

PUBLIC POLICY AND TAXATION

**Professional 2
December 2002**

MARKING SCHEME

The logo for CIPFA, featuring the letters 'CIPFA' in a serif font. The letter 'I' is stylized with a decorative flourish that loops over the top of the 'P'.

Answers to Public Policy examination questions, especially to those parts requiring analysis and evaluation, are inevitably shaped by the personal subjectivity of candidates. This individual subjectivity is welcome, but it does mean that it is not possible to produce a marking scheme that is fully comprehensive. Credit will always be given to candidates for points not included in the marking scheme but which, nevertheless, are relevant to the questions asked.

Question 1

(a) Traditional Public Administration/Liberal Democratic Model

Ministers are responsible for policy formulation and to Parliament for the conduct of their Departments.

Civil servants are answerable to Ministers and provide neutral advice to them and implement ministerial policy.

½ mark for identifying model, up to a 1½ for description

Liberal Bureaucratic/New Administration Model

Does not exclude the possibility that a Minister may dominate and impose his/her will on a Department.

However, it suggests a variety of factors (eg numbers, permanence, expertise, control of information) that tilt the balance of power in favour of civil servants.

It portrays a fundamentally adversarial relationship between civil servants and ministers where civil servants often obstruct and/or sabotage ministerial decisions.

½ mark for identifying model, up to 1½ for description

“Whitehall Village” Model

The relationship is more complex here.

Relationships are both cooperative and adversarial and operate across Departments as well as within them.

Civil servants, through their common culture and networks of contacts, prepare the ground for ministerial decisions.

½ mark for identifying model, up to 1½ for description

Power-Bloc Model

Seeks to portray civil servants as an “establishment” veto group, reflecting that the composition/structure of the civil service has traditionally been dominated by individuals from privileged economic backgrounds.

Civil servants deploy their administrative expertise and exploit their permanency in order to facilitate reactionary policy and thwart radical policy.

½ mark for identifying model, up to 1½ for description

Bureaucratic Over-Supply Model

This model is linked to the right-wing critique of Big Government, prevalent since 1970.

It proposes that self-interested civil servants seek to maximise their own interests (eg status, pay, other employment conditions) and to exploit sources of power in their relationships with Ministers.

This has led to the creation of an excessively large, bureaucratic civil service.

½ mark for identifying model, up to 1½ for description

(10)

- (b) *This question requires candidates to analyse the balance of power, in the UK governmental decision making process, between Ministers and civil servants. The “textbook answer” to this question is shown below. But the “textbook answer” is extremely detailed and unlikely to be reproduced even by excellent candidates. Candidates’ answers will be shaped by their own subjectivity and full credit will be given for relevant points not included in the marking scheme and for answers which focus on and evaluate only those models perceived as the best explicators of the civil servant/minister relationship.*

1 mark for each relevant point up to a maximum, of 3 marks per model and overall maximum of 15

In the late 1970s, the civil-servants/Ministers relationship was frequently portrayed (especially by the Labour government, looking for scapegoats on whom to blame policy failure) as resembling either the liberal bureaucratic or the power bloc models.

The main factors which, at that time, were seen as tilting the balance of power away from Ministers to civil servants included: the large numbers of civil servants relative to Ministers; the permanent status of civil servants; the expertise of civil servants; the networking and co-coordinating role of civil servants; civil servants’ control of information; civil servants’ ability to delay policy implementation; the multiplicity of demands (and hence large

workloads) of Ministers; and the fact that few Ministers had been trained for office or had any expertise relating to their Departments.

Civil Service reforms since 1979 aimed at curtailing civil servants' privileges, increasing the efficiency of "Whitehall" and transforming the culture of civil servants have probably resurrected the **traditional liberal democratic/public administration** model as the best explainer of the current relationship between civil servants and ministers.

The Conservative government led by Mrs Thatcher reasserted control over the Civil Service, inspired by New Right theory. Subsequent governments, regardless of their political persuasion, have not sought to reverse this process.

These reforms were in part inspired by perceptions that the civil servants-Ministers relationship resembled the **bureaucratic over-supply** model. Although the model was politically influential, few academics now consider it of value in explaining the behaviour of civil servants. The motivation of officials cannot be reduced to departmental empire-building and the key Whitehall departments have always been – and remain – small departments such as the Treasury.

