

The Chartered Tax Adviser Examination

May 2018

Application and Interaction Question 5 VAT and Other Indirect Taxes

Suggested solution

DRAFT REPORT TO THE EXECUTIVE COMMITTEE, DUNCHESTER RUGBY FOOTBALL CLUB

1. Scope of Review.

The scope of our review is set out in the Club's Secretary's letter of 23 April 2018 attached at Annex A. In accordance with your instructions and our letter of engagement, our conclusions and recommendations are set out here.

2. Executive Summary.

- 1) The sale of the Club's current site will be exempt from VAT. Although the Club will benefit by opting to tax the property, it should consider whether such an election is broadly in its best interests, given that the increased charge to Stamp Duty Land Tax ("SDLT") borne by DH is likely to exceed the VAT savings which accrue to the Club (see section 3).
- 2) The acquisition of the Club's new site will be exempt from SDLT (see section 4.1).
- 3) On balance, we consider that the construction of the clubhouse will be zero-rated (section 4.2). If we are incorrect in so concluding, subject to the application of the standard method over-ride, we consider that approximately 72% of the VAT incurred will be deductible (see section 5.3(3)).
- 4) The Club's current method of deducting VAT complies with statutory requirements and, on the basis of the information supplied by the Club, it will be appropriate for 2019/20. Our calculations suggest that the Club under-claimed VAT of £2,514 in 2016/17, and possibly in earlier years (see section 5.1(4)(b)).
- 5) The sale of the naming rights to Minato Holdings will not be chargeable to UK VAT. VAT on associated expenditure is deductible in full (see section 6).
- 6) The sponsorship income of £100,000 received from Douglas Homes Ltd ("DH") in 2015/16 and 2016/17 will be subject to a corporation tax charge of up to £19,000. We recommend that the Club notifies HM Revenue & Customs ("HMRC") immediately of this fact in order to mitigate the penalty arising on the late notification of the Club's chargeability to tax. The Club should also make a payment on account of £9,500 in respect of 2015/16 to halt interest (section 7.1).
- 7) We confirm the Secretary's conclusion that, with effect from 2019/20, income from bar and catering sales to non-members, along with income from the sale of the naming rights to Minato Holdings and the new sponsorship deal with DH fall outside the Club's charitable tax exemption. We suggest that these activities be undertaken by a newly incorporated trading subsidiary company ("Subco"), and it should donate its taxable profits to the Club by way of Gift Aid to shelter its profits chargeable to corporation tax (see section 7.2).
- 8) On the face of it, the sponsorship payments made by DH to the Club in 2015/16 and 2016/17 are not tax-deductible by DH in contrast to those to be made under the proposed contract (see section 7.3).
- 9) Our conclusions on the accounting treatment of payment for the naming rights and the RFU grant are set out in section 8.
- 10) In order to secure exemption from insurance premium tax ("IPT") on incapacity risks, we suggest that the Club's broker arranges a contract which exclusively covers this risk (see section 9).
- 11) Where a machine offers a choice of games, it is chargeable to machine games duty ("MGD") at the highest cost/largest cash prize (see section 10).

Our detailed conclusions are set out below.

3 Sale of current site

The sale of the site to DH will be exempt from VAT. If the Club opts to tax ("OTT") the site, the transaction will be standard rated thereby enabling the Club to reclaim VAT of £12,000 incurred on the planning and sale costs, plus insignificant VAT attributable to the Club's VAT exempt supplies in 2016/17. The OTT may also result in further recovery of input tax previously incurred where the site is subject to unexpired capital goods scheme intervals.
(VAT: 2 marks)

To make an OTT, the Club must notify HMRC within 30 days of its decision by completing online a form VAT1614A. Since the site has been used to make exempt supplies during the last ten years, the permission of HMRC is required but, in this case, it would be forthcoming automatically.
(VAT: 1 mark)

However, opting to tax will involve extra cost for DH. SDLT is chargeable on the VAT-inclusive consideration; thus, DH would suffer additional SDLT of £19,000.
(SDLT: 2 marks-1 mark for identifying consideration chargeable, 1 mark for computation)

Also, DH may suffer a cash flow disadvantage if there is a delay between completion and DH obtaining its VAT deduction on the basis that it will be making zero rated supplies of the new dwellings.

