



Chartered
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The Chartered Tax Adviser Examination

November 2020

Domestic Indirect Taxation

Suggested Solutions

ANSWER 1

From: cfb@anytowntax.co.uk
To: fdaley@xocabs.co.uk
Date: 11 November 2020
Subject: VAT Visit

Dear Freda,

Thank you for your e-mail about the questions raised by HMRC.

Treatment of Drivers

Most mini-cab businesses operate with at least some self-employed drivers who make their supplies directly to passengers. Whether that is the case is a matter of fact and the lack of formal contracts with the non-employed drivers may be unhelpful. However, the facts that the employed drivers have employment contracts and are required to work specified shifts in return for a wage, while the other drivers are free to work when they please, can take on "private" work, do not receive payment from the company and do not have to report on fares collected, suggests that they are not employees.

Person supplied

Even if HMRC accept that the majority of your drivers are self-employed it is necessary to consider whether the self-employed drivers supply their services to the passengers, or to XO Cabs Ltd. In the latter case, XO Cabs Ltd would be required to account for VAT on the fares paid. You may have seen from your online forums that there have been a number of VAT cases on this area. In the case of *Hamiltax*, the tribunal held that the self-employed drivers supplied their services to the firm, who then made an onward supply to both cash and account customers. However, in the cases of *Triumph and Albany Car Service* and *Frederick George Carless* the firm was found to be acting as an agent for the drivers for both cash and account work, and the final supply to the passenger was therefore always made by the drivers.

The lack of a formal contract with the self-employed drivers may be unhelpful but the facts that the company does not receive any information about the fares charged, (which are kept by the drivers) and that the company charges booking fees, and for the use of taxi meters and radios suggest that the drivers supply their services directly to the passengers and not to the company. I would be cautiously optimistic that if we put these facts to HMRC, they will accept that, with the exception of the employed drivers, the drivers make their supplies to the passengers and not to XO Cabs Ltd.

For the future, I would recommend that the current, informal, arrangements with drivers who you consider to be self-employed should be put in writing.

Account Customers

Your invoices to account customers show that the sums collected by XO Cabs Ltd are received on behalf of the drivers named on the bills. However, the 5% "account charge" seems to be a payment for a supply that XO Cabs Ltd makes and HMRC is likely to take the view that you have underdeclared VAT on this income. Over the last four years, the underdeclaration would be under £700 but if HMRC are able to show that it was XO Cabs Ltd, who made the supplies of transport to the account customers, this would increase to just under £14,600. If HMRC take this point successfully, it may be possible to charge VAT to at least some of the account customers as they may be able to recover it. We will need to look at the account arrangements to see if this is a possibility and then negotiate a payment, and revised billing arrangements, with the account customers. Where account customers agree to meet additional charges for VAT, we will need to make VAT adjustments to reflect the increase in VAT.

Possible Penalty

If HMRC find that you have underdeclared VAT, they are likely to impose a misdeclaration penalty as well as collecting the underpaid VAT. As the errors were revealed as a result of HMRC's visit, any penalty is likely to be in the range of 15% to 30% of the tax, provided HMRC considers this error to be careless. No penalty will be charged if we can show that the errors were made despite the application of "reasonable care". There may be scope for suspending any penalty too.

Insurance

Typically, the supply of insurance is exempt from VAT, but when it is integrated with the supply of, say, a hired car, HMRC usually takes the view that there is a single supply of an insured car that is subject to standard rate VAT. Again, there has been a case on this (*Wheels Private Hire Ltd*) where it was confirmed that a separate charge for optional insurance of hired mini-cabs was not subject to VAT. As in your case, the insurance offered to drivers was as an “add on” and the charges covered the cost of the insurance paid and a small profit. The fact that XO Cabs Ltd offers insurance under its block policy for drivers’ own cars as well as those hired from it supports the proposition that the insurance is separate from the supply of hired cars. Consequently, I am of the view that it is an exempt supply. We should consider whether the exempt supplies of insurance might lead to a restriction in the recovery of VAT on overheads. The amount may however be small and therefore de minimis (which means that there will be no restriction of input tax).