Indeed, many analysts argue that governments' New Right approach to the civil service has pushed the civil-servants/Ministers relationships beyond the traditional liberal democratic/public administration model. In particular, it is often argued that the civil service's traditional detachment and impartiality has been eroded, with the civil service becoming politicised.

This does not mean that policy making is totally the preserve of Ministers while civil servants are limited to a purely administrative role. Instead it means that Ministers' influence is primarily over the relatively small number of top Departmental decisions and over the formulation of policy strategy.

It is argued by some that traits of the **power bloc** model are still discernible. It remains broadly true that the higher civil service is largely recruited from socially privileged groups. But such groups no longer refuse to carry out radical government policy, curb the reformist ambitions of radical politicians or constitute a monolithic bloc in terms of views and perceptions.

Some analysts argue that the **liberal bureaucratic** model still retains validity as an explainer of the civil servants-Ministers relationship. It remains relevant in those situations where weak Ministers are "captured" by their civil servants and also to describe occasions when the scales of Departmental power tilt towards the civil servants. However, the reassertion of political control over civil servants means that the liberal bureaucratic model is now applicable in relatively few instances.

The **Whitehall village** model draws attention to the cooperation between Ministers and civil servants within Departments and to the role of inter-Departmental collaboration in preparation for decision making. There is a sense in which a “single government community” exists, characterised by agreement on the rules of the game and on the desirability of excluding outsiders. However, the Whitehall village model is criticised as being too limited to capture the reality of the “single government community”. In particular, it ignores the “community’s” external relationships such as those with pressure groups and ideological think tanks.

The lines of conflict are now rarely between Ministers and their civil servants within a Department but rather between Departments. Each Department’s Ministers and civil servants combine to advance and defend Departmental interests against Ministers and civil servants in other Departments combining to do the same.

(25)

Question 2

- (a) *½ mark for each institution/organisation identified and a maximum of 1½ marks for discussion of each institution/organisation up to an overall maximum for part (a) of 9 marks*
Other relevant institutions/organisations, not explicitly incorporated in the marking scheme, to be awarded credit, subject to the overall maximum of 9 marks
Pragmatism needed over interpretation of institution/organisation

Parliament

Debates and votes upon Government's annual tax and spending plans.

Power to influence is dependent on size of Government majority in the Commons.

But it is argued that Parliamentary scrutiny of government policy proposals is being steadily reduced. This reflects the increased role of the media in policy debate; and the fact that many of the more detailed aspects of policy implementation and change occur without parliamentary scrutiny.

Core Executive

Much policy is initiated by the Executive.

The adequacy of the core executive in formulating and implementing economic policy is normally a key issue in general elections, and usually dominates election manifestos.

Civil Service

The Treasury and many of the major spending Departments (education, health and social security) usually have a major impact on policy.

Departmental spending is determined via the Comprehensive Spending Review, hence, the treasury is very powerful in determining economic priorities and resource allocation.

Pressure Groups

This category can include sectional groups (eg TUC, CBI, BMA, NUT) and cause groups (eg Greenpeace, BMA). Pressure groups which are "insider groups" have far more influence than those which are "outsider groups".

Amongst these groups, the unions used to be highly influential, but have over the past 15 years suffered a significant loss of power and standing.

Industry lobby groups tend to be influential. For example, the CBI is believed to be having a major impact on the Blair Government's attitude towards the UK's future membership of the Euro.

Quangos

A good example is the Bank of England which, although having to achieve inflation targets set by the Government, has independence in terms of formulating and implementing monetary policy aimed at meeting the inflation target.

Media

The national press in particular frequently initiates/sustains campaigns on economic issues. Good examples here are believed to be Government attitudes towards pensions and Euro-membership policies.

The media, as commentators on government policy proposals and implementation, frequently influence change in official policy.

- (b) Fiscal policy involves management of the UK economy through the manipulation of taxation and public spending. 1

In practice, since the early 1980s UK governments have focused their attention on supply-side economic policies and tools. This has effectively relegated/limited the role of the revenue component of fiscal policy to securing a balanced current budget over the medium term. However, the capital budget is not required to balance. This facilitates expansion in capital expenditure from time to time, such as that recently announced for education, the NHS and transport. 2

Monetary policy involves the management of liquidity, economic activity and inflation through the adjustment of interest rates. 1

In the UK, it is the Bank of England that sets interest rate levels through the interest-rate maneuvering of its Monetary Policy Committee. MPC interest-rate decisions are shaped by the Government which sets inflation targets (currently on RPIX of 2.5%) and holds the MPC accountable for achieving these targets. 2

(6)

- (c) *This is an open-ended question in which candidates are required to select, briefly describe and comment upon the significance of two major structural economic changes that have occurred in the UK in recent decades.*

1 mark should be awarded for each relevant point made, up to a maximum of 3 marks per structural change and 6 marks in total.

