



The Chartered Tax Adviser Examination

May 2018

VAT on UK Domestic Transactions, IPT & SDLT

Suggested solutions

1. TOMMY BARNES

From: bjack@taxadv.co.uk
To: tbarnes@animalinvestmentgroup.co.uk
Date: 2 May 2018
Subject: Confidential - Project BigBulldog

Dear Tommy

Thanks for your e-mail.

VAT structuring

As costs will be incurred by Bidco456 Ltd it is important that it is registered for VAT so it can recover the VAT incurred on its costs.

It could be registered as a single entity VAT registration provided it makes taxable supplies. This could be achieved by providing a management service to subsidiaries but that would create a VAT cost in some of the recipient companies due to them being partially exempt.

Alternatively, if management services were only provided to BigBulldog Holdings Ltd then there would need to be an apportionment on costs recovered by Bidco456 Ltd on the basis of *Larentia + Minerva* (C-108/14) – see further detail below.

As a separate option, Bidco456 Ltd would be eligible to form a VAT group with BigBulldog Holdings Ltd and BigBulldog Ltd from the date it acquires the shares in BigBulldog Holdings Ltd and therefore satisfies the control criteria. BigPitbull Ltd could not be part of the VAT group as there is an insufficient shareholding to satisfy the control test.

The advantage of a VAT group is that it simplifies VAT compliance as only a single return is submitted and any intra-group supplies are disregarded. However, the favourable partial exemption special method and the formal ruling would no longer apply to the new group.

Bidco456 Ltd would still need to have economic substance and actively manage its subsidiaries to be able to permit VAT recovery - this could be achieved by providing a management service to subsidiaries, some of which would be intra-VAT group supplies and disregarded.

As there are two holding companies it may be advisable to consolidate the group structure in the future and have only one holding company actively managing the group.

I would suggest that you consider forming a VAT group between all eligible entities to simplify the VAT position and avoid VAT on future recharges to Big Bulldog Ltd; then look to agree a sectorised partial exemption method based on the recent favourable agreement and ruling albeit there is a small risk it could be refused.

Recent cases

Three of the most important cases in recent years are: *BAA Limited* [2013] England and Wales Court of Appeal Civ 112, *Airtours Holidays Transport Ltd v HMRC* [2016] UKSC 21 and *Larentia + Minerva* (C-108/14).

The BAA case held that there are two conditions in order to support recovery of VAT by holding companies. The costs must be incurred by a taxable person in the course of an economic activity and there must be a direct and immediate link between the costs and the taxable supplies made by that taxable person.

Relating to your scenario, it is critical that Bidco456 Ltd has an intention to make taxable supplies post completion and that it documents this intention. This could still be achieved with recharges through to Big Pitbull Ltd.

It is also important to ensure Bidco456 Ltd is registered from earliest available date. If any supplies are fully consumed prior to the date of registration, then it is not possible to recover VAT.

The Airtours case considered a company in financial distress seeking a loan. The lender requested that a report was prepared by an advisor on its behalf but that the fee was paid by the company. The case concerned whether the company was able to recover the VAT.

The case was specific to the particular facts but held that VAT was not recoverable by the company as the engagement letter was not addressed to the company and the reports prepared were for the sole use of the lender.

Relating to your scenario, it is crucial to consider who is the recipient of the supply for each cost incurred. Jimmy Bulldog will be the recipient of the personnel tax advice provided to him and therefore no VAT can be recovered by BigBulldog Holdings Ltd on those costs.

It is important to review each engagement letter and report in respect of the project to ensure that the addressees reflect the correct position and show Bidco456 Ltd and / or BigBulldog Holdings Ltd as appropriate.

Larentia + Minerva held that costs incurred by a holding company are only recoverable to the extent they relate to an active shareholding as opposed to a passive shareholding. An active shareholding being one where the holding company actively managed the subsidiary rather than a passive shareholding where it merely held shares in the subsidiary.

Relating to your scenario, it is important to consider whether the holding companies are actively or passively managing their subsidiaries and therefore whether any apportionment is required.

Please contact me if you have questions.

