might be disruptive or difficult for them to manage.

Questions and concerns about the change mostly related to software. Those who were not already using MTD-compatible software wanted to know the cost and implications of changing to compatible software as well as guidance on choosing a package that was right for them. There were also questions about how the process of submitting a VAT return would differ from the current system and whether this would impact how they managed their finances. Questions included:

- how will it be different to the current VAT return?
- what data will HMRC need?
- what format does the data need to be in?
- can I use my existing software package?
- which software is right for my business?
- how difficult or time consuming will it be to set up?
- how will the change impact me?

Participants tended to use the same sources for information to answer their queries that they had used to become aware of MTD. As such, most relied on information provided by HMRC both in communications sent to them about MTD for VAT and using GOV.UK to find specific information. Some participants who wanted guidance with choosing software said they searched for this on GOV.UK and although they found a list of compliant software packages, they did not feel this was useful without some advice about what type of package might suit a business like theirs and how much this might cost.

3.3 Reasons for signing up

This section explores the reasons businesses had for voluntarily signing-up to MTD for VAT including who was involved in the decision, reasons for signing up as well as any benefits and costs or drawbacks they expected from using MTD for VAT.

Decision making

The decision to sign-up to MTD for VAT voluntarily was typically made by the owner or director of the business. In businesses with more than one owner or director, the decision was normally made by the person responsible for managing the business finances. The decision to sign-up was not always considered to be important enough to be discussed with others in

the business, especially if the business was already using compatible software or if finances were handled solely by one person. This decision was generally only discussed if the responsibility to manage finances was shared or if moving to MTD was likely to cost a significant amount.

Businesses that used an agent did not tend to contact them for advice about MTD and so agents were generally only involved in the decision if they raised it with the business⁷. In cases where agents were involved, they tended to encourage sign-up and for the participant to use full software, often recommending specific products.

Software providers also played a role. Participants that were already using MTD compatible software said that they received messages from the provider about MTD, with prompts to sign-up and a countdown to the launch date.

Reasons for signing-up

Participants discussed a range of reasons for signing up to MTD:

- **Not aware sign-up was voluntary:** Most participants knew that they were not required to use MTD for VAT unless their turnover exceeded £85,000, but not all were aware, and some believed that they had to sign-up. Reasons for thinking sign-up was mandatory included: assuming they were required to sign-up because HMRC had sent them direct communications about MTD for VAT; believing that the 'voluntary' decision was about registering for VAT, but that all VAT-registered business would need to use MTD; and misinformation or misunderstanding information provided by their agent, or in online articles.

'In retrospect, the communications sent by HMRC were a bit opaque...but maybe I was inattentive at the time and missed it.'

Turnover below £50k, typically pay VAT, paper to bridging software

Reactions to learning that they had not been required to sign-up varied. Some participants were relaxed about this, reasoning that if they would need to sign-up by April 2022 then it would not make much difference overall. This was especially the case for any businesses already using MTD-compatible software. Others said that they would have put off signing up if they had been aware this was an option. This reaction was more common among participants that were using paper or spreadsheets and were not convinced that they would benefit from using software.

⁷ Please note, this research specifically focused on businesses who had signed up for MTD for VAT directly, excluding those who had been signed up by their agent.

‘The way it was worded online was that I had to do it. All things being equal, I would have preferred not to.’

Turnover below £50k, typically pay VAT, spreadsheet to bridging software

- **Expected to exceed the threshold:** This was the most common reason given by participants that were aware sign-up was voluntary. These participants believed, or hoped, that they would exceed the threshold and signed up in anticipation of this. Some expected this to happen within a year or two, while others were unsure of when it might happen but wanted to plan and work towards it. These participants wanted to ensure that they had the right processes and systems in place ahead of time to avoid needing to make changes during a busy or inconvenient time. This was the most common reason given by businesses with a turnover of £75k-£84k as they were closest to the threshold, but it was also the main reason for new, fast growing businesses with lower turnovers.

‘It was only a matter of time before I went over the threshold, so it made sense to get registered, it's not good to be rushing around to get set-up.’

Turnover £75k+, typically pay VAT, spreadsheet to bridging software

- **Getting ahead of the curve:** This was the main reason given by participants that knew sign-up was voluntary but did not expect to exceed the turnover threshold. These participants assumed that they would have to move to MTD for VAT eventually so thought it was better to do it sooner rather than later. This reason was common for businesses already using MTD compatible software but was also given by businesses using other systems. Some were encouraged to sign-up by their agent who told them they should not wait for a deadline and make the change in their own time. There was a feeling that there might be a benefit to being early adopters and that it might improve efficiency, but participants were not sure how exactly.