Each candidate's choice of two structural changes is likely to be drawn from the following, but full credit should be awarded for alternative, relevant changes.

The relative decline of the manufacturing sector and the relative growth of the services sector.

A large-scale shift of ownership from the public to the private sector.

Significant increases in both inward and outward capital investment.

The discovery and development of offshore oil and gas resources.

Important labour-market changes including declining employment in manufacturing, greater flexibility (eg multi-skilling and part-time working) and a rise in self-employment.

Changing long-term patterns of trade, and consequent changes in both the current and capital accounts of the balance of payments.

The UK's growing integration with Europe, as what was originally the European Coal and Steel Community (which did not include the UK) has evolved into becoming a single European market.

Growing prosperity for the UK population (ie faster GDP growth and increased per capita GDP wealth) alongside (paradoxically) relative UK economic decline in an international context.

Domestically, a (questionable) growing division between the relative prosperous South and the less well-off North.

- (d) The dilemma this posed for the MPC was how to respond to simultaneous pressures (from within and outside the MPC) for both higher and lower interest rates. 1

The recession in the internationally-exposed manufacturing sector generated pressures from the "doves" for lower interest rates. This would help the manufacturing sector by reducing its debt-servicing costs and by lowering the value of the pound to make exports more price competitive and imports less price competitive. 1

The consumer spending boom was largely underpinned by rapid personal credit expansion. This generated pressure from the “hawks” for higher interest rates in order to dampen demand and thus reduce the risk that rapid consumer spending and debt accumulation would generate inflationary pressures and push the RPIX above its 2.5% target. 1

In mid 2002, the MPC’s dilemma was compounded by the global equity market setback which threatened to undermine the economic recovery. 1

(4)

(Appropriate credit to be awarded to candidates who focus of manufacturing sector’s problems in terms of weak exports and competition from rising imports)

(25)

Question 3

- (a) *½ mark for identification of each role. Up to 1½ marks for discussion of each role, subject to an overall maximum of 8*

Service Provision

The planning and provision, directly or indirectly, of individual local services.

Regulation

The regulation of the economic behavior of individuals or other agencies in the public interest by insisting on their compliance with standards, rules and procedures of various kinds for exchange or provision of goods or services. This is where the licensing, inspection, monitoring, registration and certification come in.

Strategic Planning

The provision of a longer term planning framework to influence the activities of internal departments and external organisations in relation to individual service areas or authority-wide issues.

Promotion and Advocacy

The persuasion of one or more other organisations (eg private industry, voluntary bodies) to carry out activities that are likely to benefit the local community (eg by loans to small businesses, by grants to voluntary organisations).

(Appropriate credit to be awarded for other plausible roles such as revenue collection, implementing central government policy, etc)
(8)

- (b) Democratic deficit is concerned with a low level of democratic accountability in local government. Examples/sources include:

- The shift of some local government responsibilities to unelected and unaccountable bodies.
- The reduction in numbers of councillors. For example, France has one elected member for about every 120 citizens whereas the UK has one for about every 2,600.

3

- (c) *½ mark for identifying each model. Up to 1½ marks for description of each model, subject to an overall maximum of 8*

Local government as agency for central government; simply implements/administers policies for central government.

The central-local relationship is seen as a partnership with both sides working to common ends. Central government is invariably the more powerful partner, but local government is not totally subordinate as in the agency relationship.

Stewardship model. Central government, in the role of “master”, delegates considerable authority and discretion to local government.

Power-dependence model. Each side has sources of power that it can exert against the other. The relationship is one of bargaining, exchange and negotiation.

(Appropriate credit to be awarded for alternative models such as federal unitary government and devolved or centralised government)
(8)

- (d) *½ mark for identifying each model. Up to 1½ marks for discussion of each model subject to an overall maximum of 6*

Participative relationship

Members of the electorate share in local government decision-making and service provision. Individuals may be co-opted on to the Council decision making bodies, tenants may participate in the running of their estates, etc. This model makes the greatest contribution towards addressing and overcoming the democratic deficit.