Kind regards

Barnaby

MARKING GUIDE

| TOPIC | MARKS |
|---|-----------|
| Post-completion structuring | |
| Bidco456 Ltd is only eligible to form a VAT group with the target from the date it acquires the shares in BigBulldog Holdings Ltd | 0.5 |
| BigPitbull Ltd not eligible to join the VAT group as does not satisfy control condition | 0.5 |
| Requirement to have economic substance (business activity) in a holding company in order to permit recovery | 1 |
| Favourable partial exemption special method and HMRC ruling are at risk if form a VAT group as single registration will be cancelled | 1 |
| Alternative would be register Bidco456 Ltd as a single entity but would need to be making taxable supplies to partially exempt subsidiaries | 1 |
| Providing a suggested recommendation with supporting commentary i.e. VAT group and aim to agree a sectorised partial exemption method in line with current agreement or single registration as partial exemption method clearly important but requirement for entity to actively manage group post completion creates a VAT cost. (Credit will be awarded for other supported recommendations). | 1 |
| Recent cases and impact on recovery | |
| Brief summary of BAA case - conditions of economic substance and direct and immediate link | 1 |
| Relate to question - importance of documenting intention at time of acquisition as well as managing administrative side of VAT registration application | 1 |
| Relate to question - whether any supplies have been fully consumed prior to acquisition and registration | 1 |
| Brief summary of Airtours case | 1 |
| Relate to question - importance of contractual position and who is the recipient of the supply in order to support recovery | 1 |
| Relate to question - recommend reviewing engagement letters and addressees on reports etc. | 1 |
| Importance of recent CJEU case in Larentia + Minerva in relation to actively managing subsidiaries post completion when compared with passive shareholdings | 1 |
| Relate to question - ensure that Bidco456 Ltd provides management services to all subsidiaries post completion or would need to apportion recovery based on active and passive shareholdings | 1 |
| Relate to question - need to assess position for Bidco456 Ltd and BigBulldog Holdings Ltd; in the future may be beneficial to consolidate the group structure and have one holding company | 1 |
| Presentational & Higher Skills | 1 |
| TOTAL | 15 |

2. IMRAAN

Client address

Our address

1 May 2018

Dear Imraan

Follow up to recent meeting regarding property transactions

Change of use

The initial lease of the building by HelpHousing Ltd would have been zero rated as it was used for charitable purposes.

The possible letting of two floors could potentially result in a change of use of the building and impact on the VAT position - it would depend on the use of the floors by the new tenant.

If the floors are let to a taxable business then there is a VAT charge calculated as if the part of the building being let had not been zero rated on the initial lease.

Had it not been zero-rated, the lease would have been subject to £200,000 of VAT.

The change of use only relates to 40% of the building due to the 2 out of 5 floors impacted - $40\% \times £200,000 = £80,000$ VAT. The change of use provisions cover a ten year period and only six years remain - $6/10 \times £80,000 = £48,000$ self-supply VAT charge.

If the property was opted by the HelpHousing Ltd then VAT would be due on the rental income and any premium, and the £48,000 self-supply charge VAT would be recoverable in full. It would however be necessary to consider the likely users of the property to assess whether or not it creates a cost to them.

An alternative would be to lease the two floors to a charity for charitable purposes and there would be no change of use resulting in no self-supply and no irrecoverable input tax as referred to above. The tenant would need to certify its charitable use.

HelpHousing Ltd would have exempt income relating to the ongoing rental income received from the charity and would need to assess its partial exemption position although costs directly related to the lease are not likely to be significant.

Project Phoenix - VAT

The purchase of the land could be subject to VAT or exempt from VAT depending on whether it has been opted to tax. However, VAT will be incurred in relation to construction of the building for example, on professional fees and the purchase of materials.

As DevCon Ltd is using in-house building services and the open market value of the services is over £100,000 per property a self-supply charge needs to be considered. However, as the works would have been zero rated if performed by a third party there is no self-supply charge levied.

The short term lease of the residential flats would be exempt from VAT and impact on the recoverability of VAT incurred on the construction. The de-minimis thresholds are unlikely to impact on recovery given the leases are likely to be for two or three years.

If the dwellings can be sold then the sale of a major interest (either the freehold or a lease exceeding 21 years) would be a zero-rated sale and enable full recovery on costs associated with building the dwellings.

Alternatively, if the properties cannot be sold then my advice would be to incorporate a new company and make a zero-rated sale to that connected party and then the connected party makes the short-term exempt leases. This enables full recovery of the costs incurred in building the dwellings as the costs

are directly attributable to a taxable supply. As the supplies would be between group companies there would be no SDLT as there is a specific group relief available.

This arrangement is specifically approved by HMRC and is not considered to be abusive planning.

Another alternative would be to set up another company to purchase the land and use DevCon Ltd for design and build services.

The services supplied by DevCon Ltd to the new company would be zero rated so no irrecoverable VAT for the new company. In addition, DevCon Ltd would be able to recover the VAT charged on the purchase of materials and professional fees on the basis it was attributable to a taxable supply.

