Institution **CIOT - CTA**
Course **APS VAT and Other Indirect Tax**

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Answer-to-Question-_1_

To: Andrew Dixon

From: Alex Lee

Date: 14 November 2024

Subject: Crammton Farm Project

1. Scope

This report looks to address the tax queries provided by Andrew Dixon (AD) within his letter dated 1 November 2024. Specifically, this report focuses on:

- The proposed sale of two of AD's three investment properties and which combination is most efficient and commercially appealing from a tax perspective.

- The proposed development of the Crammton Farm property and the various tax implications that both option 1 and option 2 have.

- The VAT treatment of specialist electrical works to the project.

- The process for submitting a DIY Housebuilder Scheme refund for AD.

Please note, this report is based solely on the information provided to us. If any of our assumptions are incorrect, please inform us as this may affect the outcome of our advice. The contents of this advice should not be disclosed or relied upon by any third party that is not included within our engagement letter. If you wish to disclose the content of the report to a third party you would require our prior written approval.

We note that your accountants and other third parties may wish to view the contents of this report. If this is the case, we would need to provide hold harmless letters for their signature.

2. Executive Summary

2.1 We would advise that AD proceeds with the sale of the River Mews property as he will be able to benefit from Private Residence Relief, which consequently reduces the capital gain on the property to £1,278 and gives AD proceeds of £428,722, as per Appendix 1.

2.2 We would also recommend that AD proceeds with the sale of the Parks Street property. While Gulliver Avenue gives higher proceeds after CGT of £381,040, compred to the Parks Street property proceeds after CGT of £363,520, as per Appendix 1 below. Given that the Gulliver Avenue property has rapidly increased in value compared to the Parks Street property, we would recommend that the Gulliver Avenue property is kept as an investment as there is more growth potential in the future. The total proceeds generated from our recommended sales is £792,242.

2.3 Gains of residential property should be reported within 60 days of completion of the sale. AD should note this is different to a sale of other capital items.

2.4 Under option 1 of the project, the SDLT payable by AD would be £59,660. Under option 2 the SDLT payable would be £3,000. This is mainly due to the increased value that AD will pay under the purchase of the property of option 1 and the fact he will pay the higher residential rates given his other London property. Please see section 4 and Appendix 2 and 3 for further explanation.

2.5 Under option 1, the onward supply of the property will be a zero rated sale for VAT purposes by DQS Partners of a converted non-residential property into a dwelling. Giving DQS Partners entitlement to full VAT recovery. Please see Section 4.1 for further detail.

2.6 In both option 1 and 2, materials supplied will be subject to VAT at 20%, and the reduced rating of 5% will apply to services converting the barn into a dwelling as this will be a qualifying conversion for VAT purposes. Please see section 4 for further detail of the VAT treatment of the conversion works.

2.7 Under option 2, AD could use the DIY Housebuilders Scheme to recover input tax incurred on the project. Please note, as per Section 4.2, some of this input tax is irrecoverable under the DIY Housebuilders Scheme.

2.8 As per the cost summary in 4.3, option 2 provides a lower cost to AD of the project of £928,000. This is £33,660 cheaper than proceeding with option 1. In addition to the lower cost of the project, option 2 also gives AD creative control, something we understand it very important as he intends to live in this house fopr the rest of his life. On this basis, we recommend that AD proceeds with the project under option 2 and files a DIY Housebuilders Scheme application for the input tax.

2.9 Please note, as per Section 4.2, the hi-spec electrical works are likely to be ineligible for recovery through the DIY Housebuilders Scheme given that these are building materials not ordinarily incorporated in a dwelling. As such, £25,000 of input tax will be irrecoverable.

2.10 A DIY Housebuilder Scheme application must be filed to HMRC within six months of the completion of the property. Please note, to recover the VAT, it must have been charged correctly by the contractors and sub contractors. We would recommend that all invoices are maintained to support the claim to HMRC.

2.11 The DIY Housebuilder Scheme application should be filed online through the Government Gateway, using AD's credentials that he will use to submit his self assessment tax returns.

2.12 Under option 2, the sourcing of materials by AD should not be an issue as input tax can be recovered. We note that AD can achieve a lower cost if procuring himself and as such we recommend that he proceeds with acquiring the materials he can himself under option 2.

3. Sale of Investment Properties

3.1 Sale of River Mews

Regarding the sale of your investment properties, we note that the occupation of the River Mews property will allow AD to claim Private Residence Relief (PRR) on the gain made upon the River Mews property.

Please note, this PRR will be reduced given that it has been let out to a tenant from November 2024. However, as noted in Appendix 1, PRR always deems the last nine months as occupation for calculating the relief. Therefore, as per the calculation in Appendix 1, the sale of River Mews would generate £428,722 of proceeds for AD after CGT of £10,563 had been deducted from the proceeds. This is also assuming the annual exempt amount of £6,000 is used.

