

THE CHARTERED INSTITUTE OF TAXATION

APPLICATION AND PROFESSIONAL SKILLS

VAT and Other Indirect Taxes

November 2023

TIME ALLOWED

3 HOURS 30 MINUTES

- In order to secure a pass in this exam, you will be required to demonstrate competence in each of three skills.

You will be assessed across your answer as a whole for Structure. A pass or fail grade will be awarded.

You will be assessed for competence in a number of broad topics for the following skills:

- Identification and Application
- Relevant Advice and Substantiated Conclusions

For each topic for each of these two skills, a grade will be awarded. The grades for those topics will be weighted and averaged to produce a final grade for each skill of 0, 1, 2, 3 or 4. A grade of 3 or 4 is required to demonstrate competence.

- All workings should be shown and made to the nearest month and pound unless the question specifies otherwise.
- Candidates who answer any law elements in this paper in accordance with Scots law or Northern Ireland law should indicate this where relevant.
- Scots law candidates may provide answers referring to Land and Buildings Transaction Tax rather than Stamp Duty Land Tax.
- Unless otherwise indicated by the provision of additional information in the question, you may assume that 2022/23 legislation (including rates and allowances) continues to apply for 2023/24 and future years. Candidates answering by reference to more recently enacted legislation or tax cases will not be penalised.
- You must type your answer in the space on the screen as indicated by the Exam4 guidance.

You are a tax manager at Bacon & Swann LLP, a firm of Chartered Accountants based in Larketon. You have received a letter (**EXHIBIT A**) from Margaret Robinson, the Chair of the Board of Trustees of Larketon Festivals Ltd, which is a long-standing client of the firm.

Larketon Festivals Ltd is a local charity which runs cultural events in the town of Larketon. It has recently taken a long lease over Larketon Courthouse from the Ministry of Justice. Larketon Festivals Ltd has now instructed builders to carry out significant works to the Courthouse, funded principally by grant-making bodies.

The following exhibits are provided to assist you:

EXHIBIT A: Letter from Margaret Robinson

EXHIBIT B: Business Plan for Larketon Courthouse project

EXHIBIT C: Summary Building Plan prepared by Cranshire Construction Ltd, appointed Project Managers for the Larketon Courthouse project

EXHIBIT D: Pre-seen information

Requirement:

Prepare a report for the Board of Trustees, advising on the tax issues raised by Margaret's letter and recommending the best approach to the Courthouse project.

Continued

EXHIBIT A

Letter from Margaret Robinson

C T Adviser
Bacon & Swann LLP
17 High Street
Larketon
Cranshire
DR6 8YY

8 South Parade
Larketon
Cranshire
DR6 4LP

26 October 2023

Dear C T,

Larketon Festivals Ltd: Larketon Courthouse project – Request for Advice

Thank you for your time on the phone last week. As we discussed, I am now writing to you to set out the Board's discussions to date and the key areas of doubt.

Background

As you know, Larketon Festivals Ltd ("the Charity") is a registered UK charity which purchased a 999-year lease over Larketon Courthouse for £1 on 1 September 2023. This purchase was made under the Ministry of Justice's scheme to encourage the use of heritage buildings by charities for approved purposes.

The building project has secured funding of £1.5 million from a number of grant-making bodies. The two biggest are the Department of Culture and the UK Lottery Cultural Fund. Naturally, the grants impose certain restrictions on the use of the funds they provide.

I have enclosed a Business Plan (**EXHIBIT B**) which helps to illustrate the Charity's plans and the principal restrictions on its actions. The Business Plan also includes some forecast financial figures for the Charity over the next few years. You will also see that it is hoped that the Courthouse's various activities will generate considerable income. However, the expected cash balance by 30 September 2025 is very small.

Key issues

The Courthouse project is a significant one, as is clear from the report from the Project Manager enclosed (**EXHIBIT C**).

Works are due to begin in January 2024 and are expected to be completed in June 2024. It is hoped that the first events will take place in that month.