Project Phoenix - SDLT

Base the calculation on the additional contingent consideration being received.

| | |
|---|----------------|
| Consideration = £1.3m + £0.6m + £0.3m = | £2.2m |
| SDLT = £100k x 2% + £1.95m x 5% = | £99,500 |

Project Sunrise - SDLT - Standard Calculation

Additional 3% applicable to companies purchasing dwellings.

| £1.0m sales price | | | |
|-------------------|------------|------|---------|
| | £ | Rate | SDLT |
| First | 125,000 | 3% | 3,750 |
| Next | 125,000 | 5% | 6,250 |
| Next | 675,000 | 8% | 54,000 |
| Next | 75,000 | 13% | 9,750 |
| | £1,000,000 | | £73,750 |

| £1.5m sales price | | | |
|-------------------|------------|------|----------|
| | £ | Rate | SDLT |
| First | 125,000 | 3% | 3,750 |
| Next | 125,000 | 5% | 6,250 |
| Next | 675,000 | 8% | 54,000 |
| Next | 575,000 | 13% | 74,750 |
| | £1,500,000 | | £138,750 |

Project Sunrise - SDLT - Multiple Dwelling Relief Calculation £1.0m sales price

| £1.0m / 5 = £200k | | | |
|-------------------|---------------------------|------|---------|
| | £ | Rate | SDLT |
| First | 125,000 | 3% | 3,750 |
| Next | 75,000 | 5% | 3,750 |
| | £200,000 | | £7,500 |
| | £7,500 x 5 | = | £37,500 |
| | Not less than 1% of £1.0m | = | £10,000 |
| | So the SDLT payable | = | £37,500 |

£1.5m sales price

| £1.5m / 5 = £300k | | | |
|-------------------|---------------------------|------|---------|
| | £ | Rate | SDLT |
| First | 125,000 | 3% | 3,750 |
| Next | 125,000 | 5% | 6,250 |
| Next | 50,000 | 8% | 4,000 |
| | | | |
| | £300,000 | | £14,000 |
| | | | |
| | £14,000 x 5 | = | £70,000 |
| | Not less than 1% of £1.5m | = | £15,000 |
| | So the SDLT payable | = | £70,000 |

As there are only five dwellings the rates cannot be treated as non-residential.

Conclusion

Taking multiple-dwelling relief into account, the difference in SDLT is £32,500 on spend of either £1.0m or £1.5m so is unlikely to be a determining factor for a prospective purchaser.

Let me know if you have any additional queries.

Yours sincerely

Tim Advisor

MARKING GUIDE

| TOPIC | MARKS |
|---|-----------|
| Capital goods scheme and change of use | |
| Initial lease of the building by the charity would have been zero rated as used for charitable purposes | 1 |
| Sub-letting the two floor would potentially result in a change of use of the building and impact on the VAT position | 1 |
| If sub-let to a taxable business then calculate the VAT charge as if the building had not been zero rated - so £200k VAT would have been payable | 1 |
| The change of use only relates to 40% of the building due to the 2 out of 5 floors impacted - $40\% \times £200k = £80k$ | 1 |
| The change of use provisions cover a ten year period and only six years remain - $6/10 \times £80k = £48k$ self-supply | 1 |
| If the property was opted then VAT would be due on the rental income and the £48k would be recoverable in full otherwise the £48k would be irrecoverable | 1 |
| Alternative lease to a charity for charitable purposes results in no change of use | 1 |
| The alternative would not result in a change of use so there would be no self-supply and no irrecoverable input tax | 1 |
| DevCon Ltd | |
| Concerns regarding short term lease being exempt and impact on recovery of costs such as building materials | 1 |
| Potential self supply of services due to in-house building services over £100k cost but the construction services would have been zero rated if procured from a third party so no self-supply is required | 1 |
| Advise make zero rated sale to connected person and then an onward lease to enable recovery of costs - HM Revenue Customs accept this is not abusive planning | 1 |
| Connected person would have exempt income and then a zero rated sale but unlikely to incur significant VATable costs so better approach | 1 |
| Alternative option would be to set up another company to purchase the land and use DevCon to construct the building | 1 |
| DevCon Ltd would be making a zero rated supply of construction supplies to the new company and so no irrecoverable VAT for the new company and full recovery for DevCon Ltd | 1 |
| Stamp Duty Land Tax | |
| Accurate computation of SDLT taking into account contingent consideration and correct rates | 1 |
| Accurate computation of SDLT applying multiple-dwellings relief and including uplift to 1% | 2 |
| Conclusion that SDLT difference is not significant enough to impact on the saleability of the property | 1 |
| Presentational & Higher Skills | 2 |
| TOTAL | 20 |

3. ALFRED BARLOW

From: Jude Duxbury <jduxbury@ablip.com>
To: Alfred Barlow <abarlow@ablip.com>
Date: 1 May 2018
Subject: Mellor Brook Mobiles Ltd

Dear Alfred,

Thanks for the notes you provided.

