

Institution **CIOT - ATT-CTA**  
Course **CTA Adv Tech Domestic Indirect Tax**

Event **NA**

Exam Mode **OPEN LAPTOP + NETWORK**

Count (s)	Word (s)	Char (s)	Char (s) (WS)
Section 1	<b>522</b>	<b>2430</b>	<b>2940</b>
Section 2	<b>542</b>	<b>2552</b>	<b>3084</b>
Section 3	<b>562</b>	<b>2539</b>	<b>3083</b>
Section 4	<b>412</b>	<b>1972</b>	<b>2368</b>
Section 5	<b>541</b>	<b>2599</b>	<b>3201</b>
Section 6	<b>615</b>	<b>3035</b>	<b>4134</b>
Total	<b>3194</b>	<b>15127</b>	<b>18810</b>

Answer-to-Question-\_1\_

### **VAT implications**

#### Cessation of business

Stanley Wilks Ltd (SW Ltd) will need to deregister for VAT as it has ceased carrying on a taxable trading activity. There will be a deemed supply for SW Ltd at the date of deregistration of on all the assets that are held on the date of deregistration. The output tax charged will be charged on the replacement cost of the asset. Note there is no charge if there was no initial input tax recovery or where the deemed output tax due comes to GBP 1,000 or less.

#### Liquidation

If there is an appointment of a trustee in liquidation over the affairs of SW LTD, then it is necessary to notify HMRC of the fact within 21 days of the appointment.

Once the appointment is made, the current VAT return is divided into two parts separated by the date of appointment. The first parts due date will be 2 months after the date of the appointment.

When creditors are paid off by the liquidator, preferential creditors are second only to creditors holding a fixed charge over an asset of the business. With regards to your outstanding payment to HMRC, HMRC's preferential claim in an insolvency is abolished under Enterprise Act 2002 s.251.

#### Bad debt relief (BDR)

I note SW Ltd has outstanding debts from a number of

customers and some of the debts are over 4 years old. Bad debt relief can be claimed by SW Ltd where the output vat has been accounted for paid to HMRC, and where six months has elapsed from the later of payment due date and date of supply. However, the claim must be made within 4 years and six months from the later of those dates.

Accordingly, there is scope for SW Ltd to claim BDR on its final VAT return on the outstanding debts which meet these conditions. Unfortunately, a claim cannot be made for any outstanding debts over the 4 years and 6 months mentioned above.

A business cannot issue a credit note to a customer for unpaid VAT instead of claiming BDR. A credit note can only be issued where there is a genuine mistake, overcharge or an agreed reduction in consideration.

#### VAT recovery

I note that SW Ltd incurred VAT following cessation which it believes to be recoverable. Once deregistration has been agreed HMRC will issue a final VAT return (VAT193) for completion. This return will outline all the output tax and input tax to date of deregistration. Once the business is deregistered, it should require no further contact with HMRC.

#### Adjustment of output tax

I note SW Ltd over declared VAT on protective boots which should have been zero-rated. Subject to the usual 4 year limitation period, retrospective claims may be possible. Such claims must be based on contemporaneous accounting records and are analysed by VAT period. Claims must take account of any input VAT restrictions flowing from SW Ltd being partially exempt. HMRC may refuse the claim if they can show that SW Ltd

will be "unjustly enriched" by showing the that the economic burden of the VAT charge was passed to the customer.

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-----ANSWER-1-ABOVE-----  
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-----ANSWER-2-BELOW-----  
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Answer-to-Question-\_2\_

**VAT**

\_\_\_\_\_The 999-lease from Three Countries College (TCC) to Riverdale Developments Ltd (RD Ltd) will be an onward exempt supply for VAT purposes. Irrespective of a peppercorn rent, any input tax incurred by TCC in relation to the proposed development will not be recoverable given it has a direct and immediate link to an onward exempt supply.

This is an issue for TCC as the fit out costs will be subject to standard rate VAT for TCC which is GBP 1,000,000 + GBP 200,000 VAT, so the VAT would be non-recoverable.

TCC could opt to tax (OTT) the freehold land, however the option would be disappplied. I consider TCC a "development financier" as defined in the anti avoidance legislation. "Development financier" is widely defined and covers any person who finances the acquisition of the land and buildings. This is not confined to monetary funding. HMRC consider for example this it covers an end-user who makes a site available to a developer for no charge or less than market value, where on completion of the proposed works, the developer sells or leases back the building to the end user. Here the lease is peppercorn. As a result the OTT would be disappplied, meaning the onward supply would continue to be exempt and input tax irrecoverable by TCC.