Consultative relationship

Significant consultation of local people occurs as input into council decision-making, even though no direct part is taken by local citizens in decision-making. There are a variety of ways of consulting local citizens and the extent to which this consultation impacts on decision making also varies widely. The contribution of this model towards addressing and overcoming the democratic deficit lies approximately mid-way between the contributions of the two alternative models.

Informative relationship

The relationship between local authorities and citizens is restricted to one of information provision through, for example, “one-stop shops” or information lines. This relationship makes the least contribution to addressing and overcoming the democratic deficit. However, this relationship is no longer sustainable, given local authorities’ obligation, under Best Value, to consult their local communities.

(6)

(25)

Question 4

(a)

Income:

- (i) This is non-trading income. £10,000 should be deducted when computing the Schedule D Case I assessment. The interest receivable in the accounting period will be assessed under Schedule D Case III on the accruals basis. There are no income tax implications since the interest has been paid between UK companies on or after 1 April 2001. 1
- (ii) This is also non-trading income. £27,500 should be deducted when computing the Schedule D Case I assessment. The rents receivable in the period will be assessed under Schedule A on the accruals basis. 1
- (iii) This is also non-trading income. £12,000 should be deducted when computing the Schedule D Case I assessment. The premium is discounted by 2% for each year of the lease (other than the first year) and then assessed under Schedule A. The amount assessable is £11,040 (£12,000 less 8%). 2
- (iv) This is (in effect) negative depreciation and is not trading income. £880 should be deducted when computing the Schedule D Case I assessment. The sale proceeds of the plant (or its original cost, if less) will be deducted from the pool balance in the company's plant and machinery capital allowances computation. If the plant has been disposed of for more than original cost, any gain arising will be assessable as a chargeable gain, unless covered by the chattels exemption. 1

Expenditure:

- (i) If the debentures were issued for trade purposes, the interest payable in the period is an allowable trade expense. Otherwise, £30,000 should be added back in the Schedule D Case I computation and the interest payable will instead be deductible under Schedule D Case III as a non-trading debit (on the accruals basis). The company must account to the Inland Revenue for the 20% income tax deducted at source from interest payments made during the period. 1
- (ii) £2,450 (entertaining customers) and £1,000 (gifts of food, drink or tobacco) are disallowed and should be added back in the Schedule D Case I computation. The remaining expenses are allowable. The employees who benefit from the staff function will each be taxed under Schedule E on income of £90, since the cost of the function exceeds £75 per head. 1
- (iii) The staff loan written off and the increase in the general provision are disallowed, so a total of £900 (£600 + £300) should be added back in the Schedule D Case I computation. 1
- (iv) The property expenses of £6,190 are disallowed under Schedule D Case I but are deductible from the company's Schedule A income from the period (so long as the expenses were incurred wholly and exclusively for the purposes of property letting). 1

- (v) The Gift Aid donation is disallowed and should be added back in the Schedule D Case I computation. The amount paid in the accounting period will however be treated as a charge on income and will be deducted when computing the company's chargeable profits. 1
- (vi) If the debentures were issued for trade purposes, the legal fees payable on their issue are an allowable trade expense. Otherwise, £18,000 should be added back in the Schedule D Case I computation and the fees will instead be deductible under Schedule D Case III as a non-trading debit. The £3,000 payable in connection with the disposal of the office building will be disallowed under Schedule D Case I but taken into account when computing the gain or loss arising on the disposal. 1
- (vii) The car's list price exceeds £12,000. Therefore the allowable amount of the hire charge is restricted. The mid-point between £12,000 and £20,000 is £16,000, so the allowable charge is equal to £4,160 ($£5,200 \times £16,000/£20,000$). The balance of £1,040 is disallowed. 2
- (13)

(b)

	£	<i>Original cost</i>	<i>Rebasing</i>	
	£	£	£	
Disposal proceeds		250,000	250,000	1/2
Less: Incidental disposal costs		3,000	3,000	1/2
		247,000	247,000	
Less: Acquisition cost	50,000			1/2
Incidental acquisition costs	600			1/2
Enhancement in 1981	13,000	63,600		1/2
Market value 31/3/82		183,400	73,000	1/2
		183,400	174,000	
Less: Enhancement in 1986		18,000	18,000	1
		165,400	156,000	
Less: IA on MV 31/3/82 $(175.2-79.44)/79.44 = 1.205$ $1.205 \times £73,000$	87,965			1
Less: IA on 1986 enhancement $(175.2-97.85)/97.85 = 0.790$ $0.790 \times £18,000$	14,220	102,185	102,185	1
		63,215	53,815	