Insurance intermediary services

For the supplies to be exempt from VAT there needs to be a close enough connection with the exempt insurance contract.

The provision of administration services can be exempt if the services directly provide assistance in performance of the insurance contract. However, general administrative services, such as secretarial services, are taxable.

Commission earned in return for arranging an insurance contract is exempt from VAT.

Based on this analysis, the £10 fee is taxable and the £30 fee is exempt.

Accordingly, the figures included in the October 2017 and January 2018 working papers are incorrect and need amending to take account of the output tax that is payable in relation to the administrative services income.

As the contract is silent on VAT the price paid for the administrative services is considered to be inclusive of VAT and as such £1,667 and £1,141 is the output tax due in the October 2017 and January 2018 returns respectively.

There would also be a reduction in the amount of exempt income, meaning the input tax figures would also need recalculating.

As the contract only began in August 2017, the errors can be corrected within the two outstanding returns relating to October 2017 and January 2018.

These returns should either be signed by a director or if there are none available, marked as "submitted from the books and records of the company", as you were not appointed during those periods.

Quarter ended April 2018

Output tax

| Output | Amount (£) |
|---|--------------|
| Refunds to customers returning handsets | (211) |
| Sale of handsets | 1,116 |
| Administrative income | 233 |
| Rental income | 500 |
| Total | 1,638 |

Note - commission income is exempt from VAT and the compensation payment is outside the scope of VAT.

Input tax analysis

| Input | Amount (£) | Analysis |
|----------------------------------|-------------------|-------------------------|
| Rebate income from main supplier | (409) | Attribute fully taxable |
| Purchase of handsets | 2,148 | Attribute fully taxable |
| Rent of 1 Central Drive | 6,000 | Overhead |
| Sundry expenses - VATable | 2,154 | Overhead |

Partial exemption calculation

| Value of taxable supplies (excluding VAT) | Amount (£) |
|--|-------------------|
| Refunds to customers returning handsets | (1,055) |
| Sale of handsets | 5,580 |
| Administrative income | 1,167 |
| Rental income | 2,500 |
| Total | 8,192 |

| Value of exempt supplies | Amount (£) |
|---------------------------------|-------------------|
| Quarterly commission income | 4,200 |
| Total | 4,200 |

Taxable / Total = 8,192 / (8,192 + 4,200)

= 66.11%

Roundup to nearest whole number = **67%**

| Recoverable input tax | Amount (£) |
|---------------------------------------|-------------------|
| Rebate income from main supplier | (409) |
| Purchase of handsets | 2,148 |
| Residual overhead pot (67% x (8,154)) | 5,463 |
| Total | 7,202 |

Repayable **£5,564**

Sale of building

The 14 Turf Moor building cost over £250,000 (excluding VAT) so would be considered a capital item. VAT is recoverable in line with the expected use but subject to a ten year adjustment period.

The initial amount recovered would have been based on fully taxable income. However, an adjustment is required to reflect subsequent exempt use.

The adjustment is calculated by reference to months of use in each interval in the adjustment period and the extent to which the building is used to make exempt supplies. The intervals will be for the year to 30 April and the adjustment should be made in the September return.

If the property is sold, the remaining intervals will be considered to be fully taxable and therefore VAT is recoverable in full for the remainder of the adjustment period.

Shop leases

The lease on 1 Central Drive is over 20 years old. The landlord should be approached to see if it would be willing to disapply its option to tax thus making the rent exempt from VAT and reducing the amount of irrecoverable input tax.

No VAT will arise on the other leases as these have not been opted.

Deregistration

At the point there is an intention to no longer make taxable supplies there is an obligation to notify HMRC and deregister for VAT purposes. However, HMRC will usually agree to the retention of the registration for a short period after the cessation of taxable supplies to permit the orderly wind up of the business and recovery of related input tax.

There will be a deemed supply of any assets held on deregistration where input tax was recovered.

The easiest option would be to ensure all invoices are received prior to deregistration then the input tax can be recovered on the final return.

VAT incurred after deregistration can be recovered by making a claim on Form VAT 426. Goods must have been supplied prior to deregistration but services can be received pre or post deregistration.

