

VAT

The Pitfalls of Cash Accounting

Businesses with a taxable turnover (excluding VAT) of <£1.35m can use Cash Accounting.

This means that VAT is only accounted for on Sales, when the cash is actually received.

This enables the business to have instant bad debt relief, as VAT is never paid over to HMCR until the money has been received.

VAT is never claimed on purchases until they have been paid for.

The system is simple, and if properly applied can be readily reconciled against the bank statement and petty cash book.

There are a number of key errors that can occur in accounts when being prepared.

Clients maybe tempted to claim VAT on purchase invoices that have not been paid within the quarter to reduce the VAT bill.

Purchases maybe counted twice in error, when a bill is put through early as above, and then counted again when the cash is paid.

Where sales are banked and mixed together with private money, it can become very hard to separate out taxable income. A debtors account is essential in these cases, and there should be a solid attempt to reconcile Sales invoices with banked receipts.

There are more details of Cash Accounting in Notice 731

<http://www.hmrc.gov.uk/home.htm>

Businesses and Corporations – VAT
Information and Guides
Special Schemes and Options
Cash Accounting

The threshold for cash accounting was raised in the 2007 budget, and applies for all periods after 1st April 2007. There was no change to the levels in 2010.