BASICS ABOUT SALES TAX IN DYNAMICS 365

This document will show the basic logic of creation of tax transactions.

Chapter 1: Setup – what is required for Dynamics 365 in order to generate a Sales tax code?

You lost the overview of the setup?

How many Sales tax codes do we need? And when do we need them?

Chapter 2: The Sales tax code is generated => what is controlled by the Sales tax code?

Ledger posting group: these are the ledger accounts where the tax amounts are posted.

Sales tax percentage:

Tax authority:

Settlement period:

Mapping with country specific reports:

Chapter 3: Where should the Sales tax group be entered?

Chapter 4: Where should the Item sales tax group be entered?

How and where is the setup used?

What, if the ledger account used in the journal line has no Item sales tax group setup?

Chapter 5: special taxes – Use tax

How does Dynamics 365 know about Use tax?

Chapter 6: special taxes - posting of import turnover tax

Chapter 7: Sales tax direction

What is the impact of the sales tax direction?

How is the sales tax direction created?

Is it possible to change the sales tax direction manually?

Last hint:
Basic principles for generating a sales tax code respectively a sales tax transaction.

A **Sales tax code** will **only** be generated if **2 records** are available **for a transaction**:

1. **Sales tax group**
2. **Item sales tax group**

Criteria for the **Sales tax group**: this is information about the customer / vendor. Standard information: **WHERE** is this customer / vendor located.

Criteria for the **Item Sales tax group**: this is the information about the item. Standard information: **HOW** is this item taxable (full, reduced)

All following examples are shown with a regular sales tax percentage of 19 %, reduced sales tax percentage is 7 %

**Chapter 1: Setup – what is required for Dynamics 365 in order to generate a Sales tax code?**:

**Sales tax group**:

The following situations are normally relevant:

a) the customer / vendor is located in your own country

b) the customer / vendor is located in the European union

c) the customer / vendor is located somewhere else
**Item sales tax group:**

a) the item is **fully** taxable

b) the item is taxable with a **reduced** percentage

c) the item is **not taxable** at all (so normally we don’t need a sales tax transactions)

**Example:**

A) we sell a **notebook** to a **domestic** customer

The combination of Item sales tax group **FULL** and Sales tax group **AR-Dom** will generate a sales tax code.

B) we buy **food** from a **domestic vendor**

The combination of Item sales tax group **RED** and Sales tax group **AP-Dom** will generate a sales tax code.
You lost the overview of the setup?

Then go to Tax – Indirect taxes – Sales tax – Sales tax codes.
Select a sales tax code, click SALES TAX CODE

select Included in item sales tax groups
the relevant Item sales tax group is displayed

Repeat the same steps – now
click SALES TAX CODE

select Included in Sales tax groups
the related Sales tax group is displayed

= > The setup shows that the combination of Item sales tax group FULL and Sales tax group AR-DOM will pull the Sales tax code VAT19
How many Sales tax codes do we need? And when do we need them?

In principle it can be said: each time we have to report a certain sales tax – then you should create an own sales tax code for each kind of sales tax which has to printed on the sales tax report. Even if the sale or purchase is tax free it is very common that companies are obliged to report the base amount of tax free sales/purchases.

Chapter 2: The Sales tax code is generated => what is controlled by the Sales tax code?
**Ledger posting group:** these are the ledger accounts where the tax amounts are posted.

It is useful to setup one Ledger posting group for each Sales tax code with its own sales tax direction (more details about sales tax direction in chapter 7). This setup helps to avoid errors – especially when the ledger account fields are only filled for tax directions where a specific tax code is meant for. That ensures that the user will receive an error message in case the tax direction is incorrect.

**Required setup in Chart of accounts:** these ledger accounts need the field Posting set to 'Sales tax'

<table>
<thead>
<tr>
<th>A</th>
<th>B</th>
<th>C</th>
<th>D</th>
<th>E</th>
<th>F</th>
<th>G</th>
</tr>
</thead>
<tbody>
<tr>
<td>Ledger posting group</td>
<td>Description</td>
<td>Sales tax receivable</td>
<td>Use tax payable</td>
<td>Sales tax payable</td>
<td>Settlement account</td>
<td>Use tax expense</td>
</tr>
<tr>
<td>D19Pay</td>
<td>Domestic payable 19%</td>
<td></td>
<td></td>
<td>222200</td>
<td>222180</td>
<td></td>
</tr>
<tr>
<td>D19Rec</td>
<td>Domestic receivable 19%</td>
<td>130800</td>
<td></td>
<td></td>
<td>222180</td>
<td></td>
</tr>
<tr>
<td>D7Rec</td>
<td>Domestic receivable 7%</td>
<td>130805</td>
<td></td>
<td></td>
<td>222180</td>
<td></td>
</tr>
<tr>
<td>D7Pay</td>
<td>Domestic payable 7%</td>
<td></td>
<td></td>
<td>222207</td>
<td>222180</td>
<td></td>
</tr>
<tr>
<td>EU_P19</td>
<td>EU purchases 19%</td>
<td></td>
<td>222100</td>
<td></td>
<td>222180 130750</td>
<td></td>
</tr>
<tr>
<td>EU_P7</td>
<td>EU purchases 7%</td>
<td></td>
<td>130755</td>
<td>222180</td>
<td>222107</td>
<td></td>
</tr>
<tr>
<td>IMP</td>
<td>Import Tax</td>
<td>130810</td>
<td></td>
<td></td>
<td>222180</td>
<td></td>
</tr>
</tbody>
</table>
Sales tax percentage:

Go to Tax – Indirect taxes – Sales tax – Sales tax codes.

Select a sales tax code, use button Value – enter the percentage in the field Value.

Tax authority:

The tax authority setup is especially needed to define the country specific report (if available).

You should also enter the address (which is used when you start the monthly report). In this example the German report layout is selected.

Note: it is not mandatory to select a vendor account for the authority. If this field is left empty the settlement account in the Ledger posting group will be used as offset account for the sales tax payment voucher.
**Settlement period:**

We need a Settlement period to provide the information to Dynamics 365 how often and when sales tax has to be reported and paid. In this example monthly payment is setup.

### Sales tax settlement periods

<table>
<thead>
<tr>
<th>Settlement period</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>Mon</td>
<td>Monthly settlement</td>
</tr>
</tbody>
</table>

**General**

<table>
<thead>
<tr>
<th>Authority</th>
<th>Terms of payment</th>
<th>Period interval unit</th>
<th>Period interval duration</th>
</tr>
</thead>
<tbody>
<tr>
<td>TA</td>
<td></td>
<td>Months</td>
<td>1</td>
</tr>
</tbody>
</table>

On tab Period intervals you just have to enter the first period – use button Add. For further periods you can use the button New period interval.

### Period intervals

<table>
<thead>
<tr>
<th>From date</th>
<th>To date</th>
<th>Bi</th>
</tr>
</thead>
<tbody>
<tr>
<td>11/1/2017</td>
<td>11/30/2017</td>
<td></td>
</tr>
<tr>
<td>12/1/2017</td>
<td>12/31/2017</td>
<td></td>
</tr>
<tr>
<td>1/1/2018</td>
<td>1/31/2018</td>
<td></td>
</tr>
<tr>
<td>2/1/2018</td>
<td>2/28/2018</td>
<td></td>
</tr>
<tr>
<td>3/1/2018</td>
<td>3/31/2018</td>
<td></td>
</tr>
<tr>
<td>4/1/2018</td>
<td>4/30/2018</td>
<td></td>
</tr>
</tbody>
</table>
**Mapping with country specific reports:**

If a country specific report is available, you have to tell Dynamics 365 **where** the amounts have to be printed on the form respectively for which section of the transfer file the amount is related to. This is done by using **Reporting codes** (Tax – Setup – Sales tax – Sales tax reporting codes).

This is different in each country and related to the individual report layout. Here is an example.

The reporting codes are setup on the Sales tax codes, tab Report setup
Chapter 3: Where should the Sales tax group be entered?

a) on Customer accounts – tab Invoice and delivery

DE-011 : Northwind Traders

b) on Vendor accounts – tab Invoice and delivery

DE-001 : Opal Audio
c) on Ledger accounts – tab Legal entity overrides. Select the Legal entity and then the button Sales tax is enabled. This button opens the form where default values can be entered.
Chapter 4: *Where should the Item sales tax group be entered?*

a) on Ledger accounts – same as illustrated one page before: – tab Legal entity overrides. Select the Legal entity and then the button Sales tax is enabled. This button opens the form where default values can be entered.

b) on Released products (in Product information management – Products – Released products) – on tab Purchase – and on tab Sell

Now the setup is finished.
How and where is the setup used?

➔ when creating a new **sales order** the **Sales tax group** will be taken from the **customer** account,
the **Item sales tax group** is taken from the item number

➔ when creating a new **purchase order** the **Sales tax group** will be taken from the **vendor** account,
the **Item sales tax group** is taken from the item number

➔ when creating a new **journal line** the **Sales tax group** will be taken from the **customer or vendor** account,
the **Item sales tax group** is taken from **ledger account**.

➔ when creating a new **journal line** which consists of **ledger accounts only**:

  ➢ the **Sales tax group** will be taken from the **Main account**.
    If there is no setup on the Account it will be taken from the **Offset account**

  ➢ the **Item sales tax group** will be taken from the **Account**.
    If there is no setup on the Account it will be taken from the **Offset account**
What, if the ledger account used in the journal line has no Item sales tax group setup?