Kind regards

Jude Duxbury

MARKING GUIDE

| TOPIC | MARKS |
|--|-----------|
| Insurance intermediary services | |
| Summary of insurance intermediary rules - basic administration / back-office services are taxable supplies | 1 |
| £10 fee is taxable and £30 fee is exempt - the contract states the values are inclusive of VAT (£1,667 and £1,141 output tax in the October 2017 and January 2018 return periods respectively) | 1 |
| The working papers for the October 2017 and January 2018 returns need amending to correct the liability error and the impact on partial exemption calculations for input tax recovery | 1 |
| The receiver should submit the two outstanding VAT returns and include corrections for the errors | 1 |
| The receiver should mark the returns as being submitted from the books / records of the company | 1 |
| April VAT return | |
| Computational element - calculation of output tax taking into account the split between income that is subject to VAT and income that is not subject to VAT | 1 |
| Computational element - calculation of input tax taking into account the expenses that are subject to VAT and income that is not subject to VAT, including the restriction on overhead costs and calculating the partial exemption percentage <i>[Note - it is acknowledged that it is not clear if the domestic reverse charge will apply to the handset purchase or whether each separate purchase is de minimis - credit will be given for either assumption].</i> | 3 |
| Property | |
| The building was over £250,000 so is a capital asset and VAT would have been recovered in line with the expected use | 0.5 |
| The expected use would have been fully taxable but the building has been put to an element of exempt use since August 2017 | 0.5 |
| Adjustment period is 10 years so if opted and sell the building need to charge VAT but all remaining periods considered fully taxable | 1 |
| Lease on 1 Central Drive was entered over 20 years ago so could approach the landlord to disallow their option and therefore reduce the level of irrecoverable VAT | 1 |
| Post deregistration | |
| Obligation to deregister from point no longer have an intention to make taxable supplies | 0.5 |
| VAT incurred by the company post deregistration cannot be included on the final VAT return and must be recovered through VAT Form 426 | 0.5 |
| Only recover input tax incurred on supplies of goods prior to cancellation of the registration but scope to recover input tax on some supplies of services received after cancellation | 1 |
| Presentational & Higher Skills | 1 |
| TOTAL | 15 |

4. BRIAN HARE

Our address

Client address

1 May 2018

Dear Brian,

Possible store acquisition – VAT issues

Thank you for your letter of 27 April.

It is probable that Sobaki and Kuski Ltd ("SK") will be able to acquire the business as a VAT-free "Transfer of a Going Concern" (TOGC). However, there are some complications arising from the transaction itself and the various options for the future of the business. I have set out the details below.

Conditions for TOGC Treatment

HM Revenue & Customs ("HMRC") consider that the key requirements for a business to be transferred to a new owner as a VAT-free TOGC are that: -

- 1) the assets are to be used by the purchaser to carry on the same kind of 'business' as the seller
- 2) where the seller is a taxable person, the purchaser must be a taxable person already or become one as the result of the transfer
- 3) where land would be standard rated if it were supplied, the purchaser must notify HMRC that it has opted to tax the land by the relevant date (usually the completion date), and must notify the seller that their option has not been disapplied by the same date
- 4) where only part of the 'business' is sold it must be capable of operating separately

One business or two?

The department store and internet operation carried on by Randals could be seen as separate businesses. The nature of the internet operation suggests that it is part of the wider department store business but it is possible that HMRC might challenge this, especially if it is closed down immediately on acquiring the business. If any value is attributable to the internet operation when you buy the business (and I would imagine that you would wish to avoid paying for something that will be wound up almost immediately), Randals (and HMRC) might consider that VAT should be charged on that element of the payment. Carrying on the internet operation for a time after the transfer should minimise the risk of a challenge and persuading Randals to wind up the internet operation before selling the business would avoid it altogether.

Assuming that any VAT charged by Randals was properly due, SK should be able to reclaim it as input tax (subject to the normal rules about having a VAT invoice). We should look closely at any suggestion that Randals wishes to charge VAT on any of the sale price as HMRC will not normally allow sums wrongly charged as VAT to be reclaimed as input tax and recovering wrongly charged VAT from Randals may not be a simple process.

Same kind of Business?

HMRC accept that the term "same kind of business" does not mean that the business operations before and after a transfer have to be identical. A change from a department store to a furniture store should not affect the VAT-free TOGC treatment of the purchase but a more radical change of use might do so (e.g. if the use of the building were to be changed from retail to offices).

Similarly, if the store was closed for a short period immediately following the transfer, that should not prejudice the TOGC treatment either (albeit a lengthy closure might do so). If you operate the store for a time (e.g. while arrangements for any closure and details of the work to be carried out are agreed), that should avoid these issues.

Option to tax

If Randals has opted to tax the property, it would be necessary for SK to do so too, and to provide a certificate to Randals to that effect, to avoid the need for VAT to be charged on the conveyance of the freehold (and the increased SDLT liability that would result from that). As SK will be using the building to make exempt supplies (of finance), any VAT on the conveyance of the property would be partly irrecoverable and hence would be a cost to SK in addition to the extra SDLT cost.