For these reasons, we consider that the Club need not OTT if, taking all relevant facts into account, its best interests is better served by not doing so, but instead it should seek adequate compensation for the loss of input tax from DH.
(VAT: 1 mark)

4 Acquisition of new facilities

4.1. Acquisition of new site - SDLT

The acquisition of the Club's new site will be exempt from SDLT given that it will be used in furtherance of the Club's charitable purposes.
(SDLT: 1 mark)

4.2 Construction of clubhouse - VAT reliefs

Zero-rating applies to:

- 1) Services supplied in the course of the construction of a building intended for use solely by a charity as "a village hall or similarly in providing social or recreational facilities for a local community". The fact that the building will be used substantially in furtherance of the Club's business activities (for VAT purposes, the provision of services to Club members constitutes a business activity) does not preclude zero rating under this heading, but it would do so under the heading which allows for zero-rating on the construction of a new building to be used by a charity mainly for non-business purposes.
(VAT: 1 mark)
- 2) A limited range of building services which meet the needs of disabled persons.

4.2.1 *Provision of social and recreational facilities similar to a village hall*

The following principles apply when considering the availability of zero-rating on the construction by a charity of a facility similar to a village hall to be used by the local community for social or recreational purposes:

- 1) Use by a charity solely "as a village hall or similarly". "Similarly" is not concerned with the physical characteristics of the building, but its function. Accordingly a clubhouse or pavilion may qualify where it is intended to meet the social and recreational needs of the local community. Although HMRC consider that a building designed for a particular sporting activity, for example, a cricket pavilion cannot be similar to a village hall because the club determines how the building is used, rather than the wider community, case law shows that priority of use, while significant, is not determinative.
- 2) What constitutes a local community is matter of fact.
- 3) While the management of the facility by a section of the community is not decisive, wider community representation may assist in securing zero-rating.
- 4) The local community must be the final consumer as recipient of the construction services in the sense that it uses the services for activities in which local persons participate directly.
- 5) The facilities may be used for either social or recreational activities (thus sports facilities are covered).
- 6) HMRC envisage that the facility should be hired out to the local community at a modest fee for use by a range of local clubs/groups and activities. Accordingly the building should - at the very least - include a large multi-purpose hall.

(VAT: 2 marks - ½ mark for each of the above principles, subject to maximum of 2 marks)

Since the legislation is directed at the intended use of the building at the time of construction and the onus is on the taxpayer to establish this, it is crucial that the Club documents the building's projected use by the local community. If, within ten years of its completion, the facility is no longer used for such purposes, a charge to VAT may ensue based upon the VAT relief secured.
(VAT: 1 mark)

Also, the relief is conditional upon the Club issuing the builder with a certificate in the form set out in Notice 708. The incorrect issue of a certificate may attract a penalty of 100% of the tax which would otherwise have been payable.
(VAT: 1 mark)

On balance we consider that the works qualify for zero-rating for the following reasons:

- 1) The clubhouse will be used for a wide range of sporting, recreational and social activities by diverse groups within the local community.
- 2) The Club's catchment area represents a local community.
- 3) The facility will be managed on a non-commercial basis. The Club is not concerned with profiting from its use by others; rather such use enables it to meet the public benefit requirement for registered charities. Furthermore, Club members cannot hire the facility at preferential rates.

- 4) The fact that the Executive Committee does not include members of the local community is not determinative, but co-opting onto it one or more persons whom represent local interests may strengthen the case for zero-rating.
- 5) The design of the clubhouse enables it to be used in a manner similar to a village hall.
- 6) Although there are factors (i.e. the facility will be constructed principally to meet the Club's requirements and its needs take priority) which militate against it being similar to a village hall, they are balanced by other factors (for example, all users will be accommodated and the period when the Club exercises priority is limited to the rugby season).
- 7) The predominant use of the clubhouse will be by persons other than the Club, with such use neither secondary nor ancillary to that of the Club.