‘The longer you leave these things, the more stressful they become so if I thought if I just bite the bullet now it will save a lot of hassle down the line.’

Turnover £50k - £75k, typically pay VAT, software to full software

- **Ease and efficiency:** Participants who were already using MTD-compatible software thought it made sense to sign-up as they could simply click to submit through their software rather than log into the VAT portal. These were businesses that had generally been established after MTD for VAT was launched and were using MTD from the start as they thought it made sense to begin with the most automated, up-to-date system.

‘I believed it to be quicker and easier than any alternative and it did not cause me any inconvenience.’

Turnover below £50k, typically pay VAT, full software from start

- **Improve compliance and working relationship with HMRC:** Though uncommon, this was important for a small number of participants who hoped MTD would lead to more accurate record keeping and reduce errors. Some also hoped that MTD for VAT would change

HMRC's approach to identifying error and fraud, leading to fewer traditional compliance checks and reducing the burden for both HMRC and businesses. They thought this could lead to a better working relationship and improve businesses' perceptions of how HMRC managed VAT. These participants tended to have considerable experience handling VAT, dealing with compliance checks, and of other taxes that have already moved to digital systems.

'I hope it will mean that HMRC builds better relationships with businesses around VAT as their relationship on other taxes like PAYE and Corporation Tax is much better than it was because of the availability of online information.'

Turnover below £50k, typically receive VAT refunds, full software from start

- **MTD made sense for new businesses:** New businesses who had signed up to MTD for VAT from the outset of establishing their business felt that using MTD and full software from the start, to monitor their day-to-day finances and compile their VAT returns made sense, and that it would be illogical not to use it. They explained that almost all the other services that they accessed on a regular basis, whether for business or personal use, were online or accessible via mobile apps.

'MTD is a 'no brainer' ... it's obviously where things are going, so it just makes sense [to sign up to MTD] from the beginning.'

Turnover below £50k, typically receives VAT, new business

Expected benefits to moving to MTD for VAT

Participants primarily saw MTD for VAT as a change to the way they submitted their VAT return rather than how they would manage their business finances and because of this, most did not think there would be any significant benefit to moving to MTD. As they focused on submission rather than record keeping, they assumed that the main benefits of MTD for VAT were for HMRC rather than businesses but they were comfortable with this. There was a general feeling that all systems would become more automated over time and that they should accept and keep up with this change rather than resist it.

'Doing it on paper should have gone out with the ark so it was a push into changing to a spreadsheet.'

Turnover below £50k, typically pay VAT, paper to bridging software

Business owners who did expect to benefit from the move to MTD for VAT tended to focus on saving time with making VAT submissions and with improving their record keeping. Their expectations of how they might benefit and how significant the benefits might be depended on their pre-MTD record keeping systems.

- **Those who were already using MTD compatible software:** These participants had the clearest idea of how MTD for VAT might benefit them, although these benefits were thought to be marginal. As these businesses were already using full software, the only

change they anticipated was clicking a button to submit a return rather than using the VAT portal. They expected this would save them a small amount of time.

‘MTD means submitting my VAT takes a matter of minutes, rather than ten minutes.’

Turnover £50k - £75k, typically pay VAT, software to full software

- **Those who were using software not compatible with MTD:** Participants using other software packages also expected MTD to save a small amount of time, but some also hoped it would reduce errors. These participants were used to managing their records in software and then writing down their VAT figures and manually entering them using the VAT portal. Some were aware that this step could easily introduce errors into their return and that MTD would remove this risk.
- **Those who were using a spreadsheet:** These participants tended to be happy with their existing record-keeping practices and were often not aware of the possible advantages of using a software package. This meant that they tended to struggle to see benefits of MTD apart from a vague sense that it might be more efficient for them.

‘I thought MTD would mean maybe a move on to a new more efficient system.’

Turnover below £50k, typically pay VAT, spreadsheet to full software

- **Those who were using a paper-based system:** These participants were aware their systems were old-fashioned but were happy with them. This was because they believed their finances were simple enough to be managed in this way and that they would not benefit from moving to a digital system. Consequently, they could not identify any benefits to MTD.

Expected costs or concerns about moving to MTD for VAT

Business owners who were already using MTD-compatible software did not expect to incur any costs and did not have any concerns about the change.