The chargeable gain is £53,815. All except £25,000 of the sale proceeds have been invested in a qualifying depreciating asset within the period beginning one year before the disposal and ending 3 years after it. Therefore £28,815 of the gain may be held over. The remaining £25,000 is immediately chargeable. 1

The held-over gain would normally become chargeable no later than 10 years after the date of acquisition of the depreciating asset (10 April 2011). However, if the company acquires an office building in 2006 for £225,000 or more, the held-over gain of £28,815 may then be rolled-over against the cost of the new building.

1

(8)

- (c) A close company is one which is controlled by five or fewer participators or by any number of participator-directors. The term “participator” normally applies only to a company’s shareholders, so a close company is generally one which is controlled by five or fewer shareholders or by its shareholder-directors. For this purpose, the rights of a participator’s associates are aggregated with the participator’s own rights. Broadly, the term “associate” covers family members and business partners.

1

The main consequences of close company status are:

- Any benefits in kind provided to participators (or to their associates) are treated as distributions. The effect of this rule is that the cost of such a benefit is disallowed in the company’s tax computation and that the person receiving the benefit is taxed as if he or she had received a dividend equal to the amount of the benefit. However, this treatment does not apply in some cases, notably if the benefit is taxable under Schedule E because the person receiving it is a P11D employee of the company.
- Any loans made to participators (or to their associates) are generally assessed to tax. The company must pay an amount of tax equal to 25% of the loan. This tax is repayable when the loan is repaid or written-off. If the loan is written-off, the participator (or associate) is deemed for tax purposes to have received net income equal to the amount written-off. This amount is grossed-up at the Schedule F ordinary rate. Further tax will be due if the participator (or associate) is a higher-rate taxpayer. Loans made in the normal course of the company’s business and certain other loans are excluded from this treatment.

1

1

If special tax rules did not apply to close companies, it would be possible for the small number of participators involved to manipulate the company’s financial affairs in such a way as to avoid tax. In particular, participators might be able to withdraw profits from the company without incurring a personal tax liability. This would be beneficial since rates of corporation tax are generally lower than those which apply to individuals.

1

(4)

(25)

Question 5

(a)

	<i>Non- savings</i>	<i>Savings</i>	<i>Dividends</i>	
	£	£		
Schedule E:				
Salary	30,000			½
Bonus (receipts basis)	3,900			1
BSI (188 x 100/80)		235		1
Schedule F (297 + 33)			330	1
	33,900	235	330	
<i>Less: Personal allowance</i>	4,535			½
Taxable income	29,365	235	330	
 <i>Income tax due:</i>				
Non-savings: 1,880 @ 10%	188.00			½
27,485 @ 22%	6,046.70			½
Savings: 163 @ 20%	32.60			½
72 @ 40%	28.80			½
Dividends: 330 @ 32.5%	107.25			½
	6,403.35			
<i>Less: CTC 4,932 @ 10%</i>	493.20	(see below)		1
	5,910.15			
<i>Less: Tax deducted under PAYE</i>	5,735.00			½
	175.15			
<i>Less: Tax deducted from BSI</i>	47.00			½
	128.15			
<i>Less: Tax credits on dividends</i>	33.00			½
Income tax payable	95.15			

The tax payable of £95.15 is likely to be collected by adjusting Edward's PAYE tax code for tax year 2002/03. Alternatively, this amount could be paid over directly to the Inland Revenue on or before 31 January 2003.

1

Notes:

- (i) ISA interest is exempt from income tax.
- (ii) The grossed-up Gift Aid donation of £128 (£100 x 100/78) extends the basic rate band to £27,648 (£27,520 + £128).
- (iii) A total of £402 (£72 + £330) of taxable income is taxed at the higher rate or at the Schedule F upper rate, so the CTC is reduced by £268 (2/3 x £402) to £4,932. (It is assumed that Edward is the higher-earning partner. A mark is given if the CTC is not shown in the computation because it has been assumed that Edward's wife is the high-earning partner and this is clearly stated).