Recovery of VAT on cars

Generally, the VAT on the purchase of cars is not recoverable, when they are available for private use. However, the VAT on taxis and mini cabs and cars offered for hire (on the condition that the cars not available for private use) can be reclaimed. As you have not reclaimed VAT on cars used in the private hire business and on those hired to drivers, you should now be able to make a claim to recover the VAT on those acquired in the last four years, provided that you have evidence of the VAT paid (essentially, the invoice issued by the supplier). Such a claim may reduce (or even eliminate) the potential under declarations and penalties mentioned above. You should note, however, that if you reclaim the VAT on these cars, you will have to charge VAT when you sell them. We should discuss the position if any cars bought in the last four years have been sold already. I suggest that we meet in the next few days to discuss the above.

Regards

Charles

MARKING GUIDE

TOPIC	MARKS
Treatment of Drivers	
Discussion of employment vs self –employment	1
Person supplied	
Discussion of “person supplied” by drivers and consequences of a finding that drivers supply XO Cabs Ltd (no need to mention case names for credit)	3
Advice on documenting position	1
Account Customers	
Consideration of treatment of account fares	1
Calculation of potential under declarations, basis for them and possible future adjustments	2
Discussion of penalties for misdeclarations including level of penalty	1
Discussion of “reasonable care” and penalty suspension	1
Insurance	
Consideration of charges for insurance	1
Single/multiple supplies and application to XO Cabs Ltd	3
I/T restriction if making exempt supplies of insurance	0.5
VAT recovery on cars	
Discussion of input VAT recovery on taxis and hire cars	1
Four year claim subject to evidence	1
Output tax on sales of qualifying cars	0.5
Offset of misdeclarations and cars input tax claims	1
PHS	2
TOTAL	20

ANSWER 2

Mr B Booth
Lizzellex plc,
Lizzellex Court,
Anytown,
XY7 6AB

Mereguild LLP,
Mereguild Tower,
Anytown,
XY1 4XX

11 November 2020

Dear Ben

Group restructuring

Thank you for your letter of 28 October 2020.

Disposal of Lizzellex (Car Parts) Ltd

The sale of the shares in Lizzellex (Car Parts) Ltd will be an exempt supply and may give rise to a restriction on the recovery of related input VAT. The VAT on the legal costs associated with the sales is likely to be irrecoverable and there may be some impact on the recovery of VAT on Lizzellex plc's overheads. A sale of the assets, rather than the company, should avoid this issue. We should discuss this further once the nature of the disposal is clearer.

A sale of shares will result in SD at ½% for the purchaser, so if the value of the shares were £1m (assuming the value of the company is predominantly made up with the value of the factory) then SD of £5,000 would be paid. Whereas a sale of the factory itself for £1m would result in SDLT of £39,500 for the purchaser. Additional tax costs to them might influence which route the purchaser wants to pursue.

Warehouse transfer

Normally, the transfer of a freehold property valued at £1.5 million, would be subject to SDLT of £64,500. However, Lizzellex (Car Parts) Ltd and Lizzellex (White Goods) Ltd are members of a stamp duty land tax group, as both are wholly owned by Lizzellex plc so stamp duty land tax group relief should be available for the transaction, meaning that no duty needs to be paid. It is still necessary however to report the intra-group transaction to HMRC and to claim group relief. The land transaction return should be submitted within 14 days of the transaction. The subsequent sale of Lizzellex (Car Parts) Ltd, the vendor in the transaction, will not affect the group relief as the property will remain in the ownership of the stamp duty land tax group.

For VAT purposes the transfer should be exempt from VAT as there is no indication that the property has been the subject of an option to tax, where VAT would have to be charged, – but this should be checked.

Input Tax Recovery

a) Viability Study

The recovery of input VAT on viability studies was considered by the Supreme Court in the case of *Airtours Holidays Transport Ltd* [2016] UKSC 21. The case concerned a viability study in relation to a refinancing and the Court found that the supply of the study was to the bank involved, and not to the company so it was not entitled to recover the VAT on the invoice. Whilst Big Bank plc received some elements of the report in confidence, other parts were for the benefit of Lizzellex plc and they were used by its board in formulating its future plans for the group. Consequently, it appears that the group has received and used recommendations from the report and the House of Lords decision in *Redrow Group plc* [1999] BVC 96 supports the proposition that Lizzellex plc should be able to recover the VAT on the viability study. Whilst I would be optimistic about securing a positive result, this is not a certain position and I would recommend that we discuss this with HMRC.

