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Institute of  
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# Application and Interaction

(Ensure this number matches your candidate number on your desk label and on your candidate attendance letter)

Centre Code

Date of Examination

Tick box if you have answered in accordance with Scots Law

Tick box if you have answered in accordance with Northern Ireland Law

## Instructions

Your script will be scanned electronically. Failure to comply with these instructions may lead to your paper not being marked. You must:

- Complete the details on this page and on the answer pages using BLACK or BLUE ballpoint pen only.
- Write on one side of the page.
- Not write in the margin areas indicated.
- If you have used additional pages, please add your candidate number and the question number to these pages.
- Do not put blank pages into the envelope at the end of the exam.

**Please do all of the above before the end of the examination.**

	Tick question attempted	For use by examiner only
1		
2		
3		
4		
5		

FORMAT & STYLE OF ANSWER	MAXIMUM MARKS	MARKS AWARDED
<p>The answer is set out in the format demanded. Thus, if it is a letter, it will be properly set out as a letter with addresses, date, "Dear X" and conclude "Yours sincerely" etc. If it is a report, it will give some indication as to what it is about and who it is for.</p>	1	
<p>The report or letter should contain an introduction setting out the terms of reference, information being relied on etc. It should also contain a summary of the key findings and recommendations.</p>	2	
<p>The body of the letter or report should be laid out in a clear way with appropriate headings so that the reader can navigate around it easily and spot the key areas without reading the entire document to try to find a discussion of, for example, income tax on some employment related shares.</p>	1	
<p>The answer "flows" so that a logical chain of thought presented to the reader rather than a series of random comments (which may nevertheless be technically correct).</p>	1	
<p>The style of writing should be appropriate to what is being produced. For example, a report to a client or lay person (which will always be the main element of a question) should not contain large numbers of legislative references whereas a technical note to the tax partner should. Technical advice should be conveyed in style appropriate to the reader.</p>	2	
<p><b>RELEVANCE OF ANSWER</b></p>		
<p>The answer does not contain large amounts of irrelevant material which would only serve to confuse a client.</p>	2	
<p>Technical knowledge (which will be rewarded through the technical marks and should not affect the awarding of these marks) has been directly applied to the specific circumstances of the reader and has this resulted in an answer tailored to their circumstances.</p>	3	
<p>The question(s) posed has/have been answered.</p>	2	
<p><b>PROVISION OF ADVICE</b></p>		
<p>The report gives advice. This means that where possible it should come off the fence and suggest the best option rather than simply giving a list of unweighted possibilities which fail to give the client an answer to their real problem: what should I do?</p>	4	
<p>Advice should include relevant and appropriate planning for the future.</p>	2	
<p>Advice should be commercial. This means that candidates should consider the bigger picture rather than narrowly focussing on saving tax.</p>	2	
<p><b>TOTAL HIGHER SKILLS AND PRESENTATIONAL MARKS</b></p>	22	

Email to Syd

To : Syd Smith

From : Tax Manager

Subject : C+K Holdings - Letter for client

Date : 8th November 2017

Attached : Draft letter for client

Hi Syd,

As requested, I have prepared the attached letter for the CEO of C+K Holdings Sdn Bhd.

Please let me know if you require any changes.

Kind Regards  
Tax Manager.

LETTER

Any Tax Advisers  
1 Central Place  
Anytown  
AS1 1AB

CEO

C+K Holdings Sdn Bhd  
First Street, Anytown  
AD12 4FG

Dear Ho Luan Dong:

Development Activities in UK

Thank you for your previous correspondence.

I have set out my advice below,  
covering your questions in the recent  
letter.

## Executive Summary

- UK branch involved in imports of hardware from Malaysia. There will be customs duty and import VAT consequences
- UK branch of holding company may be making economic activities. VAT registration should be considered.
- C+K Commercial will be incurring VAT on the development costs. The recovery of this input VAT must be maximised where possible.
- C+K Commercial may potentially be making exempt supplies. This is problematic for VAT recovery and we should address potential ways to minimise the restriction.
- C+K Residential will incur input VAT on development costs in its joint

	Venture arrangement; all of which should be recoverable	
o	All three companies will require a VAT registration to be in place.	
o	Potential for VAT grouping the 3 companies as eligibility criteria met.	
o		

① C+K Holdings Sdn Bhd - UK Branch

The first point I would like to discuss is the provision of hardware and software to the UK branch, from the head office

Initially it is important to consider whether these are considered a supply of goods or services. This will effect the VAT treatment and customs duty treatment of each.

(a) Software:

You explained that the software was developed in house in Malaysia and, for that reason, it is my understanding that this is bespoke software.