(10)

(b)

	£	
Primary Class 1 contributions: (£29,900 - £4,535) x 10%	2,536.50	1
Secondary Class 1 contributions: (£33,900 - £4,535) x 11.9%	3,494.43	1 (2)

(c) *Living accommodation and ancillary services:*

- The basic benefit is equal to the annual value of the property or (if rented by company) the greater of annual value and the rent paid by the company.
 - A further benefit arises if the accommodation cost the company over £75,000, calculated by applying the official rate to the amount by which cost exceeds £75,000.
 - For properties acquired more than 6 years before being made available to the director, the cost of the property may be replaced for BIK purposes by its market value when first occupied by the director.
 - No benefit arises if the accommodation is job-related.
 - The cost to the company of any ancillary services provided in relation to living accommodation (eg cleaning, heat and light etc) is assessed on the director as a further benefit-in-kind, but this benefit is restricted if the accommodation is job-related (to 10% of net emoluments).
- 3

Company cars and fuel:

- The benefit is based on the list price of the car when new, including accessories other than mobile telephones (capped at £80,000) less any contribution made by the director towards the cost of the car (capped at £5,000).
 - For 2001/02 the benefit is computed by applying a percentage to the above figure, depending upon the number of business miles driven in the year, as follows:
35% (<2,500 miles) 25% (2,501-18,000 miles) 15% (>18,000 miles).
 - The benefit is reduced by one-quarter if the car is more than 4 years old at the end of the tax year.
 - The benefit is also reduced by any contribution made by the director for private use of the car.
 - For 2002/03 and beyond, the benefit will be graduated according to the car's emissions and will not be affected by the number of business miles driven or by the age of the car.
 - A separate benefit (ascertained by consulting a standard table) arises if fuel is provided by the company for private motoring, with no deduction for any partial reimbursement made by the director.
- 4

Beneficial loans:

- A taxable benefit generally arises if a company lends money to a director either interest-free or at a rate of interest which is lower than the official rate.
- The director is taxed on the difference between the interest actually paid (if any) and interest calculated at the official rate.
- No assessable benefit arises if the total amount outstanding on all of the beneficial loans made to a director does not exceed £5,000 at any time during the tax year.

2

Assets loaned for private use:

- If a company lends an asset to a director for private use, the director is assessed each year on 20% of the cost of the asset concerned.
- If the asset is subsequently sold or given to the director, a further benefit arises equal to the *greater* of:
 - (i) The asset's market value on the date of the sale or gift, less any amount paid for the asset by the director; and
 - (ii) The asset's market value when first loaned to the director, less amounts already assessed during the period of the loan, less any amount paid for the asset by the director.
- The loan of computer equipment is exempt from tax so long as the assessable benefit would not exceed £500 per annum.

3

Report presentation 1

Other significant benefits in kind to be awarded credit, subject to the overall maximum of 13
(13)

(25)

Question 6

(a) The VAT rules relating to companies which make exempt supplies as well as taxable supplies are as follows:

- Input tax suffered on goods and services used exclusively for the making of taxable supplies is “attributed to taxable supplies” and is recoverable.
- Input tax suffered on goods and services used exclusively for the making of exempt supplies is “attributed to exempt supplies” and is not recoverable.
- A proportion of any remaining input tax is attributed to taxable supplies and is therefore recoverable; this proportion generally depends upon the ratio of taxable supplies to total supplies.
- If the total amount of input tax not attributed to taxable supplies is no more than £625 per month (on average) and does not exceed 50% of all input tax, this input tax may also be recovered.

4

(b) The VAT consequences of offering discounts to customers are as follows:

- If a trade discount is given, output tax is based upon the price charged to the customer after this discount has been deducted.
- If a cash discount is offered for prompt payment, output tax is based upon the price that would be charged to the customer if the maximum available cash discount were deducted. This is the case whether or not the customer actually takes advantage of the cash discount.

2

(c) The tax point of a supply is the date on which the supply is deemed to have occurred for VAT purposes. For a supply of goods, the basic tax point is the date on which the goods are removed or made available to the customer. For a supply of services, the basic tax point is the date on which the services are performed. However, the tax point of a supply may differ from the basic tax point in the following circumstances:

- If a tax invoice is issued or payment is received on a date which is earlier than the basic tax point, then that date becomes the tax point.
- Otherwise, if a tax invoice is issued within 14 days after the basic tax point, then the invoice date becomes the tax point.