b) Acquisition Costs

As Lizzellex plc supplies management services to the companies that make up its group and intends to supply similar services to Metal Bashers Ltd following its acquisition, I would not expect any problems over the recovery of input VAT on the acquisition costs. In the case of *Ryanair Ltd* (Case C-249/17), the CJEU found that an intention to supply management services to an acquisition target was sufficient to justify the recovery of VAT on input costs. The cases of *Norseman Gold* [2016] BVC 504 and *African Consolidated Resources plc* [2014] TC 03705 suggest that VAT recovery may not be possible when there is no obligation to pay for the services or where, in practice, there is no payment for management services, so provided that Lizzellex plc continues to collect payment for its services, these cases support, rather than prejudice, input VAT recovery. The First-tier Tribunal decision in the case of *Tower Resources plc* [2019] UKFTT 0442 provides further support for this proposition.

Tax costs on Metal Bashers acquisition

The purchase of the shares in the company will be exempt from VAT so there will be no VAT to pay on them. However, the shares will be subject to Stamp Duty, which will be payable by Lizzellex (White Goods) Ltd. The duty on shares costing £10 million will be £50,000.

VAT Grouping Metal Bashers Ltd

Even though Metal Bashers Ltd will not be wholly owned, it is still eligible to be VAT grouped with the Lizzellex companies as all three companies will be under common control. VAT grouping all three companies may be administratively convenient as it would avoid the need for VAT accounting on transactions between them. One point to bear in mind here is that the companies would be jointly and severally liable for the VAT debts of the group. This may be a concern for the minority shareholders in Metal Bashers Ltd.

Yours sincerely

Tara Ashford

MARKING GUIDE

TOPIC	MARKS
Disposal of Lizzellex (Car Parts) Ltd	
Partial exemption issue as a result of share sales + opportunity to avoid if use TOGC	1
Warehouse transfer	
Recognition and calculation of potential SDLT liability	1
Availability of group relief and need to claim it	1
No SDLT group relief clawback when vendor sold	1
Exempt for VAT subject to OTT	1
Input Tax Recovery	
Viability Study	
Impact and facts of Airtours case (no need to mention the case name for credit)	1
Recognition that Lizzellex received something in return for its money and impact of Redrow case	1
Acknowledgement of technical uncertainty and recommendation to approach HMRC	1
Acquisition Costs	
Supply of management services validate Input Tax recovery	1
Formalise management services agreement re terms and due dates	0.5
Consideration of relevant caselaw including Ryanair, Norseman Gold and Tower Resources – credit given for other relevant cases	2
Tax costs on Metal Bashers Acquisition	
Share purchase exempt from VAT	0.5
Share purchase subject to Stamp Duty	0.5
Calculation of Duty and person liable	0.5
VAT Grouping Metal Bashers Ltd	
Recognition that the three companies satisfy the “Companies Act control” test	0.5
Recognition of possible issue with joint and several liability and minority shareholding	0.5
PHS	1
TOTAL	15

ANSWER 3

Briefing Note

Kuska Ltd (“Kuska”)

Kuska probably makes a mixture of taxable supplies and exempt sales and lettings of refurbished dwellings and any “unopted” commercial buildings. It is likely to be “partly exempt” and the VAT relating to the exempt activities will be irrecoverable.

We should consider which partial exemption method Kuska uses. There may be merit in using a special method, though we would have to get HMRC’s approval before using it.

Contractors working on the construction of new houses and new flats should not charge VAT on their supplies as the zero rate is in point.

The work related to:

- converting commercial property into a dwelling (or dwellings),
- renovating residential properties that have been empty for two years

is subject to VAT at the lower (5%) rate.

Any work renovating commercial property would be standard rated.

And of course, any contractor that is not registered for VAT will not be charging you VAT irrespective of the work they do.

Any VAT charged incorrectly would not be recoverable, so Kuska should monitor the VAT invoiced by contractors and ensure that the appropriate rate is charged.

The supply of domestic appliances, “white goods” etc. is standard rated even if they are supplied and installed in the course of the construction of a new dwelling or a qualifying conversion. Kuska should not reclaim input VAT charged on such goods when installed in dwellings.