Given the PRR that can be utilised to reduce the CGT payable, we would highly reccommend that the River Mews property is sold as a priority in addition to another property which we have considered below.

3.2 Sale of Parks Street or Gulliver Avenue

As noted in Appendix 1, the sale of the Parks Street property will generate proceeds, after CGT, of £363,520. While the Gulliver Avenue property has proceeds after CGT of £381,040.

While the Gulliver property generates higher proceeds for AD and a lower CGT by £2,520. We do note that these properties are held as investment properties and the Gulliver Avenue property has seen a much higher growth, overtaking the Parks Street property value.

Based on this, we would advise that the Gulliver Avenue property is kept as an investment property, which could potentially reach greater value in the future while being held as an investment as compared to the Parks Street property. We note that the shortfall of the project will be made up by your cash savings regardless, hence the £17,520 difference between the two properties may be exceeded by the overall growth of the Gulliver Avenue property in the future.

The overall proceeds from our recommendations of the sale of the River Mews property and the Parks Street property are £792,242.

4. Development of Crammton Farm

Below we will consider the two options of the development of the project.

4.1 Development of Crammton Farm - Option 1

4.1.1 SDLT

Within option 1, the purchase of the property after completion will result in SDLT payable by AD of £59,660. This is due to the fact that the purchase of the developed property will qualify for the residential SDLT rates. Additionally, we note that AD is intending to keep another residential property he currently holds, hence, the higher rates will be applied to the purchase of an the addtional property as detailed in Appendix 1 below.

4.1.2 VAT

The conversion of a non-residential property for VAT purposes will attract the reduced rating for VAT purposes at 5%.

Therefore, DQS Co and its other sub contractors should charge VAT at 5% on the construction works and materials, if supplied together that relate to the reconstruction of the property. As per Appendix 2, we estimate this value of input tax will be at £31,600. We have assumed DQS Co is CIS registered and would therefore expect the supplies from its sub contractors to it to be under the Domestic Reverse Charge (DRC) Scheme. We would recommend that DQS Dev Co does not issue end user notifications however as this will provide it with a cash flow advantage.

The onward supply of the converted property from DQS Partners to AD will be zero rated for VAT purposes, as this is a conversion of a non-residential property to a dwelling. This will mean that DQS Partners can recover the input tax it incurs in developing the property. DQS Co's input tax will also be recoverable apart from materials that are not ordinarily incorporated in a dwelling. This will mean the input tax will be blocked on certain elements such as white goods and carpets.

4.1.3 Income Tax (IT)

Given AD is part of DQS partners, we have considered the implications in regards to his IT of the sale of the property by DQS partners.

As a third equity share owner of DQS partners, any sale by the property will be subject to IT for the partnership as the asset is within trading stock and is being developed with the intention to sell it to AD. Therefore, AD will pay 45% IT on any profits received. We do not have access to DQS Partners profit sharing figure, so are unable to provide a value for this. Class 2 and Class 4 National Insurance contributions would also be due on the profit received.

4.1.4 CGT and Private Residence Relief

AD will acquire the property and £902,000 will be AD's base cost. This should be noted as any sale of the property in the future will need to use this, however, we note that you intend to live in this property for the rest of your life. Please note, where two residences are owned, only one election can be made for Private Residence Relief, such that you would not be able to secure PRR on the sale of the Marland Street property.

4.2 Development of Crammton Farm - Option 2

4.2.1 SDLT

Purchasing the property prior to its development will mean that AD will benefit from the non-residential rates given that the property is a farm at the time of purchase. As per Appendix 3, this will mean AD will have an SDLT liability of £3,000.

4.2.2 VAT

The sale of the property by DQS Partners will be exempt for VAT purposes as no Option to Tax (OTT) has been notified over the property by DQS Partners. Any OTT on the property could have been disapplied regardless giving OTT. DQS Partners may need to consider any VAT implications of making an onward exempt sale.

The conversion of the non-residential property into a dwelling will mean AD can use the DIY Housebuilders scheme to recover some of the input tax incurred on the project. The DIY Housebuilders Scheme will mean that AD will not be required to register for VAT and make any onward supplies in order to be eligible to recover this input tax.

As AD will be contracting DQS Co for the development of the property. DQS should charge AD VAT at 5% for qualifying conversion works and building materials that are supplied with these services. We note that this will apply to the conversion of the barn itself, but may also apply to any works such as garages or driveways if included under the same contract and considered part of the overall qualifying conversion. Under the DIY Housebuilders scheme, AD will be able to recover this input tax relating to the conversion. It is important to note however, in order for AD to be eligible to recover the input tax through the DIY Housebuilders scheme, the VAT must have been charged correctly.

We also note that under this option, AD will purchase all the materials and equipment personally, with the exception of the hi-spec electrical equipment (considered below). Please note, input tax incurred on building materials will be subject to VAT at 20%. This will also be recoverable through the DIY Housebuilder's Scheme.