Participants that needed to either change or start using software were more concerned about the potential costs of this. The focus for most participants who were choosing software for the first time was to find the cheapest option, even it meant using software with limited functionality. Even participants that were happy to spend more to access greater functionality said that cost was a key factor when deciding on which package to purchase.

As most participants did not think they could expect any significant benefits from moving to MTD, even spending relatively small sums to comply were viewed as a cost rather than an investment.

‘It's an irritation to pay for something you don't really want but that is part of running a business. It's not a huge amount to be fair.’

Turnover below £50k, typically receive VAT refunds, spreadsheet to full software

Those that were already using other software were also concerned about the potential disruption of changing packages and possibly providers but, overall, they were comfortable with the idea of having to do this. However, many participants with no experience of purchasing software said they were unsure where to start with this and some said they lacked confidence in making the right decision.

3.4 Experience of moving to MTD for VAT

This section describes the experiences of businesses who signed up for MTD for VAT voluntarily of moving to MTD for VAT, including how they chose MTD-compatible software and their experience of signing-up with HMRC.

Upgrading or choosing a software package

The transition to MTD was easiest for participants that were already using MTD-compatible software. For them, it was simply a case of enabling the MTD function in the software, signing up to MTD with HMRC, and they were set-up. These businesses said that their software providers had made the change as easy as possible and they could not recall any issues with the transition.

‘The update happened in the background I think and then I just had to tick a box on the software to use the MTD function. That was it.’

Turnover below £50k, typically receive VAT refunds, full software from start

Participants who were using software that was not compatible with MTD tended to stay with the same provider if possible. These participants looked for a compatible package available from the same provider as they assumed the packages would be similar in look and feel and easier for them to learn to use. They also hoped that their provider would support them with the transition and hoped it would be less disruptive to the business.

Participants who changed providers generally did this either because their current provider did not have a suitable product available or because the product they offered cost more than they wanted to pay. These participants either searched online for suitable packages, mainly focussing on the HMRC list of software providers, or relied on recommendations from their agent or other businesses.

For those choosing software for the first time, cost was the main factor considered when searching for a package. These participants often reported lacking confidence in being able to identify an appropriate package for their needs. They also tended to assume that their business finances were too simple to justify paying for a package from a well-known provider.

‘I was going to use [well known software provider], it's quite expensive, but I think it would have been like using a sledgehammer to open a nut. I needed something much less powerful and cheaper.’

Turnover £50k - £75k, typically pay VAT, spreadsheet to full software

Participants without a trusted source of advice (such as an agent or others using MTD software) tended to rely on the list of packages on GOV.UK⁸ and then searched online to find out more information, specifically what they would cost. Some participants said they took advantage of free trials of different packages to find one they were comfortable with, but many ended up choosing a product based on cost. Deciding purely on cost led many to choose bridging software as it was often the cheapest option.

‘It's one of the lowest priced options for MTD software. It's not as all singing, all dancing ...but I don't need that.’

Turnover below £50k, typically pay VAT, paper to bridging software

Bridging software was also appealing to those who were wedded to their existing record keeping systems and preferred the idea of retaining these rather than moving to a completely new system. These participants were primarily looking to ‘comply’ rather than ‘improve’ and so they wanted to spend and change as little as possible.

‘I still use my spreadsheet so I just needed something I could upload my figures to for generating a return, it's pretty simple.’

Turnover £75k+, typically pay VAT, spreadsheet to bridging software

Participants who moved from a spreadsheet system to full MTD software generally did this either because they were recommended a specific package by their agent or another business, or because they found a package for free or at low cost.

Signing-up for MTD with HMRC

The process of signing-up for MTD for VAT through GOV.UK was generally a step that most struggled to remember much about. They said this meant it was probably a straightforward process.

‘I don't remember and the reason I don't remember is probably because it was seamless.’

Turnover below £50k, typically receive VAT refunds, full software from start

The only part that some participants could remember about signing-up was waiting for the security information to be sent to them by post and this did feel like a hold up for businesses that were keen to get set-up quickly. However, they understood the need for security processes and said this did not have a negative impact on their experience.

⁸ Businesses can search for MTD-compliant software on GOV.UK. HMRC tests the software products to make sure they function as required after which they are included on the Software Choices page. Please see: <https://www.gov.uk/guidance/find-software-thats-compatible-with-making-tax-digital-for-vat>

3.5 Impact of MTD for VAT on businesses

This section describes the impact that moving to MTD had on businesses who signed up voluntarily, including examples of positive, negative and neutral impacts and improvements that businesses suggested could be made to the service.