It is likely to be advantageous for Kuska to opt to tax the commercial properties that it refurbishes as that will enable the recovery of VAT on the cost of the work, marketing costs, etc. The decision should be taken on a property by property basis as sometimes it is better not to opt.

The “construction services reverse charge” (to be introduced wef 1 March 2021) will apply to “specified services” - broadly speaking, building works (and related materials) reportable under the Construction Industry Scheme that are liable to VAT at the standard or reduced rates of VAT. Under the scheme, affected contractors will not account for the VAT shown on their invoices, but their customer has to account for it (and reclaim it as input tax if appropriate). The reverse charge does not apply to consumers and other “end users” (e.g. businesses that do not make onward supplies of the building and construction services in question). As Kuska will be using the building work it buys in in connection with its property letting or trading activities, it will be treated as an “end user” so it should not have to account for reverse charge VAT on the work it buys in. The onus will be on Kuska to satisfy its contractors that they should charge and account for VAT in the normal way by making a suitable written confirmation of its status.

Archie Potts

Provided that the lodge has not been used as a dwelling for at least 10 years, and is not used for business purposes, Archie should be able to file a claim under the “DIY builders” scheme to recover much of the VAT on the conversion of the lodge. If he does begin a business, Archie can use one room as an office without affecting his claim. Archie will need to complete HMRC’s form 431C and send it with the supporting invoices to HMRC within three months of practical completion of the dwelling.

The issue of a certificate of completion by the planning authority, or occupation and use of the property, will be evidence of its practical completion. HMRC may refuse late claims.

The VAT on:

- fitted furniture (other than kitchen cupboards),
- carpets and most electrical and gas appliances,
- the hire of equipment used during the build (e.g. scaffolding, etc.) and
- professional fees (e.g. architects' or surveyors' fees)

cannot be reclaimed. The VAT on specialist equipment for the indoor pool (e.g. diving boards) cannot be reclaimed but the VAT on materials used to construct the pool should be recoverable provided the pool is built into the existing building and not into a separate enclosure unattached to the house. More details of the items that qualify as "building materials" are in HMRC's Notice 708.

As this is a qualifying conversion, contractors should charge VAT at 5% on their work, and on the materials that they supply. This is important as HMRC will refuse to meet claims for VAT that has been wrongly charged at 20%. It would then be necessary to seek a refund from the contractor concerned, which may prove difficult in some cases. Monitoring the liability of the works as they take place and challenging any liability errors as they occur would be advisable.

MARKING GUIDE

TOPIC	MARKS
Kuska Ltd	
Recognition of the liability of Kuska's supplies	1
Possible partial exemption issues and methodologies	1
Discussion of liability of contractors' supplies and importance of rejecting incorrect VAT charges	1
VAT on "white goods" etc. not deductible	1
Opting to tax commercial properties on a building by building basis to secure input VAT recovery where that would be advantageous	1
Explanation of Construction Services reverse charge	1
Conclusion that it should not apply to Kuska as it is an end user	0.5
Archie Potts Self-Build Claim	
Converting a commercial property into residential can qualify for a DIY claim	1
Need for the lodge to be independent of any future shooting business carried on in the rest of the estate	1
Claim process and evidence – <i>Form number not required for mark</i>	1
Time limit for claim	0.5
Triggers for "practical completion"	1
Non-deductible items	1
Recognition that contractors working on the project should charge lower rate VAT on the work and materials used	1
Consequences of incorrect VAT charges and need to monitor as work progresses	1
PHS	1
TOTAL	15

ANSWER 4

From: Jim.May@dit.co.uk
To: Ruby.J.Lockhart@dedara.co.uk
Date: 11 November 2020
Subject: Intragroup charges

Dear Ruby,

Below is my analysis of the position with regards to the indemnity provided by Dedara Insurance.