(VAT: 3 marks-½ mark for each of the factors identified, subject to maximum of 3 marks)

In concluding that the works qualify for zero-rating we have drawn on our professional experience and judgment; however, it is for the contractor to assess whether the works may be zero-rated. We shall be happy to liaise with it on the matter to enable it to reach a conclusion.

The Club's responsibility goes no further than the issue of a certificate of qualifying use. On the facts presented to us, we consider that it is entitled to issue it on the basis of objective factors and - unlike the contractor - it is not required to assess whether the conditions for zero-rating are met.

(VAT: 1 mark)

Zero-rating does not extend to services supplied by professional consultants engaged by the Club. Some VAT savings could be achieved if the consultants were engaged by the contractor (existing contracts with the Club may have to be novated) and their services subsumed into the building services, for example, under a JCT Design & Build contract. Given that we have concluded that the Club may be able to reclaim 72% of VAT incurred on the facility (see 5.3 3), we do not consider that the potential VAT savings on the consultants' services are significant enough to warrant the Club forming a captive construction company to undertake the works.

(VAT: 2 marks - 1 for identifying scope to secure relief on professional fees and 1 for conclusion)

4.2.2 *Building services to meet the needs of disabled persons.*

If zero-rating does not apply to the construction of the clubhouse, construction of the disabled toilet will be zero-rated. However, the lift will not qualify as the building is neither a residence nor day centre for disabled persons.

(VAT: 2 marks - 1 mark for each discrete point)

5 Recovery of VAT on expenses

5.1 Current basis for recovery of VAT

We reviewed the basis under which the Club reclaimed VAT on its expenses in the year to 31 May 2017. In the absence of the written agreement of HMRC, the Club must operate the standard method.

(VAT: 1 mark)

The current methodology substantially reflects the terms of the standard method as set out in the regulations: firstly, the Club attributes VAT incurred

directly to its taxable and exempt income and secondly, VAT incurred on costs not directly attributable to its taxable or exempt supplies has been pro-rated by reference to the value of taxable supplies to the total value of all supplies made in the year to 31 May 2017.

(VAT: 1 mark)

We have the following observations on the calculations:

- 1) The recovery rate should be rounded up to the next whole number i.e. 77%.
(VAT: 1 mark)
- 2) In computing the recovery rate, the Club has included in the denominator exempt supplies of bank interest (£50), along with pitch (£800) and clubhouse (£1,500) lettings. Under the standard method, the values of incidental financial and real estate transactions are to be excluded from the pro-rata calculation.
(VAT: 1 mark)

We consider that these income streams are "incidental" because they are essentially passive in character, they require little of the Club's VAT-bearing resources and finally, their inclusion is possibly distortive. The effect of excluding them would be to increase the recovery rate to 78% (i.e. £148,200/190,200, rounded up to the nearest whole number).

(VAT: 1 mark)

- 3) Other than perhaps VAT of £1,500 incurred on rugby equipment, we consider that VAT of £3,000 incurred on players' kit and travel expenses, along with maintenance of the pitches, should be treated as residual input tax (and therefore partially recoverable), rather than exempt input tax (wholly irrecoverable) since there is a direct link between these costs and taxable supplies of admission charges, programme sales and the advertising services supplied to DH. The effect of this adjustment increases overhead input tax from £3,750 to £6,750 which falls to be apportioned by reference to the recovery rate.
(VAT: 2 marks)
- 4) The Club has treated members' subscriptions as exclusively exempt from VAT representing sporting services supplied by a non-profit making body to those participating in sport or physical recreation. While this treatment is acceptable, it could be argued that the VAT exempt services of the right to participate in rugby and the provision of insurance cover, along with the zero rated ("taxable") supply of "Swing Low" are independent supplies to be assessed by reference to their VAT status. If so, then subscription income should be apportioned between the identified supplies on any fair and fair basis.
(VAT: 1 mark)

Fortunately the Club does not have to rely upon an analysis of existing caselaw, but instead it may avail itself of the terms of extra-statutory concession ("ESC") 3.35 which permits non-profit making bodies which make a mix of supplies to their members to apportion subscription income (and hence its VAT liability) by reference to the benefits which accrue to members, disregarding a predominant benefit.

