Chapter 5

The VAT Return and the VAT Control Account

In this chapter we will look at how VAT is accounted for and how it is reported to HMRC. We will see how normally VAT is reported to HMRC every three months. We will look at various alternative schemes of reporting VAT and how VAT is treated on imports and exports. We will also look at how the VAT on bad debts is recovered.

The main accounting record of any VAT registered business is the VAT control account. It is here where all the VAT from all the transactions is recorded. The balance on the account will show how much VAT is owed to or is due from HMRC.

VAT Control Account

We looked at the VAT account (also called the VAT control account as it is a summary of the VAT element of transactions a business makes) in the Basic Accounting I & II units at the Level 2 Certificate Level. You should already be aware of how to record VAT on sales, purchases and equipment. If you are not then it is recommended that you cover this in the Basic Accounting I & II book. This book is available from Premier Books.

You should know that the entries in the VAT account are:

Dr		VAT Account			Cr
Date	Details	£	Date	Details	£
VAT on Purchases			VAT on Sales		
VAT on the purchase of Fixed Assets			VAT charged on other income		
VAT on expenses			VAT on Purchase Returns		
VAT on Sales Returns					
VAT on relief for bad debts					

Remember that the figures are first recorded in books of prime entry (such as a Sales Day Book or a Purchases Day Book. See Basic Accounting I & II available from Premier Books):

- The VAT on purchases on credit will probably come from the purchases day book.
- The VAT on cash purchases will probably come from the cash book.

- The VAT on the purchase of a fixed asset will probably be made in a journal or a fixed asset register (see the Accounts Preparation units for fixed asset registers)

- The VAT on expenses will probably come from the purchases day book, the petty cash book or the cash book.
- The VAT on sales returns will probably come from the sales returns day book.
- The VAT relief on bad debts will probably be made in a journal (but see later in this chapter)
- The VAT on credit sales will probably come from the sales day book.
- The VAT on cash sales will probably come from the cash book.
- The VAT on other income will probably come from a journal.
- The VAT on purchase returns will probably come from the purchase returns day book.

Remember that HMRC can go back over six years when looking at VAT transactions, so all these books of prime entry should be kept for that length of time.

HMRC give an example of what should be in a control account which is not exactly the same, and is not strictly double entry. You may come across such a VAT Control Account.

Dr		**VAT Account**			Cr
Date	Details	£	Date	Details	£
VAT on Purchases			VAT on Sales		
(*less credit notes received)*			(*less credit notes issued)*		
VAT allowable on acquisitions			VAT due on acquisitions		
Net overclaim of input tax from previous returns			Net understatement of output tax on previous returns		
VAT on relief for bad debts			Adjustments for retail schemes		
TOTAL TAX DEDUCTIBLE			**TOTAL TAX PAYABLE**		
			Less **TOTAL TAX DEDUCTIBLE**		
			PAYABLE TO HMRC		

You should remember that this is only an example and as long as records are kept clearly then any layout is acceptable.

The layout here nets off the VAT on purchases and purchase returns as well as the net of sales and sales returns. This reflects the way it must be shown on the VAT return. Acquisitions are purchases from EU countries. We saw in the previous chapter how the VAT on acquisitions is treated, but you will see that an entry goes on both sides of the account.

Errors of less than £10,000 on a previous VAT return can be adjusted here. The £10,000 must be the net value of the error. The net value of the error is the difference between what was due to HMRC and what was reclaimed from them. If the net error is above this

£10,000 threshold but below £50,000 the error can still be corrected on the VAT form provided the amount of the error is less than 1% of the turnover (shown in box 6 of the VAT return).VAT errors above these thresholds must be reported to HMRC on the VAT form 652. If you make an adjustment for an error you may make a disclosure to HMRC of the circumstances of the error. If HMRC decide it was a genuine error and steps have been taken to correct this error in your accounts as well as on the VAT return then no penalty will be levied. If the error is careless or deliberate a penalty will be charged but you can ask for HMRC to consider a reduction of the penalty which would have been charged had you not disclosed the error.

We will see later in this chapter how relief for bad debts is applied. Adjustments are also made for certain retail schemes, but you will not be asked to calculate this. You will simply need to know that retail schemes are available.

EXAM ALERT!

You may have to create a VAT control account, and you may be asked to complete a VAT return (VAT 100) (see later in this chapter) from other business records. Students often make the mistake of including VAT on all cash book entries. Remember that under the standard scheme, VAT is only accounted for when the sale is made and not when it is paid for. For example if a credit customer pays his invoice which was raised several weeks ago then the sale was made several weeks ago and the VAT would be accounted for then. No more VAT is due just because the customer pays for it at another date.

Care is always needed when using the cash book to calculate the VAT to be reported to HMRC. A payment to or a receipt from HMRC is not reported again on the VAT form. This will be the balance to pay or the balance received from an earlier return. Remember that cash sales, cash purchases and payments made in cash for any expenses are the only cash book items which will require an input to the VAT account.