The Board wants a high standard of finish to the building works. From the Courthouse it then wants to provide generous outreach activities to local disadvantaged children. All of this will require money.

Accordingly, the Charity wants to ensure that it can optimise its tax position, particularly with regard to avoiding a VAT cost on the works to the Courthouse.

However, the Board is also aware that any tax planning will need to consider Corporation Tax on the income from the Courthouse. As property is involved, the Board has also asked if it needs to worry about Stamp Duty Land Tax.

However, the Board has insisted that any tax planning must be achieved ethically and in line with best practice for charitable trustees. Moreover, the Board has indicated that many of the trustees are uncomfortable with complex financial and tax matters. As a result they would prefer an effective approach which was both easy to understand and easy to carry out.

Continued

Continuation

Suggested Approaches

After discussions, the Board has identified two possible options going forward:

Option 1

Under Option 1, the Charity would simply build out the Courthouse project in its own name.

Option 2

Under Option 2, the Charity would set up a wholly-owned trading subsidiary. The intention would be for the trading subsidiary to operate the Courthouse site for the Charity in future, paying a market rent for its occupation.

Request for Advice

The Board would like you to consider both options and to advise in a report on which is the best approach for the Charity to take, considering the tax impact of each. Please also advise on any variations to improve the outcomes from the above options, which is in line with the ethical guidelines mentioned above.

I look forward to hearing from you. Please do not hesitate to let me know if you need any further information.

Yours sincerely

Margaret Robinson
Chair of the Board of Trustees, Larketon Festivals Ltd

Continued

EXHIBIT B

Business Plan for Larketon Courthouse project

Larketon Festivals Ltd is excited to begin the project at Larketon Courthouse. From the expected completion date of June 2024, all of Larketon Festivals Ltd's activities will take place in the Courthouse site, as opposed to being external events as previously. Whilst future external events are not ruled out, we expect the new site to allow a big expansion in our activities and so will concentrate on this for the present.

Our plans for the Courthouse site are as follows:

- 1) To build a bar and café complex selling to attendees at our performances. We also wish to operate the bar and café when performances are not taking place and we have applied for a liquor licence accordingly. The bar and café are intended to be open 300 days per year, on all those days when some activity is taking place at the Courthouse
- 2) To create a performance space inside the Courthouse for theatrical, musical and choreographic productions. Performances are expected to take place on 180 days per year.
- 3) To offer outreach and educational programmes to underprivileged local children for free. It is expected that these events will take place on 50 days per year.
- 4) To offer "foodie" events, with leading local chefs providing catering and displays of their culinary skills, to paying guests. It is expected that these events will take place on 50 days per year.
- 5) To offer an "open mic" facility to local performers in music, comedy and writing to allow them to perform. Entry to these events will be free, but the Board expects that we will earn money from related bar sales. These events are expected to take place on 20 days per year.

These activities reflect the charitable objects of Larketon Festivals Ltd, and also the expectations of our generous funding bodies.

We also note the following important restrictions on use of the Courthouse under the head lease:

Extract from Lease between Larketon Festivals Ltd ("Lessee") and the Ministry of Justice ("Lessor") in respect of 999-year lease over Larketon Courthouse

"Any use or occupation of the Property by any party other than the Lessee is strictly prohibited and will constitute a breach of the terms of this Lease. For the avoidance of doubt, this prohibition includes any licence, lease or other agreement made by the Lessee which would permit occupation by any other party, including a party connected with or controlled by the Lessee. However, in return for the payment of an Alteration Fee of £10,000 (plus VAT as applicable) and the submission of the relevant documentation, the Lessor will give its agreement to the occupation of the Property by a party which is wholly-controlled by the Lessee. Occupation by any other party may only be granted by the exceptional permission of the Lessor."

In addition to restrictions on the use of the Courthouse, two of our grant-funders have imposed specific conditions.

