



Association of Taxation Technicians

Examination

May 2007

PAPER 5

VAT

ANSWERS
(without marking guide)

Answers

1. Tax Points

The first tax point is on 15 May 2006 when payment is received.

The tax due is $\text{£}2,000 \times 7/47 = \text{£}297.87$

The second tax point is the day of collection, 30 June.

The tax due is $\text{£}6,000 \times 17.5\% = \text{£}1,050 - \text{£}297.87$ (already paid) = $\text{£}752.13$

2. Reclaimable Input Tax

Input tax is not recoverable on:

The purchase of the car as input tax is blocked on cars with private use.

The restaurant meal as input tax is blocked on business entertainment.

The unpaid tax invoice which is one year old as it is subject to bad debt relief restriction.

3. Colin's Corner Shop uses Apportionment Scheme

a) Proportion of standard rated purchases = $\text{£}60,000 / (\text{£}60,000 + \text{£}20,000) = 75\%$

Proportion of standard rated sales = $75\% \times \text{£}120,000 = \text{£}90,000$

Output tax liability = $\text{£}90,000 \times 7/47 = \text{£}13,404.25$

b) An annual adjustment is required as it ensures that any distortions in the expenditure pattern in individual quarters is smoothed out by calculating the figures over a full year.

4. Less Detailed Invoice

A less detailed invoice must contain:

- The name and address of the supplier
- The registration number of the supplier
- The time of supply
- A description of the goods or services
- The total amount payable including VAT
- For each rate of VAT, the gross amount payable and the rate of VAT applied.

The maximum value is $\text{£}250$.

5. The $\text{£}2,200$ payment is allocated on a FIFO basis therefore:

	Net	VAT	Gross	Payments on account
16/04/06	790	-	790	790
22/05/06	1,000	175	1,175	1,175
18/08/06	400	70	470	235
24/09/06	1,240	217	1,457	
18/08/06	$(470-235) \times 7/47 = \text{£}35$			
24/09/06	$1,457 \times 7/47 = \text{£}217$			

Total claimed in VAT return period to 30/4/07 = £252

6. Advantages include any two of the following:

- i) Supplies between group members are normally disregarded for VAT purposes.
- ii) Only one consolidated VAT return needs to be declared.
- iii) Centralisation of VAT affairs.
- iv) Can include exempt companies which otherwise would not be able to register and therefore possibly allow greater input tax recovery (see disadvantage).
- v) Higher tax turnover will increase the threshold for misdeclaration penalties.

Disadvantages include any two of the following:

- i) Joint and several liability
- ii) Inclusion of an exempt business will make the group partially exempt, which may reduce the input tax recovery.
- iii) Cash flow advantages may be lost (e.g. loss of repayments to zero-rated companies)
- iv) Centralisation of VAT affairs to allow production of one return may create problems with timing and collection of the separate figures.

7. Significant known or anticipated non-business use of the van would mean that full deduction of input tax on the purchase, without any adjustments to account for the non-business use at any stage, would be incorrect.

One option would be to make an initial reasonable adjustment to the input tax to account for the anticipated personal use by employees.

As an alternative, the Lennartz mechanism would allow the business to keep all the original input tax, but account for output tax on the non-business use of the van as a supply of services (usually based on straight-line depreciation over 5 years).

8. Kall Kwik Answers

a) The company's partial exemption percentage is

$100/120 = 83.3\%$. This must be rounded up to 84%

Exempt input tax

$£7,500 \times 16\% = £1,200$

Directly Attributable = 350

Total Potentially Irrecoverable = £1,550

So long as the relevant input tax in any period is less than both;

- £625 per month on average; and
- one half of all the input tax for the period concerned

all such input tax in that period is treated as attributable to taxable supplies.

All the exempt input tax is de minimis, therefore the total input tax is recoverable = £37,850

b) The annual adjustment must be completed on the first return of the next VAT year, which in this case is June 2007.

9. TOGC Answers

a) Any VAT liability will be transferred to the new owner

b) Any records should be transferred to the new owner. The new owner takes over the obligation to keep and preserve them.

If both parties agree the vendor may keep the records – however HMRC must be advised of this.

c) Business records have to be kept for six years unless HMRC have agreed a shorter period.

10. EU Law Answers

If a provision of community law has direct effect, it gives rise to rights or obligations which an individual may enforce before the national courts.

Direct applicability means that a regulation automatically becomes part of national law, without intervention by the authorities of the Member States.