Insurance contract

There is no definition of insurance in the UK's IPT legislation however the following indications of an insurance are listed in Notice IPT1:

- The existence of an insurable risk: the risk that commitments to Konyat cannot be fulfilled. **[0.5 mark]**
- The premiums due are calculated in relation to the claim value: the premiums are set in relation to the profits from the contract, which are proportional to the revenue. **[0.5 mark]**
- The conditions, which trigger the compensation are defined: assistance will be required when delays or quality issues arise. **[0.5 mark]**

Dedara UK and Dedara Italia have passed their risk of financial penalties resulting from their non-performance under the contract with Konyat to Dedara Insurance and the 25% fee represents the premium payable for this. **[0.5 mark]** The insurance contract was concluded through an enforceable agreement, whereby an offer was made and accepted with the consideration passing to Dedara Insurance. **[0.5 mark]**

IPT implications

Insurance contracts are subject to IPT based on the place where the insured risk is located, **[0.5 mark]** which for a legal entity is where the entity to which the risk relates is established. **[0.5 mark]** Assuming each company bears the loss relating to its own non-performance under the contract, then the premiums charged to Dedara Italia will be exempt from UK IPT but the premiums to Dedara UK will be subject to IPT. **[0.5 mark]** Dedara Insurance may need to account for IPT in Italy, subject to local requirements.

An IPT registration obligation arises when the intention to receive taxable premiums is crystallised and Dedara Insurance was required to register on 5 July 2019, when the group agreement to provide the insurance cover was made **[0.5 mark]** and its late registration should be notified to HMRC.

IPT becomes chargeable when the tax point arises, which is when the premiums are received by the insurer unless special accounting scheme is used. **[0.5 mark]** Under the special accounting scheme premiums recognised based on the projected profits instead of the cash payments received would result in the IPT being chargeable sooner **[0.5 mark]**. This would have cashflow implications for the Dedara group and increase the misdeclaration error and therefore it is not recommended **[0.5 mark]** Because Dedara Insurance has received the payments, despite not issuing any documentation to the insured parties, it was required to charge and account for the 12% standard rate of IPT on the value of the premiums received from Dedara UK. **[0.5 mark]**

IPT penalties

The late notification of the registration obligation will not trigger an additional penalty as there were no taxable premiums received during the period of delay and no tax liability arose. **[0.5 mark]**

Dedara Insurance has filed nil returns for the periods, in which IPT was chargeable. This constituted a misdeclaration error. **[0.5 mark]** This error cannot be corrected on the next IPT return as this method is restricted to errors of up to £10,000 or 1% of the net value of taxable premiums declared on the return, the error not exceeding £50,000. **[1 mark]** The premium equals the chargeable amount plus the IPT due and the resulting error is £25,714.29 ($(£80,000 * (12/112) * 3 * 12\%)$) **[0.5 mark]** and as

Dedara Insurance has no taxable premiums to report on its next return, the errors correctable in the return are capped at £10,000. **[0.5 mark]**

The underdeclaration errors must be disclosed to HMRC through the error correction procedure by way of letter and they may be subject to penalties **[0.5 mark]**. The penalty regime is behaviour based and, assuming HMRC accepts that the underdeclaration was not a result of a deliberate action, the maximum penalty which can arise is 30% of the IPT due (£8,640). **[0.5 mark]** This penalty may be mitigated if Dedara Insurance can demonstrate that it took reasonable care to get things right. On the face of it, given that nil returns were submitted, and there is no evidence of earlier advice being taken, there is possibly little evidence to suggest that there are grounds for mitigation, but this is an area that we should discuss further.**[1 mark]**

HMRC may also suspend the penalty for up to 2 years **[0.5 mark]** subject to certain conditions but the penalty would become payable if another penalty was to be assessed during the suspension period **[0.5 mark]**

In addition to the misdeclaration penalty, HMRC may charge 3% interest on the underdeclared IPT from the date it was due to the date it is paid **[0.5 mark]**, for this calculation the last date of the period is assumed to be 31 October 2020.

Premium received	31 Dec 2019	31 Mar 2020	30 Jun 2020	Total
	£	£	£	£
due date	31 Jan 2020	30 Apr 2020	31 Jul 2020	
premium	80,000	80,000	80,000	240,000
IPT due 12%	8,571.43	8,571.43	8,571.43	25,714.29

Up to 1 mark available for calculations

Please do not hesitate to contact me with any questions.