Then the Item sales tax group is defaulted in Journals from GL parameters, tab Sales tax, field Item sales tax group.
Chapter 5: *special taxes – Use tax*

Probably this kind of tax is named differently in individual countries – therefore a short explanation:

In general - this is a purchase tax. If the Use tax has to be applied in a purchase posting it has the following effect:

1. the tax amount is posted as a tax payable amount
2. the tax amount is posted again as a tax receivable amount

= > so the result is: 0,00.

The basic purpose of this procedure is to have the amounts in the tax report. These tax transactions provide the base amount (Amount origin), the tax receivable amount and the tax payable amount. They have to show up on the tax report on individual lines. This is normally applied if an EU company purchases goods from another EU company. But it can also occur in other tax situations in other countries.

Note: there are some countries using the same principle for domestic purchases and then name it ‘reverse charge’.

Note: when the company is not authorized to refund tax receivable (by setting up a value in the Tax code setup of Value – field % of Tax exempt) then the result will not be 0,00 (this is typically a hospital or a public sector company).

*How does Dynamics 365 know about Use tax?*

On the *Sales tax group* – when adding a new Sales tax code - activate the field Use-tax:
If this field is marked on the Sales tax group, the tax amounts are posted to the ledger accounts of the Ledger posting group in the columns Use tax expense and Use tax payable.

<table>
<thead>
<tr>
<th>Ledger posting group</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>EU_P19</td>
<td>EU purchases 19 %</td>
</tr>
</tbody>
</table>

**General**

<table>
<thead>
<tr>
<th>Sales tax payable</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>EU0</td>
<td>Intra-Comm. acquisition 0 %</td>
</tr>
<tr>
<td>EU19</td>
<td>Intra-Comm. acquisition 19 %</td>
</tr>
<tr>
<td>EU7</td>
<td>Intra-Comm. acquisition 7 %</td>
</tr>
</tbody>
</table>
Chapter 6: **special taxes - posting of import turnover tax**

The import tax has to be paid if goods are purchased from a vendor located in a non-EU country. This vendor who delivers the goods does not charge sales tax on the invoice.

Instead the import tax is claimed when the goods cross the boarder and are declared at the customs.

The import turnover tax will be invoiced either by the customs office – or in a typical scenario a truckage company was ordered to import the goods: then the truckage company issues an invoice including the tax amount (which is a tax receivable), which they paid for us in advance.

**What is particular in this situation?**

No base amount exists. We post the tax amount directly.

Vendor invoice journal

<table>
<thead>
<tr>
<th>Date</th>
<th>Voucher</th>
<th>Account type</th>
<th>Account</th>
<th>Account name</th>
<th>Invoice date</th>
<th>Invoice</th>
<th>Description</th>
<th>Debit</th>
<th>Credit</th>
<th>Currency</th>
<th>Offset account type</th>
<th>Offset account</th>
<th>Sales tax group</th>
<th>Item sales tax type</th>
</tr>
</thead>
<tbody>
<tr>
<td>5/7/2018</td>
<td>APIN000004</td>
<td>Vendor</td>
<td>DE-01001</td>
<td>Property Management</td>
<td>1805975</td>
<td></td>
<td></td>
<td>250.00</td>
<td>EUR</td>
<td>Ledger</td>
<td>130810-001-023</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

This is the only situation when the sales tax code is manually entered in the Vendor invoice journal on tab General.
In the invoice journal you see: invoice amount = tax amount

The tax amount has to be posted on the ledger account for Sales tax receivable of the Ledger posting group IMP

This Ledger posting group is assigned to Sales tax code IMP
Chapter 7: *Sales tax direction*

The sales tax direction is automatically created for each tax transaction:

**Posted sales tax**

<table>
<thead>
<tr>
<th>Voucher</th>
<th>Date</th>
<th>Source</th>
<th>Sales tax code</th>
<th>Sales tax direction</th>
<th>Transaction</th>
<th>Amount origin</th>
<th>Calculated sales tax amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>FIV-30000003</td>
<td>5/8/2018</td>
<td>Free text inv...</td>
<td>EUS</td>
<td>Tax-free sale</td>
<td>EUR</td>
<td>22,000.00</td>
<td>0.00</td>
</tr>
<tr>
<td>FIV-30000000</td>
<td>5/8/2018</td>
<td>Free text inv...</td>
<td>VAT19</td>
<td>Sales tax payable</td>
<td>EUR</td>
<td>1,500.00</td>
<td>250.00</td>
</tr>
<tr>
<td>APIN000024</td>
<td>5/7/2018</td>
<td>Voucher</td>
<td>IMP</td>
<td>Sales tax receivable</td>
<td>EUR</td>
<td>0.00</td>
<td>250.00</td>
</tr>
<tr>
<td>PIV-110000056</td>
<td>5/7/2018</td>
<td>Purchase or...</td>
<td>EU19</td>
<td>Use tax</td>
<td>EUR</td>
<td>480.16</td>
<td>91.23</td>
</tr>
<tr>
<td>APIN000021</td>
<td>5/7/2018</td>
<td>Voucher</td>
<td>EU19</td>
<td>Use tax</td>
<td>EUR</td>
<td>500.00</td>
<td>95.00</td>
</tr>
</tbody>
</table>