11. The main aim of a letter of engagement is to set out the terms of business and the scope of the engagement.

It should include as a minimum:

- The nature of the services to be provided;
- The responsibilities of the client, including the obligation to provide full information
- Quality of service and complaints procedures
- Fee arrangements

12. When faced with a conflict of interest of this nature your choices would be:

- To act for neither party.
- To advise both clients of the conflict and give both the opportunity to consider whether or not they wish you to act or whether they wish to seek alternative representation.
- To act for only one client (generally this will be the client who first sought advice).

13. Any four of:

Clients should be advised in writing of the name and status of the person to be contacted in the event of a complaint.

Clients should be advised of their ability to complain to the ATT.

The complaint procedure should be included in the engagement letter.

Complaints should be acknowledged promptly in writing.

Complaints should be investigated thoroughly and promptly by someone not involved in the act giving rise to the complaint.

Clients should be advised of the investigation and its outcome.

Appropriate action should be taken if the complaint is upheld wholly or in part.

Q1

To: John Macey
From: Fred Bloggs
Subject - VAT query

It was great to hear from you. Congratulations on the success that you are having with the business.

Before going into detail with regard to the implications of each VAT return, I thought that I would provide you with some information in general.

Completion of VAT returns

VAT return should be completed and paid to HMRC on a timely basis. For information, the VAT return must reach HMRC by the due date not later than the last day of the month following the end of the return period.

Surcharge Liability Notice

A surcharge liability notice is issued when HMRC does not receive either or both the payment and return by the due date.

A surcharge liability notice lasts from the date of the notice to the first anniversary of the last day of the VAT period which was late

Any subsequent late submission or payment in a 12 month period will result in the Surcharge Liability Notice period being extended for a further 12 months and a default surcharge may be incurred.

Default Surcharge

A default surcharge is levied when a business is within a Surcharge Liability Notice period and fails to make payment of a VAT return by the due date.

The default surcharge is calculated at a percentage of the tax due and increases on each default. The rates are 2%, 5%, 10% and 15%

HMRC will not issue a surcharge assessment at the 2% or 5% rates for an amount of less than £400.

VAT Returns

Given the details that you have provided, I have summarised the implications of each of the VAT returns;

VAT Return	Submitted	Paid
12/2005 On time	31/01/06	31/01/06
03/2006 Late SLN issued to 31/03/2007 – no default surcharge	05/05/06	05/05/06
06/2006 Payment Late – SLN extended to 31/07/07 Default surcharge (£474 - £96) x 2% = £7,560	31/07/06	07/08/06

09/2006 30/10/06 30/10/06
On time (½mark)

12/2006 14/02/07 14/02/07
Late – SLN extended to 31/12/2007
Default surcharge (£780 - £222) x 5% =£27,900

Reasonable Excuse

In deciding whether or not to reduce a penalty, HMRC will take into account whether the circumstances giving rise to the default could have been foreseen and, if so;

- what steps were taken to make alternative arrangements
- whether HMRC were contacted
- whether sufficient priority was given to completing the VAT return
- and whether VAT was paid by the due date

Examples of reasonable excuse are;

- Computer breakdown
- Illness
- Loss of key personnel
- Loss of records

Please advise if any of the above applied to your business in the period affected. If not, it would be highly unlikely that HMRC would accept reasonable excuse do not fall into any of the above categories

New Contract

It is noted that you have failed to account for VAT of £175,000 on the September 2006 VAT return.

Due to the size of the error, it being greater than £2,000 this must be reported to HMRC via a voluntary disclosure.

You should also note that if the error is not voluntarily reported to HMRC it may be subject to a misdeclaration penalty, which is administered, in this case, if the error exceeds the lessor of;

- £1million; or
- 30% of the gross amount of tax (the total amount of input tax and output tax that should have been reported in the period)

I have completed the calculation and am happy to confirm that in this case a misdeclaration penalty will not be applicable.

$30\% \times (555,000 + 320,000 + 175,000)$

However, you will incur interest when payment is made to HMRC.

Please give me a call if you would like to discuss.

Q2

1) The computer is **worth more than £50,000** and therefore is a capital item under SI 1995/2518 Reg 113a and is subject to input tax adjustments over a **period of 5 years** Reg 114 (3) a.