(VAT: 1 mark)

In 2016/17 the cost of members' benefits was £67,770, with the zero-rated supply representing 5.32%. Accordingly, under ESC 3.35, subscription income of £2,234 (£42,000 x 5.32 %) may be attributed to taxable supplies, with the balance (£39,766) representing the value of exempt supplies made to members. Although the apportionment has

been based on the relative costs of members' benefits, any alternative fair and reasonable basis may be adopted.
(VAT: 1 mark)

Given our findings:

- (a) Under ESC 3.35, the recovery rate for 2016/17 is 80% ($(£148,200 + 2,234) / 190,200$).
- (b) Taking account of the re-attribution of input tax referred to in paragraph 3, VAT recoverable on general overheads would be £5,400 ($£6,750 \times 80\%$), compared with £2,886 deducted by the Club, i.e. an additional credit of £2,514 is due to the Club.
(VAT: 2 marks)

We recommend that the Club reviews the annual adjustments made for the years 2013/14 to 2016/17 inclusive and, where appropriate, make an error correction notification to HMRC for under-claimed input tax. We shall, of course, be pleased to assist in formulating the disclosure.
(VAT: 1 mark)

5.2 Future basis for recovery of VAT

Having regard to the matters covered in the paragraph above and, if the Club's profitable non-primary purpose trading activities were conducted through Subco, we consider that the current methodology will meet the Club's requirements until the end of 2019/20, subject to the Club and Subco being VAT-grouped.

An application is required to form a VAT group. Once approved, the Club and Subco will be treated as a single entity for VAT purposes, with supplies between them disregarded, but they will be jointly and severally liable for the Group's VAT debts. The Group will be allocated a new VAT number, and it may continue to operate the standard method without formal approval from HMRC.

At the end of 2019/20 we recommend that Club review the suitability of the method in the light of current trading.

Although you have not asked us to comment on the matter, we consider that the RFU grant will be outside the scope of VAT given that the Club will not be providing a discernible service in return. Furthermore, given the grant is intended to underwrite non-VAT bearing employment costs, there is no basis for restricting input tax incurred by the Club.
(VAT: 2 marks)

5.3 Recovery of VAT on capital works

During 2018/19, the Club will incur VAT of £95,000 on the pitches, and perhaps up to £130,000 on the construction of the clubhouse (if zero-rating is not in point).

We consider that VAT incurred on both capital projects falls to be treated as non-attributable input tax, and accordingly is deductible provisionally by reference to the recovery rate for 2017/18.
(VAT: 1 mark)

Both projects will be subject to the operation of the capital goods scheme, with the credit for VAT incurred adjusted essentially over ten years to reflect the extent to which the assets are used to effect taxable supplies.
(VAT: 1 mark)

On the basis that the value of supplies arising in 2017/18 and 2018/19 will be similar to those for 2016/17, adjusted for the loss of £50,000 sponsorship income from DH and discounting the value of incidental supplies of £2,350 (income from the hire of the clubhouse and pitches and bank interest received), the value of taxable and exempt supplies will be £98,200 and 42,000 respectively. These figures must be adjusted to reflect the zero rated printed matter supplied to members. On that basis:

- 1) The recovery rate for 2017/18 will be 72%, calculated as follows:

	Total £	Standard/zero rated income £	Exempt income £
Adjusted value of supplies	140,200	98,200	42,000
Members' subscriptions reallocated (see below)		2,280	(2,280)
	<u>£140,200</u>	<u>£100,480</u>	<u>£39,720</u>

Subscription income allocated to taxable supplies to reflect the supply of zero rated printed matter, based on relative costs incurred in the year - 5.43% (£3,800/70,000) x £42,000 = £2,280

Projected recovery rate 2017/18 - 72% (£100,480/140,200).
(VAT: 2 marks)

- 2) The recovery rate for 2018/19 will be 72%, calculated as follows:

	Total £	Standard/zero rated income £	Exempt income £
Adjusted value of supplies	140,200	98,200	42,000
Members' subscriptions reallocated (see below)		2,171	(2,171)
	<u>£140,200</u>	<u>£100,371</u>	<u>£39,829</u>