Engagement with the principles of MTD

The extent to which participants understood and engaged with the idea of MTD depended on whether they saw it as a change to how they managed their business' finances, or whether they saw it as simply a different way to submit a VAT return. Their level of buy-in affected:

- **Which software they chose (trading off between functionality and cost):** Participants that had not fully engaged with the principles of MTD chose cheaper options, with more limited functionality, in order to keep their record-keeping practices as similar as possible to their pre-MTD systems. Some participants chose bridging software as a compromise between fulfilling the requirements of MTD and keeping their established systems in place.
- **The extent to which they embraced the software's functionality:** Those who did not understand, or did not want to understand, the full potential of their software did not feel the full benefit of using it regularly to manage their business finances.
- **Their post-MTD record-keeping practices:** The extent to which they embraced the idea of updating their VAT records as they went, logging receipts at the time of purchase (using mobile apps) or generating invoices from the software itself.

Those who had understood and engaged with the principles of the policy fully tended to feel the most benefit, whereas those who had not reported more negative experiences. Most businesses, however, could not identify any impact from MTD.

Neutral impact from MTD

MTD for VAT had a neutral impact on most businesses interviewed. New businesses and those that did not make any changes to their record-keeping practices could not identify any impact, positive or negative, from signing up to MTD for VAT.

As mentioned in Section 3.3, new businesses that registered for MTD from the outset felt that it made sense to do so, and they found it difficult to identify any impact from MTD as they had no previous system with which to compare their experiences.

The second group who felt MTD had a neutral impact on their businesses were participants who had kept their pre-MTD record-keeping practices. These were businesses who either:

- had established pre-MTD record-keeping practices that they were confident in, usually involving a spreadsheet and who had moved to bridging software; or
- were already using full software prior to MTD.

These participants saw MTD as simply a new way of submitting information to HMRC and subsequently did not see any positive or negative impacts.

‘It’s exactly the same accounts as I’ve always done. There’s been no change in process, it’s just a different way of logging into HMRC.’

Turnover £50-75k, typically pay VAT, spreadsheet to bridging software

Positive impact from MTD

Participants that had fully understood and engaged with the principles of the policy experienced the most positive impacts from MTD. These were businesses that had either upgraded or moved to full software and were using their software to its full potential for day-to-day financial management and real-time record keeping.

Participants reported the following positive impacts as a result of moving to MTD:

- **Real-time record keeping:** Having cloud accounts and mobile apps meant that participants could update their finances in real-time, for example, logging receipts at the point at which they made business purchases. This provided an up-to-date picture of both their overall financial position and whether they would be paying or reclaiming VAT. Those that had embraced real-time record keeping felt they spent less time compiling their VAT returns. They were also less likely to miss receipts or make errors in their returns as they were recording receipts and invoices in real time and then checking before submission.

‘I get a receipt, I photograph it, input it, and then that’s finished with [...] I love it. It’s made it so much easier for me, because everything’s already been put in and it automatically puts in in date order. It comes to the end of the quarter, I click on one button. It’s shows you what you’re sending to HMRC and then off it goes. It’s as quick as that. Brilliant!’

Turnover £50-75k, typically pay VAT spreadsheet to full software

- **Automation providing speed and simplicity:** Participants also reported that automation made processes quicker and reduced the scope for human error, as the software linked directly to their bank account(s), was able to generate invoices, and provided the option to duplicate a previous invoice for repeat customers.

‘It cuts a manual step out of the process by taking the figures and copying them into the six boxes on the online form that you fill in on the HMRC website, so it does reduce the margin for error [...] It’s nice that it gets the figures directly from the accounting package and doesn’t rely on me messing up a manual process.’

Turnover below £50k, typically pay VAT, full software from start

- **Reassurance and getting taxes right first time:** Some also benefitted from additional reassurance, in clear reminders about when VAT returns were due and helpful advice on which VAT rates to attribute to items, as well as providing reassurance that claiming VAT back on some expenses was legitimate.

‘We use accountants who specialise in the pub trade and they set up software for us to use. We probably pay a bit more for it, but it’s all set up to show the current VAT rates on different drinks and food, and the accountant will update it whenever there’s a change.’

Turnover above £75k, typically pay VAT, spreadsheet to bridging software

Negative impact from MTD

Participants who reported negative impacts from using MTD for VAT had not fully understood or engaged with the principles of the policy. These participants reported the following negative impacts as a result of moving to MTD:

- **Cost of purchasing software:** Those who chose to use the most basic bridging software, with little to no functionality for wider financial management, resented the cost of setting up and using a new system – even when they acknowledged the amount they paid was nominal.