If VAT rates change, the tax point of a supply determines the rate of tax which is applicable to that supply. The tax point of a supply also determines the VAT period in which output tax relating to the supply must be accounted for or the VAT period in which input tax relating to the supply may be reclaimed.

4

- (d) Two examples of non-recoverable input tax are input tax on business entertaining and input tax on the purchase of motor cars (unless acquired wholly for business use).

2

- (e) Indirect taxes are those where the formal incidence of the tax is different from the effective incidence of the tax. VAT is an indirect tax because formally it is a turnover tax payable by businesses but effectively (since the tax is passed on to customers) it is borne by those who buy goods or services from businesses.

A regressive tax is one where the proportion of income or wealth paid in tax decreases as the amount of income or wealth increases. VAT is essentially regressive, since the amount of VAT payable when a specific item of goods or services is purchased is based solely upon the price of the item and is not influenced in any way by the buyer's financial circumstances. For example, the VAT payable on a litre of petrol represents a much higher proportion of the income of the average student accountant than it does of the average millionaire.

A poll tax of a fixed amount per head of the population is perhaps the most regressive form of tax conceivable and (if implemented) would make the UK tax system more regressive rather than less.

3

- (f) With the advent in recent years of self-assessment for companies, there is now some broad similarity between the way in which VAT is assessed and collected and the way in which corporation tax is assessed and collected. The main relevant points are as follows:

VAT

- VAT is generally assessed and collected on a quarterly basis. Most VAT-registered businesses submit a quarterly VAT return to HM Customs & Excise, showing the amounts of output tax and input tax for the period covered by the return. Any tax due is then payable within a month of the end of the quarter concerned. However, some small businesses make annual returns and certain businesses choose to make monthly returns.
- VAT is largely a self-assessed tax. Registered businesses are required to maintain a VAT account in their books (together with supporting documentation) and to use the information contained in this account to complete the VAT return and compute their tax liability. The main role of HM Customs & Excise in relation to VAT is to issue VAT returns, receive the completed returns, collect the VAT due from registered businesses and arrange repayments of tax where necessary.
- The fact that VAT is mostly self-assessed places an administrative burden on registered businesses but greatly reduces the costs of assessing and collecting VAT. However, it is the duty of HM Customs & Excise to check that businesses are operating the system correctly and regular "control visits" are made to all registered businesses. Formal VAT assessments may be made by HM Customs & Excise if a an incorrect return is submitted or if a return is not submitted at all.

Corporation tax

- Corporation tax is (in general) assessed on an annual basis. The main means of collecting information is a tax return (form CT600) which is sent by the Inland Revenue to companies just after the end of each accounting period and which should be filed within 12 months of the end of that period. In general, corporation tax is payable 9 months after the end of the period to which it relates but some companies are required to pay by instalments.
- A system of self-assessment applies to companies and the legal responsibility for assessing the amount of tax due falls upon the company concerned. The Inland Revenue's main role is to issue tax returns, check self-assessments, send statements of account to companies and ensure that the right amount of tax is paid.
- A further duty of the Inland Revenue is to audit a proportion of tax returns and to conduct enquiries into the financial affairs of companies where irregularities are discovered.

Penalties

Both HM Customs and Excise and the Inland Revenue are able to impose a range of financial penalties to punish non-compliance with the tax system. Penalties may be imposed for not submitting a tax return, submitting a late return, submitting an incorrect return and so forth. Interest and surcharges may be levied if tax is paid late. In an era of self-assessment, these sanctions make it more likely that most businesses will provide the correct information on time and pay the right amount of tax on time.

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(g) For local authorities (and other statutory bodies):

- Many supplies made by such a body fall outside the scope of VAT since they are not made in the course of business. However, some of the body's activities may be regarded as business activities, in which case supplies made in the course of these activities will fall within the scope of VAT.
- Although input tax is generally not recoverable if incurred in connection with non-business activities, a special refund scheme permits local authorities and other statutory bodies to recover such input tax.
- Special partial exemption rules apply to local authorities and other statutory bodies which make both taxable and exempt supplies. Input tax which is attributable to exempt supplies can generally be recovered if it is insignificant (ie no more than £625 per month or less than 5% of all input tax incurred by the body).

VAT treatment of NHS bodies, educational bodies etc also acceptable 3

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