Kind regards

Jim May

Extra point:

You might have candidates talk about them being connected persons so we would need to check that the premiums are market value as HMRC can make directions for 'open market conditions'

MARKING GUIDE

TOPIC	MARKS
Insurance contract	
Insurance contract characteristics: insurable risk	0.5
Insurance contract characteristics: premium value	0.5
Insurance contract characteristics: conditions for assistance	0.5
Passing of risk from subsidiaries to Dedara & premium	0.5
Conclusion of an insurance contract	0.5
IPT implications	
Place of insurable risk	0.5
Place of risk where the entity who bears the loss is established	0.5
Taxable risk in the UK	0.5
Registration obligation & late notification	0.5
Special accounting scheme accelerates IPT	0.5
Special accounting scheme not beneficial	0.5
IPT tax point	0.5
IPT rate applicable	0.5
IPT penalties:	
Nil returns and misdeclaration error	0.5
IPT return correction limits	1
Value of misdeclaration	0.5
Return correction capped at £10,000	0.5
No penalty for late registration	0.5
Error correction process and penalty exposure	0.5
Maximum penalty applicable incl. value	0.5
Reasonable care mitigation	1
Suspension of penalty for up to 2 years	0.5
Suspension conditions violation	0.5
IPT penalty calculations:	
Interest accrual period	0.5
Premium due by period	1
Presentation and higher skills	1
TOTAL	15

ANSWER 5

Jonathan Zipper
25 Poplar Lane
Duffield
YO8 23BA

Jane Trivet
Nott & Coss LLP
Crown House
Chesterfield Road
Selby
YO8 1AA

11 November 2020

Dear Jonathan

Sale of Poplar Barn

Further to our recent meeting, I am writing with regard to the disposal of Poplar Barn.

As Poplar Barn has been opted to tax all supplies of it are subject to 20% VAT **[0.5 mark]**. Sparkfly's supplies of welfare services are subject to exemption under Schedule 9, Group 7 of VATA 1994 **[0.5 mark]** and the VAT charged by you on the sale would become a cost to them. **[0.5 mark]**.

Revocation of OTT

As you opted to tax in 1998 one solution to avoid a charge to VAT on the sale would be to revoke your option to tax. **[0.5 mark]**.

As you have held the option to tax for over 20 years **[0.5 mark]** the option can be revoked provided:

- No capital goods scheme adjustment is required by you **[0.5 mark]**.
As the property was purchased more than 10 years ago unless improvements have been made to it in the last 10 years it is unlikely that any CGT adjustments are needed **[0.5 mark]**
- Supplies of a relevant interest have been made at an open market value in the 10 years before the revocation **[0.5 mark]**
There is no information about the rental charged to the farmer, but I assume that an open market value was charged **[0.5 mark]**. The low value of rental charged for the roof lease may be questionable by HMRC but it seems that additional consideration is being received as per my analysis below **[0.5 mark]**
- No taxable supplies related to the building have been prepaid over a period more than 12 months after the revocation **[0.5 mark]**
The farmer has already terminated the lease and the roof lease accrues monthly so there does not appear to be any prepaid supplies invalidating this condition **[0.5 mark]**

HMRC's permission to revoke the option is not required provided the conditions are met. **[0.5 mark]**. You will need to submit Form 1614J to HMRC to inform them of your decision to revoke the option to tax. **[0.5 mark]**. However, if any of the conditions is not met you would need HMRC's permission to revoke the option, but it is unlikely this would be refused as you or anyone else are not going to receive a VAT benefit as a result of the revocation **[1 mark]**.

Roof lease to the electricity company

You appear to have been a barter transaction and you received an additional consideration for the lease of the roof by way of a discount on the price of electricity charged to you **[1 mark]**. Where a non-monetary consideration has been received it must be valued in reference to the subjective value assigned to it **[0.5 mark]**, the additional consideration you have received is £1,380 **[0.5 mark]**. The total consideration for the lease is therefore $8 \times £10 + £1,380 = £1,460$ **[0.5 mark]** with VAT of £243.33 ($£1,460 \times 1/6$) inclusive **[0.5 mark]**. You should make a correction to your VAT return if all errors in the period do not exceed £10,000 or 1% of box 6 figure (up to £50,000) **[1 mark]** otherwise you will need to disclose the error on form VAT652 **[0.5 mark]**.