‘It’s not a lot of money, and the business doesn’t miss it, but it feels annoying to have to pay for something that was provided for free on government Gateway [VAT portal]⁹ before.’

Turnover below £50k, typically pay VAT, software to bridging software

- **Scope for error:** Business owners who were wedded to their pre-MTD systems and continued to use them alongside their bridging or full software found that moving to MTD meant they were spending more time on their recordkeeping and VAT returns as a result. Some were copying values from their own spreadsheets across to their bridging or full software¹⁰. Under MTD, HMRC expects that providing quarterly updates directly from digital records will help to prevent errors that can happen when businesses undertake manual calculations or transcribe information from one format to another. Where businesses continued to manually copy values over from their own spreadsheets, this potential for error still remains.

‘I think to be honest, you get to an age where you like things the way you like them. Young people will probably be more comfortable with this kind of change but I’m not. I like my spreadsheet so I use that and then go into the software and I always have

⁹ Some participants referred to the VAT portal as ‘government Gateway’, likely because they had to use their government Gateway ID to log in.

¹⁰ Manually copying figures into bridging or full software is not compliant with MTD rules.

problems with it. Before I was just sending to my agent so I didn't have to deal with the return part at all so it has created more work.'

Turnover below £50k, typically receive VAT, spreadsheet to full software

- **Additional time:** Those who were not digitally confident, or who struggled to understand new software that they found less intuitive or reliable than their previous systems, also felt that their record keeping and VAT returns now took longer.

'Everybody raves about [full software] being so simple, but I don't actually find it that intuitive to use. I don't know, maybe if I sat down intensively and was fiddling around with it every day for a week, but actually it's that kind of business where you need to be on it all the time.'

Turnover below £50k, typically pay VAT, spreadsheet to full software

- **Quarterly record keeping:** Participants who had not embraced real-time record keeping resented the fact that using software made it more difficult to make corrections to their VAT returns once they had submitted them, if they later found receipts they had not logged, for example.

'Logically it's given us accurate VAT returns, it's just not allowed any adjustments and adjustments are legitimate and necessary sometimes... It's accurate within the parameters of what it will allow us to do... It's an accurate picture of what it's picking up but it's not a true picture.'

Turnover below £50k, typically pay VAT, spreadsheet to full software

Aside from those with low engagement with MTD, there were a handful of cases where participants had experienced unforeseen technical difficulties with MTD for VAT. These (few) cases showed that having three parties involved (the customer, HMRC, and the software provider) made issues potentially more challenging to resolve, as the business owner was unsure who to approach first, or how to resolve the issue. For example, those that discovered issues explained that their software provider could not alter any information sent by HMRC, and HMRC could not advise on individual software packages, meaning that resolving any issues usually meant back and forth between both parties.

Improvements to MTD for VAT

With the exception of those with low engagement with MTD (who reported negative experiences), businesses thought that MTD for VAT worked well overall. Where they had suggestions for improvement, these were focused on software.

- **Which software to choose:** Participants thought they, and other businesses considering signing up to MTD, would benefit from more guidance from HMRC on the different

packages available. They wanted guidance or a recommendation on software that would be well-suited to smaller businesses with more straightforward finances¹¹.

‘If HMRC could give smaller businesses guidance on how to choose an accounting software provider, that would help. If they could tier it by income amount, or complexity of accounts.... I was lucky I had the advice, but some business might not.’

Turnover £50-75k, typically pay VAT, spreadsheet to full software

- **Financial support for software:** Businesses with tighter margins, and those that resented having to pay for software when the VAT portal had been free¹², suggested grants for the smallest businesses to help purchase software and comply with MTD. In the absence of a grant, there was strong appetite for an HMRC-developed or HMRC recommended software package designed for small businesses (as noted above).
- **Clearer explanation of the pros and cons of bridging and full software:** Some participants did not realise that their bridging software would have limited functionality compared to full software at the point at which they were signing up to MTD for VAT. Those with low engagement with MTD were also unaware, or unconvinced, of the potential benefits that full software could have on their day-to-day financial management practices.

‘HMRC could put out in-depth tutorials to say, ‘here’s the benefits, here’s what you could get from this and here’s how you do it’ [...] If you’ve got a process that works, then you don’t want to mess with it unless you’ve got a good reason to.’