First, the grant of £800,000 from the Department of Culture explicitly states the funding can only be used as follows, and that no change to these restrictions is possible without the prior written permission of the Department of Culture:

- 1) Monies paid out under this Letter of Offer may only be received by the named recipient of the grant, that is, Larketon Festivals Ltd.
- 2) Monies paid out under this Letter of Offer may only be used by Larketon Festivals Ltd for capital expenditure. This capital expenditure must appear on Larketon Festivals Ltd's balance sheet.
- 3) Larketon Festivals Ltd may only apply funds for the benefit of another party where that party is a wholly-owned subsidiary or similarly connected entity.

Continued

- 4) Monies are paid on the assumption that VAT cannot be reclaimed by Larketon Festivals Ltd. If this is incorrect, then the Department must be informed of the extent of any VAT refund made by HMRC. The Department will then consider whether any grant monies must be repaid.

We are concerned that this might prevent us from benefiting from any VAT refund.

Secondly, the grant of £250,000 from UK Lottery Cultural Fund is less restricted. It makes it clear that the funding can be used where the following conditions are met:

- 1) Any connected body is a wholly-owned subsidiary under the control of the Board of Trustees of Larketon Festivals Ltd.
- 2) The expenditure in question is in support of the goals of the Business Plan prepared by the Board of Trustees for the project.
- 3) The expenditure supports the charitable objects of Larketon Festivals Ltd.
- 4) The other terms and conditions of this Letter of Offer are met in full.
- 5) Grant monies are agreed regardless of the recoverability of VAT in the hands of Larketon Festivals Ltd or any connected body.

The Board has also drawn up the following financial projections for the Courthouse. The Board is concerned that the cash balance as at 30 September 2025 is very low, and that it would seem to be difficult to sustain the outreach activities if there is an ongoing deficit on income and expenditure.

Financial Projections for y/e 30 September 2024 and y/e 30 September 2025

<u>Income Statement</u>	<u>y/e 30 September</u> <u>2024</u> £	<u>y/e 30 September</u> <u>2025</u> £
<u>Income</u>		
<u>Revenue Grants Received:</u>		
Department of Culture	20,000	20,000
UK Lottery Cultural Fund	10,000	10,000
Cranshire County Council	50,000	50,000
Maecenas Foundation	20,000	10,000
Private Donations	<u>5,000</u>	<u>5,000</u>
Total Grant Income:	105,000	95,000
<u>Income from Activities:</u>		
Ticket Sales	320,000	425,000
Foodie Event Sales	120,000	250,000
Café Sales	140,000	290,000
Bar Sales	<u>300,000</u>	<u>550,000</u>
Total Activities Income:	<u>880,000</u>	<u>1,515,000</u>
Total Income:	<u>£985,000</u>	<u>£1,610,000</u>
<u>Expenditure</u>		
<u>Courthouse Expenses:</u>		
Admin	55,000	60,000
Performance Staff	80,000	160,000
Bar and Café Staff	125,000	280,000
<u>Performance costs:</u>		
Performer fees	75,000	150,000
Overheads	100,000	220,000
<u>Bar and café costs:</u>		
Costs of sale	250,000	600,000
Overheads	15,000	35,000
Depreciation	<u>28,600</u>	<u>25,740</u>
Total Courthouse Expenditure:	728,600	1,530,740

Continued

Continuation

Outreach Expenditure:

Admin	40,000	45,000
Programme Resources	125,000	150,000
Other	<u>15,000</u>	<u>20,000</u>
Total Outreach Expenditure:	<u>180,000</u>	<u>215,000</u>
Total Expenditure:	<u>£908,600</u>	<u>£1,745,740</u>
Surplus/(Deficit):	<u>£76,400</u>	<u>(£135,740)</u>

Balance Sheet

As at 30 September
2024
£

As at 30 September
2025
£

Assets

Fixed Assets:

Courthouse Site	1	1
Courthouse Building	1,312,800	1,312,800
Fixtures & Fittings	248,400	223,560
Office Equipment	<u>9,000</u>	<u>8,100</u>
Total Fixed Assets:	1,570,201	1,544,461

Current Assets:

Stock (Bar & Café)	35,000	40,000
Debtors	8,000	9,000
Bank	121,000	28,000
Cash on Hand	<u>2,500</u>	<u>2,500</u>