Subscription income reallocated - 5.17% (£4,000/77,500).x £42,000 = £2,171

Projected recovery rate 2018/19 - 72% (£100,371/140,200).
(VAT: 2 marks)

- 3) On the basis of these calculations, 72% of the VAT incurred of £225,000 on these capital projects will be deductible (you should appreciate that if - as is likely to be the case - there is a variance in the recovery rates for 2017/18 and 2018/19, then it must be reflected in the Club's partial exemption annual adjustment for 2018/19).
(VAT: 1 mark)

- 4) When the annual adjustment is carried out for 2018/19, the Club must consider the application of the standard method "over-ride". It is intended to deal with situations where there is a "substantial difference" between VAT reclaimed under the standard method and any fair and reasonable alternative methodology which more closely reflects the extent to which the input tax will be used to effect taxable supplies. A difference is "substantial" if it exceeds £50,000.

You say that just 20% of the floor area of the clubhouse will be used to effect standard rated services. The difference between VAT deductible on that basis and the standard method would be £67,600 (£130,000 x 52% [72%-20%]), sufficient to trigger the override. However, your figure of 20% fails to take account of partial taxable use of the other parts of the building (for

example, the kitchen on the ground floor, the committee rooms hired out on match days, etc) - once the floor area of these parts has been weighted to reflect taxable use, it is highly unlikely that the override will apply.

At present we have insufficient information to conclude on whether the over-ride may be triggered in relation to the deduction under the standard method of input tax incurred on the pitches, and accordingly we recommend that the application of the over-ride be considered in depth in mid-2019.

(VAT: 2 marks)

6. Naming rights - VAT

Since the sale of the naming rights will be accompanied by other identified benefits, initially we must consider if the transaction for VAT purposes is a single composite supply or two or more independent supplies which are to be assessed independently. In making such an assessment, we must have regard to all the circumstances in which the transaction takes place. The transaction's essential features must be considered from the perspective of a typical customer and, in particular, a single supply arises where one or more its elements constitute the principal service, with the other ancillary elements sharing the tax treatment of the principal service. A service is ancillary to a principal service if it does not constitute from the customer's point of view an aim in itself, but a means of better enjoying the principal service.

(VAT: 2 marks)

Having regard to these principles, we consider that the sale of the naming rights is, from the typical customer's perspective, the principal service (one of advertising), with the other services ancillary thereto.

(VAT: 1 mark)

The naming rights are chargeable to UK VAT if they are treated as made in the UK. The general rule is that services supplied to a business customer are made in the UK if the customer is established here.

(VAT: 1 mark)

It is necessary, therefore, to identify the recipient of the supply and where it is established. The contract is made with Minato Holdings ("Holdings") and the invoice is to be addressed to it. The facts point to the naming rights being used by Holdings in order to promote its standing in Japan and globally. The fact that payment is made by Chiyoda Ltd is not determinative, and the benefits which accrue to it are minimal; in particular, there is no association between its name and Minato Fields.

Accordingly, it follows that the supply is made to Holdings which is established in Japan, so the Club's supply is outside the scope of UK VAT, with the right to deduct in full VAT in incurred on associated expenditure.

(VAT: 2 marks)

One exception to the general rule is where the service relates to land. It is taxed where the land is situated. However, for this exception to apply, the land must be a central and essential element of the supply. In our view the exception does not apply here; objectively land is not a central and essential element of the supply.

(VAT:1 mark)

7 Corporation Tax

7.1 Notification of charge to corporation tax

We confirm that DH's sponsorship income received in the accounting periods ending 31 May 2016 and 2017 is not exempt from corporation tax. Since it is unlikely that significant expenses will be deductible from this source of income, we estimate that there is a charge to tax of £9,500 in each of these periods

(CT: 1 mark)

Having identified a liability to tax, the Club is duty bound to notify HMRC of this fact - it cannot ignore it. Failure to make full disclosure will have a material effect on the penalties imposed on the Club, and very probably result in a wide ranging HMRC enquiry into the Club's tax affairs. Furthermore, given that we are now aware of the matter, under the regulations issued by the firm's professional body, if the Club does not make full disclosure to HMRC, the firm is required to consider its position and very probably will cease to act for the Club. In addition, the firm has to consider whether it should make a report to the authorities under the money laundering regulations, and it will be required to disclose the reasons for ceasing to act for the Club to a successor firm which seeks professional clearance.
(Ethics: 1 mark).

