

A photograph of an older man with a full white beard and hair, wearing a white shirt, a dark bow tie, and a dark denim apron. He is smiling and looking down at a tablet computer he is holding in his hands. The background is a stone wall. The entire image has a semi-transparent magenta/pink overlay.

# What is Making Tax Digital? A guide for small businesses and the self-employed

by Sam Bromley

# Hello, we are Simply Business

one of the UK's largest business insurance providers. Since we started life in 2005, we've helped three million small businesses and self-employed people find the protection that's right for them, from builders to bakers and personal trainers (we cover landlords, too).

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Answer a few questions about your business and we'll show you quotes from a range of insurers. After you buy, our Northampton-based team will be with you through every step of your cover, whether you have questions about your policy or you need to make a claim.

Join over **600,000 customers** and get your tailored policy in minutes.

HMRC introduced the first phase of its new digital tax initiative, Making Tax Digital (MTD), on 1 April 2019. There are further deadlines for small businesses and the self-employed scheduled beyond 2020.

Here's what you need to know – from HMRC's Making Tax Digital guidance to what software you should use to comply.

## What is Making Tax Digital?

HMRC's Making Tax Digital plans involve getting small businesses and the self-employed to complete digital tax records and returns, with the eventual aim of going completely paperless.

HMRC says that MTD is how they're delivering on making it "easier for individuals and businesses to get their tax right and keep on top of their affairs."

HMRC already introduced the [personal tax account](#) in 2015, which is a digital tax account that aims to make it easier for people to manage their tax affairs.

Then came the first phase of MTD in 2019 – Making Tax Digital for VAT. This involves keeping digital records and using [accounting software](#) to complete VAT tax returns.

Eventually, keeping paper records won't meet the requirements of tax legislation.

## Making Tax Digital deadlines

HMRC is introducing Making Tax Digital gradually. Making Tax Digital for VAT started from **1 April 2019**, affecting VAT-registered businesses with a taxable turnover above the VAT threshold of £85,000.

Next all VAT-registered businesses will need to comply with Making Tax Digital for VAT from April 2022.

And from April 2023, Self Assessment taxpayers will need to comply with Making Tax Digital for Income Tax.

Here are the Making Tax Digital deadlines:

- **April 2019:** VAT-registered businesses with a taxable turnover above the VAT threshold of £85,000 need to keep digital records and submit digital VAT returns using compatible software. Some 'more complex' businesses were given a six-month deferral (read more below)
- **October 2019:** more complex businesses who were deferred need to comply with Making Tax Digital
- **April 2022:** MTD will be compulsory for businesses with a turnover below the £85,000 VAT threshold
- **April 2023:** MTD will apply to taxpayers who file Income Tax Self Assessments for business or property income of more than £10,000 a year

'More complex' businesses include trusts, 'not for profit' organisations that are not set up as a company, VAT divisions, VAT groups, those

public sector entities required to provide additional information on their VAT return (such as government departments and NHS Trusts), local authorities, public corporations, traders based overseas, those required to make payments on account and annual accounting scheme users.

## Making Tax Digital for business

At the moment Making Tax Digital only affects [VAT-registered businesses](#) – but eventually, all businesses will have to comply.

Here's how to register for Making Tax Digital, making sure you're complying with the right phases.

## Making Tax Digital for VAT

VAT-registered businesses with taxable turnover above the VAT registration threshold (£85,000 currently) now need to keep digital records and send digital VAT returns. For lots of businesses, this means from accounting periods starting on (or after) the 1 April 2019 Making Tax Digital deadline.

If your business has a taxable turnover below the VAT threshold, you can still sign up to Making Tax Digital voluntarily. HMRC encourages this, claiming the software will help you “better understand how your business is performing.”

In August 2020, the government announced that businesses below the VAT registration threshold would have to use Making Tax Digital starting in April 2022.

HMRC says the digital records you need to keep include:

- business name and contact details
- VAT number and details of any schemes used
- VAT on supplies made and received
- adjustments to returns
- time of supply (tax point)
- rate of VAT charged on supplies made
- reverse charge transactions (if your software doesn't record them, you need to record them twice as a supply made and a supply received)

- daily gross takings (DGT) if you use a retail scheme
- purchases of assets you can reclaim tax on if you use the Flat Rate Scheme
- value of sales made and total output tax on Gold Accounting Scheme purchases (if applicable)
- documents covering multiple supplies made or received on behalf of your business (by volunteers, third party businesses or employees)

You should use compatible software to submit your returns (see examples of compatible software below). This will pull information from your digital records, which need to be preserved for up to six years.

You can use spreadsheets to calculate or summarise VAT transactions and work out what information you need to send to HMRC. But ultimately you'll need to use compatible software to send that information. You might also need what HMRC calls 'bridging software', which converts your records to the right format before you submit.

## Making Tax Digital for sole traders

Making Tax Digital for Income Tax will launch properly in April 2023 for self-employed people and landlords who make over £10,000 annually.

So while it's not compulsory (yet), if you fill in a Self Assessment tax return, you can sign up [for a digital tax returns pilot scheme](#).

The pilot lets you keep records digitally and send [Income Tax](#) updates to HMRC instead of filing a Self Assessment tax return. The government estimates that so far, around 30 per cent of businesses and landlords have signed up voluntarily.

HMRC says it will lead to a more real-time system, which lets you see how much Income Tax you owe as you go. Signing up will also give you time to get used to the process before the 2023 deadline.

**Both sole traders with income from one business and landlords who rent out UK property (excluding furnished holiday lettings) can sign up.**

You'll need to use compatible software to keep records and send an income and expenses summary to HMRC every three months. You'll be able to see estimates of how much tax you'll owe.

At the end of the accounting year, you'll send a final report and your tax for the year will be calculated. This is the point at which you'll claim any allowances and reliefs.

## Making Tax Digital for Corporation Tax

There's not much information about when (and if) Making Tax Digital will be introduced for [Corporation Tax](#). HMRC is waiting to see how the full VAT rollout goes first before making any decisions.

## Making Tax Digital for landlords

If you make more than £10,000 a year from your rental properties, you will need to sign up for Making Tax Digital by April 2023.

At the moment, you can join the scheme voluntarily, should you wish to.

## Making Tax Digital software

Businesses will need to use compatible software to send digital tax returns. Your digital records don't all have to be on one piece of software, but HMRC says that you "must have links between the software you use by your first VAT period after 1 April 2021."

Some of the ways you can link software includes by **emailing records, linking cells in spreadsheets and downloading and uploading files.**

We have a guide to the [best accounting software for small business](#).

The product you use to submit digital tax returns needs to be compatible with the tax authority. [HMRC has a list of compatible software](#) – examples include Xero, Quickbooks, and Zoho.

Businesses that don't already use accounting software are likely to face one-off and ongoing costs. There are also likely to be costs when training staff to use the software and comply with Making Tax Digital.

While the government has estimated costs of £70 a year over four years for small businesses implementing Making Tax Digital, the Institute of Chartered Accountants in England and Wales puts it at £1,250.

[Read about how much Making Tax Digital is costing businesses.](#)

# Further reading

The self-employed guide to Self Assessment tax returns

[Click here for more >](#)

What can I claim as self-employed tax deductible expenses?

[Click here for more >](#)

HMRC reveal the worst tax return excuses and failed expense claims

[Click here for more >](#)

Is public liability insurance tax deductible?

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