**What is the impact of the sales tax direction?**

a) it determines, which ledger accounts of the [Ledger posting group](#) are used for posting the tax amount
Sales tax direction *Sales tax receivable* will take the ledger account of the column Sales tax receivable
Sales tax direction *Sales tax payable* will take the ledger account of the column Sales tax payable
Sales tax direction *Use-tax* will take the ledger accounts of the columns Use-tax expense and Use-tax payable.

b) it determines, which Reporting codes are summed up and printed on the sales tax report.

Tax transactions with Sales tax direction *Sales tax payable* will be summed up for all Reporting codes setup on the Sales tax code in field group *Sales*.

Tax transactions with Sales tax direction *Sales tax receivable* will be summed up for all Reporting codes setup on the Sales tax code in field group *Purchase*.

Tax transactions with Sales tax direction *Use tax* will be summed up for all Reporting codes setup on the Sales tax code in field group *Import*.

The country-specific setup of the Reporting codes is too individual. Thus it is not explained within this document.
How is the sales tax direction created?

Note: the sales tax direction is NOT generated by the tax code

A) If there is customer account used in a voucher => it is sales tax payable

B) If there is vendor account used in a voucher => it is sales tax receivable (or use-tax)

C) If there are only ledger accounts used in a voucher (normally entered in a General journal) => ?????

In a General journal you enter an account and an offset account. The rule for creation of the sales tax direction is:

Dynamics 365 3.0 takes the setup of the account - the offset account is ignored

Steps how to setup a Sales tax direction on Main accounts:
In General ledger – Chart of accounts – Accounts – Main accounts: select the relevant account. In Tab Legal entity overrides add the company for which this value should be valid.
Then click Sales tax. On the right side of the screen you can now select the according value in field Sales tax direction.

![Sales tax settings in Dynamics 365](image)
It is useful to setup the Sales tax direction on all ledger accounts which are used in a certain way. F.e. if the ledger account is named „Office supply costs“ then it is recommended to set it to „Purchase“. If the ledger account is named „Revenue“ then it is recommended to set it to „Sale“. If the use of the ledger account is not unique, then leave the field empty.

Note: The field Sales tax direction on the ledger account will only be considered if a journal line consists of ledger accounts only!

What, if the ledger account has no information about sales tax direction?

If the field Sales tax direction of the account is empty the rule is:
- Debit posting = sales tax receivable
- Credit posting = sales tax payable
Is it possible to change the sales tax direction manually?

Yes, you can do that.

In exceptional cases it can be needed that a vendor transaction has to be posted with sales tax payable, or a customer transaction has to be posted with sales tax receivable.

In a general journal and in invoice journal it is possible to activate the field Sales tax direction on tab General:
Now the tax transaction of this vendor transaction is created based on the setup of ledger account 401300:

Sales tax transactions

<table>
<thead>
<tr>
<th>General</th>
<th>Amount</th>
<th>Adjustment</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sales tax code</td>
<td>Quantity</td>
<td>Amount origin</td>
</tr>
<tr>
<td>VAT19</td>
<td>0.00</td>
<td>2,000.00</td>
</tr>
</tbody>
</table>

The activation of the field Sales tax direction in a journal means:
ignore the customer/vendor account – just apply the Sales direction setup of the ledger account

**Last hint:**

Some explanations why the Ledger posting groups should be setup only with the relevant ledger accounts – and the other fields should be left empty.
With this trick you can avoid errors in creation of sales tax direction.

Example: If sales tax code VAT19 is used .......

<table>
<thead>
<tr>
<th>General</th>
<th>Amount</th>
<th>Adjustment</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sales tax code</td>
<td>Name</td>
<td>Percentage/Amount</td>
</tr>
<tr>
<td>VAT19</td>
<td>Value added tax 19 %</td>
<td>19.00000</td>
</tr>
</tbody>
</table>

in the related Ledger posting group setup nothing is selected in field Sales tax receivable. Because Tax code VAT19 meant for tax payable only.
If accidentally a transaction is created with the wrong sales tax direction 'Sales tax receivable' you can not post because ....

Then the user can check the actual transaction before posting ... avoiding a lot of reconciliation work afterwards.