Although the Club has not received a notice to file a return, nevertheless it should have notified HMRC in writing within three months of the start of the accounting periods (i.e. by 31 August 2015 and 2016 respectively) of its chargeability to tax.
(CT: 1 mark)

Failure to give notice will not incur a penalty if the Club has a reasonable excuse.
(CT: 1 mark)

In the absence of notification of the Club's chargeability to tax and a notice to file a return, it is required to notify HMRC within 12 months of the end of the accounting period in which it was chargeable to tax. Accordingly, the Club should have notified HMRC on or before 31 May 2017 of its liability to tax in respect of the accounting period ending 31 May 2016, and by 31 May 2018 in relation to the accounting period ending May 2017.
(CT: 2 marks)

Failure to notify timeously may render the Club liable to a penalty based on a percentage of the "potential lost revenue" of £9,500 ("PLR"). The percentage is dependent on the Club's behaviour, namely whether it acted:

- (a) carelessly (by failing to exercise reasonable care):
 - (b) deliberately; or
 - (c) deliberately and it took steps to conceal the error.
- (CT: 1 mark)

The maximum penalty for each type of failure is:

Type of failure	Maximum penalty payable (% PLR)
Careless	30%
Deliberate	70%
Deliberate and concealed	100%

The Club's failure is likely to be seen by HMRC as careless. In order to limit the penalty (to £950), we recommend the Club notifies HMRC promptly of its liabilities, makes full disclosure of the facts and assists them to establish the tax due.
(CT: 2 marks)

A penalty levied by HMRC is non-deductible for tax purposes.
(CT: 1 mark)

The tax due in respect of the accounting periods ending 31 May 2016 and 2017 should have been paid on 1 March 2017 and 2018 respectively. Accordingly, interest at 3% will be charged on its late payment.
(CT: 1 mark)

7.2 Mitigating corporation tax

In relation to the 2019/20 accounting period, since bar and catering sales will not be restricted to members and their guests, we agree that this income, along with that accruing from the sale of the naming rights and DH's new sponsorship deal, will attract a tax charge of up to £36,290 (£80,000 naming rights+£101,000 (net bar receipts) +£10,000 sponsorship) x 19% dependent upon the quantum of deductible expenses.

(CT: 2 marks)

Since the Club will be undertaking profitable non-primary purpose trading activities, we recommend that these be conducted through a Subco. Subco may use Gift Aid relief to reduce or eliminate taxable profits by donating them to the Club.

(CT: 1 mark)

A charitable donation is deductible against Subco's profits to the extent that it has been paid within nine months of the end of its accounting period. The donation is exempt from tax in the hands of the Club so long as it is applied in furtherance of its charitable objects.

(CT: 1 mark)

HMRC and the Charity Commission regard these arrangements as an acceptable method of mitigating a charity's potential tax liabilities.

(CT: 1 bonus mark will be awarded for this point)

Finally, cost-sharing arrangements may be effected between the Club and Subco or a service charge made by the Club to Subco to fairly reflect the costs incurred in operating Subco. Such arrangements are subject to the UK:UK transfer pricing legislation but, given that both the Club and Subco are likely to be classified as small enterprises, the legislation will not apply.

(CT: 1 mark)

7.3 DH - deduction of sponsorship payments

In this matter we are instructed by the Club on the basis that the sponsorship arrangements are conditional on DH's ability to claim a deduction for the payments. In accordance with best professional practice and our Institute guidelines, we must act independently in the interests of our client. Mindful of the potential conflict of interest, at the outset we raised the matter with both the Club Secretary and the managing director of DH. DH has confirmed in writing that it is content for us to report on the matter.