Total Current Assets: 166,500 79,500

Total Assets: £1,736,701 £1,623,961

Liabilities

Long-term Liabilities:

Deferred Income – Capital Grants 1,500,000 1,500,000

Current Liabilities:

Trade Creditors	25,000	40,000
PAYE	10,000	10,000
VAT	25,000	30,000
Other Creditors	<u>5,000</u>	<u>8,000</u>

Total Current Liabilities: 65,000 88,000

Total Liabilities: £1,565,000 £1,588,000

Net Assets: £171,701 £35,961

Represented By:

Reserves £171,701 £35,961

Notes on Fixed Assets:

- 1) Figures are shown net of depreciation.
- 2) Depreciation is applied at 10% per annum reducing balance to fixtures and fittings and to office equipment.
- 3) The Courthouse building is not depreciated as it is a heritage asset.

Continued

EXHIBIT CSummary Building Plan prepared by Cranshire Construction Ltd, appointed Project Managers for the Larketon Courthouse projectLarketon Courthouse projectTotal Expenditure

£1.2 million plus VAT, to include labour and materials, and fixtures and fittings for the Courthouse building. Professional fees in addition.

All labour and materials to be sourced by Cranshire Construction Ltd.

Breakdown of expenditure set out below.

Scope of Work

- 1) Complete refurbishment of existing Courthouse building.
- 2) Conversion of existing Court Room 1 into Performance Space, to include stage, lighting, removable seating, fire exits and other amenities.
- 3) Conversion of existing Court Room 2 into changing rooms and support space for performances.
- 4) Conversion of existing Judge's Chambers into offices and other ancillary space for Larketon Festivals Ltd staff.
- 5) Extension to existing Courthouse building made up in part of the existing structure and part new-build works. This extension to include:
 - (a) Café Culture with seating for 100 people
 - (b) Bar with seating for 150 people
 - (c) Kitchen facilities
 - (d) Storage and fridge facilities
 - (e) WC and related facilities
 - (f) Staff room for bar and café staff

Expected Timelines

- 1) Finalisation of plans: November 2023
- 2) Finalising contracts with suppliers and subcontractors: December 2023
- 3) Works to begin: January 2024
- 4) Works to be completed: June 2024

Breakdown of Total Estimated Expenditure

<u>Category of Expenditure</u>	<u>Amounts (net of VAT)</u>
	£
<u>Construction works for Courthouse:</u>	
Labour	420,000
Building Materials	550,000
Fixtures & Fittings: Theatre Space	125,000
Fixtures & Fittings: Bar	75,000
Fixtures & Fittings: Café	30,000
Total Construction Costs:	1,200,000
<u>Professional fees:</u>	
Architects	100,000
Legal	12,000
Other	12,000
Total Expenditure:	£1,324,000
Plus VAT @ 20%	264,800
<u>Total Gross Expenditure</u>	<u>£1,588,800</u>

Continued

Continuation

Sources of Funding

<u>Source of Funding</u>	£
Department of Culture: capital grant	800,000
National Lottery Heritage Fund: capital grant	250,000
Cranshire County Council: capital grant	175,000
Maecenas Foundation: capital grant	100,000
Duchy of Cranshire Trust: capital grant	80,000
Friends of Cranshire Culture: capital grant	75,000
Private donations	<u>20,000</u>
Total Grants & Donations	1,500,000
Charity's own resources	<u>88,800</u>
Total Funding:	<u>£1,588,800</u>

Continued

EXHIBIT D

Pre-seen information

Client

Larketon Festivals Ltd, a registered charity

Legal status

Company limited by guarantee

Date of incorporation

31 May 1999

Year End

30 September

Company number

11399901

Administration Office and Registered Address:

8 South Parade
Larketon
Cranshire
DR6 4LP

Board of Trustees: Key Directors

Margaret Robinson – Chair of the Board of Trustees
A P Gabriel, OBE – Artistic Director
Dr R S Irvine – Education and Outreach Director
M K Sharma – Finance Director

Contact Name

Margaret Robinson, Chair of the Board of Trustees

Tel: 01233 456 7803

Email: margaret@robinsonsolicitors.co.uk

Principal Activities

Larketon Festivals Ltd operates cultural events in the small town of Larketon in the UK. Historically these events have been held outdoors and in the streets of Larketon. The highlight is the annual Festival, held in July each year.

