



Association of Taxation Technicians

Examination

May 2007

PAPER 5 – PART II

VAT

TIME ALLOWED – 3 HOURS
(for Part I and Part II)

- You are required to answer **all** questions in Part I (printed separately) and Part II.
- The maximum number of marks for each question in Part II is shown in brackets.
- For Part II, start each answer on a new sheet of paper.
- All workings should be shown and made to the nearest month and pound unless the question requires otherwise.
- Marks are specifically allocated for good presentation.

1. You have recently received an email from one of your dearest friends, John Macey. Two years ago he started a small double glazing firm and, due to the great customer service that he provides, the business has become extremely successful.

“Dear Fred

I hope that you don't mind me emailing you like this – I could do with a little advice.

As you know my focus, since starting the business, has been on the service that I provide to my customers and I have been having some difficulty keeping my financial records up to date.

Over the past twelve months or so, the VAT returns have been completed and submitted (however not always on time!) and I have received various letters from HM Revenue & Customs, including penalties which seem to be extremely large. I do not understand all of the paperwork and terms used and would be grateful if you could enlighten me and confirm that the penalties have been administered correctly.

For information, the VAT returns were submitted as follows;

<u>VAT Return</u>	<u>Submitted</u>	<u>Paid</u>	<u>Output Tax</u> £	<u>Input Tax</u> £
December 2005	31 January 2006	31 January 2006	250,000	57,000
March 2006	5 May 2006	5 May 2006	420,000	74,000
June 2006	31 July 2006	7 August 2006	474,000	96,000
September 2006	30 October 2006	30 October 2006	555,000	320,000
December 2006	14 February 2007	14 February 2007	780,000	222,000

Is there any way that I can get the penalties rescinded – it is hard enough building a business as well as trying to keep on top of all of the paperwork!

In August 2006, I was lucky enough to win a new contract – however I was so busy, that although I raised the invoice, I forgot to account for the output tax in the VAT return. The value of the contract was £1million plus VAT. I am considering just putting this omission on my next VAT return – can you confirm that this is acceptable?

I look forward to hearing from you soon.

Kind regards

John”

You are required to draft a response to John. Your reply should:

- 1) Explain when VAT returns should be submitted and outline the rules regarding default surcharges. (8)**
- 2) Explain the default surcharge consequences of each of the VAT returns submitted by John. (4)**
- 3) Explain whether any of the penalties incurred may be rescinded. (4)**
- 4) Explain how John should account for the output tax still due and whether any penalty may be incurred in relation to this. (4)**

Total (20)

2. Modcon Ltd makes a mixture of exempt and taxable supplies. On 8 July 2003 the company bought a new computer for £100,000 plus VAT. The taxable use of the computer was as follows:

VAT year ending 31 March 2004 = 50%

VAT year ending 31 March 2005 = 45%

VAT year ending 31 March 2006 = 60%

Modcon Ltd sold the computer for £8,000 plus VAT on 15 August 2006. Taxable use from 1 April 2006 until the date of sale was 40%.

You are required to:

1) Calculate, with explanations, the input tax adjustments needed in each of the relevant VAT years. (9)

2) State on which VAT return the final adjustment should be made. (1)

Total (10)

3. You have received the following note from one of your VAT registered clients, Sir Lostalot. The client file shows that Sir Lostalot has not elected to waive exemption on the Hall.

“Ted,

My inheritance has all gone in taxes and I need to raise some cash from the Estate. I want to get the VAT right because I do not want any more unexpected tax bills. Please could you tell me what the VAT liability will be on the proposed income? I have heard that income from property is VAT exempt – is this true?

I am going to have paying guests in the Hall for bed and breakfast at £80 a night and will also let it out for conferences at £100 per delegate per day – including use of the ballroom for the conference and lunch in the dining room. I am also opening the Hall to the public a few times a year. Probably charge £5 a head. If I say a £5 minimum donation is required, will it be VAT-free? I think that is what they do at some places.

I am levelling the top field and will hire it out for rugger and football matches. At least one of the local schools has said that they will use it every week during term time. The other users are more likely to be one-offs. Might as well put the river to good use too, the salmon runs are terrific in season. Thought I would let the local gentry hire individual stretches of the bank for a season at a time. I hope they will not be put off by the campers on the riverbank. In the past you told me to charge VAT on the money I get from hiring out pitches for tents, but surely that is just land too and should be exempt?

Finally, you may have noticed that I am doing up the stable block and the old gardener’s cottage. I intend to charge people to keep their horses on the Estate. The owners will not be allocated any set stable as we need to move the horses round, just certainty that their horse will be in covered accommodation overnight – they will be in the fields most days. I am not sure what to do with the gardener’s cottage. It will either be advertised and let out to holiday makers or I might let it to one of the families in the village. Again, will all these items be exempt as they are property related? I also need to rationalise my land holdings. So I am selling those two office buildings which we own in the village. Shame really because one was only built last year. The other has been there for years and it is a bit tatty. I am wondering if I should refurbish it first. If I do, can I get the VAT back on the cost of works? If so, how, and are there any drawbacks?

I think that’s all for the time being.

Yours etc

Larry Lostalot”

You are required to draft a letter to Sir Lostalot replying to his questions and giving reasons for your advice. (20)

4. Several interested businessmen from your local round table group have invited you to explain to them some of the VAT issues involved when doing business with foreign companies. To help you prepare for the event some of the members have sent you specific questions in advance.

You are required to draft responses to these questions:

- 1) **My firm has been awarded a very significant contract by a UK VAT registered company to erect a series of stages at exhibitions all over Germany. Are there any VAT implications that I should be aware of? (2)**
- 2) **The business I manage is not VAT registered as it operates just below the VAT registration threshold (and would be partially exempt anyway). Could I save money by employing an Indian accounting firm to provide VAT-free services from India? (3)**
- 3) **On a recent business trip to Spain, I incurred significant expenses with Spanish VAT on them. Is there a process whereby I can reclaim this and, if so, can you tell me what it is? (3)**
- 4) **I am considering buying & importing some electrical goods from China for resale in the UK. How will these goods be valued for VAT purposes? (2)**

Total (10)