Bespoke software, for VAT purposes is a service. The supply of services between branches are not deemed supplies for VAT purposes. This is based on the ruling in the FCE Bank case, where it was

stated that the supply between head office and branch is a supply between the same legal entity. There is no VAT implications on this supply of software between the head office and UK branch.

(b) Hardware:

The supply of hardware is a supply of goods for VAT purposes. The place of supply of goods is ordinarily where the goods are located, and in this case this <sup>at time of supply</sup> would be Malaysia.

There are, however, specific rules when goods come from outside the EU. In this case, the supply is seen as in import.

When goods come from outside the EU, as is the case here, Customs Duty and import VAT will be due by the importer.



C+K Holdings will be the importer in this situation, and must deal with all the necessary customs and import VAT requirements.

In order to import goods you must obtain an EORI number.

Customs duty will be due on the goods at the point of entry into the EU (I am assuming this is the UK, in this situation).

The customs duty payable will be dependent on the classification of the goods and the valuation of the hardware.

It is important you get both of these correct to ensure you pay the correct amount of duty.

We are happy to provide any necessary help on this issue.

Goods are declared to customs on the CBS document and normally customs

duty is paid outright at import.

Import VAT is also payable on imports, ~~at~~ at the same rate as if the goods had been supplied in the UK. This is based on the correct value of goods i.e. customs value plus incidental expenses, customs duty etc.

Again, if required, we can provide advice on valuation.

Import VAT is also payable at import. There are however ways to defer payment of both duty and VAT on import, by using a deferment scheme. This gives you until the 15<sup>th</sup> of the month following import to pay.

This is beneficial for cash flow purposes. We should discuss your future plans on importing to determine whether this would be a potential option for you going forward.

Once G+K Holdings pays the duty and VAT we should consider whether any is recoverable.

Firstly, customs duty is never recoverable and will be a cost to the business. This is why it is so important to get it correct.

Import VAT is recoverable, subject to normal rules. A C79 certificate is used as evidence of import VAT paid and is issued to you by Customs.

We therefore now must consider whether G+K Holdings can recover the import VAT they incur.

## ② Activities by G+K Holdings

In order to determine potential recovery of VAT, we need to look at

The activities the holding company is carrying out. I am also aware that they are not currently registered for VAT.

(a) supplies of software and hardware to UK subsidiaries

I understand that G+K Holdings will provide the hardware and software to the UK subs from its UK branch.

Although you state that no payment is received for this, it is still deemed to be a supply for VAT purposes. As the holding company is not registered for VAT at present, there are no VAT consequences at present on these.

I would however like to know the value of these supplies to determine if a VAT registration is required on the basis of these, & if the

£83,000 threshold would be exceeded, once you make these supplies

(b) provision of management services

I also understand you will provide management services to the subs in the UK.

There is the potential for such supplies to constitute an economic activity for VAT purposes. This is dependent on the services provided ~~by~~ being a formal agreement between the two parties.

Without a charge, this may be difficult to argue.

I believe it is beneficial for a holding company to be seen as carrying out an economic activity as this allows for a VAT registration.

I therefore suggest you formalise these agreements between the UK branch and the UK subs before any supplies are made.

To do so, you should ensure a formal Management Service agreement is in place for the supplier.

This must detail the exact nature of the services to be provided, the fees chargeable and the payment schedule.

By doing so, this will provide sufficient evidence that the holding company is carrying on an economic activity.

This will allow for a potential VAT registration, if required and/or desired. I will discuss this point later in the letter.

### (c) Provision of loans

I am also aware that G+K Holdings intends on providing loans to both UK Subs to fund the projects.

There is also the potential for the provision of loans to be deemed an economic activity for VAT purposes.

For this to occur, there again must be formal agreements in place. There must be a strict and formal repayment schedule, the interest rate should be commercial etc.

I am not sure what your current plans on this are, but we can discuss further if required

branch of

3) VAT registration for UK holding company

Having looked at the supplies you propose to make from the branch, it is my understanding that there is the potential for taxable supplies to be made eg mgmt services

The provision of taxable supplies allows for a VAT registration for the ~~branch~~ company.

A VAT registration would be beneficial as it would allow for recovery of the import VAT incurred on the hardware.

I advise a VAT registration is obtained for this company



(4) CHC Commercial

I understand this company will be involved in 2 development projects:

- ① Office Park
- ② Financial District

I will look at each in turn.

(a) Office Park:

Looking initially at the acquisition of the site, I understand no VAT was incurred on the purchase of the site.

This is beneficial as we do not have to consider whether input VAT would be recoverable.