Concessions

A straightforward arrangement where designated space in the store is let to concessionaires who use it to sell their own stock, via separate tills, etc., should not be controversial. On the other hand, arrangements where the concessionaires claim to sell goods to Randals immediately before they are sold to customers in the store might be viewed by HMRC as a device to create an artificially VATable supply (of "selling services") in place of what otherwise might be seen as a VAT exempt supply of a licence to occupy space in the store (which might have implications for input VAT recovery). It would be advisable to look closely at the terms of the concessions as HMRC are usually concerned about "VAT leakage" in relation to any but the most straightforward of concession arrangements. .

You will doubtless be discussing with your lawyers the basis on which the concessions might be terminated, if you choose to do that.

Partial exemption

The new store, (whether retained as a department store or converted to a furniture store), is in the same line of business as the existing business of SK and so the existing partial exemption special method that SK agreed with HMRC recently is likely to continue to produce a "fair and reasonable" result. However, this should be verified once we have details of the expected trading pattern for the new store and we can then raise the issue with HMRC if need be.

Capital Goods Scheme

The refurbishment carried out by Randals a few years ago is probably a capital item. If so, following the TOGC, SK will be responsible for carrying out the remaining adjustments to the input VAT claimed when the work was done. It will be necessary to find out what the original VAT recovery was, when the refurbishment was taken into use, and to determine how many "adjustment intervals" have passed (including the one that will end on the date of the transfer) and hence how many of the 10 intervals remain for SK to deal with. Note that SK will need to calculate the adjustments on the basis of the anniversary of the TOGC, rather than after the end of the normal partial exemption year.

Yours sincerely

Andy Weir

MARKING GUIDE

| TOPIC | MARKS |
|--|-----------|
| Outline of TOGC requirements | 1 |
| Consideration of whether one business or two and consequences of a possible conclusion that the web business is separate, including risk that wrongly charged VAT would be irrecoverable | 2 |
| Whether change from department store to furniture retailer matters, including effect of short-term continuation of the department store business | 1 |
| Impact of closure of the web-based selling operation | 1 |
| Impact of closing the store for refurbishment | 2 |
| Options to tax - | |
| Explanation of option to tax and need to investigate whether transferor had opted - and opted effectively | 2 |
| Transferee option and certification to transferor if need be | 1 |
| Impact of failing to comply with the requirement to opt and certify if need be | 2 |
| Concessions – consider nature of agreements and risk of HMRC challenge to them | 1 |
| Partial Exemption - possible need to review partial exemption method following the acquisition | 1 |
| Capital Goods Scheme | |
| Takeover of adjustments for remaining intervals in CGS 10 year adjustment period | 1 |
| Need to find out amount of transferor's original input tax claim and when the refurbishment was taken into use to identify what intervals remain | 1 |
| Timing of adjustments following TOGC | 1 |
| Possible impact on price payable for the business | 1 |
| Presentation and higher skills | 2 |
| TOTAL | 20 |

5. WIDGET MANUFACTURING LTD

1 May 2018

Widget Manufacturing Limited ("Widget")
Briefing paper - Bad Debt Relief (BDR)

Current Regime

A claim for a refund of the VAT on an outstanding debt can be made if:

- The debt is over six months old (the six months "waiting time" runs from the later of the due date for payment and the tax point for the supply (usually the invoice date)).
- The debt has been written off in the refunds for bad debt account (this can be maintained outside the normal accounting systems).
- The claimant has already accounted for and paid the tax being reclaimed.
- For supplies of goods made before 19 March 1997 relief is only available where property has passed to the customer. This condition is met if the customer has sold the goods and the purchaser has acted in good faith.
- The value of the supply concerned cannot exceed the open market value.

Mechanics of claiming

A claim is made by including the relevant amount in box 4 of the VAT return covering the period in which all the conditions are satisfied.

If the mismatch between the bad debt relief time limit and the VAT return cycle would result in some claims going out of time before the VAT return is filed, a separate claim could be made.

HMRC require claimants to keep a copy of the VAT invoice (or an equivalent document) for 4 years from the date of the claim. This requirement will sometimes extend the normal 6-year retention requirement for VAT records.

Goods sold on credit

Where goods are sold on credit, two supplies are made – the goods and the associated VAT exempt supply of credit. If the buyer defaults, an adjustment is required to exclude the VAT exempt interest element from the claim, so it reflects only the goods element. This should correspond with the written down capital value in the company's records.

Also, as part of the consideration is on credit terms, BDR would not be available until 6 months after the due date for the relevant instalment.

Time Limit for Claims

BDR claims must be made within 4 years and six months of the due date for payment. As Widget has not been making claims, there would be some urgency to avoid potential claims going out of time.