Charitable use disapplication

Alternatively of you revoking the option as outlined above, the option may be disappplied on the sale if Sparkfly was to use Poplar Barn for charitable purposes per Schedule 10, para 7 of VATA 1994 **[0.5 mark]** and HMRC accepts that 5% of the intended use may not be for charitable purposes for this option to apply **[0.5 mark]**. If Sparkfly meet this condition, then they will need to confirm this to you but no certificate is required **[0.5 mark]**. If Sparkfly notify you to disapply the option, then you will have no choice but to treat the sale as exempt **[0.5 mark]**. It would be recommended that you obtain a written confirmation of the intended use from Sparkfly in case of a challenge from HMRC in the future **[0.5 mark]**.

VAT on Costs

The revocation of the option to tax allows you to make the sale as exempt **[0.5 mark]** and VAT incurred on purchases related to this sale would potentially be blocked from recovery **[0.5 mark]** unless it fits in the de-minimis rules **[0.5 mark]**. However, as you are soon to cease trading there should be minimal impact on your partial exemption position **[0.5 mark]** and we could mitigate this cost in the contract by obligating Sparkfly to compensate you by increasing the sale price **[0.5 mark]**.

Transfer of a going concern (TOGC)

There is a possible option to treat the sale as a TOGC and be outside the scope of VAT, if the lease of the roof was to be continued by Sparkfly and it opted Poplar Barn to tax **[0.5 mark]**. This option would place the responsibility of meeting the conditions on Sparkly, which would be outside of your control so it should not be the preferred choice **[0.5 mark]**. TOGC would allow you to avoid the financial penalty under the PPA and preserve your ability to reclaim input VAT on sale costs **[0.5 mark]** and I would be happy to discuss it in more detail if it would be of interest.

Please contact me if you would like to discuss this further.

Kind regards

Jane Trivet

MARKING GUIDE

TOPIC	MARKS
Supplies of Poplar Barn are taxable	0.5
Sparkfly provides exempt welfare services	0.5
Sparkfly not able to recover VAT	0.5
OTT revocation	
Able to disapply	0.5
20 years	0.5
Capital goods scheme	1
Roof lease at OMV	1
Prepaid taxable supplies	1
Disapplication permission from HMRC not required	0.5
Form 1614J to notify HMRC	0.5
Need HMRC permission if any condition not met	1
Roof lease	
Barter transaction	1
Subjective value of non-monetary consideration	0.5
Additional consideration is £1,380	0.5
Total consideration for the roof £1,460	0.5
VAT on total consideration £243.33	0.5
Error correction through VAT return	1
VAT652 disclosure	0.5
Charitable use disapplication	
Possibility of Sparkfly using the property for charitable purposes	0.5
5% of use can be non-charitable	0.5
Confirmation but no certificate required	0.5
If charitable use notified, then must exempt	0.5
Written confirmation of intended use advised	0.5
VAT on Costs	
Revocation or disapplication: exempt supply	0.5
Potential VAT block, unless de-minimis	0.5
Impact on partial exemption likely minimal	0.5
Compensation for irrecoverable price to be included in the price	0.5
TOGC	
Possible if lease to be continued and Poplar Barn opted to tax by Sparkfly	0.5
Risks related to TOGC	0.5
Benefits of TOGC	0.5
Presentation and higher skills	2
TOTAL	20

ANSWER 6

To: CCroak@Jonco.co.uk
From: Chase.Squire@dnt.co.uk
Date: 11 November 2020
Subject: VAT queries

Dear Carly,

Thank you for your email.

Product File Review

I address the liability queries below:

- Sausage rolls baked on premises and kept hot in a heated display cabinet are subject to VAT at the standard rate. They are intentionally kept warm, they are a takeaway food offered for sale hot and fall within VATA 1994, Sch 8, Group 1 Note 3(b) and Notice 709/1 **[1 mark]**

The resulting VAT under declarations are £393 in quarter to 31 July and £328 in quarter to 31 October. **[1 mark]**

- When a mixed supply of zero-rated (honey) and standard-rated (spoon) items is made, it is necessary to consider if there was one or two separate supplies. **[0.5 mark]** The individual honey jars sell for £3.50 with 25% mark-up, making the cost £2.80 each **[0.5 mark]**, the spoon cost £0.70, which was 11% of the total cost ($2 \times £2.80 + £0.70 = £6.30$). **[1 mark]** The linked supplies concession applies as the spoon cost no more than £1 and 20% of the cost of all items in the set and no separate price was charged for it and the set can be zero-rated. (Notice 700/7). **[1 mark]**