Whether or not RD Ltd OTT the land (it would be in their interest to do so to recover VAT), similarly TCC as a development

financier will occupy the building for ineligible purposes so i would expect their OTT to be disallowed too.

It is recommended that a market value premium and rent is charged as this will result in TCC not being regarded as a development financier. This would be subsequent to TCC opting to tax the property and notifying HMRC of the OTT within 30 days using Form 1614A. Accordingly, the lease will be subject to standard rate VAT and VAT recoverable on the fitting out works in line with TCC's partial exemption method (if applicable).

### **CGS**

The fitting out works will fall under the Capital Goods Scheme. This is where the VAT on capital expenditure (capitalized and on the fabric of the building above GBP 250,000 (including VAT) is adjusted for taxable use over a 10 year period.

Accordingly, TCC use of the building will be theatre and studios for educational and ticketed performances - that is a mix of exempt and taxable use. Accordingly, (providing the above recommendation is followed) TCC can recover VAT in the first year using its partial exemption percentage as baseline recovery. From years 2-10, this will need to be adjusted for taxable use, resulting in VAT payable or recoverable to TCC.

### **SDLT**

SDLT is payable on leases by the leasee on the VAT inclusive value. For leases this is payable on the NPV of the lease and any lease premium.

In this case, both TCC and RD Ltd would pay SDLT, but SD Ltd may be able to claim some relief on land used for building residential buildings/dwellings.

TCC will pay SDLT on the 997-sub lease, on both any premium and the NPV of the lease rentals.

The purchaser/leasee must deliver a land transaction return (SDLT1) to HMRC within 14 days of the effective date.

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-----ANSWER-2-ABOVE-----  
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-----ANSWER-3-BELOW-----  
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Answer-to-Question-\_3\_

     **VAT implications**

I note Fashion Holdings Ltd (FH Ltd) plans to sell its subsidiaries Bid Co Ltd and Bargain Bags Ltd.

I also note that FH Ltd has incurred costs in the region of GBP 2,000,000 plus GBP 400,000 VAT, which if it cannot recover then becomes an additional cost.

     VAT registration

Currently, FH Ltd cannot recover the VAT given it is not VAT registered, as the only income is outside the scope dividends and it has no trading activities. However it is possible to group a holding company with its trading subsidiaries. I therefore propose that FH Ltd is added to the current fully taxable VAT group consisting of Bid Co Ltd and Bargain Bags Ltd.

     Sale of subsidiaries

A share of shares of Bid Co Ltd and Bargain Bags Ltd by FH Ltd will be outside the scope of VAT. Accordingly, in principle any input VAT will not be recoverable since it has a direct and immediate link to an onward exempt sale. This will make the VAT group partially exempt.

     Deduction of input tax



In order to claim a deduction of input tax the company needs to be VAT registered and the following:

- There must be a supply of goods or services to the claimant which is chargeable to VAT
- There must be evidence of the VAT charged in the form of a tax invoice
- The claimant must have 'received' the supply
- The input tax must be used by the registered person for the purpose of his taxable business activities.

In accordance with the decision of the CJEU in Kretzechink, VAT incurred on the sale of shares can be treated as "residual pot" on the basis. On this basis, the VAT group can recover the VAT of GBP 400,000 in accordance with the VAT group's partial exemption recovery rate. I should note, however that FH Ltd simply joining the VAT group does not give it an entitlement to recover the input tax. FH Ltd would need to make genuine management services to the members of the VAT group for the VAT to be considered under the "residual pot". For this, it is recommended that the employees contracts are transferred to FH Ltd and FH Ltd makes management charges to the VAT group members in this regard. This should allow the VAT group to recover the input tax relating to the sale of the subsidiaries in line with the partial exemption method.

Who received the supply of professional fees?

The VAT group can only recover VAT if FH Ltd received the supplies subject to VAT for GBP 400,000. I note that the sale is by Frank Private Equity LLP but the contracts are with FH Ltd.

With regard to the case of Redrow where they chose and instructed the estate agents and therefore were deemed to benefit from the supply, similarly in this case the contract for

professional services is held by FH Ltd so they should be regarded as the recipient of the supply who benefit from the supply.

Bargain Bags additional costs

I note that Bargain Bags Ltd incurred some additional costs in relation to the planned sale by Frank Private Equity LLP. The issue of VAT recovery depends on whether Bargain Bags actually received and benefitted from the supply - only then does it have an entitlement to recover the VAT.