Larketon Festivals Ltd is funded through a mixture of grant income and sales of tickets to its events. Its supplies for VAT purposes have historically fallen under the VAT cultural exemption.

Larketon Festivals Ltd's charitable objects include:

- 1) The promotion of cultural events in the town of Larketon and the county of Cranshire more widely.
- 2) Encouraging the development of artistic talent among local performers.
- 3) Enabling the personal development of local children, especially those from disadvantaged backgrounds.

Continued

Continuation

The Company's registered charity number is 1160844ZY and the Company's UTR: 99623 81422.

For Corporation Tax purposes HMRC have previously confirmed that all of the Company's supplies which fall under the VAT cultural exemption were "primary purpose trading" and therefore also exempt from Corporation Tax. The Corporation Tax exemption does not however extend to the sale of food or drink as this would not be regarded as "primary purpose trading", and so remains subject to taxation.

Larketon Festivals Ltd is not VAT-registered.

Unaudited Accounts y/e 30 September 2023

<u>Income Statement</u>	<u>y/e 30 September</u> <u>2022</u> £	<u>y/e 30 September</u> <u>2023</u> £
<u>Income</u>		
<u>Revenue Grants Received:</u>		
Cranshire County Council	45,000	50,000
Maecenas Foundation	20,000	20,000
Friends of Cranshire Culture	5,000	5,000
Private Donations	<u>6,000</u>	<u>5,000</u>
<u>Total Grant Income:</u>	76,000	80,000
<u>Income from Activities:</u>		
Ticket Sales	<u>118,000</u>	<u>115,000</u>
<u>Total Income:</u>	<u>£194,000</u>	<u>£195,000</u>
<u>Festival Expenditure</u>		
Admin	28,000	32,000
Performance costs:		
Performer fees	48,000	44,000
Overheads	<u>62,000</u>	<u>63,000</u>
<u>Total Festival Expenditure:</u>	138,000	139,000
<u>Outreach Expenditure:</u>		
Admin	8,000	10,000
Programme Resources	15,000	17,000
Depreciation	92	83
Other	<u>2,908</u>	<u>2,917</u>
<u>Total Outreach Expenditure:</u>	26,000	30,000
<u>Total Expenditure:</u>	<u>£164,000</u>	<u>£169,000</u>
<u>Surplus/(Deficit):</u>	<u>£30,000</u>	<u>£26,000</u>

Continued

Continuation

<u>Balance Sheet</u>	<u>As at 30 September</u> <u>2022</u> £	<u>As at 30 September</u> <u>2023</u> £
<u>Assets</u>		
<u>Fixed Assets:</u>		
Courthouse Site	0	1
Office Equipment	<u>830</u>	<u>750</u>
<u>Total Fixed Assets:</u>	830	751
<u>Current Assets:</u>		
Debtors	4,000	6,000
Bank	74,000	105,000
Cash on Hand	<u>500</u>	<u>500</u>
<u>Total Current Assets:</u>	78,500	111,500
<u>Total Assets:</u>	<u>£79,330</u>	<u>£112,251</u>
<u>Liabilities</u>		
Total Long-term Liabilities:	<u>0</u>	<u>0</u>
<u>Current Liabilities:</u>		
Trade Creditors	2,000	1,000
PAYE	1,500	2,000
Other Creditors	5,000	4,000
<u>Total Current Liabilities:</u>	<u>8,500</u>	<u>7,000</u>
<u>Net Assets:</u>	<u>£70,830</u>	<u>£105,251</u>
<u>Represented By:</u>		
Reserves	<u>£70,830</u>	<u>£105,251</u>