We understand you are considering the instructing a specialist electrician. As he is VAT registered, VAT will be charged at 20%. Please note, while the works provided by a general electrician regarding the conversion of a property would typically be recoverable unde the DIY Housebuilder Scheme. For VAT purposes, electrical appliances are generally not building materials for VAT purposes where they are not designed to heat space or for waste disposal to provide an example. Therefore, our view is that the works you have described by Gary will be blocked from recovery under the DIY Housebuilders Scheme. This will mean that £25,000 of VAT will be irrecoverable in relation to Gary's works. We have only assumed these costs are goods as there is no indication of the amounts that would be charged for solely service.

Additionally, the costs of the project management will also have VAT charged on them at 20%. This input tax will be recoverable on the basis it relates to the conversion of the property into a dwelling. Invoices and contracts from the project management firm should be kept.

4.2.2.1 Operation of the DIY Housebuilders Scheme

As discussed, the DIY Housebuilders Scheme will allow Andrew to recover input tax charged upon most of the works relating to the property. In order to submit a an application, AD will need to keep all the invoices provided for which he wishes to recover input tax upon. This will include the purchase of the building materials and the goods and services supplied by DQS Co. This will total input tax of around £49,750 (£180,000*20% + £275,000*5%), as the input tax on the supply and fitting of the electrical equipment will be blocked for VAT purposes given the reasons above. There will also be some blocked input tax on other items that are not ordinarly incoprorated within a dwelling, such as carpets.

The DIY Housebuilders Scheme application must be submitted within six months of the completion date of the property. AD will likely get a certificate certifying that the property has been completed and AD should consider the six month deadline from this date to make the application to HMRC.

As noted above, VAT must have been charged correctly in order for the input tax to be payable, so it is paramount that VAT is correctly charged. The application can be made under using AD's Government Gateway ID. As AD submits self assessment returns, it will just be this same Government Gateway login in order to make the claim under the scheme.

We would advise that all contracts are also maintained alongside the invoices to support a claim. Please note, payment also has to have been made for the goods and services that are being claimed by AD.

4.2.3 Income Tax (IT)

Given AD is part of DQS partners, we have considered the implications in regards to his IT of the sale of the property by DQS partners. This option will result in a smaller profit for AD to pay Income Tax on, given the partnership will be selling the property for considerably less at £270,000.

4.2.4 CGT and Private Residence Relief

Again, for CGT purposes, the base cost of the asset will be £270,000 upon acquisition. However, enhancement expenditure will also apply uplifting the base cost of the property. However, as above, we note that you do not intend to sell this property so have not considered this further.

4.3 Our Recommendation

On the basis of the summary costs below, we note that option 2 achieves the development of the property at £928,000, saving £33,660 as compared to option 1. As option 2 also gives you the creative control to install your creative control, this gives further reason to proceed with the development under option 2, given that you will be living in the property for the rest of your life.

	Option 1 £	Option 2 £	Comments
Cost	902,000	925,000	Hi spec costs are irrecoverable and assuming DQS Dev Co undertakes design and build contract with project management so the input tax is not a cost.
SDLT	59,660	3,000	
Total cost	961,660	928,000	

Appendix 1 - Sale of Investment Properties

Private Residence Relief (PRR) for 15 River Mews:

Months of ownership (assuming a November 2025 sale) = 355

Months of occupation (AD will automatically get the last 9 months as deemed occupation as part of PRR) = 340

£250,000 - (£250,000 * (340/355) = £10,563

Sale of 15 River Mews London:

	£		
proceeds	430,000		
less acquisition cost	(180,000)		
gain	250,000		
less PRR	(239,437)		
gain after PRR	£10,563		
annual exempt amount	(6,000)		
gain after annual exempt amount	4,563		
CGT @28%	(1,278)		
proceeds after CGT and annual exempt amount	428,722		

Sale of 73 Parks Street Kidderminster:

	£		

proceeds	410,000		
less acquisition cost	(244,000)		
gain	166,000		
CGT @28%	(46,480)		
proceeds after CGT	363,520		

Sale of 11 Gulliver Avenue Worthing:

	£		
proceeds	425,000		
less acquisition cost	(268,000)		
gain	157,000		
CGT @28%	(43,960)		
proceeds after CGT	381,040		

Appendix 2 - Option 1 Crammton Farm

SDLT on purchase by AD at £902,000:

SDLT basic rates will be increased by 3% as we note that AD is keeping another of his homes in London and this will consitute an additional residential property.

	£		
3% of £250,000	7,500		
3% of £250,000	52,160		
Total SDLT	59,660		

Appendix 3 - Option 2 Crammton Farm

SDLT on purchaseby AD:

The purchase of the property prior to development will mean the non-residential rates are used.

	£		
0% of £150,000	nil		
2% of (£250,000 - £150,000)	2,000		
5% of (270,000 - £250,000)	1,000		
Total SDLT	3,000		