Error identified

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-----ANSWER-3-ABOVE-----  
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-----ANSWER-4-BELOW-----  
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Answer-to-Question-\_4\_

### **Pentalty and assessment position**

#### Assessment

I note that HMRC intending on raising assessments on Petstuff Online Ltd (PO Ltd)base on information prvided to them during a VAT insplection.

It appears that PO Ltd have been treating some of their supplies incorrecly for VAT purposes.

The supply of medications/flea treatments shall be stadard rated as it does not fall under Schedule 8 VAT. This would explain why the VAT due on the VAT return for the period ending 31 March 2021 is not 20% of the total sales (which must have rasied red flags for HMRC)

Accordinly, for the period PO Ltd have understated output VAT by GBP 3,000 (GBP 15,000 x 20%).

#### Penalty

It is recommended that PO Ltd make a voluntary disclosure to HMRC of the error of the VAT treatment on the medications/flea treatment.

The voliuntary disclosure will be in the form of an Error Correction notice or in writing to HMRC.

HMRC will impose a penalty as a percentage of the potential lost revenue (PLR). This has been calculated as GBP 3,000 above.

Since the issue has been identified by HMRC during a VAT inspection, any disclosure would be considered 'prompted'.

Furthermore, since HMRC raised the VAT treatment of the medication/flea treatments seven years ago, it is likely HMRC will consider the error as "deliberate but not concealed".

Accordingly, it is my view the minimum penalty for this error will be 35% of the PLR. Accordingly, the penalty will be GBP 1,050 for the error.

#### Interest

Since PO Ltd will need to pay VAT for a past period on the basis of an assessment, they will certainly be charged interest from the due date from that earlier period until settlement. HMRC will regard the interest as mere "commercial restitution", without requiring any blame to attach to the late payment.

#### Historic position

Given this incorrect VAT treatment has been identified in the VAT period ending 31 March 2021 and this issue was raised 7 years ago, it is likely the PO Ltd have incorrect previous VAT returns. In this regard, it is advised that PO Ltd make an unprompted disclosure to HMRC for these errors. This will reduce penalty to 20% of PLR.

It should be noted that the time limit for an assessment is four years after the end of the prescribed accounting period

concerned. In this regard, VAT periods prior to period ending 31 March 2017 are time barred and no disclosure is required for errors in these VAT returns.

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-----ANSWER-4-ABOVE-----  
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-----ANSWER-5-BELOW-----  
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Answer-to-Question-\_5\_

**1) SDLT consequences**

The purchase of Blackacre land by Housebuilders Ltd (H Ltd) will be subject to SDLT in the VAT inclusive consideration. The chargeable consideration for the transaction will be the consideration for the land transaction in money or money's worth, including:

- Carrying out of works on the land
- Provision of services

It is important to note while Farmer Mcghee has opted to tax the land, since H LTD intend to build dwelling on the land, the option will be dissapplied and the sale will be exempt from VAT.

Where three conditions are satisfied, the value of the works is excluded from the value of SDLT, these are:

- the works are carried out after the effective date of the transactions
- the works are carried out on the land qcquired under the transaction
- it it not a condition of the transcation that the worls are carried out by the vendor.

Accordingly, SDLT will be due on the acquisition value of the land which is GBP 1.2 million (OTT is dissplied so no VAT is included as exempt sale).

Since the construction of the access road is "part of the

agreement" the recharged amount of GBP 40,000 will be part of the consideration subject to SDLT.

It appears the further consideration of 5% of the future sales proceeds of the dwellings, is also a condition of the agreement and therefore will need to be included in the chargeable consideration.

It should be noted, the 5% proceeds would represent uncertain consideration as the amount depends on an uncertain future event. In this case, SDLT is payable on the basis of a reasonable estimate of the value of the uncertain consideration. An application for the postponement of tax is possible to defer the payment of tax provided the uncertain consideration falls to be paid on one or more future dates, at least one of which is more than six months after the effective date of the transaction.

Chargeable consideration:

	GBP
Acquisition price	1,200,000
Conditional works	40,000
5% of future proceeds*	<u>50,000</u>
Chargeable consideration	1,290,000

\*estimated future proceeds 1,000,000 for example.

SDLT:

100,000 @ 2%	2,000
1,040,00 @ 5%	<u>52,000</u>
SDLT payable	52,000

H Ltd must deliver a SDLT return (SDLT1) to HMRC within 14 days of the effective date. As mentioned above, there is scope for the payment to be deferred.

