



FREE GUIDE

Making Tax Digital: What Sole Traders Need to Know

A plain-English guide to the biggest change in self-assessment since it launched, and what you need to do about it.

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If you are a sole trader in the UK, there is a significant change coming to the way you report your income to HMRC. Making Tax Digital for Income Tax (MTD for Income Tax) requires certain self-employed individuals to keep digital records and submit quarterly updates to HMRC, rather than filing a single annual tax return.

This is the biggest structural change to self-assessment since it was introduced, and it affects how you record your income and expenses, what software you use and how often you report. If you currently file your own tax return once a year, this guide explains what is changing, what you need to do and how to prepare.

What is Making Tax Digital for Income Tax?

Making Tax Digital (MTD) is HMRC's programme to move the UK tax system onto a digital footing. MTD for VAT has been in place for several years, requiring VAT-registered businesses to keep digital records and file returns through compatible software. MTD for Income Tax extends that approach to self-employed individuals and landlords.

In practical terms, it means moving from one annual self-assessment return to a system of four quarterly updates, an end-of-period statement for each business and a final declaration that replaces the traditional tax return. The quarterly updates summarise your income and expenses for each three-month period, and the final declaration pulls everything together at year end.

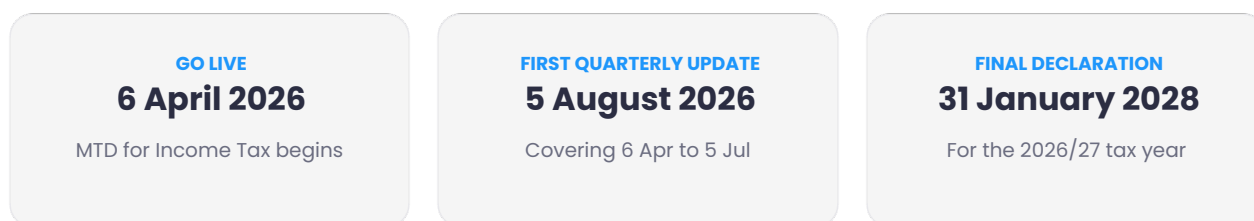
Does this apply to you?

MTD for Income Tax applies if you are a UK-resident individual with total qualifying income from self-employment and property above the MTD threshold. If that describes your situation, you will need to comply from the start of the relevant tax year.

It does not apply to limited companies (they continue to file corporation tax returns as normal). However, if you are a company director who also has self-employment or property income, the self-employed element may still fall within scope.

Not sure if you are in scope? Check your total self-employment and property income against the current threshold. HMRC has been writing to affected taxpayers, so you may already have received a letter confirming your status. If you are unsure, this is a good reason to speak to an accountant sooner rather than later.

Key dates



Quarterly update deadlines fall one month after each period end. So a quarter running from 6 April to 5 July would need to be submitted by 5 August. The end-of-period statement and final declaration are due by 31 January following the end of the tax year, which is the same deadline you are used to under self-assessment.

What changes in practice

Under the current system, most sole traders gather their records once a year (or hand them to an accountant in January) and file a single tax return. MTD replaces that with a more regular rhythm.

You will need to keep digital records of each transaction, including the date, amount and category. Those records must be held in MTD-compatible software, which could be a cloud accounting package like Xero, QuickBooks or FreeAgent, or a spreadsheet linked to HMRC through bridging software. You cannot simply type figures into the HMRC website as you might do now. Every quarter, your software will submit a summary of your income and expenses to HMRC.

This is not a tax calculation or a payment trigger. It is an update that gives both you and HMRC a clearer picture of where things stand throughout the year. At the end of the tax year, you finalise everything through an end-of-period statement and a final declaration, which is where capital allowances, adjustments and reliefs are applied.

Common misconceptions

It is just filing my tax return online

This is the most common misunderstanding. MTD for Income Tax is not a new way of filing the same return. It introduces quarterly digital updates and requires compatible software throughout the year. It is a structural change to how you report, not just a different front end.