The figures provided suggest that £127,275 of VAT should be reclaimable on the April 2018 VAT return as follows:

| Period | VAT Amount £ | Recoverable | Reason |
|-----------------|--------------|-------------|-----------------------------------|
| December 2017 | 12,350 | Not yet | Qualifying period not yet elapsed |
| November 2017 | 7,000 | Not yet | Qualifying period not yet elapsed |
| 17 Oct 2017 | 2,750 | Not yet | Qualifying period not yet elapsed |
| 1 Oct 2017 | 1,650 | 1,650 | |
| Jan – Sept 2017 | 17,800 | 17,800 | |
| Yr to Dec 2016 | 29,925 | 29,925 | |

| | | | |
|----------------------------|--------|------------------|-------------------------|
| Yr to Dec 2015 | 34,750 | 34,750 | |
| Yr to Dec 2014 | 36,250 | 36,250 | |
| Nov to Dec 2013 | 6,900 | 6,900 | |
| Oct 2013 | 4,250 | Possibly in part | Check dates of invoices |
| Jan to Sept 2013 | 24,450 | No | Out of Time |
| | | | |
| Total (pre further checks) | | £127,275 | |

If they remain unpaid, invoices issued in November 2017 and subsequently, will be eligible for BDR claims once 6 months and 21 days have elapsed since their issue. It would be advisable for Widget to establish a process for identifying potential future BDR claims, including in relation to any future defaults where credit has been allowed (where the qualifying period will run from the due date for the relevant payment(s)).

Retrospective Claims

Following the Court of Appeal's decisions in the cases of *British Telecommunications PLC [2014] EWCA Civ 433* and *GMAC (UK) PLC [2016] EWCA Civ 1015*, VAT on bad debts suffered between 1 April 1989 and 19 March 1997 can be reclaimed provided there exists satisfactory evidence that the bad debts occurred and that the VAT has not been reclaimed already. HMRC consider that the onus is on the claimant to establish that bad debts were incurred on supplies of goods made under retention of title terms, that no previous claim was made and that any amount claimed now is correct.

Assuming that Widget's turnover grew evenly from 1980 to 1997 and that the figure of 1% for bad debts is right, there could be something like £150,000 - £200,000 of BDR to be claimed if records exist to substantiate the claim. Experience suggests that the absence of records going back to 1989 will make it almost impossible to establish a claim, but it would be sensible to check. No claim is possible in relation to supplies made earlier than 1 April 1989.

Repayment of BDR

If a payment is received in relation to a debt on which BDR has been claimed, the relief claimed (or part of it if only a partial recovery is achieved) must be repaid. This is done by way of an adjustment on the VAT return for the period in which the payment was received.

MARKING GUIDE

| TOPIC | MARKS |
|---|-----------|
| The Current Bad Debt Relief Regime: | |
| Conditions for claiming including refunds for bad debts account | 2 |
| Mechanics of claiming | 2 |
| Goods sold on credit | 1 |
| | |
| Time limit for claims: | |
| Basics: Time for claiming runs from later of tax point and due date for payment; 21 days after invoice date in Widget's case and later in the case of credit sales | 1 |
| Assessment of quantum of Widget's "in time" claims, including reference to 2017 and 2018 amounts not yet eligible for claim and possible 2013 claims (especially credit sales that may still be in time | 3 |
| Mismatch between time limit expiry and VAT return on which a claim would ordinarily be made, and possible action to overcome it | 2 |
| Retrospective claims | |
| "In time" claim | 1 |
| Possible 1/4/89-19/3/97 claim, including estimate of quantum of potential claim and reference to BT and GMAC cases | 2 |
| | |
| Repayment of Bad Debt Relief | 1 |
| | |
| TOTAL | 15 |

6. ANYCOVER INSURANCE INC

To: cgrant@xotax.com
From: aclark@xotax.co.uk
Date: 1 May 2018
Subject: Anycover Insurance Inc - UK Insurance Premium Tax

Dear Charlotte,

Thank you for your email.

General

IPT applies to general insurance of risks located in the UK. Policies relating to risks located outside the UK are exempt. Long term insurance (e.g. life insurance) is exempted from IPT – so if Anycover Life expands its operations to include the UK, it is likely that its products will be exempt from IPT. If Anycover Life only sells exempt insurance contracts then it will have no liability to notify or indeed register for IPT.

Rates of IPT

Most taxable policies are subject to IPT at 12% but a 20% rate applies to most travel insurance (see below) and, among other things, to mechanical breakdown insurance (MBI) sold through car dealers.

Travel Insurance

Where the individual is the insured

The fact that travel insurance covers risks associated with travel outside the UK does not mean that the risk is outside the UK: the place of residence of the insured determines the place of the risk for such policies.