(Ethics: 1 mark)

It appears that DH's payments in 2015/16 and 2016/17 were motivated by firstly, the need to stabilise the Club and secondly, to promote DH to the membership and local community. If so, case law is consistent on this point. Unless the expense has been incurred exclusively for the purposes of a trade, it is non-deductible. Once duality of purpose is established, it matters not that the business purpose predominates or that the purpose was merely a necessary and intermediate step in promoting DH. On the face of it, the law may well be against DH and strictly there is no deduction for these sponsorship payments. However, by concession a deduction for part of cost may be allowed by HMRC, but the treatment must be fully disclosed when DH's returns are filed.

(CT: 2 marks)

In contrast, on the basis of the information that you have supplied, duality of purpose does not arise in relation to the proposed sponsorship deal for the 2019/20 season and thereafter. On the face of it, payments under the contract will represent deductible advertising services incurred exclusively for the purposes of DH's trade.

(CT: 1 mark)

8. Accounting - naming rights and the RFU grant

- 1) The payment for the naming rights covers 5 years, commencing 1 October 2019. Under the accruals concept, the payment attributable to the accounting periods 2020/21 to 2024/25 must be included on the Club's 2019/20 balance sheet as a liability (deferred income) and thereafter released to the profit and loss account each financial year to reflect the economic reality.
(Accounting: 1 mark)
- 2) Since the RFU grant is intended to subsidise the Club's employment costs associated with the operation of the its rugby academy, it should be netted off against these costs to give effect to the concept of matching.
(Accounting: 1 mark)

9. Insurance Premium tax ("IPT")

IPT is a tax on premiums payable on taxable insurance contracts. However, an exclusively long-term insurance contract covering incapacity consequential upon injury arising from an accident, sickness or infirmity is an exempt contract. The period of cover must exceed 5 years, with limitations on the insurer's right to terminate the contract. Medical insurance is excluded from the exemption. Medical insurance essentially covers medical, dental or optical consultation, diagnosis, treatment, convalescent care and associated goods and services.
(IPT: 1 mark)

On the basis of the information that you have supplied, it appears that IPT will be charged on the full premium at the rate of 12% because the proposed contract does not exclusively cover incapacity on account of an injury sustained while participating in a Club game or training. The legislation does not allow for the apportionment of the premium where the contract covers both incapacity and medical insurance, so we recommend that you ask the broker to arrange a separate contract of insurance which exclusively covers incapacity risk.
(IPT: 2 marks)

10. Machine Games Duty ("MGD")

If a machine offers a choice of dutiable machine games, some within and others out with a particular type of machine, a single rate of MGD applies to all of the machine's games by reference to the highest stake/prize, even if no one ever plays such games. Given that the machine here has a number of games with a stake of £10 which is outside the parameters which apply to Types 1 & 2 machines, all of its takings are chargeable to MGD at 25%.
(MGD: 2 marks)

Lewis Waters LLP
2 May 2018

MARKING GUIDE

TOPIC

MARKS

Sale of site:

Exempt, unless OTT made with further input tax recoverable.	2
Procedure for making OTT.	1
SDLT implications	2
Cash flow implications for DH and conclusion	1

Acquisition of new facilities:

Acquisition of new site	
(a) Scope of charitable SDLT exemption (<i>a bonus mark will be awarded where the conditions of the relief are stated</i>)	1
Construction of clubhouse - VAT reliefs	
(a) Identifying scope for zero-rating on the construction of a building similar to that of a village hall (<i>where candidates focus simply on the relief of a building by a charity for non-business purposes, no more than 2 marks will be awarded, inclusive of a bonus mark for a full answer</i>).	1
(b) Principles relevant to zero-rating of a building similar to a village hall (1/2 mark for each item, subject to a maximum of 2 marks).	2
(c) Importance of documenting projected use by community.	1
(d) Relief conditional upon issue of certificate.	1
(e) Specific factors relevant to this matter in support of zero-rating and conclusion (1/2 mark for each relevant factor, subject to a maximum of 3 marks).	3
(f) Contractor to assess liability status of works based on certificate issued by charity.	1
(g) Scope for extending zero-rating on professional services (1 mark) and conclusion (1 mark).	2
(h) Extent of relief on building services to meet the needs of disabled persons and absence of relief on lift).	2