- Interval 1: VAT year ending 31/3/04 = £100,000 * 17.5% = £17,500 then * 50% = **£8,750 recoverable from HMRC.**
- Interval 2: VAT year ending 31/3/05 = (£17,500/5) * (50%-45%) = **£175 to be repaid to HMRC.**
- Interval 3: VAT year ending 31/3/06 = £3,500 * (50%- 60%) = **£350 to be reclaimed** from HMRC
- Interval 4: In the year of sale, the asset is treated as if it was used for the whole of that interval i.e. to 31/3/07 = £3,500 * (50%-40%) = **£350 to be repaid to HMRC**
- Interval 5: Final adjustment = £3,500 * (50% -100%) * 1 year left = **£1,750**
- However due to SI 1995/2518 Reg 115 (3) the sum reclaimed from HMRC will be limited to £8,000 * 17.5% = **£1,400**

2) The £1,400 (final adjustment) should be reclaimed in **VAT period 9/07**, i.e. the second VAT period following the interval in which the supply as a result of a sale relates.

Q3

Ted Accountant
Address
Date

Sir Lostalot
{address}

Dear Sir Lostalot,

Thank you for your recent note. I am setting out below the VAT treatment of the various activities you enquired about.

You are correct to state that income from property is often exempt, but there are exceptions to this rule and these will affect many of the activities you propose.

The hire of rooms in the hall for bed and breakfast will be liable to VAT as income from accommodation provided in a hotel, inn or similar establishment is not exempted. However, the income from day delegates will be partly exempt and partly liable to VAT. This is because some of the charge is deemed to represent hire of the Hall which is exempt and some a charge for catering which is liable to VAT. Admission to the premises is also liable to VAT. The income could only be treated as a donation if it was genuinely a voluntary payment. A 'minimum' donation implies that the payment is compulsory and therefore VAT should be charged on this income.

The rules applicable to sporting facilities are unfortunately more complicated. If you make a series of ten lets or more at a time to the local school, then it will be exempt provided there is no more than two weeks between each let. (This could be an issue in holiday periods). Other occasional lets of the sporting area will be liable to VAT. The letting of fishing rights is also liable to VAT and I confirm the advice previously given that income from the letting of pitches for tents is also

liable to VAT as, although it is income from land, it is an item which is specifically identified as not being exempt.

The income you earn from stabling horses will not be exempt from VAT as you are not granting an interest in any specific area of land.

The future use of the cottage will determine whether or not VAT is charged. Long term lets as living accommodation will be exempt from VAT, but if the property is advertised as being holiday accommodation then the income will be liable to VAT.

In respect of the office buildings, the newest building will be liable to VAT as the sale of a new commercial building cannot be exempted. 'New' applies to any commercial building which is less than three years old.

For the other building, the sale will be exempt from VAT unless you elect to waive the exemption. If you waive the exemption, then you will need to charge VAT on the sale price. This will make the property less attractive to businesses that cannot reclaim VAT, either because they are not VAT registered or they make exempt sales. It will, however, enable you to reclaim the VAT incurred on the refurbishment. If you do not waive the exemption, then you will not be able to reclaim the VAT on this expenditure

I hope that this answers your questions, in full but if you require further information please do not hesitate to ask.

Yours Sincerely

A Candidate

Q4

- 1) The place of supply for services relating to exhibitions is where the work is performed which in this case would be Germany. The supply would be outside the scope of UK VAT, but may result your business becoming liable to registration in Germany for German VAT (subject to local registration thresholds). The advantage of registration in Germany would be to allow recovery of German input tax through the German VAT return.
- 2) No. This is because accountancy is a Sch. 5 service and is therefore considered supplied where received, in this case by you in the UK. If you were registered you would need to account for VAT on this transaction using the reverse charge procedure which would mean you must account for output tax in Box 1 of your VAT return, calculated on the full value of the supply received, and include the VAT as input tax in Box 4 correctly apportioned against relevant exempt supplies. You would also include the full value of the supply in both boxes 6 and 7. Although you are currently not registered you should note that if this reverse charge adds sufficiently to your taxable turnover then it would make you liable to register for VAT and suffer the input tax attributable to your exempt supplies
- 3) The process you need to follow to reclaim your Spanish VAT is called an 8th Directive claim. You must be VAT registered in the UK and you are required to complete a claim form, which will be available from the Spanish authorities and

send it to the address they specify. With this form you must also provide proper evidence of the purchases made. The Spanish authorities must repay the VAT within six months of receipt if they are satisfied with your claim

4) The value of the goods on importation from China into the UK will be calculated as follows:

- a) The price in money paid for the goods.
- &
- b) All taxes, duties and other charges levied on importation of the goods into the EC (other than VAT).
- &
- c) All incidental expenses such as commission, packing, transport and insurance costs up to the point of arrival in the EC.

The import VAT on these goods will be calculated on the sum of a, b & c added together.