Can you join the VAT annual accounting club?

During a routine visit the Taxman suggested using the annual accounting scheme to reduce your VAT admin. This sounds like a good idea, but there can be further benefits to the scheme. How can you take advantage?

Why annual accounting?

As far as the Taxman is concerned, the point of the VAT annual accounting scheme (AAS) is to help businesses reduce admin by allowing them to submit a single return form covering a whole year rather than one for each quarter. That's helpful, but the AAS can also be used to improve, or at least smooth out, your cash flow.

Basic rules - fixed payments

Under the AAS you're required to make nine monthly payments equal to 10% of the VAT you paid in the previous year. If this isn't enough to cover your actual VAT liability for the year, a balancing payment must be made.

Tip 1. If your sales are on the up, the AAS will give you a cash flow advantage because you'll be paying VAT based on last year's lower turnover.
Note. Newly registered businesses don't have previous VAT records and so must estimate their turnover for the year ahead and pay 10% of this each month.

Tip 2. Instead, a new business can choose to pay 25% of the estimate each quarter, meaning you get to keep the VAT in your bank account a little longer.

Tip 3. If the interim payments appear too high, say because turnover is falling, you can agree a lower figure with the Taxman.

The scheme mechanics

Payments under the AAS don't start until the end of the fourth month of the scheme year (see below). Ten months later your annual VAT return is due and a month after that, the balancing payment. In other words, it's payable two months after the end of your VAT accounting year - another minor cash flow advantage. This might sound a fiddly process, but we can assure you it's easy to follow once you're using the scheme.

Tip. Where your trade is seasonal, choosing a year-end date for the AAS that's as far away from your high season as possible will give you another cash flow advantage.

Example. Acom Ltd's income is generated mainly in the summer. For 2011/12 its VAT bill was £200,000, of which £100,000 fell in the quarter ended August 31. Acom applies to join the AAS and chooses a start date of June 1 meaning its first AAS accounting year-end is May 31 2013. AAS payments began on September 30 2012 at £20,000 per month (i.e. 10% of its VAT bill for the previous twelve months). This is despite sales over the months of June to August 2012 generating VAT of £110,000. Compared to the VAT payable under the normal rules Acom has paid £90,000 less for this period.

Can you join the scheme?

You can apply to use the AAS by completing Form 600AA at any time, even from the point you first register (see **The next step**). However, HMRC will only approve this where you expect your VATable turnover for the next year to be no more than £1,350,000. Once in the AAS you don't have to leave until your actual VATable turnover for the preceding year was greater than £1,600,000.

The next step

For information on how to join the AAS, visit **http://tax.indicator.co.uk** (TX 13.03.07).

Annual accounting gives a cash flow advantage where your turnover is rising by allowing you to pay VAT in equal monthly instalments based on the previous year's turnover. The advantage is greater where your trade is seasonal. You can join if you project your turnover for the next year to be £1,350,000 or less.