As you are ~~constructing~~ refurbishing offices to be used as offices again, the costs of such work will be subject to VAT at the standard rate.

When looking at the construction of the new offices, again the costs of such work will be subject to VAT at the standard rate.

As all costs of construction and renovation on this site will incur VAT at 20%, we must determine the best way of recovering such VAT incurred.

In order to recover input VAT, the new offices must be used for making taxable supplies.

You have advised that you will let these offices out to professional services firms and retail outlets.

These tenants will be fully taxable and will be able to recover any VAT you charge them.

For this reason, I suggest that you opt to tax each of the offices (OTT). By doing so, you can treat the supplies as taxable supplies.

Without the OTT, the leases would be exempt, preventing VAT recovery.

By making taxable supplies, you will be entitled to full input VAT recovery on the costs incurred.

As can be seen in Appendix 1, you will incur input VAT of £250,000 in 2019 on this construction work.

It is therefore important that we ensure you can recover this VAT.

In order to make taxable supplies and allow for input VAT recovery, we need to ensure a VAT registration is in place for C+IC Commercial.

You cannot do this at present as you are not currently making taxable supplies, however you will be able to register as an intending trader.

You will be able to evidence your intent of trading once your option to tax is in place on the buildings as discussed.

Again, referencing the £250,000 of ~~work~~ input VAT that will be incurred in 2019, this should be recoverable in full as it relates to the taxable leases that you will be making of the offices in 2020.

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You should ensure the VAT registration of the company is in place before these costs are incurred to allow for input VAT recovery promptly.

The leases/agreements between you and the tenants should also provide sufficient evidence that you are an intending trader, allowing for a VAT registration before you make your first taxable supply.

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(b) Financial District :

As you will be involved in the construction of new commercial buildings, all ~~VAT incurred will be at the standard rate~~ construction costs will incur VAT at the standard rate.

Again, it is important we try to recover this VAT, where possible.

Looking at Appendix 1, you will incur VAT of £250,000 on this work in 2019.

You have advised that your tenants or those of offices will be banks and insurance companies i.e. partially exempt businesses.

They will not find VAT on the rents attractive, so an OTT would not be commercially wise in this situation.

On this basis, the leases you grant will be exempt.

This means the £250,000 of input VAT will be directly attributable to exempt supplies, and not recoverable.

We would need to determine a way in which you could make a taxable supply of these offices:

(i) firstly, would it be worth considering whether you should opt the offices?

We should commercially consider whether this would deter tenants.

Perhaps, the price could be arranged to cover the additional VAT charge so the tenant does not suffer.

i.e. drop the price (NET) so that the gross price remains same for tenant.

Therefore, there will be no worse off even though you have opted the

buildings.

You however must account for 1/6th of the rent as output VAT

By doing this, you would, with your taxable leases, remain a fully taxable business and could recover input VAT in full.

It could however, negatively effect your profit margin to the extent that it outweighs your VAT recovery advantage.

If you desire, we can look in both this option further.

(ii) Alternatively, you could restructure the development project, so that you construct the offices, make a freehold sale (taxable) of new commercial property to a connected party who then leases the offices to the tenants.

Again we can look at this further. We must be aware that often the



corporate tax consequences in this situation outweigh the potential VAT benefits

This is because you will have to account for corporate tax on the disposal to the connected party.

This will also lead to <sup>VAT</sup> recovery issues for the connected party.

(iii) Another option is to OTT the offices, lease to a connected party who will then make the exempt leases to the tenants.

This would allow for your recovery on the construction costs again as you will make taxable supplies

Overall, I feel it would be beneficial to make taxable supplies of the offices in the financial district due to the

value of the input VAT incurred on construction.

I do however feel that before any decision is made on how we could do this, we look at all tax and commercial implications of the proposal. Perhaps, the £250,000 input VAT loss is just something that just has to be accepted.

### 5) Corporate tax implications for G+K Commercial

→ capital allowances will be available on certain expenditure when constructing + refurbishing  
 on Plant + Machinery  
 on fixtures and fittings

→ once developed, the properties are to be retained as investments. This will require movement on the balance sheet so that they are held in fixed assets.

the properties will need to move from current assets to fixed assets at market value. A gain is likely to be recognised, on which corporate tax will be chargeable @ 20%

6) Other tax implications for C+K Commercial

→ A number of the offices and properties are likely to fall within the capital goods scheme. Adjustments must be carried out for those over a 10 year period, depending on taxable activity each year.

The scheme begins when the assets are first used i.e. in 2020 when leases are granted to tenants

## 7) C+K Residential

I understand this company will be involved in the provision of design and construction services.