**2) VAT implications**

As mentioend above, the seller has opted to tax, but since H Ltd plans to build dwellings, the option will be dissapled. H Ltd shold provide a certificate to the seller to confirm the qualifying use of the land,and upon the recipet the seller cannot charge VAT on the sale.

The economic reality of the recharge for the construction of the road will, however, be standard rated. This is becasue it is a grant of an interest in civil engineering work, which fall outsdie the land exemtion.

Since H Ltd onward supply will likely be zero-rated first grant of dwelligns, so the relating the VAT can be recovered. In the case of exempt residential leases, the relating input tax cannot be recovered. Please note that white goods will need to be standard rated however. Also, the purchase of white goods is specifically blocked for recovery.

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-----ANSWER-5-ABOVE-----  
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-----ANSWER-6-BELOW-----  
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Answer-to-Question-\_6\_

**VAT**

White Goods and Beyond Ltd (WGB LTD) is a partially exempt since it sells taxable supplies (white goods) and exempt supplies (insurance). Since it is a partially exempt trader it can only recover VAT in line with its partial exemption method.

HMRC, following the VAT visit, have effectively questioned this partial exemption method by stating that too much VAT has been recovered. The information should be checked to see whether HMRC are correct. I have done this below:

Based on values base standard method for VAT quarter 12/20:

Recovery percentage:  $1,000,000 / 1,500,000 \times 100 = 67\%$

	Total	Taxable
Exempt		
Purchase of stock	125,000	125,000
Rent of opted property (100,000 x 67%)	100,000	67,000
33,000		
Other overheads (38,000 x 67%)	38,000	25,460
12,450		
Marketing leaflets production	7,500	7,500
Website Costs (1,000 x 67%)	1,000	670
330		

Legal services retainer (13,000 x 67%)	13,000	8,710
4,290		
Call centre costs	4,000	
4,000		
<b>Total</b>	<b>288,500</b>	<b>234,340</b>
<b>54,160</b>		

Notes:

- The purchase of stock, and marketing leaflets are all directly attributable to taxable supplies under the standard method. The leaflets are zero-rated printed matter.
- The call centre costs are wholly for exempt insurance business and therefore non recoverable as directly attributable to exempt supply.
- The remaining input tax is residual as it relates to the whole business.
- The exempt input tax is not de-minimus.

Accordingly, using the standard values based method for the recovery for input tax it appears HMRC are incorrect that WGB Ltd has recovered too much VAT.

I have also checked the figures using a used based method, should an override be required

Based on used based standard method for VAT quarter 12/20:

	Total	Taxable
Exempt		
Purchase of stock	125,000	125,000
Rent of opted property (100,000 x 3%)	100,000	97,000
3,000		
Other overheads (38,000 x 67%)	38,000	25,460

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12,450		
Marketing leaflets production	7,500	7,500
Website Costs (1,000 x 90% exempt)	1,000	100
900		
Legal services retainer (13,000 x 85% ex)	13,000	1,950
11,050		
Call centre costs	4,000	
4,000		
<b>Total</b>	<b>288,500</b>	<b>257,010</b>
<b>31,400</b>		

Notes:

- Proxy used for ret=nt of opted property is 3% of the total sq.ft usage by insurance team
- Proxy used for other overheads is income based.
- Proxy used for website is 90% for insurance use relating to 'forms'.
- Prixy used for legal services is time is hours worked. It is recommended the law firm split their invoice accordingly.

Accordingly, a standard method override is not required using a used based method. In fact, WGB Ltd's recovery position is better using a use based standard method. I see no issue with WGB Ltd current method, so it should be dicsussed with HMRC why they belive WGB Ltd current partial exemtoion method does not provide a fair and resonable apportionment of input tax. WGB Ltd should provide the calcualtions above to support that too much VAT has not been recovered in the period. Subsequently, WGB Ltd should start to use use based standard method as their partial exemotion method as this give a better recovety rate.

IPT

WGB Lld supply contracts of insurance with a UK risk, and on that basis they should be registered for IPT. Mechanical breakdown insurance is subject to higher rate IPT oof 20%. IPT is only due where the risk is located in the UK, and since the customers are habitually resident in England and Wales, this consitues a UK risk. Thereforem GWB LTd need to account for 20% IPT on the insurance premiums.

I note it is note mentioned whether GWB Ltd are registered for IPT. If not, they will need to immediatly register. There will penalties as a percentage of potential lost revenue if they are not registered for IPT.