

Cash accounting



**ASSIGN
BUSTER**

Cash accounting - Explaining its necessity and understanding when and how to go for it
TABLE OF CONTENTS
Defining Cash Accounting
Working of Cash Accounting

Understanding the Advantages and Disadvantages of Cash Accounting

Distinguishing Between Zero-Rated and Exempt Supplies

Defining Cash Accounting

Tax accounting is a special type of accounting system that is eligible to you, if you are a registered trader having a turnover that will not exceed 1, 350, 000 pounds in the next 1 year. Unlike general accounting systems that are based on the invoices issued and received, cash accounting enables you to account for and pay Value Added Tax (VAT) based on the cash received and paid. VAT is an indirect sales tax, that you need to pay on various taxable products and services during their stages of production and distribution, which are based on the value added at those stages.

Working of Cash Accounting

To use cash accounting, you need to apply for it; rather you should make all necessary VAT returns. You also have to satisfy the HM Revenue and Customs by clearing any VAT payment arrears to use the cash accounting scheme. When you start using the cash accounting scheme, it is must to use it for the whole business and it is desirable to continue it for a period of 2 years. However, you can quit the scheme at any moment, provided it does not contribute to your business as well as your accounting system does not support the necessary requirements for the scheme. While starting with cash accounting, you need to be very much careful that you do not re-account for any VAT on receipts and payments that are already dealt with.

In cash accounting the main accounting record is kept in a cash book

<https://assignbuster.com/cash-accounting/>

summarizing all the payments made and received. It has a separate column where you can specify the relevant VAT. In the cash book, you also need to record the corresponding tax invoices and provide an efficient system for cross referencing.

Understanding the Advantages and Disadvantages of Cash Accounting

The benefit of the cash accounting scheme primarily depends on the time period between the issuing of the sales invoice to receiving payments from the customers. Cash accounting is likely to be more beneficial when this time period extends. There is also no due on output tax for your business until the business receives the payment against the sales invoices, which in turn, helps in automatic bad debt relief. Cash accounting also simplifies the bookkeeping requirements where you can control many businesses with the help of an appropriate cash book.

However, there are disadvantages as well of this scheme. The primary disadvantage of cash accounting is that when you receive a tax invoice, you cannot take the credit for VAT. You need to wait for it until the payment is actually made.

Distinguishing Between Zero-Rated and Exempt Supplies

The zero-rated and exempt supplies are two types of supplies used in the cash accounting scheme where the rate at which VAT is charged is zero. However, the primary difference between them is that zero-rated supplies are taxable whereas exempt supplies are non-taxable. You can claim the input tax in respect of the goods or services that are used to make zero-rated supplies as a deduction, which you cannot do in case of exempt supplies. However, the difference between these two supplies is significant regarding registering for VAT. It is because, unlike exempt supplies, a person

making zero-rated supplies can go for a VAT registration.

Bibliography

1. " Zero-rated Supplies - VAT Information Leaflet No. 7."

2. " Cash Accounting Scheme."

http://www.rothman-pantall.co.uk/content/forums_vat/vatcas.html

3. " Economic & Commercial Concepts and Terms."