You will be supplying these to a developer who is building new dwellings to sell on.

The services you provide will qualify for VAT at the ~~8%~~ zero rate under VATA 1994 Sch 8 Group 5

You will incur VAT at the standard rate on your building costs of £1,000,000. The VAT you incur will be £1,66,667 in 2019.

You will want to recover this input VAT so a VAT registration will be required.

You should register this company as an intending trader once you incur the costs.

The input VAT incurred will be directly attributable to your taxable supplies to AB Land and recover in full.

The company will receive proceeds of £1,500,000 in 2020 from the sale of the dwellings by AB Land.

This sale will qualify for zero rating so no output VAT will be due on this income.

This is because the supply ~~is~~ is the first grant of a major interest in a newly ~~developed~~ constructed dwelling.

## ⑦ Potential VAT grouping:

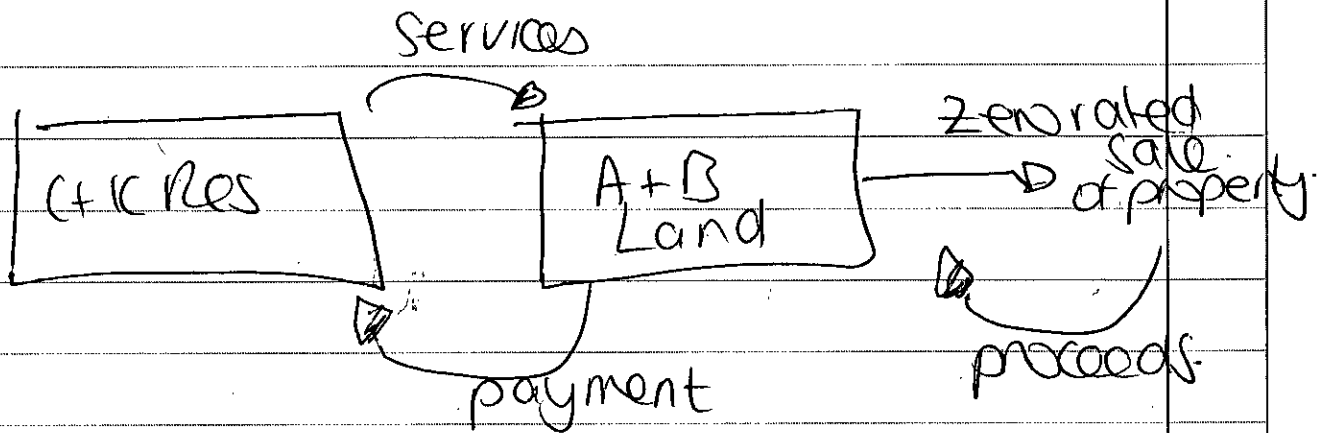
As all companies would ~~benefit~~ need to be VAT registered (as earlier discussed), we should also consider the potential of VAT grouping all of the 3 companies as they meet the eligibility criteria.

One benefit is that any supplies between group companies eg management services would be disregarded for VAT purposes.

However, as C.K Commercial may be making exempt supplies to tenants (financial district), this may affect input VAT recovery for all companies.

Due to this, I see no real benefit in VAT grouping and feel all companies should ~~remain~~ <sup>be</sup> separately VAT registered.

9) Corporate structure for joint venture



- The two companies should remain separate corporate entities
- A+B Land will be responsible for the CT implications of the sale as they are disposing of the property held in their name.
- C+K Res will simply provide the services and receive payment for those services
- Proceeds from dwelling buyer provided directly to A+B Land.

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I hope this has been helpful

Kind Yours Sincerely

Syd Smith

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Appendix 1 - CK Commercial

(Assuming all figures provided are VAT inclusive)

Review of income + expenditure

2017 :

Income = £7,500,000 loan from parent  
 → non business income

expenditure = £250,000 professional cost.  
 - these will have incurred VAT at the standard rate  
 VAT incurred = £ 41,667

As they are making notaxable supplies in 2017, a VAT registration will not be required. As they are not VAT registered so this input VAT may not be recoverable.

2018:

- NO income
- NO input VAT incurred <sup>on land cost</sup> as no input VAT charged on land acquisition
- £1,000,000 spent on library construction  
∴ VAT of £166,666 incurred.

2019:

- NO income.
- input VAT incurred on construction of:
  - (a) office park - £1,500,000 spend  
= £250,000 VAT incurred
  - (b) financial district - £1,500,000 spend  
= £250,000 VAT incurred

2020 :

→ Taxable income of 600,000 (provided  
OTT is put in place on office park development.)

→ Exempt income of 600,000 (potentially).