The errors for the last two quarters may be corrected in the current VAT return, if the net value of all errors does not exceed £10,000 or 1% of the Box 6 figure, up to a maximum of £50,000, **[1 mark]** otherwise they must be disclosed on form VAT 652 or by letter. **[0.5 mark]**

Calculations under the Direct Calculation Scheme 2 should be reviewed for all periods to 30 April 2020. If the liability of the purchases was incorrectly classified, the Estimated Selling Price and the stock records would have been incorrect, and this will have impacted the output tax declaration. **[1 mark]**

Mobile data cards

Mobile data cards are excluded from the domestic reverse charge provisions in SI 2010/2239. **[0.5 mark]** and should the transaction be found to involve MTIC, the provisions of the *Axel Kittel* (C-439/04) judgment would apply. HMRC may disallow the input tax if it can show that Jonco Stores Ltd ("Jonco") knew or should have known that the transaction was connected to fraud in the supply chain (e.g. if a participant in the chain has deliberately not accounted for output tax). **[0.5 mark]**

Under the Kittel principle, the taxpayer may be found that it should have known about it from the specific circumstances of the transaction. **[0.5 mark]** Such knowledge is attributed to the business, which includes its directors, senior employees and third parties **[0.5 mark]** and it can be inferred from the circumstances and any decisions based on them. **[0.5 mark]**

HMRC may regard the business as effectively a participant in the evasion, if the only reasonable explanation for the transaction was that it related to fraud. (Mobilx [2010] EWCA Civ 517) **[0.5 mark]**

The indicators of fraud include:

- Unsolicited approaches offering profit on high-value deals
- Deals offered carry no commercial risk
- Introduction of a seller and a buyer for the same quantity and specification of goods
- Preferential payment terms

- Small, newly established business offering goods cheaper than an established supplier
- Uncertainty regarding the existence of the goods or their condition

[1 mark] [0.5 mark per 3 valid indicators]

Before Jonco commits, it is advised to verify the integrity of the supply chain and request more information about the parties. If they are new to Jonco and it is not familiar with them, it should review their track record via market intelligence services or request trade references. **[0.5 mark]** Jonco should obtain copies of Certificates of Incorporation and VAT registration certificates and verify the VAT registration of the supplier through HMRC. **[0.5 marks]** To be able to fully assess the risk, Jonco also needs to understand where the cards are being supplied from and by whom and to verify that the goods exist and are legitimate. **[0.5 marks]**

In my opinion reasonable grounds to suspect fraudulent activity exist and Jonco should understand why it has been offered this deal by an unknown intermediary despite its lack of any experience in this market. Jonco should scrutinise if its participation is commercially reasonable. **[0.5 marks]**

It will be assumed that Jonco had reasonable grounds for suspicion if the price paid for the cards was lower than would be reasonably expected on an open market and Jonco should verify that the prices agreed for this transaction are realistic. As Jonco has no prior experience of similar transactions, my advice is to undertake market research and consult an expert experienced in the telecommunications market before proceeding. **[0.5 mark]**

Please do not hesitate to contact me with any questions.

Kind regards

Chase Squire

MARKING GUIDE

TOPIC	MARKS
Sausage rolls	
Sausage rolls liability	1
Sausage rolls liability error quantum	1
Honey sets	
Mixed supply consideration	0.5
Consideration and cost of jars	0.5
Cost of the spoon	1
Linked supplies concession	1
Errors	
Disclosure of errors to HMRC, corrections through VAT return	1
Disclosure of errors to HMRC: disclosure or letter	0.5
Impact of errors on past periods under Direct Calculation Scheme	1
MTIC	
Mobile data cards not subject to domestic reverse charge	0.5
Kittel applies if transaction found to be fraudulent, input disallowed	0.5
Kittel principle 'should have known'	0.5
'Should have known' from transaction circumstances	0.5
Knowledge attributed to the business	0.5
Participant in the evasion, 'the only reasonable explanation'	0.5
Indicators of fraud relevant to the scenario – 0.5 marks per 3 points	1
Advice to Jonco on checks to undertake	
Verify integrity of the supply chain	0.5
Verify goods are legitimate	0.5
Verify VRN and corporate registration	0.5
Verify reasons for being involved in the transaction	0.5
Verify prices are realistic	0.5
Presentation and higher skills	1
TOTAL	15