I can carry on with spreadsheets

You can use spreadsheets, but only if they are linked to HMRC via bridging software that can send the data digitally. You cannot manually copy figures from a spreadsheet into the

HMRC website. For most sole traders, a cloud accounting package will be simpler and more reliable than a spreadsheet-plus-bridging setup.

My accountant will handle everything without me changing anything

Your accountant will still play a central role, but they will need timely, digital data from you throughout the year. The days of dropping off a carrier bag of receipts in January are over. You will need to keep your records up to date on a regular basis so that quarterly submissions can be made accurately and on time.

Quarterly updates mean quarterly tax payments

Not necessarily. The quarterly updates provide estimated figures to HMRC, but the actual tax liability is still calculated after year end through the final declaration. Payment dates have not changed. However, having a clearer picture of your profits each quarter can help you plan ahead for your tax bill, which is a positive side effect.

What this means for professional services sole traders

If you work as a consultant, coach, freelancer or in another professional services role, you are likely to have a mix of recurring invoices (retainers, project milestones, hourly billing) and regular business expenses (software subscriptions, professional memberships, travel, insurance). This type of income and expenditure pattern is well suited to cloud accounting software with bank feeds and digital invoicing.

Setting up your chart of accounts so that your expense categories map cleanly to the headings HMRC uses for quarterly updates will save time and reduce the risk of errors. If you are close to the VAT registration threshold, you will also want to make sure your MTD for Income Tax setup works alongside MTD for VAT, as both require digital records but cover different datasets. For contractors who work with a small number of clients, keeping clear digital records of your business activity (multiple clients, marketing costs, professional insurances) also supports any future conversations around IR35 status, where evidence of genuine business-to-business trading is important.

How to prepare



1 Confirm you are in scope. Check your total self-employment and property income against the MTD threshold. If HMRC has written to you, read the letter carefully. If you are unsure, ask your accountant.

- 2 Choose your software.** HMRC maintains a list of recognised MTD-compatible software. For most professional services sole traders, a cloud accounting package with invoicing, bank feeds and an expense app will be the most practical option. Your accountant may be able to provide software as part of a fixed-fee package.
- 3 Set up your records.** Create a chart of accounts that reflects how your business operates: income categories for different types of work, expense categories for software, travel, marketing, insurance and professional fees. The cleaner your setup now, the smoother your quarterly updates will be.
- 4 Connect your bank feed.** Linking your business bank account to your software means transactions flow in automatically. Reconcile regularly, ideally weekly or at least monthly, so your records stay current.
- 5 Replace paper processes.** If you are still using paper invoices, manual mileage logs or keeping receipts in a drawer, now is the time to switch to digital equivalents. Online invoicing, mileage apps and receipt-capture tools will make MTD compliance far easier.
- 6 Agree a timetable with your accountant.** Plan when each quarter will be closed, when you will share any missing information and when the submission will be made. A routine that works for both of you will prevent last-minute scrambles.

Penalties for getting it wrong

MTD for Income Tax sits alongside HMRC's points-based penalty regime. Each late quarterly update adds a penalty point, and once you reach the threshold, a financial penalty is applied. Late payment of tax also triggers interest and potential additional charges depending on how long the amount remains unpaid.

Persistent failure to keep proper digital records or to use compatible software could lead to compliance interventions and further penalties. The regime is designed to be proportionate (the occasional late submission will not be catastrophic), but consistent lateness will add up.

The positive side

MTD is often presented as a burden, but there are genuine benefits for sole traders who embrace it. Keeping your records up to date throughout the year gives you a much clearer picture of how your business is performing. You can see your profit position each quarter rather than waiting until January to find out what you owe. That clarity supports better decision-making, whether that is investing in your business, setting money aside for tax or

planning when to take on new work.

For professional services businesses in particular, the discipline of regular financial housekeeping often leads to tighter invoicing, faster payment collection and fewer surprises at year end.

Not sure where to start?

We help sole traders in professional services get MTD-ready with an all-inclusive package covering software, bookkeeping, quarterly returns and your annual declaration, from £62.50+VAT per month.

[Book a Free Discovery Call](#)

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