A short-term policy (one of up to 4 months duration) is treated as covering a UK risk if it is taken out by phone, internet or post by a person in the UK.

Where a longer-term policy (e.g. an annual policy covering travel risks over a full year) is written for an overseas resident person visiting the UK, the place of the risk is where the traveller is ordinarily resident (i.e. his home country) and the policy premium will not be subject to IPT even though insured events may happen in the UK.

A traveller who gives a UK address when taking out a policy will normally be treated as resident in the UK when he takes out a new policy, even if his habitual place of abode is overseas.

Where a business is the insured

Travel policies covering a UK employer against expenses incurred by employees travelling on business (where the employee cannot claim directly on the policy) are considered to be a form of employer liability cover and unlike "personal" travel insurance, such policies are chargeable with IPT at the standard (12%) rate of IPT. Such policies written for an employer established overseas would be exempt from UK IPT.

MBI

MBI taken out to cover the costs of car breakdowns when a UK registered vehicle is taken abroad is considered to be vehicle cover, rather than travel insurance and Anycover's policies would be generally subject to 12% IPT. If Anycover's policies were sold by or arranged through a motor dealer, however, they would be subject to the 20% rate of IPT.

If, in addition to the breakdown cover, the policies cover travel risks (e.g. loss of luggage), it will be necessary to apportion the premium between the standard and higher rated elements. The

apportionment must produce a fair and reasonable result - and HMRC might challenge it if it considers that it does not.

If Anycover's MBI is sold through brokers or agents affiliated with motor traders any policy that relates to a vehicle sold by the affiliated dealer, should be treated as higher rated. However, HMRC accept that if the "connected" transactions are not distinguishable from others that are not related to vehicles sold by the affiliated dealer, and the insurance is not provided as part of a systematic scheme to sell insurance to customers of a connected supplier of relevant goods or services, the premium will not be subject to the higher rate.

"Premium" for IPT purposes

The premium on which IPT is due includes "commission" paid to brokers.

Where Anycover collects payment of a premium by instalments, the service charge paid by policyholders should be included in the premium on which IPT is due.

If Anycover provides what is, in effect, a loan to pay the premium, under a separate contract governed by the Consumer Credit Act, the interest charges will not be subject to IPT. However, if Anycover simply charges an increased premium split into monthly instalments, the whole payment (including any uplift to reflect delayed receipt of the premium) will be subject to IPT.

Occasionally, the "premium" can include fees charged by a broker to the insured. If Anycover writes a "standard" MBI policy for an individual, and that individual also pays a fee to a broker as a condition of entering into the insurance contract, the broker should include its fee in the "premium" notified to Anycover for IPT purposes. If, for example, a broker requires a customer to pay a fee of, say, £10 in connection with a standard MBI policy available for a standard premium of, say £200, the broker should inform Anycover that the "premium for IPT purposes is £210.

Brokers that arrange travel insurance which is taxable at the higher rate will be required to register as Taxable Intermediaries and account for IPT on their fee charged to the policy holders. In this case, Anycover will not have to account for IPT on the fee as responsibility for accounting for it, is passed to the brokers.

Kind regards

Arthur Clarke

Other points to gain credit:

- *Notification of registration will be required now as the company intends to receive taxable insurance premiums*
- *A tax rep can be appointed*
- *There are penalties for late notification*
- *Returns will need to be made quarterly, the 'tax point' will need establishing (cash receipt/written premium method)*
- *Dealers that disclose a commission to the insured for MBI will be required to register as taxable intermediaries and account for HR IPT on their fee (same as for travel insurance above)*

MARKING GUIDE

| TOPIC | MARKS |
|--|-----------|
| General description of IPT and coverage | 1 |
| Rates of IPT and application of standard and higher rates | 1 |
| Travel Insurance | |
| Higher rating | 1 |
| Place of Risk | 1 |
| Treatment of short term policies | 1 |
| Treatment of long term/annual policies | 1 |
| Renewals while overseas policyholder is in UK | 1 |
| Treatment of "employer" policies | 1 |
| Breakdown Insurance | |
| Impact of involvement of motor dealers in sales of "travel type" breakdown insurance | 1 |
| Apportionment of premium if cover provided for "travel type" risks | 1 |
| Mechanical breakdown cover sold through affiliated brokers or agents | 1 |
| Premium for IPT Purposes | |
| Includes commission paid to brokers | 1 |
| Also includes administration charges and premium uplifts for payment by instalments unless the arrangement involves a loan - when interest is not subject to IPT | 1 |
| Can include amounts charged under linked contracts | 1 |
| Other valid points: registration, penalties, tax reps, accounting, tax points | 3 max |
| Presentation and higher skills | 1 |
| TOTAL | 15 |