Recovery of VAT on expenses:

Tax year 2016/17:	
(a) Requirement to operate standard method.	1
(b) conclusion that Club substantially meets requirements of standard method.	1
(c) Recovery rate to be rounded up.	1
(d) Identifying the exclusion from the pro rata calculation of income arising from incidental real estate and financial transactions (1 mark) and conclusion (1 mark - credit will be given for any well reasoned conclusion which differs from the suggested answer).	2
(e) Re-attribution of input tax incurred on playing and pitch expenses.	2
(f) Basis of apportionment of members' subscription under CPP and related cases (<i>a bonus mark will be awarded for a full response, irrespective of the conclusion</i>).	1
(g) Scope of ESC 3.35.	1
(h) Quantifying impact of apportionment (credit will be given for any reasonable calculation).	1
(i) Qualifying under-claim of input tax in 2016/17.	2
(j) Recommendation in the light of under-claim of input tax.	1

Projection 2019/20: conclusion on suitability of the standard method to 2019/20 (credit will be given for any reasonable conclusion which differs from the suggested answer (1 mark) and identifying and examining VAT group treatment (1 mark).	2
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Recovery of input tax on pitches and clubhouse:

(a) Attribution of VAT incurred on pitches and clubhouse and basis of recovery of input tax and CGS.	2
(b) Computation of estimated recovery rate for 2017/18.	2
(c) Computation of estimated recovery rate for 2018/19.	2

(d) Conclusion on tax deductible on capital items.	1
(e) Consideration of override.	2
<i>(Where candidates have concluded that the construction services in respect of the clubhouse are not zero rated and members' benefits are exclusively VAT exempt, up to 7 marks may be awarded based on any alternative methodology which takes account the taxable use of the clubhouse, the recommendation of a PESM which reflects taxable use to discrete areas, etc)</i>	
<u>Naming rights:</u>	
(a) Single/multiple supply principles to be applied (2 marks) and conclusion (1 mark).	3
(b) Place of supply - general rule.	1
(c) Conclusion that supply not connected with land.	1
(d) Conclusion on identifying recipient of supply (1 mark for relevant factors, subject to a maximum of 2 marks).	2
<u>Corporation Tax</u>	
Chargeability to tax on DH sponsorship	
(a) Computation of tax payable.	1
(b) Obligation to notify HMRC of chargeability to tax	1
(c) Defence of reasonable excuse.	1
(d) In the absence of notice to file return, Club required to notify HMRC by 31 May 2017 and 2018.	1
(e) Identify penalty for failure to notify.	1
(f) Quantify potential penalty and advice given.	2
(g) Penalty non-deductible.	1
(h) Payment dates of tax due.	1
(i) Payment date and Interest	1
(j) Ethical considerations	1
Scope to shelter chargeable profits from tax:	
(a) Conclusion that Club will be outside the scope of CT exemption in 2019/20.	2
(b) Activities chargeable to tax should be operated through a wholly-owned subsidiary, with chargeable profits sheltered by Gift Aid.	1
(c) Gift Aid - application and payment.	1
(d) Attitude of HMRC and Charity Commission to structure (a bonus mark will be awarded for this point).	
(e) Transfer pricing implications.	1
<i>(Bonus mark will be awarded for reference to HMRC and Charity Commission guidance on the structure)</i>	
Deduction of sponsorship payments by DH:	
(a) Analysis and conclusion on the deduction of sponsorship payments of £50,000 in respect of the 2015/16 and 2016/17 seasons.	2
(b) Conclusion on deductibility of sponsorship payments under proposed contract.	1
(c) Ethical considerations	1
<u>Accounting</u>	
Accounting treatment on naming rights (1 mark) and RFU grant (1 mark)	2
<u>Insurance Premium Tax</u>	
(a) Scope of exemption in exclusively long-term insurance contracts covering incapacity, excluding medical insurance	2
(b) conclusion and advice	1
<u>Machine Games Duty</u>	
Rate applicable where a choice of games offered	2
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	78
Presentation	22
Total marks	100
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