Turnover below £50k, typically pay VAT, previously used software

- **Digital payments to HMRC:** Some participants wanted to make their tax more digital with the option to pay tax bills automatically through their software and to allow direct debits (as with credit card bills), meaning that payment could be taken automatically.

3.6 What would they say to other businesses?

Businesses who signed up to MTD for VAT voluntarily were asked what message they would give to other businesses considering signing up to MTD for VAT. The messages they gave depended on their own experiences with MTD, and the record-keeping practices of the business considering signing up.

Participants would recommend MTD for VAT to a business already using software, or to those who were using spreadsheets but were digitally confident.

¹¹ Please note, HMRC are not be able to recommend specific commercial products to businesses.

¹² Free MTD software is available. The participants who mentioned the cost of software were not aware that free software exists.

‘If you’ve got robust digital records then absolutely do it. If you don’t have robust digital records, then a) get robust digital records and b) sign up! Otherwise it’s one of these things that in the near future people will say ‘I didn’t know I had to sign up’ or ‘I can’t do it’ and it’ll just be one big great mess. A cautious do it - depending if they’ve got good systems in place already.’

Turnover below £50k, typically pay VAT, software to bridging software

‘It’s hard to have one message as businesses have such different processes and different packages, but certainly if you’re a small business using [full software], then just go ahead. It’s easy peasy and it does make things better.’

Turnover below £50k, typically pay VAT, used software previously

They thought it made sense for new businesses to sign up for MTD for VAT (on full software) from the start, to avoid getting used to one system and then having to change it. Those who had fully understood and engaged with the idea of MTD emphasised the time-saving aspects of a fully digital approach.

‘I’d encourage anyone setting up a business to get started with MTD from the start, rather than wait and have to change later. You’d then have more time to familiarise yourself with MTD at the start, compared to once the business is up and running.’

Turnover below £50k, typically pay VAT, used software previously

‘I don’t know why anyone would do anything non-digitally when they could do it digitally. It just saves time, money, all sorts...’

Turnover below £50k, typically pay VAT, used software previously

However, participants that had experienced negative impacts as a result of moving to MTD for VAT were unlikely to recommend it to other businesses. They suggested delaying signing up for MTD until they had to and emphasised the time and cost that it took to become familiar with their new software.

‘[If businesses aren’t using software at the moment] don’t do it until you need to, because you’re clearly going to have to invest time and money into moving to MTD software to do this.’

Turnover £50-75k, paper/software previously now full software

‘If you’re already using the software then go for it because that’s what MTD is really about. If you’re like me and prefer spreadsheets then think carefully about it because it isn’t all that easy and you do have to pay.’

Turnover below £50k, spreadsheet to full software

4. Conclusions

The main reason businesses had for voluntarily signing up for MTD for VAT was that they thought they had to, or knew they would need to in the near future.

Confusion about information sought or received on MTD led some businesses to believing that all VAT registered businesses were required to sign-up straightaway so they did not believe they had a choice.

Businesses that were aware that sign-up was voluntary, assumed that they would be required to make the change within a year or two. These businesses either expected to reach the VAT threshold and be required to sign-up, or simply assumed that all VAT-registered business would be told to make the switch at some point in the next few years. For these businesses, signing-up voluntarily allowed them to transition on their own terms and in their own time, rather than doing so reactively.

Secondary reasons for voluntary sign-up were to improve efficiency, by removing a step in the process of submitting a VAT return and to improve compliance, hopefully reducing the risk of being subjected to a traditional compliance check.

Most businesses that took part in the research experienced a neutral impact as a result of signing up to MTD for VAT. This was because they were either new businesses who had signed up for MTD for VAT from the outset or because they had not changed their record keeping practices as a result of moving to MTD.

The full benefits of MTD for VAT were felt by businesses that invested in software with greater functionality and using it to its full potential to facilitate real-time record keeping. These businesses reported saving time on their record keeping and felt the benefit of being able to quickly and easily monitor their current financial and VAT position.

Businesses that reported negative experiences tended to be dissatisfied with their software package either due to low functionality or struggling to use the functionality available. Many of these businesses reported continuing to use their old record keeping systems alongside their new software, resulting in additional time spent on financial and tax management as well as a greater risk of errors.

Businesses readily recommended MTD for VAT to businesses that were likely to find the move to MTD straightforward, namely those who were already using software, or those who would find moving to software simple. Their reasons for recommending MTD for VAT to other businesses mirrored their own reasons for deciding to sign up – that they would need to do so eventually and signing up voluntarily afforded the opportunity to get used to the new systems in their own time.

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